

8-1-2013

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### Recommended Citation

Sanusi, Anwar and Dwiputranti, Septiana (2013) "Institutional Arrangement and Policy for Improving Competitiveness and Innovation in Local Government Investment," *BISNIS & BIROKRASI: Jurnal Ilmu Administrasi dan Organisasi*: Vol. 20 : No. 1 , Article 5.

DOI: 10.20476/jbb.v20i1.1864

Available at: <https://scholarhub.ui.ac.id/jbb/vol20/iss1/5>

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# Institutional Arrangement and Policy for Improving Competitiveness And Innovation in Local Government Investment

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**Abstract.** There are three specific objectives outlined in this paper, the first objective is to identify and describe existing condition of institutional arrangement of public services in several local governments, the second objective is to examine problems and challenges in providing public services in the areas of investment, the last is to provide recommendations on institutional models and strategies or innovations which can be applied in order to improve performance in investment services; understanding how regional government institutions can contribute significantly to improve investment for economic growth. Qualitative method was employed to evaluate the effectiveness of increasing customer satisfactions, reducing red-tape, and improving coordination amongst government institutions, an in-depth interviews conducted with resource persons as representatives from stakeholders, including government officials, businessmen (entrepreneurs), and experts from local universities. By evaluating City Government of Batam as the best practice in the institutional arrangement for investment, the main potential contribution of this study is to provide valid information about the most crucial problems and challenges in institutional arrangement for investment affairs in local government to which their investment target could be achieved by using the institutional model provided.

**Keywords:** institutional arrangement, public investment policy, local government, investors' satisfaction

**Abstrak.** Ada tiga tujuan tertentu yang digariskan di dalam makalah ini, tujuan pertama adalah untuk mengenali dan menjelaskan kondisi yang ada sekarang dari susunan kelembagaan pelayanan publik di beberapa pemerintahan daerah, tujuan kedua adalah untuk mempelajari masalah-masalah dan tantangan-tantangan di dalam hal penyediaan pelayanan publik di daerah-daerah tujuan penanaman modal, tujuan terakhir adalah mengajukan rekomendasi di dalam hal model kelembagaan dan strategi atau inovasi yang dapat diterapkan untuk meningkatkan kinerja pelayanan penanaman modal; pemahaman bagaimana lembaga-lembaga pemerintah daerah dapat menyumbang secara bermakna untuk meningkatkan penanaman modal demi bertumbuhnya ekonomi, mengurangi birokrasi dan meningkatkan koordinasi di antara lembaga-lembaga pemerintah. Metode kualitatif digunakan untuk mengevaluasi efektivitas peningkatan kepuasan pelanggan dan meningkatkan koordinasi antar lembaga pemerintah, wawancara mendalam dilakukan dengan para narasumber yang mewakili para pemangku kepentingan, termasuk pejabat pemerintah, pengusaha, dan para ahli dari universitas-universitas setempat. Dengan mengevaluasi Pemerintah Kota Batam sebagai penerapan terbaik dari penataan kelembagaan di dalam hal penanaman modal, kontribusi utama penelitian ini adalah penyediaan informasi yang sah mengenai masalah-masalah dan tantangan-tantangan yang paling penting yang dihadapi penataan kelembagaan untuk urusan penanaman modal di pemerintah daerah dalam rangka mencapai target penanaman modal melalui penggunaan modal penataan kelembagaan yang tersedia.

**Kata kunci:** penataan kelembagaan, kebijakan investasi publik, pemerintah daerah, kepuasan investor

## INTRODUCTION

Investment is one of the most crucial services to be concerned by the Government of Republic Indonesia, as a result of the multiplier effect of growing investment for increasing the economic growth, reducing unemployment and alleviating poverty. The importance of investment is recognized properly by the government as it was presented by the Minister of Administrative Reform by stating that investment has broad implications in economic and political life. He believes that improvement of public services, for upgrading economic life and increasing confidence in prospective

investors, is necessary. In addition, he mentioned that the poor performance of the public service bureaucracy is the major factor of the declining interest to invest in this country. Furthermore, based on studies related with public services delivery by government officials, various aspects of public services delivery still do not meet the expectation of the society. The public still feel that procedures and mechanisms in public services are complicated, non-transparent, non-informative, non-accommodating and inconsistent (Natapura, 2009). Eventually the public feel that these procedures and mechanisms do not ensure legal certainty, untimely, and also costly.

In May 2008, Euromoney held an international

conference titled “The Indonesia Investment” held at the Westin Resort, Nusa Dua, Bali. The conference was held in order to encourage greater participation of foreign investors in various development programs in the public and private sectors. The conference discussed various issues concerning among others economic development, investment prospects, development of infrastructure, capital markets and banking, and the potential development of Sharia-compliant investment instruments. At the conference, the Minister of Finance delivered a keynote speaker presentation contains the views and policies of the Government in the areas of investment, such as reforms in the areas of policy and service delivery, including through combating corruption and increasing transparency and accountability of public services, and improving the investment climate and competition market.

Several government policies in the areas of investment reaped positive results. Kuncoro (2007) provided data of increment of the total investment realization recorded by the Investment Coordinating Board (BKPM). Total investments approved during January-March 2007 amounted to Rp 204.3 trillion, an increase of 447.2% over the same period in 2006. From these data Kuncoro further questioned if this phenomenon meant the end of the dry season, and marked improvement of investment climate in Indonesia. However, the implementation of various policies hatched by the government is not sufficient to fully raise the level of investment in Indonesia. In his study, Kuncoro further shows that Indonesia’s investment climate is worse than that of China’s, Thailand’s, Vietnam’s and other ASEAN countries’. He emphasised that, backed by many other studies, the decentralization has somewhat deter the investment climate in Indonesia for two main reasons. The first reason is the low public service delivery marked by costs of uncertainty and the length of time required by the bureaucracy to process licensing. The second is the lack of clarity of law and numerous regulations which are not “pro-business”. These are identified as a proof that the business climate is not conducive for investment.

The experience of China in attracting foreign capital need to be examined. In China, in order to provide investment permit, perspective investors just need to contact the Office of Foreign Investments. While for investors whose investment are over US\$ 30 million must get permissions from the central office, investments which are less than US\$ 30 million will simply need to contact the Office of Foreign Investment in the local area. The approval process for foreign investment is maximum three days. If until three days there was no notice of from investment office, the foreign investment application

would automatically be deemed as accepted by authority.

Sense of service (or simply called service) according to the American Marketing Association, quoted from Donald W. Cowell (1984), is an activity or benefit offered by one party to the other party and essentially intangible and does not result in ownership of anything, the production process may or may not be linked with a physical product. Meanwhile, according to Christopher H. Lovelock (1991), service is an intangible product, short-lived and perceived or experienced.

The definition of the above mentioned services emerged from the private world which then affected the perception of the public service. There are misunderstandings from most people when it comes to meanings of public service. Some people think that the public service concerned only with administrative things (such as correspondence, recommendations, etc.), whereas the scope of the public service is very wide, including provision of physical services or goods, to services such as provision of facilities and utilities, roads, bridges, and other infrastructure, the economy, transportation, waste management, street lighting, and so forth. Service in this sense also covers regulation and control (licensing, peace and order), coaching services (community empowerment, education, health and socio-cultural). Similarly, the service in the provision of information, dissemination, outreach and consultation, and other services related to the duties and functions of the state apparatus, such as legal service, security provision, and others.

Decree of the Minister of Administrative Reform (MenPAN-RB) Number 63 of the Year 2003 on General Guidelines for Implementation of Public Services was published in an effort to promote the establishment of public service excellence to meet the expectations and needs of the community, as well as to promote the improvement of the system and procedures of institutional services. This decree public classifies services into three groups: Group of administrative services, Group of goods services, Group of services. Moreover, the Law Number 25 of the Year 2009 on Public Services explained that the scope of public service includes the services of public goods and public services and administrative services set out in the legislation which includes education, teaching, jobs and businesses, housing, communication and information, environment, health, social security, energy, banking, transportation, natural resources, tourism, and other strategic sectors. Furthermore, the opinion of a matching comes from Institute of Public Administration (1998) in which the public service is defined as any form of public service activities undertaken by government agencies at the central and local, and in the state / local enterprises in the form of goods and / or services, whether in meeting

the needs of community as well as in the implementation of the provisions of legislation. Meanwhile, the Ministry of Home Affairs' Integrated One-Stop Service Module Development (2004) calls the service as a public service, and defines it as an aid process to others in certain ways that require sensitivity and interpersonal relationships in order to create satisfaction and success.

From the definition, it can be seen that in the context of public services in Indonesia is not limited to the services of the administrative and physical nature. Moreover, public services include broader definition of services, which include goods and services, and not only for a short period of time. In addition, the public service is felt to be more specific because it was not only done by the bureaucracy and to serve customers but to serve citizens (in LAN Purbokusumo et al, 2006). Thus, the public service is an obligation of the state to the citizens to meet their basic needs so as not merely to serve, the state should also be responsible in the service process, so that the extent of services provided to the public can be affordable, convenient, fast and efficient both in time and the form of financing.

Public service providers are obliged to prepare and establish standards of care with respect to the ability of the organizers, community needs and environmental conditions. In designing and setting up service standards, service providers shall involve the public and stakeholders which is done by exercising the principle of non-discrimination, direct relation to the type of service, competence, and prioritization, deliberation and attention to diversity. It should also be related to the quality of services which must be met by the public services (which can be differentiated with service in the private sector). In the United Kingdom of Great Britain, there is UK's seven principles of public life which are further developed by Dexter (2001) into 10 basic principles of public services (which distinguishes it from other general services) in giving to the community are as follows: Selflessness, Integrity, Objectivity, Accountability, Participation and Involvement, Openness, Honesty, Leadership, Equality, and Competency.

Furthermore, the Law Number 25 of the Year 2009 stipulates apparatus who are carrying out the public service should be: (1) fair and non-discriminatory, (2) careful, (3) polite and friendly, (4) assertive, reliable and not delaying, (5) professional, (6) not complicating, (7) complying with the lawful orders of their superiors and reasonable, (8) upholding the values of accountability and integrity of state institutions, (9) not disclosing confidential information or documents in accordance with the legislation, (10) open and be able to take appropriate steps to avoid conflicts of interest, (12) not abusing the

facilities, infrastructure and public service facilities, (13) not providing false or misleading information in response to requests for information and proactive in meeting the public interest, (14) not misusing the information, position and / or authority, (15) behaving in accordance with decency, and (16) not contradictory from the procedures

Definition of investment is also provided in the Law Number 25 of the Year 2007 on Investment, which defines as any form of investment activity, both by domestic and foreign investors to do business in the territory of the Republic of Indonesia. Domestic investment (DCI) is to carry out business activities in the territory of the Republic of Indonesia by domestic investors and using domestic capital. Foreign investment (PMA) is to carry out business activities in the territory of the Republic of Indonesia by foreign investors, whether using foreign capital as well as a joint venture with a wholly domestic investors. Furthermore, still according to the Law Number 25 of the Year 2007, the implementation of investments in Indonesia aimed at improving national economic growth, create jobs, promote sustainable economic development, enhance the competitiveness of the national business, increase capacity and technological capabilities nationwide, encourages the development of economy, the potential economic process into force real economy by using funds derived from domestic and from abroad, and improving social welfare.

Increasing role of the above mentioned investments should still remain in the corridor of the planned national development policies which aims to maintaining macroeconomic stability and economic balance between regions, sectors, businesses, and community groups; supporting the role of national business as well as meeting the rules of good corporate governance. On that end, the implementation of investment in Indonesia is organized by the principles of: rule of law, openness, accountability, equal treatment and not differentiate the origin of the state, mutuality, efficiency of justice, sustainability, knowledgeable environment, independence, balance of economic progress and national unity.

In service in the areas of investment in the center, Article 27 of the Law Number 25 of the Year 2007 stipulates that the government coordinating investment policies, good coordination among government agencies, the government and Bank Indonesia, the government agencies to local governments, and between governments. The task of coordinating the implementation of investment policy is undertaken by the Investment Coordinating Board (BKPM) who coordinates the implementation of policies and investment services.

In local areas, along with the issuance of Government Regulation (PP) Number 41 of the Year 2007 regarding

Regional Organisation, investment services are carried out by various regional government organizations established as an independent agency, office or as a unit attached to the department or another agency. These various institutional conditions is not endorsed by BKPM. This condition is due to the complicated coordinations that BPKP had to do. According to BKPM, because capital investment activities are cross-sectoral, the administration of capital investment in the local area must have a coordination function. Besides, BKPM suggested an ideal form of investment organization is an Agency.

Looking at investment in the service sector, according to the Article 30 of the Law Number 25 of the Year 2007, the central and the local government need to ensure the certainty and security of capital investment. In carrying out its responsibility in the field of investment, the central government can administer it by itself, delegate it to the governor as the representative of the government, or assign it to the Regency / City Government. Further provisions regarding the division of governmental affairs in the field of investment is stipulated by Government Regulation Number 38 of the Year 2007 about Governance between the Government, Provincial Government and District / City.

### RESEARCH METHODS

This is a qualitative and descriptive research, where the size used in the study are usually in the form of qualitative such as good, bad, up, down and so on. In line with the research objectives, this research is descriptive, which attempted to describe the state of the object being studied. This is achieved by studying the material and input which derived from interviews. Through in-depth interviews, important points were explored in accordance with the purposes of the research, as an addition, direct observation of objects research in accordance with the facts or the symptoms and what they are.

Sources of data in this study are all government entities in Indonesia which perform services in the areas of investment, including the central and local governments. However, due to some limitations, not all data sources can be researched and samples taken. Sample selection was not intended to generalize the condition of overall population.

Sample selection was done by using data on local government studies Committee on Implementation and Monitoring of Regional Autonomy (Komite Pelaksanaan dan Pengawasan Otonomi Daerah-KPPOD). Since 2001 to 2005 KPPOD has carried out a study to assess the attractiveness of investment in the region based on five main factors, namely: institutional, social, political, regional economy, labor, productivity, and

physical infrastructure factors. By using factors of regional institutions as a determinant to obtain rankings, improvements in institutions could be one of the key areas to improve rankings.

According to the type of this research, the type of the data obtained is qualitative, therefore qualitative data analysis is used. The method provides interpretation of the data under the conceptual framework, and existing theories can be obtained to form a complete picture in accordance with the objectives of the study. The primary data collection method used in this study is in-depth interview, and interviews with key selected informants for necessary things. For secondary data collection, the researchers used literature study of legislation and related literatures. Key informants come from (1) Batam City Government, including the Secretary, Department of Trade and Industry and Investment Regional Government Organisation; and (2) Community, including Chamber of Commerce and Businessman/Investors.

### RESULT AND DISCUSSION

In Batam, integrated license service has been established by Batam Mayor Act Number KPTS.315/HK/IX/2001 on the Establishment of Business Licensing Service Center (One Stop Service). Under this act, all business licensing services in Batam city are performed in the Integrated Licensing Service Center Batam city, located in Sumatra Promotion Centre (SPC) Building, Batam Center. Selection of SPC is based on the agreement between the Government of Batam, Authority of Batam and the Investment Coordinating Board (BKPM), in order to integrate the licensing service to make Batam as a special economic zone. Therefore, not only does this agency integrate SPC licensing services in Batam, but more than that, it also integrates licensing services beyond local government area in Batam.

The Local Government Organizations (OPD) which are involved in the Business Licensing Service Center (One Stop Service) Batam city include: Batam City Investment Board, as the coordinator; Environmental Impact Management Agency of Batam as a member; Transportation Agency of Batam as a member; Ministry of Tourism and Culture of Batam as a member; Local Revenue Office of Batam as a member; Ministry of Settlement and Regional Infrastructure of Batam as a member; Batam City Health Department as a member; Batam City Department of Labor as a member; Ministry of Industry and Trade of Batam as a member

Furthermore, based on Decree of Mayor of Batam no: KPTS 145A/HK/VII/2006, there are some organisations who are members of the World Trade Organisation (WTO)

include: Ministry of Marine, Fisheries and Agriculture of Batam; Ministry of Land Batam City; Communication and Information Agency of Batam.

Now, the Integrated Services Licensing Service Center Batam city that is just a one-roof service, not a one-stop service. Thus each OPD has a counter which is located in one building. This condition, according to the key informants, is because according to the characteristics of the area of Batam where complex and heterogeneous society so that the service should be able to accommodate all interests. the Regional Secretariat of Batam has conducted consultation and orientation at District Government of Sragen for investment and seen the difference in the conditions in Batam City and Sragen District. Sragen is homogeneous while Batam is heterogeneous in terms of both ethnic groups and citizens.

To support the implementation of investment, the Technical Service Center for Integrated Licensing was established by the city of Batam under the Decree of Mayor of Batam City Number KPTS.163/HK/III/2009 which consist of related OPD. Technical Team of Integrated Licensing Service Center is a working group consisting of structural elements of OPD officials associated with the authority in providing licensing services. If necessary, the head of OPD can assign other staff to help the Technical Team.

The Technical Team conducts activities in the Sumatra Promotion Centre (SPC) Building, namely (1) application receiving, (2) the research requirements, (3) verification, and (4) license documents issuing and recommendations that will be signed by the relevant SKPD. All these activities are based on the Standard Operating Procedures (SOP) licensing service that is determined by the Mayor of Batam. To assist the implementation by the Technical Team, the Secretariat of Technical Team Center Integrated Licensing for Batam City is led by the Head of Secretariate, who is *ex officio* held by the Head of Investment Board of Batam City. Technical Team has a responsibility to report and receive briefing from the Head of Mayor Batam via Head of Investment Board of Batam City, as the coordinator of the Integrated Licensing Service Center.

Although generally positive, the negative outlook could still be found in Batam where employers see that the process of service in the field of investment is very convoluted and time consuming. In addition, a negative outlook is also focused on the lack of discipline and work ethic of the human resources at the local level as a result of the work culture. This condition is exacerbated by a number of government employees who act as “brokers”. There is a suggestion from businessmen in Batam City for the government officials to study the ways of working in

the Singapore Government in providing good service to investors as well as the work culture.

In the case of Batam, unlike other areas which implement one-stop service, the City is implementing an integrated one-stop service, where the one-stop service counter involves each organization of the local government (OPD) in the same building. In fact not only the OPD, this one-stop service involves other organizations outside Batam City Government, covering Batam Authority and the Investment Coordinating Board (BKPM) Center. This situation shows in practice there are variations in the application of the concept of one-stop services, although the legislation is directed at one-stop service. This is due to specific conditions of Batam city, which is a special economic zone, and the conditions of pluralistic society in which it accommodates. Special conditions or cases of Batam must be accommodated in setting up the integrated services unit.

In addition, related with the Act of Ministry of Internal Affairs Number 20 of the Year 2008, the study revealed that the settings in this act has not been fully implemented by the local government unit in the organizational management of integrated services. For example, in terms of organizational form, the Act stipulates that the Agency and / or the Office of the unified licensing service unit has the task of coordinating and organizing administrative services in the field of licensing in an integrated manner. From this setting, the point of coordinating function of that agency or office unit integrated license service is supported by a Secretariat headed by a chief, who because of his position at the same time also serves as the Head of the Head Office. From the study, none of the units of integrated services in the area follows the shape of this arrangement. Local governments follow the settings in PP. 41 of 2007 in which the office of the Head of Agency / Office of the Secretary apart from office.

In Batam, due to the nature of the integrated service as one-stop service, the centralized form chosen in this case is not connoted as a form or nomenclature of the organization, but more likely to be associated as a place where the entire licensing services co-exist. For smooth coordination, the license service centers established *ex-officio* secretariat chaired by one of the Head of Local Investment Agency. This condition is certainly not in adherence with the arrangements set out in the Act of Ministry of Internal Affairs (Permendagri) that the Agency and / or unified licensing service office is working within the units budget users. Furthermore, the organizational structure patterns in Permendagri also not followed by the local government. The study found that the structure of the organization BPPT in some areas following the settings in Government Regulation

(Peraturan Pemerintah–PP) Number 41 of the Year 2007. In fact, the BPPT has Karanganyar District Board of Technical Unit in the organizational structure.

Further related to the institutional investment services in this area, in addition to integrated licensing services unit, each region also has a unit that handles capital investment either in the form of Agency, Sector or Sub-section attached to one of the regional organizations (OPD) as in Regional Secretariat or the Department and the Agency. Under these conditions, the existence of two organizations: an integrated service unit and the unit in charge of investment, need to be considered along with the issuance of Presidential Decree Number 27 of the Year 2009 on services in the One Stop Investment governing the establishment of One Stop Services (PTSP) in capital investment in the national and local levels.

### CONCLUSION

Since the issuance of Presidential Decree Number 27 of the Year 2009, there are two types of regulations governing unit integrated services, namely: Presidential Decree Number 41 of the Year 2007, Act of Ministry of Internal Affairs number 57 of the Year 2007, and Act of Ministry of Internal Affairs Number 20 of the Year 2008 which regulates unit integrated services in general; Presidential Decree Number 27 of the Year 2009 which specifically regulates one stop service in the field of investment. Furthermore, institutional arrangements related to public service in the fields of investment, the services in the field of investment Batam City implemented by the implementing unit licence of investment services, namely integrated service unit. Batam city in this case has a special character because it is an area of special economic zones. In the city of Batam, it is translated to setting up an integrated license service Business Licensing Service Center (One-Stop Service) which, despite the name “Center”, is not a structural organization. The word “center” here refers to “one place” instead. Integrated Licensing Service Center is located in Batam City Sumatra Promotion Centre (SPC) Building, in order to integrate the Batam Center. It also provides licensing services beyond local government area in Batam. Moreover, Integrated Licensing Service Center Batam City is now one stop service which in the form of counter is in one building

In terms of organization, the Board of Investment of Batam City is an integrated service center coordinator. Furthermore, to support the implementation of the centralized task, a Technical Service Center for Integrated Licensing Batam City has been established. The purpose of the establishment of the Centre is to implementat the

task of team which is formed by the Technical Service Center Secretariat for Integrated Licensing Batam City. The secretariat is led by a Chief Secretary, who is an ex-officio chaired by the Head of City Investment Agency Services Batam.

The main potential contribution of this study is to provide valid information about the most crucial problems and challenges on the institutional arrangement for investment affairs in local government. By evaluating Batam city’s local government as the best practice on the institutional arrangement for investment affairs, the institutional model that is provided can be used by other local governments to achieve their investment targets.

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