



# Model On Legal Transformation of the Local-Owned Enterprise to Public and/or Private Local Entities towards Climate Investment Boost

Bagus Oktafian Abrianto<sup>a</sup>, Sri Winarsi<sup>b</sup>, Agus Widyantoro<sup>c</sup> & Faizal Kurniawan<sup>d</sup>, <sup>a,b</sup>Administrative Law Department, Universitas Airlangga, Indonesia, <sup>c,d</sup>Civil Law Department, Universitas Airlangga, Indonesia,

The investment climate in Indonesia, after the issuance of the Investment Law and the demands of the ASEAN Economic Community in 2016 and in line with the Nawacita program of Joko Widodo, has made investors and the nation of Indonesia more active in the realization of economic independence by mobilizing the strategic sectors of the domestic economy. Efforts to increase local revenue have come by way of establishing Local-Owned Enterprises (Badan Usaha Milik Daerah/ BUMD in bahasa) to support the synchronization and objectives of regional autonomy. BUMD form, among others, Local Enterprise, Regional Development Bank and are pioneers of business activity. Some BUMD have low financial performance, so their function as a source of regional income is not achieved because the profit / profit given to the Provincial Government, City and Regency is very small or even a loss. One cause is the corruption done by BUMD itself. Therefore, this research is conducted in the framework of the development of regional investment through the transformation of the status of Local-Owned Enterprise into Public Local Entities or Private Local Entities as regulated further by the Law on Regional Government. This research is a legal research; the method used in this research is a statute approach by needing an empirical approach and case approach to support the issue.

**Key words:** *Legal Transformation, Local Owned Enterprise, Public and/or Private Entities, Investment.*



## **Introduction**

The Republic of Indonesia is divided into provincial regions. The State recognizes and respects special regional government units that are regulated by the law (Article 18 letter b paragraph (1) of the 1945 Constitution of the Republic of Indonesia). What is meant by regional government units that are special in nature are those that are given special autonomy. Special Autonomy itself is a special authority that is recognized and given to special regions, to regulate and manage the interests of local communities according to their own initiative based on the aspirations and basic rights of the community. The regulation, concerning the existence of special autonomy, lies in Article 225 of Law Number 32 of 2004 concerning Regional Government. (Undang-Undang, 2004) This arrangement is aimed at affirming the recognition and respect of the state for special regional government units.

The journey of government reform that has taken place in Indonesia has led to paradigm shifts in governance in the context of regional formation and community empowerment. This is motivated by the fact that Indonesia is a unitary state based on the principle of decentralization which provides opportunities and freedom for regions to carry out regional autonomy. Regional autonomy in response to demands for change in a centralized state policy pattern and an authoritarian government are expected to empower the region more optimally. Thus the burden and activities in the area will be greater than the past (Achmad, 2004).

One of the efforts to find sources of government development project financing, the existence of Regionally Owned Enterprises (hereinafter referred to as "BUMD") for the Provincial, City and Regency Governments is important as an alternative to regional income sources. However, there are several BUMDs that have low financial performance so that their function as a source of regional revenue is not achieved because the profit sharing provided to the Provincial, City and District Governments is very small and even some are losing money. One form of BUMD legal entity that still has a low performance is Regional Enterprise (PD). This form of BUMD company provides social service and service duties.

In the provisions of Article 1 number 6 of the State Finance Law (Undang-Undang, 2003), a Regional Enterprise is a business entity where all or part of its capital is owned by the Regional Government. The purpose of the establishment of regional companies is to participate in carrying out regional development in particular and the development of people's needs by prioritizing industrialization and tranquility as well as the calm of work towards a just and prosperous society.



However, many Regional Enterprises, engaged in various fields, have long demonstrated low financial performance. For instance, the PDAM (Perusahaan Daerah Air Minum) in Purwakarta Regency, in general the operating profit obtained by the company during the period of 2006-2010 experienced fluctuations that tended to decline. This shows a situation that is not good for the company, because the acquisition of operational profit is usually used as a reference for measuring the company's operational performance. Thus, the profits obtained by the company should increase from the previous period. But what happened was the actually decreased in terms of obtaining an operating profit. In 2008 the profit was decreased by 50.19% or decreased by Rp.334, 159,384, from the previous year. In 2010 the profits earned by the company decreased by 21.70% or decreased by Rp.80, 147,354. (Agung, 2013) Many factors affect the performance of Regional Companies, one of which is the legal entity. Due to the Regional Government Law and its implementation regulations, BUMDs are allowed to change their legal status.

Besides that, the cause of the loss is due to acts of corruption by officials within the BUMD. Some cases of corruption related to BUMD include corruption cases of the release of assets of BUMD in East Java Province, Limited Liability Company PT.. Losses are reported, from *tempo* lists, to be as much as Rp.10, 800,000,000 (ten billion eight hundred million rupiah). (Nur, 2017)

The reasoning of the defendant, Dahlan Iskan, was to sell the assets of PT. Panca Wira Usaha Jawa Timur, was at that time forced to accept an offer to lead a Regional Enterprises after changing its status to a limited company. The request was made by the East Java Governor at the time, Imam Utomo, to Dahlan Iskan. Receiving the offer, Dahlan Iskan told Imam Utomo that Dahlan Iskan was willing to accept if the Regional Enterprises changed to a Limited Company. Dahlan Iskan argued that he could not afford it if any company decision-making was still in the form of regional companies, which had to go through a prolonged political process in the Regional Parliament (DPRD). After changing into a Limited Company, Dahlan accepted the Governor's request and took care of the company, going almost bankrupt. (Dian, 2017)

This is different from the case experienced by the East Java Provincial Company PT. Panca Wira Usaha, the Sidoarjo Regency Regional Enterprises, the Regional Business Enterprise. A case of alleged corruption in the financial management of a Regional Business Enterprise (PDAU) was raised from investigation to investigation. The Sidoarjo District Attorney's investigation team (Kejari) has received evidence of suspected financial management irregularities, between 2010-2016. There are false allegations in the contracts of various business enterprises and DTA (partners). Because the DTA was unable to pay, from 2015



until now, PT Lapindo Brantas Inc. BBG (new partners) have paid DTA dependents between Rp30 billion to Rp50 billion. (Redaksi, 2017) Sidoarjo District Attorney collects data and information related to alleged leakage of PDAU's financial management which reached billions of rupiah. (Syaihul, 2017)

Meanwhile, the Surabaya District Attorney is currently investigating the alleged corruption case of PD Pasar Surya. Several market leaders and a number of employees have allegedly misused the financial property of the area-owned company (Mansoor & Sultana 2018). These financial irregularities occurred in Keputran Market, Pasar Kembang, Wonokromo Market, and Kupang Market, with losses of hundreds of millions of rupiah. In addition, a corruption case that is now plaguing a Regional Enterprises, namely a corruption case at Delta Surya Sidoarjo Regional Water Company (PDAM). The dispute in this case has ensnared the President Director Sugeng Mujiadi as a suspect. In fact, three directors who were fired, filed a pretrial suit against the Sidoarjo Regent. The 'mafia' culture and power network, as well as political circles must be ended immediately. Corruption, collusion and nepotism (KKN) must be cleared out. Conversely, the regional government, especially the Mayor / Regent or Governor must be brave to take decisive steps by overhauling the existing system, towards a professional company, without the influence of certain circles of power or political circles. (Totok, n.d) .

Findings of irregularities in the company indicate weak control and supervision of relevant officials. This condition indicates that the company is led by people who do not have competence in their fields, not balanced by strict supervision. It could even be at a technical level, filled with mediocre people (Mansoor, Sultana & Saeed 2018). That is all very potentially mis-operational, until mis-management. It triggers abuse, from the lower levels through to the leadership levels. Therefore, returning again to the efforts to improve the regional companies, the government should reorganize, even overhauling the total system and potentially corrupt management (Mahrinasari, Haseeb, Ammar and Meiryani, 2019). Apply professional management that is effective, efficient and productive, and independent, without KKN and especially without the intervention of any group. Create a healthy company, and profit away from the lair of corruptors. Clean sweep people who do not have professionalism, instead recruit new workers who are 'fresh', full of energy, not contaminated with politics and power, and who are not corrupt. (Redaksi, 2017)

From the explanation of the background of the above problems, the formulation of this study can be designed. 1) Prospects and benefits of transformation of the form of Regional Companies in the context of developing regional investment; and 2) Criterium changes in the form of regional companies in the framework of developing regional investment.

## Methods

The research method used is normative legal research. Normative legal research is carried out by analyzing the norms in the relevant laws and regulations. This study also analyzes relevant legal principles. So, the facts are analyzed whether they are in accordance with the legislation and the legal principles or not.

## Discussion

### *Implications of Law 23/2014 on Legal Forms of Regionally Owned Enterprises*

Law Number 5 of 1974, concerning the Principles of Regional Administration, regulated two forms of Regionally Owned Enterprises (BUMD), namely Regional Enterprises and Limited Liability Companies. BUMDs in the form of Regional Enterprise is subject to the provisions of Law Number 5 of 1962, concerning Regional Enterprises and their implementing regulations, while BUMDs in the form of Limited Liability Companies are subject to the provisions of Law No. 1 of 1995, concerning Limited Liability Companies and their implementing regulations.

As of September 30, 2014, the Government has passed Law Number 23 of 2014, concerning Regional Government (Law No. 23/2014), which was subsequently promulgated on October 2, 2014. Law No. 23/2014 has been amended several times through Law Number 2 of 2015 concerning the Stipulation of Government Regulation in Lieu of Law Number 2 of 2014 concerning Amendments to Law Number 23 of 2014 concerning Regional Government (Law No. 2 / Prp / 2015) and Law Number 9 of 2015 concerning the Second Amendment to Law Number 23 of 2014 concerning Regional Government (Law No. 9/2015).

Article 331 paragraph (3) of Law No. 23/2014 jo. UU no. 2 / Prp / 2015 jo. UU no. 9/2015 states that "BUMD as referred to in paragraph (1) consists of Regional Public Enterprises and Regional Private Enterprises". Based on these provisions, the classification of the legal form of BUMDs is changed from a Regional Enterprises (PD) or Limited Liability Company (PT) to a Regional Public Enterprises (Perumda) or Regional Private Enterprises (Perseroda).

Transitional provisions, namely Article 402 paragraph (2) of Law No. 23/2014 jo. UU no. 2 / Prp / 2015 jo. UU no. 9/2015 states that, "BUMD that have existed before this Act applies, must adjust to the provisions in this Law within a maximum period of 3 (three) years from the enactment of this Law".

Based on these provisions, then at the latest, on October 2, 2017 all BUMDs must adjust their

legal form to Perumda or Perseroda. Likewise, with Regional Companies - Regional Companies throughout Indonesia.

### ***Advantages and Disadvantages of the Perumda and Perseroda Legal Form to be used as Regional Enterprise Legal Form***

Before analyzing the advantages and disadvantages of the legal form of Perumda and Perseroda, it is necessary to know the characteristics of each of these legal forms.

Broadly speaking, based on these characteristics, the basic difference between Perumda and Perseroda is as follows:

**Table 1:** The basic difference between Perumda and Perseroda

No.	Characteristics	Perumda	Perseroda
1	Aims	Mainly for public services, but still get profits and / or profits (Article 331 paragraph (4) letter c Law No. 23/2014 jo. Law No. 2 / Prp / 2015 jo. Law No. 9/2015)	Mainly for profit (profit oriented) but still able to carry out public service functions
2	Enactment and Legal Form	With the Perda which is followed up with the articles of association and obtaining legal status based on the law	With Regional Regulations that are followed up with the articles of association and obtain legal entity status if they meet the procedures and conditions for establishing a limited liability company as stipulated in the legislation
3	Shares	Not divided into shares	Divided into shares
4	Capital	All are owned by one region	1) Can be owned entirely by one region; 2) Can be owned by two regions with one region as the majority shareholder; or 3) 3) Can be owned by one

			region with the private sector provided that at least the region has 51% of the shares.
5	Company Organs	1. Head of Region; 2. Directors; and 3. Supervisory board.	1) General Meeting of Shareholders (GMS); 2) Directors; and 3) Commissioners.
6	Profit	Stipulated, approved by the regional head as the regional representative as the owner of capital and can be detained with the approval of the regional head	Defined and divided based on the resolutions of the GMS (in accordance with the provisions of the articles of association and legislation concerning limited liability companies)
7	Management	Subject to the provisions of the legislation in the field of state / regional finance and management of state / regional assets determined by the government	Freer, but still bound to the provisions of the articles of association and legislation regarding limited liability companies
8	Dissolution	Stipulated by Regional Regulation	Implemented in accordance with the provisions of the legislation concerning limited liability companies
9	Bankruptcy	Not Possible	Possible

Whereas based on the characteristics of the Perumda and the Perseroda it can be known the advantages and disadvantages of the legal form of Perumda and Perseroda with the following descriptions:

**Table 2:** Benefit and disadvantages of the legal form of Perumda and Perseroda

	<b>Perumda</b>	<b>Perseroda</b>
<b><i>Benefit</i></b>	Focusing on public service functions	Focusing on the goal of seeking profit to increase regional income

	Encouraging implementation of development	Can obtain additional capital from the private sector which is relatively large by issuing shares and bonds
	The process of establishing and obtaining legal status is easier than BUMD in the form of a limited liability company	Business continuity does not depend on leaders (Directors or shareholders)
	The highest decision maker is in the Regional Head (one door)	Employees have the status of private employees so that competitiveness between employees can improve company performance
	Cannot be bankrupted because the assets of the company are regional assets and regional assets cannot be confiscated	The management is carried out independently including the determination of tariffs, as long as they do not violate the limits specified in the legislation, including asset management
<b><i>Disadvantages</i></b>	Its management and business continuity depend on the politics of tariffs and prices from the government, especially the political leadership (Regional Head) in office	The procedure for establishment and acquisition of legal status is longer than that of the public
	All profits / profits become profits for the state / region, so that if losses, will cause losses to the country / region	Do not obtain state / regional facilities
	Its management is bound to bureaucratic rules, so it is vulnerable to be used as a political tool for certain groups	It can go bankrupt, or the assets can be confiscated by the court, because assets are separate and therefore not regional assets
	The level of productivity of employees generally under BUMD in the form of limited liability companies	

	Addition of capital depends heavily on state / regional finances	
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### ***Consideration of Regional Companies in determining the legal form of Perumda or Perseroda***

Referring to the characteristics and advantages and disadvantages of the legal form of Perumda and Perseroda, which have been described in the analysis of the first legal issue above, it is known that the things that should be considered by a Regional Enterprises in determining its legal form, among others, are:

1. The purpose of the business carried out by the Regional Enterprises;
2. Implications of changes in legal form, against:
  - a. Capital structure and its sources;
  - b. The nature of services that can be provided by the Regional Enterprises;
  - c. Assets and management and their utilization;
  - d. Organ composition and Human Resources (HR) including procedures for the appointment of directors and other organs;
  - e. Stakeholder tendency towards the continuity of the Regional Enterprises.
3. That what is meant by the purpose of a business carried out by a Regional Enterprises is related to the tendency of the Regional Enterprises to run its business, it tends to be primarily aimed at providing services to the community, in addition to obtaining profits or primarily intended to seek profit, in addition to providing services.

This is closely related to all components in the Regional Enterprises, namely the nature of the services provided, the management of assets owned and the need for qualified Human Resources (HR) in running the company to achieve its objectives. So that the determination of the objectives of the business carried out by a Regional Enterprises is the main thing that must be determined as the basis for determining the legal form that is appropriate to the character of the Regional Enterprise.

The purpose of the business of a Regional Enterprise can essentially be seen from the practices or conditions that have been running in a Regional Enterprise, where all this time a Regional Enterprise is intended to provide services to the community, although still by setting tariffs for these services, these rates are in accordance with provisions stipulated by the

regional head.

On the basis of existing conditions in a Regional Enterprise, it can be seen that a Regional Enterprise tends to have the same objectives as the Perumda legal form, so changing the legal form of Regional Companies into Local Regulations tends to be easier to implement because they are in accordance with the objectives, climate and conditions exist in the environment of the Perusahaan Daerah Air Minum (PDAM) Surya Sembada, Surabaya City.

However, in the event that Surya Sembada Kota Surabaya's Regional Water Company (PDAM) has a view or desire to change its management pattern and its purpose of being commercial, it can still be done. If so, then the Perusahaan Daerah Air Minum (PDAM) Surya Sembada Surabaya City can choose the form of Perseroda.

Furthermore, as a consideration that can strengthen the choice of legal form for the Perusahaan Daerah Air Minum (PDAM) Surya Sembada of Surabaya City, in addition to the main business objectives of the Perusahaan Daerah Air Minum (PDAM) Surya Sembada Surabaya City, it is necessary to review each legal form, both Perumda and Perseroda, against:

- a. Capital structure and its sources;
- b. The nature of services that can be provided by a Regional Enterprises;
- c. Assets and management and their utilization;
- d. Organ composition and Human Resources (HR) including the procedures for the appointment of directors and other organs.

If the Perusahaan Daerah Air Minum (PDAM) of Surya Sembada Surabaya City chooses the legal form of Perumda, then the implications for the capital of the Perusahaan Daerah Air Minum (PDAM) Surya Sembada Surabaya City only depends on regional finances, because the regional head, as the regional representative and as the owner of Perumda is the one and only capital provider for Perumda.

In addition, in terms of the nature of its services, if PDAM Surya Sembada chooses the legal form of Perumda, then the purpose of the business carried out by the PDAM Surya Sembada is the main community service, so that the nature of the service is purely for public services, so the tariff setting is determined based on the policy of the regional head. This also has implications for the business that can be carried out by the PDAM Surya Sembada in Surabaya City, where because the PDAM is devoted to the public servants, the Regional Water Supply Company (PDAM) Surya Sembada Kota Surabaya is not possible to conduct



business activities outside of public services or in other words, it cannot do any profit-oriented activities.

The nature of the services provided by these Regional Companies must also consider the acceptance of consumers or the public who have been using the services of Regional Companies. Furthermore, with regard to asset management, if the Regional Enterprises chooses the legal form of Perumda, then the assets of the Regional Enterprises cannot be cooperated with a third party, outside the purpose of improving public services. In other words, the management of Regional Enterprises assets in the form of Local Regulations cannot be implemented commercially. The implementation of asset management itself must also be subject to the provisions of the legislation in the area of regional asset management which has limited the forms of cooperation that can be carried out by Regional Companies and third parties related to asset management and utilization.

Then related to organ composition, in the case that the Regional Enterprises chooses the legal form of Perumda, the organs in the Perumda are Regional Heads as regional representatives and capital owners, Directors and the Supervisory Board; where the directors are appointed and dismissed by the regional head and are responsible to the regional head. It is different if a Regional Enterprise chooses the form of Perseroda. Regarding capital, Perseroda can obtain capital from other parties, both other regions and the private sector, as long as the local government has at least 51% of the shares. In addition, Perseroda also has the right to issue bonds and is more able to obtain credit facilities from banks, this is because the Perseroda is profit-oriented and it is easier to cooperate with third parties.

Furthermore, from the point of view of the nature of its services, Perseroda is more flexible in providing services, where the tariff determination can be carried out by the Perseroda as long as it does not exceed the basic tariff determined by the government. The manufacturer is also authorized and entitled to carry out other business activities in accordance with the limits stated in its articles of association, or in other words, in addition to operating in the field of water supply, the Regional Enterprise has the right to extend its business with commercial purposes.

In the case of asset management, if a Regional Enterprises chooses the legal form Perseroda, it will get the right to carry out asset management by commercially cooperating with third parties, not only to improve public services, but to obtain profits. Then related to organ composition, as well as limited liability companies, Perseroda has the organs consisting of GMS, directors and board of commissioners. The appointment of the directors and the board of commissioners themselves is carried out by the GMS, and is accountable to the GMS,

where the GMS itself consists of Perseroda shareholders, one of whom is the regional head as a representative of the region. This will give the distribution of responsibilities among its shareholders and the management of the Perseroda does not merely depend on the policy of one head of a region.

With regard to human resources, in managing the Perseroda is more in need of qualified and independent human resources, because the management of Perseroda relies heavily on the quality of its human resources, because Perseroda has a target to obtain maximum profit in addition to providing public services. This means that its human resources are required to be able to make decisions well, in a short time and to mitigate the risk of corporate governance, in contrast to the Perumda which only aims to provide public services in accordance with the instructions of the head of the region.

Furthermore, what is meant by stakeholder tendencies towards the survival of Regional Companies is related to the parties involved who also hold important positions in determining the legal form of Regional Companies, namely:

- Regional Head as the authorized party to issue Regional Regulations concerning changes in legal form for Regional Companies; and
- Regional People's Legislative Assembly as the party authorized to approve changes in legal form for Regional Companies.
- Whereas the asset perumda is a regional asset that is not separated so that, in accordance with the State Treasury Law, regional assets cannot be confiscated, including non-bankruptcy, while the share assets are regional assets that have been separated so that it is possible to be confiscated during bankruptcy.

Based on this, the plan to change the legal form of the Regional Enterprise to Perumda or Perseroda must be discussed and involve these two elements, namely the current Regional Head and DPRD, because the change in the legal form of the Regional Enterprise is influenced by the decisions of the two stakeholders.

## **Conclusion**

Based on the legal analysis above, it can be concluded that each legal form, both Local Government and Perseroda, has its advantages and disadvantages in terms of the existing conditions of the Regional Enterprises, where if the Regional Enterprises chooses the legal form of Perumda, the main advantage is that the Perumda has characteristics that are not much different from the existing conditions in the Regional Companies, so that changes in



the form of law into Perumda will not change existing habits. However, the main disadvantages, that can arise from the legal form of Perumda, are the emergence of monotony in the management of Regional Companies, because the entire management depends on the policy of the region and the Regional Enterprises cannot carry out business activities outside the established public services.

Whereas the main advantages of Perseroda's legal form are the freedom to operate the company independently to achieve profit objectives, including obtaining capital, asset management, and human resources management (selection of qualified employees). However, the greatest shortcomings in the laws of the Perser Regional companies today are related to changing habits; traditions and the work ethics of human resources in clear regional companies which will take longer.

### **Advice**

The basis for the Regional Water Supply Company, (PDAM) Surya Sembada Surabaya City, to determine its legal form by:

1. Ensuring the objectives to be achieved by the Company in carrying out its business, whether public services or seeking profit;
2. Ensuring in the future, the tendency of Regional Companies to bear the implications of each legal form related to capital, the nature of services, the flexibility in managing assets and management bodies related to the procedures for decision making in the management of Regional Companies; and
3. Ensure stakeholder acceptance of changes in the legal form of the Regional Enterprise into Perumda or Perseroda.



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