

*PN-ACE-442*

**INDONESIA**  
**TECHNICAL ASSISTANCE TO**  
**INDONESIA'S COMMODITIES EXCHANGE BOARD**  
**FINAL REPORT**

**USAID/FSDP II**  
**CONTRACT NO PCE-Q-00-93-00071-00**  
**DELIVERY ORDER # 809**

By  
Joseph Dial  
Frederic Spindel  
Thomas Goodbody  
James Jordan

**BARENTS**  
GROUP LLC  
2001 M Street, NW  
Washington, DC 20036

## TABLE OF CONTENTS

	<b>Page</b>
Preface	1
Introduction “The Social and Financial Value of Futures and Options Trading”	3
Chapter 1 “Recommendations Organization and Position Descriptions” Bappebti Position Descriptions	5 7
Chapter 2 “Registration, Financial Reporting and Market Surveillance” Required Filings Financial Reporting Market Surveillance Program	20 23 31 36
Chapter 3 “Report on Proposed Bappebti Rules”	44
Chapter 4 “Enforcement and Criminal Investigation” Regulation of Futures Markets Examinations Regulation of Futures Markets Criminal Investigations	62 72 81

## PREFACE

This report contains recommendations for the initiation of commodity futures trading in Indonesia. It provides a road map for the successful start-up of a commodity futures exchange and its oversight. It does this through providing organizational charts, position descriptions, forms for registration and reporting, and comments on draft legislation and regulations.

The report is the result of six field visits to Indonesia by four Barents Group advisors under USAID's Financial Sector Development Project, Phase II (FSDP II). The scope of work called for separate reports from each advisor, and FSDP II is submitting them in one volume, with annexes in additional volumes. Due acknowledgement is given for authorship of each section. USAID/Jakarta has approved this structure.

**Team Composition** Team members were

- ◆ Joseph Dial, Team Leader Former Commissioner of the U.S. Commodity Futures Trading Commission (CFTC)
- ◆ James Jordan, Commodity Futures Trading Specialist Former Director of the Kansas City Board of Trade
- ◆ Frederick Spindel, Legal Specialist Several years of experience as an attorney with the CFTC
- ◆ Thomas Goodbody, Surveillance and Enforcement Specialist Several years of experience as an attorney with the CFTC

**Report Structure** Report sections correspond to the work performed by these advisors.

- ◆ Mr. Dial made recommendations and compiled organizational structure and position descriptions for commodity futures regulation in Indonesia.
- ◆ Mr. Jordan explained the social and economic purpose of commodity futures trading, and provided forms and explanations for registration, financial reporting and market surveillance.
- ◆ Mr. Spindel critiqued recently passed legislation and regulations governing Bappebti, the Government of Indonesia's supervisory and monitoring agency for futures trading.
- ◆ Finally, Mr. Goodbody examined civil and criminal enforcement authority of Bappebti, with an appendix on criminal investigative powers.

## INTRODUCTION

### The Social and Financial Value of Futures and Options Trading by James Jordan

One of the objectives of governments worldwide is to assure adequate food supplies. This is a moral obligation. It can be accomplished directly by the government in a variety of ways, or through market pricing.

The disadvantages of direct pricing by the government include the following:

1. Prices are frequently set below market prices for social and political reasons.
2. With prices set too low, consumers will attempt to hoard commodities.
3. Also if prices are too low, farmers may withhold products from the market.
4. In the absence of adequate financial incentives, producers may curtail production.

#### Observations

1. Under market-oriented, transparent pricing systems, domestic prices will generally reach world prices. This will tend to minimize price fluctuations because domestic prices are determined by worldwide supply and demand.
2. The United States has used futures for over 100 years. It appears that this has been a factor in the country's relatively low food prices. That is, household expenditures for food are quite low as a percentage of income.
3. Under market pricing systems, governments have the obligation to assist economically disadvantaged citizens and generally do so. Under centrally planned systems, however, the same low prices are provided to all, rich and poor alike, which is an inefficient use of resources.
4. Futures and options trading systems have gained worldwide acceptance, providing transparent pricing and hedging opportunities in a wide variety of fields other than agricultural commodities. Futures and options systems appear to have minimized sharp price changes in energy, metals, raw materials, interest rates and even currencies.
5. Consider, for example, oil supplies and prices during the 1979 Gulf crisis in comparison with the 1990 Desert Storm War. In 1979 there were no energy or petroleum futures markets. There were sharp price increases - and an actual shortage of petroleum and fuel - due to uncertainty. In 1990 there were moderate price increases but no shortages, because futures and options marketing tools were in place.
6. Generally, futures markets lead to price equilibrium satisfying neither users nor producers. This is for the better. End users - consumers - always think the prices are too high. Producers are concerned about prices being too low. Markets clear at compromise prices.
7. Financially, futures markets allow for transferring price risks to third parties. This allows for bank financing of, for example, agricultural production in advance, and for

inventory price financing Facilitation of financing is one of the most important reasons for the existence of futures markets

## CHAPTER ONE

### Recommendations Organization and Position Descriptions by Joseph Dial

This chapter contains broad recommendations resulting from trips to Indonesia by four Barents Group advisors. They are based on extensive dealings with officials from the Indonesian Commodity Exchange Board (ICEB) and interviews with a broad cross-section of private and public sector representatives who are involved, in one way or another, in Indonesia's nascent futures industry. The advisors' recommendations are also based on extensive reviews of legislation, regulations and background material - including an earlier study of legal, economic and political matters related to the public trading of derivatives in Indonesia. ICEB will soon curtail activities in favor of a new organization, Bappebti.

Other recommendations, more narrow in scope, are contained later in this report. They detail possible improvements to specific regulations and legislation, paragraph by paragraph, and cannot be summarized effectively.

Voluminous attachments and annexes to this report are contained in separate volumes. They contain legislation, position descriptions for other bureaus, registration materials for brokers and traders (?) and annual reports of pertinent Indonesian organizations.

**Bappebti staffing and training** The Chairman of Bappebti should name individuals to fill key supervisory positions shown in the organizational diagrams and written position descriptions included in this report. As soon as possible thereafter, outside consultants, possibly from the CFTC and the NFA in the U.S., should be brought in to provide training for those people.

- ◆ The first position the Chairman should fill is that of the Director of the Legal Bureau. This individual should begin a thorough review of the law, Bappebti regulations, the bankruptcy law, and the legal aspects of the arbitration process to be used by the futures industry. The review should take into consideration the expert advice provided by Barents legal consultants to this project. This task should be completed before the outside consultants begin training Bappebti personnel.

**Implementing futures trading** Although Bappebti is responsible for regulating and supervising the Indonesian Futures Exchange (IFE) once it is up and running, there are a number of related actions which the agency must undertake before the public trading of futures contracts on Crude Palm Oil and Coffee is initiated.

- ◆ First, Bappebti's review of the IFE Business Plan provides for an objective analysis of the financial and managerial arrangements and practices upon which the IFE will

stand or fall. Therefore, consideration should be given to securing an outside Consultant to conduct an independent unbiased review of the Business Plan.

- ◆ Second, Bappebti must thoroughly review the terms and conditions applicable to each futures contract. This is extremely important because contract specifications will determine whether or not they possess, among other things, legal certainty and economic utility. If contracts lack these characteristics they will fail. Once again, it would be advisable to have an outside consultant do this work.

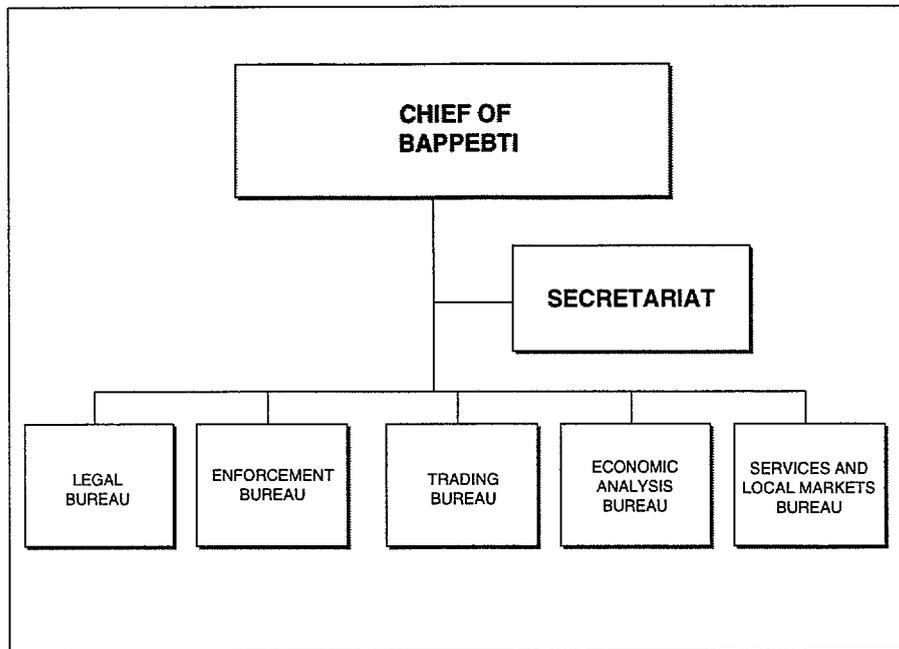
**Establish an agricultural information system to strengthen cash markets for commodities before beginning futures trading.** Work to date has set the stage for the public trading of futures in Indonesia by the year 2000. It has included passing enabling legislation, establishing Bappebti and drafting regulations for it, and laying the groundwork for opening the Indonesian Futures Exchange (IFE).

However, possibilities for agricultural commodity futures contracts to be successful depend on several factors. First among these is that underlying cash markets must generate substantial amounts of commerce. These must possess an economically efficient infrastructure and the element of price transparency. Also, underlying cash markets must operate with a minimum of government interference.

Unfortunately, agricultural commodity cash markets in Indonesia do not fulfill these requirements. Significant changes in their operations will have to take place if futures trading is to be successful.

The first step necessary to bring about such a change will require the involvement of a Non-Governmental Organization (NGO) or an independent consulting firm. One of these organizations should be secured to examine how the Government of Indonesia and the domestic agricultural sector might collaborate in the design, development and implementation of an electronic commerce/agricultural information system for the major crops and primary livestock sectors in Indonesia, beginning with Crude Palm Oil and Coffee.

## ORGANIZATIONAL CHART



## BAPPEBTI POSITION DESCRIPTIONS

### LEGAL BUREAU

***DIRECTOR*** The Director is responsible for the planning, focus, direction, emphasis and accomplishment of the program of the Bureau

The incumbent has the responsibility for planning, establishing, organizing and executing Bureau programs by defining program goals, policies and objectives and determining the organization and resources needed to meet program requirements. He supervises the final review of all cases and resources needed to meet program requirements. He supervises the final review of all cases handled by the Bureau. The Director also consults with and advises the Chairman and other Bureau Directors on all substantive legal matters relevant to the role of the Legal Bureau. He reviews all major actions arising in the Bureau to ensure consistency in the application of Bureau and Bappebti policy.

### **Division of Arbitration**

***Deputy Director*** The incumbent directs the Division of Arbitration, the mission of which is to carry out the Law's mandate that Bappebti provide a forum to resolve disputes, through mediation and/or arbitration, between any and all parties engaged in the business of exchange-traded futures/options.

## **Administration Section**

**Associate Director** The incumbent directs the Administration Section, the mission of which is to receive, record, and process written submissions for mediation and formal pleadings for arbitration

## **Hearings Section**

**Associate Director** The incumbent directs the Hearings Section, the mission of which is to seek the resolution of disputes through the use of mediation and/or arbitration. He will supervise the process whereby parties engaged in the business of exchange-traded futures/options might go before a mediator or appear before an impartial panel of arbitrators to seek redress of their differences

## **Counseling Division**

**Deputy Director** The incumbent provides guidance for the coordination and accomplishment of all the legal activities of Bappebtı by developing sound and consistent procedures in the administration and statutory interpretation of the Law, Government Regulations, Executive Orders and court decisions and assists in the formulation of the regulatory policy developed by Bappebtı. Specifically, with the Director, the Deputy Director supervises, manages, and coordinates the activities of the Division, exercising authority in the management of human resources and in coordinating activities with other parts of the agency

## **Drafting Regulation and Interpretations Section**

**Associate Director** The incumbent directs the drafting of Government Regulations, prepares Bappebtı guidelines, statements of policy and interpretation, and reviews proposals prepared by other Bappebtı Bureaus for legal sufficiency and consistency with agency policy

## **The Prosecution and Advice Section**

**Associate Director** The incumbent directs litigation involving Bappebtı, including bankruptcy proceedings and the prosecution of enforcement actions. The Associate Director will advise the Chairman and Bappebtı Directors on various policy and legal issues relevant to litigation

## **Sanction Review and Appeals Section**

**Associate Director** The incumbent will make recommendations to the Chairman concerning the imposition of sanctions, as provided for by the Law and Government Regulations. The Associate Director will supervise the review of appeals of Self Regulatory Organization (SRO) members concerning disciplinary actions taken by the Exchange and/or the Clearing House in their respective capacities as SROs. The

Associate Director is responsible for cases that deal with appeals taken from decisions rendered by the courts in Bappebti enforcement actions, suits brought against the agency, as well as petitions for review by courts of appeals of orders issued by the agency

## **ENFORCEMENT BUREAU**

***DIRECTOR*** The Director is responsible for the planning focus, direction, emphasis and accomplishment of the program of the Bureau

The incumbent has the responsibility for planning, establishing, organizing and executing the Enforcement Bureau's programs by defining program goals, policies and objectives and determining the organization and resources needed to meet program requirements. He supervises the final review of all cases handled by the Bureau. The Director consults with and advises the Chairman on all substantive matters relevant to the role of the bureau. He reviews all major actions arising in the Bureau to ensure consistency in the application of Bureau and Bappebti policy when appropriate, the Director consults with and coordinates actions taken by the Enforcement Bureau with other Bureaus

### **Disclosure, Registration, Recordkeeping, Reporting and Financial Violations Division**

***Deputy Director*** The incumbent serves as the principal assistant to the Director of the Bureau in all matters concerning disclosure, registration, recordkeeping, and reporting and financial violations. Subject to approval by the Division Director, the Deputy Director Supervises, manages, and coordinates the activities of his Division, exercising authority in the management of human resources and in coordinating activities with other parts of the agency. He oversees the conduct of investigations in civil litigation instituted by Bappebti in the courts for those areas under his supervision, including injunctions and subpoena enforcement actions. The Deputy Director develops program policies and procedures for his Division's enforcement program and evaluates the overall effectiveness of his Division. He also represents his Division in discussions of policy and program matters with the Chairman, other Divisions and Bureaus

### **Exchange, Clearing House, FPO, FTA and Traders Section**

***Associate Director*** The incumbent is the head of the team of attorneys, investigators, and support staff in the Exchange, Clearing House, FPO, FTA and Traders Section. He is responsible for the direction and management of policy development, investigation, and litigation as it pertains to this Section. The Associate Director also serves as an advisor to the Deputy Director on both specific cases and broad enforcement programs and policies. As necessary, to respond to activities requiring large-scale investigations, the Associate Director participates in cases pursued cooperatively across agency organizational lines

## **Brokers Section**

**Associate Director** The incumbent is the head of the team of attorneys, investigators, and support staff in the Brokers Section. He is responsible for the direction and management of policy development, investigation, and litigation as it pertains to this Section. The Associate Director also serves as an advisor to the Deputy Director on both specific cases and broad enforcement programs and policies. As necessary, to respond to activities requiring large-scale investigations, the Associate Director participates in cases pursued cooperatively across agency organizational lines.

## **Manipulation, Fraud and Other Illegal Trading Practices Division**

**Deputy Director** The incumbent serves as the principal assistant to the Director of the Bureau in all matters concerning manipulation, fraud and other illegal trading practices. Subject to approval by the Division Director, the Deputy Director supervises, manages, and coordinates the activities of the Division, exercising authority in the management of human resources and in coordinating activities with other parts of the agency. He oversees the conduct of investigations in civil litigation instituted by Bappebti in the courts for those areas under his supervision, including injunctions and subpoena enforcement actions. He develops program policies and procedures for the Division's enforcement program and evaluates the overall effectiveness of his Division. The Deputy Director represents his Division in discussions of policy and program matters with the Chairman, other divisions and Bureaus.

## **Manipulation Section**

**Associate Director** The incumbent is the head of the team of attorneys, investigators, and support staff in the Manipulation Section. He is responsible for the direction and management of policy development, investigation, and litigation as it pertains to this Section. The Associate Director also serves as an advisor to the Deputy Director on both specific cases and broad enforcement programs and policies. The Associate Director participates in cases pursued cooperatively across agency organizational lines to respond to activities requiring large-scale investigations, as necessary.

## **Fraud Section**

**Associate Director** The incumbent is the head of the team of attorneys, investigators, and support staff in the Fraud Section. He is responsible for the direction and management of policy development, investigation, and litigation as it pertains to this Section. The Associate Director also serves as an advisor to the Deputy Director on both specific cases and broad enforcement programs and policies. The Associate Director participates in cases pursued cooperatively across agency organizational lines to respond to activities requiring large-scale investigations, as necessary.

## **Other Illegal Trading Practices Section**

**Associate Director** The incumbent is the head of a team of attorneys, investigators, and support staff in the Other Illegal Trading Practices Section. He is responsible for the direction and management of policy development, investigation, and litigation as it pertains to this Section. The Associate Director also serves as an advisor to the Deputy Director on both specific cases and broad enforcement programs and policies. The Associate Director participates in cases pursued cooperatively across agency organizational lines to respond to activities requiring large-scale investigations, as necessary.

## **TRADING BUREAU**

**DIRECTOR** The Director is responsible for the planning, focus, direction, emphasis and accomplishment of the programs of the Bureau.

The incumbent has the responsibility for planning, establishing, organizing and executing the Trading Bureau's programs by defining program goals, policies and objectives and determining the organization and resources needed to meet program requirements. He supervises the final review of all cases, rule enforcement reviews and financial audits handled by the Bureau. The Director consults with and advises the Chairman on all substantive matters relevant to the role of the Bureau. He reviews all major actions arising in the Bureau to ensure consistency in the application of Bureau and Bappebti policy. When appropriate, the Director consults with and coordinates actions taken by the Trading Bureau with other Bureaus.

The incumbent establishes policies, procedure and priorities for the Bureau's functions. He advises the Chairman on all matters relevant to the work of the Trading Bureau. The Director coordinates actions taken by the Trading Bureau with other Bureaus and reviews all major actions arising in the Bureau to ensure consistency in application of Bureau and Bappebti policy.

## **Exchange and Clearing House Oversight Division**

**Deputy Director** The incumbent directs the activities of the Exchange and Clearing House Oversight Division and reviews all major actions taken by the Division to ensure consistency in application of Bureau and Bappebti policy. Subject to approval by the Division Director, the Deputy Director supervises, manages, and coordinates the activities of the Division, exercising authority in the management of human resources and in coordinating activities with other parts of the agency. He develops, implements, interprets and oversees enforcement of Exchange and Clearing House (SROs) rules. He also develops program policies and procedures for the Division's rule enforcement review program and evaluates the overall effectiveness of the Division. The Deputy Director represents the Division in discussions of policy and program matters with the Chairman, other divisions and Bureaus.

## **Exchange Section**

**Associate Director** The incumbent supervises the processing of the initial business plan and the application by the Exchange to trade Crude Palm Oil and Coffee Futures contracts. He directs the initial review of the SRO rules for the Exchange in order to ensure their consistency with the Law and Government Regulations. The Associate Director monitors the Exchange's Rule Enforcement Program to ensure that its members adhere to exchange rules. Among other things, this would involve a review of how the exchange carries out investigations concerning alleged violative conduct by members and their employees, as well as the number of disciplinary actions taken and the disposition of those cases as to sanctions and the compliance with those remedies by respondents. When appropriate, the Associate Director will conduct special studies of exchange practices, rules, electronic trading practices and other matters as specific problems arise. The Associate Director participates in cases pursued cooperatively across agency organizational lines to respond to activities requiring large-scale investigations, as necessary.

## **Clearing House Section**

**Associate Director** The incumbent supervises the processing of the initial business plan as submitted by the Clearing House. He directs the initial review of the SRO rules for the Clearing House in order to ensure their consistency with the Law and Government Regulations. He reviews the Clearing House's compliance with the Law and Government Regulations as they relate to segregation of customer's funds and recordkeeping rules. When appropriate, the Associate Director will conduct special studies of Clearing House practices, rules, electronic clearing of futures trading and other matters as specific problems arise. As necessary, to respond to activities requiring large-scale investigations, the Associate Director participates in cases pursued cooperatively across agency organizational lines.

## **Rule Review Section**

**Associate Director** The incumbent establishes policies, procedures and priorities for the conduct of the Section's functions. The Associate Director is responsible for reviewing, approving, denying, modifying, or requiring changes to Exchange and Clearing House rules. He serves as an advisor to the Deputy Director on both specific cases and broad rule enforcement review programs and policy. The Associate Director participates in cases pursued cooperatively across agency organizational lines to respond to activities requiring large-scale investigations, as necessary.

## **Market Professionals Division**

**Deputy Director** The incumbent establishes policies, procedures and priorities for the conduct of the Division's functions. Subject to approval by the Division Director, the Deputy Director supervises, manages, and coordinates the activities of the Division,

exercising authority in the management of human resources and in coordinating activities with other parts of the agency. The Deputy Director is responsible for supervising the conduct of trade practice investigations of all market professionals in order to detect possible violations of the Law and Government Regulations, and refers all cases that warrant serious review to the Legal and Enforcement Bureaus.

### **Brokers Section**

**Associate Director** The incumbent establishes policies, procedures and priorities for the conduct of the Division's functions that include, but are not limited to

- ◆ Supervision of the processing of applications for a license to become a Broker or a Broker's Representative
- ◆ Monitoring compliance by Brokers and their Representatives with recordkeeping, reporting, disclosure and other customer protection requirements
- ◆ Denying or revoking the application for or existing license of a Broker or Broker's Representative, if they are found guilty after affording them "due process," of violating the Law or Government Regulations

The Associate Director is responsible for the direction and management of policy development, investigation, and litigation as it pertains to this Section. He also serves as an advisor to the Deputy Director on both specific cases and broad programs and policies as they relate to licenses for Brokers and/or their Representatives. The Associate Director participates in cases pursued cooperatively across agency organizational lines to respond to activities requiring large-scale investigations, as necessary.

### **FPO/FTA Section**

**Associate Director** The incumbent establishes policies, procedures and priorities for the conduct of the Section's functions that include, but are not limited to

- ◆ Reviewing FPO's promotional material and general sales practices
- ◆ Reviewing reports covering the funds FPO's have under management
- ◆ Monitoring compliance with rules governing how FPO's and FTA's represent their hypothetical performance
- ◆ Reviewing FPO's internal control procedures
- ◆ Reviewing disclosure documents
- ◆ Monitoring the filing of annual reports by FPO's
- ◆ Reviewing the applications for licenses to operate as FPO's or FTA's

The Associate Director is responsible for the direction and management of policy development, investigation, and litigation as it pertains to this Section. He also serves as an advisor to the Deputy Director on both specific cases and broad programs and policies as they relate to the supervision of FPO's and FTA's. The Associate Director

participates in cases pursued cooperatively across agency organizational lines to respond to activities requiring large-scale investigations, as necessary

### **Traders Section**

**Associate Director** The incumbent establishes policies, procedures and priorities for the conduct of the Section's functions that include, but are not limited to

- ◆ Supervising the processing of applications for a license to become a Trader
- ◆ Monitoring compliance by Traders with trade practice requirements mandated by the Law and Government Regulations
- ◆ Denying or revoking the application for or existing licenses of Traders, if they are found guilty, after affording them "due process," of violating the Law or Government Regulations

The Associate Director is responsible for the direction and management of policy development, investigation, and litigation as it pertains to this Section. The Associate Director also serves as an advisor to the Deputy Director on both specific cases and broad programs and policies as they relate to the supervision of Traders. The Associate Director participates in cases pursued cooperatively across agency organizational lines to respond to activities requiring large-scale investigations, as necessary

### **Financial Audit Division**

**Deputy Director** The mission of the Financial Audit Division is to prevent the misuse of public customers funds committed to the futures markets, ensure the financial integrity of the futures marketplace, ensure that futures industry firms comply with regulations designed to protect the public interest and to promote just and equitable principles of trade. In order to fulfill this mission, the Deputy Director is responsible for the planning, focus, direction, emphasis and accomplishment of the programs of the Division

The incumbent establishes policies, procedures and priorities for the Division's functions. He advises the Chairman on all matters relevant to the work of the Financial Audit Division. The Deputy Director, with approval from the Director, coordinates the development or amendment of rules and audit guidelines with other agencies and non-governmental bodies, such as BABEPAN, the Central Bank, the Jakarta Stock Exchange, and futures industry SROs. He also coordinates actions taken by the Financial Audit Division with other Divisions and Bureaus and reviews all major actions arising in the Division to ensure consistency in application of Bureau and Bappebti policy. He must respond quickly to financial emergencies in the commodities industry by determining the nature of the emergency and taking necessary action or recommending an appropriate course of action for the Chairman to recommend to the Minister of Industry and Trade

## Exchange, Clearing House, FPO, FTA and Trader Section

**Associate Director** The incumbent establishes and implements policies and procedures for the conduct of the Division's functions, which include, but are not limited to

- ◆ Conducting financial audits of the books and records of the Exchange, including the Compensation Fund, the Clearing House, FPOs, and FTAs
- ◆ Conducting rule enforcement reviews of SRO's, i.e. the Exchange and the Clearing House, to determine the sufficiency of the SRO's programs for monitoring and enforcing compliance by Traders with SRO rules covering margin
- ◆ Conducting random periodic oversight audits of the financial condition of FPOs and FTAs to test the adequacy of SRO compliance programs and to address special concerns such as compliance with Bureau interpretations
- ◆ Conducting special research projects to determine if there is a need for adding or deleting financial and sales practice rule makings. Based on these analyses, recommend changes or improvements in Bappebti's regulatory policies and/or rules
- ◆ Referring suspected and actual violations to the Legal and Enforcement Bureaus and providing accounting, financial, and sales practice expertise in support of investigations and subsequent litigation
- ◆ Monitoring events in foreign markets for potential impact on Bappebti registrants and providing recommendations to the Chairman for appropriate action to protect registrants and customers
- ◆ Reviewing the implementation and execution of the Section's programs to ensure consistency in the application of Bureau and Bappebti policy
- ◆ Developing new systems, programs and regulatory initiatives to increase the effectiveness of Bappebti's oversight role and the effectiveness and efficiency of the SROs in assuring compliance of their members with financial, sales practice and internal account management regulatory requirements
- ◆ Assuring timely oversight reviews and the elimination of overlap in the conduct of such reviews
- ◆ Coordinating actions taken by the Section with other Sections and Divisions within the Trading Bureau, as well as other Bureaus
- ◆ Advising the Chairman in matters related to the Section's functions
- ◆ Issuing warning and non-compliance letters based upon audits and reviews of financial reports
- ◆ Initiating follow-up investigations of notices of reportable items by registrants

The Associate Director is responsible for the direction and management of policy development, investigation, and litigation as it pertains to this Section. He also serves as an advisor to the Deputy Director on both specific cases and broad programs and policies as they relate to Traders. The Associate Director participates in cases pursued cooperatively across agency organizational lines to respond to activities requiring large-scale investigations, as necessary.

## Broker's Section

**Associate Director** The incumbent establishes and implements policies and procedures for the conduct of the Division's functions, which include, but are not limited to

- ◆ Conducting rule enforcement reviews of SROs, i.e. the Exchange and the Clearing House, to determine the sufficiency of the SRO's programs for monitoring and enforcing compliance by Brokers and their Representatives with SRO rules covering margin
- ◆ Conducting oversight audits of financial and sales practices of Brokers and their Representatives to test the adequacy of SRO compliance programs and to address special concerns, such as the marketing of options or compliance with Bureau interpretations
- ◆ Conducting periodic direct financial audits of Brokers in order to ensure compliance with capitalization and segregation rules
- ◆ Developing a Financial Surveillance Information System (FSIS) to use in identifying potentially large market losses incurred by Brokers trading for their own account or by large traders who trade through the Broker

The Associate Director is responsible for the direction and management of policy development, investigation, and litigation as it pertains to this Section. He also serves as an advisor to the Deputy Director on both specific cases and broad programs and policies as they relate to Brokers. As necessary, to respond to activities requiring large-scale investigations, the Associate Director participates in cases pursued cooperatively across agency organizational lines.

## ECONOMIC ANALYSIS BUREAU

**DIRECTOR** The Director is responsible for the planning, focus, direction, emphasis and accomplishment of the programs of the Bureau.

The incumbent has the responsibility for planning, establishing, organizing and executing the Bureau's programs by defining program goals, policies and objectives and determining the organization and resources needed to meet program requirements. He supervises the final review of all cases handled by the Bureau. The Director consults with and advises the Chairman and other Bureau Directors on all substantive economic matters relevant to the role of the Economic Analysis Bureau. He also reviews all major actions arising in the Bureau to ensure consistency in the application of Bureau and Bappebti policy.

## Market Surveillance Division

**Deputy Director** The incumbent establishes and implements policies and procedures for the conduct of the Division's functions, which include, but are not limited to

- ◆ Maintaining daily surveillance of each active futures market to detect and prevent market manipulation, threats of market “corners” and other market disruptions
- ◆ Establishing and enforcing speculative position limits
- ◆ Maintaining oversight of trading activities to assure the market’s functions of risk transfer and price discovery is not hampered
- ◆ Monitoring daily large trader reports, futures and cash price relationships and fundamental supply and demand conditions
- ◆ Working closely with key officials at the Exchange and Clearing House and government agencies or departments in order to be fully informed of domestic and/or international events that have the potential to disrupt the futures markets
- ◆ Acting as the in-house expert in the conduct of Bappebti investigations into alleged attempts at price manipulation
- ◆ Providing the Chairman and Bureau Directors with regular weekly surveillance briefings, as well as emergency briefings, when the need arises
- ◆ Responding quickly to market emergencies in the commodities industry by determining the nature of the emergency and taking necessary action or recommending an appropriate course of action for the Chairman to recommend to the Minister of Industry and Trade

Subject to approval by the Division Director, the Deputy Director supervises, manages, and coordinates the activities of his Division, exercising authority in the management of human resources and in coordinating activities with other parts of the agency. He also coordinates actions taken by the Market Surveillance Division with other divisions and bureaus. He reviews all major actions arising in the Division to ensure consistency in the application of Bureau and Bappebti policy. The incumbent advises the Chairman on all matters relevant to the work of the Market Surveillance Division.

### **Deliverable Supply, Demand and Price Monitoring Section**

**Associate Director** The incumbent establishes and implements policies and procedures for the conduct of the Section’s functions, which include but are not limited to

- ◆ Daily review of the stocks of commodities located in exchange approved storage, for which receipts may be used in making delivery, on futures contracts
- ◆ Surveying major long and short position holders to evaluate their intentions and capabilities regarding futures deliveries, on an as needed basis
- ◆ A daily review of the overall supply and demand conditions in the cash market
- ◆ A daily review of the cash and futures prices and the relationship of those prices
- ◆ Maintaining direct communication with the Exchange’s surveillance department in order to cooperate and coordinate efforts in a joint market oversight program

## **Trader Reports and Position Evaluation Section**

**Associate Director** The incumbent establishes and implements policies and procedures for the conduct of the Section's functions, which include but are not limited to

- ◆ Establishing and enforcing speculative position limits
- ◆ Reviewing information on new traders, filed by Brokers on a Form 102 and a Form 40 filed by the traders themselves, in order to identify and track positions that exceed reportable levels for futures and/or options
- ◆ Reviewing trading accounts for aggregation violations
- ◆ Conducting audits, using 01 Forms, for determining positions of special accounts trading futures and/or options
- ◆ Reviewing Form 204 reports by hedgers
- ◆ Reviewing the report on "Commitments of Traders in All Futures Combined"
- ◆ Issuing "Special Calls" requiring a trader to report his positions with all Brokerage firms, including information on his trading and delivery activity

## **Analysis Division**

**Deputy Director** The incumbent establishes and implements policies and procedures for the conduct of the Division's functions. He advises the chairman on all matters relevant to the work of the Analysis Division. He also coordinates actions taken by the Analysis Division with other Divisions and bureaus and reviews all major actions arising in the Division to ensure consistency in application of Bureau and Bappebti policy.

## **Contract Evaluation Section**

**Associate Director** The incumbent establishes and implements policies and procedures for the conduct of the Division's functions, which include but are not limited to

- ◆ Evaluating the potential hedging and price-basing uses, as well as the terms and conditions of proposed futures contracts submitted by the Exchange
- ◆ Analyzing the economic impact of rule changes on futures contracts
- ◆ Analyzing proposed futures contracts and rule changes to existing contracts for conformity with current commercial practices, adequate deliverable supplies, and public interest considerations

## **Market Development Section**

**Associate Director** The incumbent establishes and implements policies and procedures for the conduct of the Division's functions

## Research Division

**Deputy Director** The incumbent establishes and implements policies and procedures for the conduct of the Division's functions, which include, but are not limited to

- ◆ Conducting research on futures market developments
- ◆ Conducting research on futures markets and futures trading statistics in order to establish or revise speculative position limits
- ◆ Conducting research of futures trading as a basis for supporting new or present enforcements policy, methods, and procedures
- ◆ Conducting research on special market situations and explaining what caused them
- ◆ Conducting research on problem areas and controversial issues relevant to economics in the regulation of the futures industry Recommending what action should be taken

Subject to approval by the Division Director, the Deputy Director supervises, manages, and coordinates the activities of the division, exercising authority in the management of human resources and in coordinating activities with other parts of the agency The incumbent advises the chairman on all matters relevant to the work of the Research Division He also coordinates actions taken by the Research Division with other Divisions and Bureaus and reviews all major actions arising in the Division to ensure consistency in application of Bureau and Bappebti policy

## CHAPTER TWO

### Registration, Financial Reporting and Market Surveillance by James Jordan

This chapter covers manuals and information required for registration and reporting, respectively, for traders, brokers, advisors, and clearing house and pool operators. Sample material was developed from forms and draft provided by the Kansas City Board of Trade. The chapter responds to the following questions:

- ◆ What kind of information is required for (from) the players?
- ◆ How will the players gain information from the board?
- ◆ What kind of reporting and surveillance system will be required?

Initial discussions with ICEB (Bappebti) staff indicated that assistance was needed most urgently in interpreting and analyzing current CFTC/NFA (National Futures Association) forms and adapting them to Indonesian standards. Accordingly, sample registration forms and financial forms for brokers, pool operators, and advisors were provided. Considerable time was used in discussing general exchange procedures, educational requirements, clearing house operations.

An entire day was used in discussing general regulatory topics with Bappebti's Chairman, Mr. Arifin. At Mr. Arifin's request, a social and financial justification for commodity futures trading in Indonesia was proposed in the light of their current financial crisis (copy attached).

Two commodities are being considered for futures trading: These are coffee, and crude palm oil (CPO). Correspondingly, there now exist two trade organizations, one for each commodity, and it appears that they will establish Indonesia's first futures exchange.

A day's discussions were held with the Federation of Indonesian Vegetable Oil and Fats Association (FAMNI) about the current state of the proposed exchange. Emphasis was on the extensive computer software and hardware required. It appears the cost is very high for a trading system, a price dissemination system, and a clearing system. The estimated costs are from US\$1,000,000 to US\$10,000,000. It also appears that no system or has yet been selected or, for that matter, that any system is being seriously considered.

For an exchange to open in the next two years is very optimistic. Nevertheless, the present state of preparation by ICEB-Bappebti as the national regulatory authority appears on track.

Attached in a separate annex are numerous CFTC and NFA publications, reports, forms, and educational pamphlets.

## REGISTRATION

All persons and companies that intend to do business, as futures professionals must be licensed under the law. The primary purpose of licensing is to screen an applicant's fitness to engage in business as a futures professional and to identify those individuals and companies whose activities are subject to regulation.

The law specifies certain disqualification from licensing based on prior proceedings in which the applicant was found to have violated the law or in which the applicant was formally enjoined from engaging in certain activities. Bappebt will perform background checks to determine if a disqualification exists. The disciplinary history questions require the applicant to disclose any facts about its background which might indicate disqualification. Applicants must supply explanations and official papers relating to any "yes" answer. Willingly giving a false answer to any of the disciplinary questions is a crime and a sufficient reason in itself for denying licensing. It is in the best interest of the applicant to support a "yes" answer with complete explanations. In the case of a "yes" answer, licensing cannot be granted until the nature of the potential disqualification is fully understood and supported by the appropriate documents.

The following are required to be licensed:

**Futures Broker** – A broker is a limited company, which does both the following,

- ◆ Solicits or accepts orders to buy and sell futures contracts or commodity option contracts
- ◆ Accepts money or other assets from customers to support such orders

**Futures Pool Operator** – A FPO is a limited company which operates or solicits funds for a commodity pool, that is an enterprise in which funds contributed by a number of persons are combined for the purpose of trading futures contracts or commodity option contracts. Licensing may not be required if there are less than 10 participants in the pool.

**Futures Trading Advisor** – A trading advisor is an individual or limited company which, for compensation or profit, advises others as to the value or the advisability of buying or selling futures or option contracts. Licensing may not be required for advising less than 10 persons during any one-year period.

**Futures Broker Representative**

**Futures Pool Operator Representative**

**Futures Trading Advisor Representative** - A representative is an individual who solicits orders, customers, or customers' funds on behalf of a Futures Broker, Futures Pool Operator, or a Futures Trading Advisor. This, in effect, is anyone who is a salesperson or who supervises salespersons for any categories. The licensing requirements apply to any person in the supervisory chain-of-command.

**Futures Trader** - A Futures Trader is an individual who buys or sells futures or option contracts for such individuals' own account and do this trading as an exchange member

## REQUIRED FILINGS

### **Futures Broker**

- 1 A completed FORM 3 with all attachments
- 2 Three or more completed FORM 4 as Futures Brokers representative license – one must be a director, the other two as employees or higher
- 3 Financial FORM FR1, FR2, FR3 certified by public accountant
- 4 Agreement with approved clearinghouse to maintain Brokers segregated financial statements, reports confirms, etc in accordance with Bappebti requirements (This is to ensure adequate records in a standard format for ease of Bappebti surveillance and auditing)

### **Futures Pool Operator**

- 1 A completed FORM 3 with all attachments
- 2 Financial FORM FR2, Minimum capital funds US\$500,000
- 3 Two or more completed FORM 4 as futures pool operator representative – one must be a director and one an employee or higher

### **Futures Advisor**

- 1 A completed FORM 3 with all attachments
- 2 One or more completed FORM 4 as futures advisor representative
- 3 Financial FORM FR2, minimum capital funds US\$250,000

### **Futures Broker Representative Futures Pool Operator Representative Futures Advisors Representative**

- 1 A completed FORM 4 with attachments

### **Futures Trader**

- 1 A completed FORM 4 with attachments
- 2 Copy of financial statement as required by exchange, Bappebti will accept exchange minimum financial requirements

### FORM 3

APPLICATION IS HEREBY MADE IN ACCORDANCE WITH \_\_\_\_\_ (LAW) \_\_\_\_\_ FOR A LICENSE AS

- FUTURES BROKERS' LICENSE
- FUTURES TRADING ADVISOR'S LICENSE
- FUTURES POOL OPERATORS LICENSE

Please read questions carefully before completing the application form. Please answer every question and mark "N A" if not applicable. Should there be insufficient space, please attach separate sheets properly identified, dated and certified by signature.

1 FIRM NAME \_\_\_\_\_

2 MAILING ADDRESS \_\_\_\_\_

3 PHYSICAL LOCATION (ADDRESS) of your business and financial records as required by Bappebt regulations \_\_\_\_\_

4 TELEPHONE # \_\_\_\_\_ FAX # \_\_\_\_\_

5 PLACE & DATE OF INCORPORATION \_\_\_\_\_ (attach copy)

6 Has applicant (FIRM) used any other name currently or in the past? \_\_\_\_\_

If yes, what name(s) \_\_\_\_\_

7 Name(s) of each natural person who is substantial shareholder (owner), commissioner or officer (25% or more of issues share capital)

FULL NAME	ADDRESS	TITLE	% OF OWNERSHIP	NPWP TAX ID #

8 Name(s) of each shareholder (owner) which is limited company

NAME	ADDRESS	NPWP TAX ID #	PERCENT OF OWNERSHIP

Attach schedule "A" form 3 for each entry in question #8

9 Name(s) of Chief Executive Officer

NAME	ADDRESS	NPWP TAX ID #	PERCENT OF OWNERSHIP

10 Name(s) of each manager, supervisor or director

NAME	ADDRESS	TITLE	NPWP TAX ID #

11 Name(s) of any other person(s) who is in controlling interest of the applicant either directly or indirectly

NAME	ADDRESS	STATUS OR TITLE	NPWP TAX ID #

*Please set out as an annex hereto details of each person in questions #7, 9, 10, 11 showing full name, address, date of birth, nationality, NPWP Tax #, passport number, office held, and date of appointments and academic/professional qualification*

12 Have you attached the Bappebti required certified financial records? \_\_\_\_\_

13 Have you attached an organization chart showing all officers, directors, staff and their lines of reporting? \_\_\_\_\_

14 Have you attached an outline business plan of the applicant including types of customers with whom applicant purposes to do business (your business plan must relate to the type of license applied for and in the case of pool operators must include a sample prospectus)? \_\_\_\_\_

15 FOR FUTURES BROKERS ONLY

Have you attached a copy of your membership in a commodity futures exchange?  
\_\_\_\_\_

16 FOR ALL APPLICANTS

Has the applicant or any of its substantial shareholders or their related companies

- a Been licensed or registered to trade futures, options or leveraged foreign exchange in Indonesia or elsewhere? \_\_\_\_\_
- b Been denied trading privileged, expelled disciplined or censored by any Commodity or security exchange? \_\_\_\_\_
- c Been declared bankrupt or made an assignment for the benefit of creditors in Indonesia or elsewhere? \_\_\_\_\_
- d Been convicted of any offence of are there any proceedings now pending that may lead to a conviction in Indonesia or elsewhere? \_\_\_\_\_
- e Had judgement in civil proceedings of fraud, misrepresentation, dishonesty, or are there any proceedings now pending that may lead to a judgement in Indonesia or elsewhere? \_\_\_\_\_
- f Been denied, refused, paid out on, or revoked on a fidelity or surety bond in Indonesia of elsewhere? \_\_\_\_\_
- g Are you indebted to anyone due to any activities in the futures or security industry? \_\_\_\_\_

For each "yes" answer please attach full explanation and circumstances

16 FOR POOL OPERATORS

Name of futures broker \_\_\_\_\_  
(Attach copy of work contract agreement)

DECLARATION

- 1 (Statement of law and penalty)
- 2 We declare that all information given in this application and any attachments are true and correct

NAME OF APPLICANT \_\_\_\_\_

BY NAME OF OFFICER/DIRECTOR \_\_\_\_\_

SIGNATURE \_\_\_\_\_

DATE \_\_\_\_\_

### FORM 3 – SCHEDULE “A”

1 Applicant name \_\_\_\_\_

2 Name of entity listed in item #8 of Form 3 or item #4 of Schedule “A”  
\_\_\_\_\_

3 Name(s) of each natural person that is 25% or more shareholder of item #2

FULL NAME	ADDRESS	TITLE	PERCENT OF OWNERSHIP	NPWP TAX I D #	IS FORM 4 ATTACHE D

4 Name(s) of each limited company that is 25% or more shareholder of item #2

NAME	ADDRESS	NPWP TAX I D #	PERCENT OF OWNERSHIP

*If there is no entry on item #3 above, complete another schedule “A” on each entity in item #4*

SIGNATURE \_\_\_\_\_ DATE \_\_\_\_\_

NAME \_\_\_\_\_ TITLE \_\_\_\_\_

**FORM 4**

APPLICATION IS MADE IN ACCORDANCE WITH \_\_\_\_\_ (LAW) \_\_\_\_\_ FOR A LICENSE AS

- FUTURES BROKER'S REPRESENTATIVES' LICENSE
- FUTURES TRADING ADVISORS' REPRESENTATIVES LICENSE
- FUTURES POOL OPERATORS' REPRESENTATIONS LICENSE
- FUTURES TRADER

Applicant is affiliated with Futures Broker, Futures Trading Advisor, or Futures Pool Operator

NAME \_\_\_\_\_

Please read questions carefully before completing application form Please answer every question and mark "N A" if not applicable Should there be insufficient space, please attach separate sheets properly identified, dated and certified by signature

Set out below the personal particulars of APPLICANT

1 NAME \_\_\_\_\_

2 RESIDENTIAL ADDRESS \_\_\_\_\_

3 BUSINESS ADDRESS \_\_\_\_\_

4 PRIVATE TELEPHONE # \_\_\_\_\_

BUSINESS TELEPHONE # \_\_\_\_\_

FAX # \_\_\_\_\_

5 BIRTH DATE \_\_\_\_\_ PLACE OF BIRTH \_\_\_\_\_

6 TAX SUBJECT INDEX NUMBER (NPWP) \_\_\_\_\_

7 NATIONALITY \_\_\_\_\_

8 Have you been known by and used any other name(s)? \_\_\_\_\_ if yes, give name(s) \_\_\_\_\_

9 Have you been registered in any futures or security exchange or industry? \_\_\_\_\_ if yes, provide details

10 Has the applicant

- a Been licensed or registered to trade futures, option or leveraged foreign exchange in Indonesia or elsewhere? \_\_\_\_\_
- b Been denied trading privileges, expelled, disciplined or censored by any commodity or security exchange? \_\_\_\_\_
- c Been declared bankrupt or made an assignment for the benefit of creditors in Indonesia or elsewhere? \_\_\_\_\_
- d Been convicted of any offense other than minor traffic offenses or are there any proceedings now pending that may lead to a conviction in Indonesia or elsewhere? \_\_\_\_\_
- e Had judgement in civil procedures of fraud, misrepresentation, dishonesty or are there any proceedings now pending that may lead to a judgement in Indonesia or elsewhere? \_\_\_\_\_
- f Been denied refused, paid out on or revoked on a fidelity or surety bond in Indonesia or elsewhere? \_\_\_\_\_
- g Do you now have any unsatisfied judgements a lien against you? \_\_\_\_\_

11 EMPLOYMENT HISTORY – PAST 10 YEARS

NAME & ADDRESS	NATURE OF BUSINESS	JOB TITLE	JOB DESCRIPTION	FROM	TO	REASON FOR LEAVING

12 RESIDENTIAL HISTORY – PAST 10 YEARS

FROM	TO	ADDRESS

13 EDUCATIONAL HISTORY

FROM	TO	NAME & ADDRESS OF INSTITUTION	MAJOR STUDIES	CERTIFICATE DEGREE

Attach copy of certificate or degree

14 TEST

Have you passed the Commodity Futures examination? \_\_\_\_\_

(Attach copy of test results )

**DECLARATION**

Statement of law

I declare that all information given in this application and any attachments are true and correct

SIGNATURE OF APPLICANT \_\_\_\_\_

DATE \_\_\_\_\_

I certify that I have verified applicant's statements in questions 11, 12 & 13

SPONSOR'S SIGNATURE \_\_\_\_\_

DATE \_\_\_\_\_

## FINANCIAL REPORTING

Every FUTURES BROKER, COMMODITY POOL OPERATOR, TRADING ADVISOR AND FLOOR BROKER must maintain and have available for inspection certain records that support and explain its activities. Such records must be maintained in an orderly fashion at the entities registered office. All books, records, etc. must be kept for five years and be readily accessible for the last two years.

In the case of any entity handling or holding customer segregated funds, the records and accounting functions for these segregated funds must be performed in an approved format and in the interest of efficiency and economy, it is required that a approved clearing house maintain a service bureau to do this record keeping.

Any entity holding or handling customer segregated funds must complete at least monthly a statement of computation of minimum capital requirements. Initially this statement must be submitted to Bappebti on this monthly basis. A statement of segregated requirements and location of segregated funds will be completed daily by the appointed service bureau described above. This will be done for each futures broker. Bappebti will require other financial statements at initial registration and on an annual basis.

### MINIMUM FINANCIAL REQUIREMENTS

Attached is an ICEB comparison of various countries minimum requirements. Absolute numbers are not adequate due to the various financial sizes and activities of companies. These attached forms have been designed to require varying paid in capital depending on the risk of the companies' activity. The larger the base of customers and accompanying segregated funds would require larger capital. Extensive activities in the cash and spot commodity markets also create additional risk and again would require addition or increased capital. The numbers supplied in this report seemed somewhat the consensus of the ICEB staff but in no way are they rigid.

### FORMS ATTACHED

FORM FR1 – Statement of segregated requirements and location of segregated funds

FORM FR2 – Statement of financial condition – Balance Sheet

FORM FR3 – Statement of computation of minimum capital requirements

**FORM FR1**

**STATEMENT OF SEGREGATED REQUIREMENTS  
AND LOCATION OF SEGREGATED FUNDS**

COMPANY NAME \_\_\_\_\_

LICENSE NO \_\_\_\_\_

AS OF DATE \_\_\_\_\_

SEGREGATION REQUIREMENTS	AMOUNT
1 Net Ledger Balances in Customers' Accounts	
2 Securities (at market)	
3 Unrealized Profit (Loss) in Open Contracts	
4 Net Equity of Customers (Add lines 1, 2, & 3)	
5 Add Deficit Accounts	
6 Amount required to be segregated (Add lines 4 & 5)	

LOCATION OF SEGREGATED FUNDS	
7 Segregated Cash on hand	
8 Deposited in segregated bank accounts	
9 Securities deposited by customers (at market)	
10 Margin deposits with clearing houses	
11 Net equities with other brokers	
12 Broker segregated investments in securities (at market)	
13 Total in segregation (add lines 7 through 12)	
14 Excess (Deficiency) Funds in Segregation (line 13 minus line 6)	

**FORM FR2**

**STATEMENT OF FINANCIAL CONDITION  
TO BE PREPARED BY FUTURE BROKER**

COMPANY NAME \_\_\_\_\_

LICENSE NO \_\_\_\_\_

AS OF DATE \_\_\_\_\_

ASSETS	AMOUNT		
	CURRENT	NOW CURRENT	TOTAL
1 Funds segregated from form FR1 – line 13 (Do not duplicate line 1 assets below)			
2 Cash in bank and on hand			
3 Margin deposits at clearing house			
4 Receivable for other brokers			
5 Receivable from customers (debit balances)			
6 Securities			
7 Inventories of physical commodities			
A Hedged			
B Unhedged			
8 Unrealized gains on cash forward Contracts			
9 Security deposits with clearing house			
10 Exchange memberships			
11 Investments in other limited companies			
12 Plant, property, equipment (at net book value)			
13 Other assets (itemize on attachments)			
14 Total assets			

LIABILITIES AND OWNERSHIP FUNDS	AMOUNT
15 Customers equities payable From form FR1, line 4 Do not duplicate line 15 liabilities below)	
16 Bank loans & overdrafts	
17 Loans & advances from related companies	
18 Payable to clearing houses	
19 Payable to other brokers	
20 Accounts payable	
a Expenses	
b Salaries	
c Taxes	
d Unrealized loss on cash (Forward contracts)	
e Other	
21 Subordinated loan agreements	
22 Total liabilities	
23 Ownership funds	
a Paid-in capital	
b Share premium	
c Capital reserve	
d Unappropriated profit/accumulated loss	
24 Total ownership fund	
25 Total liabilities and ownership funds	

**FORM FR3**

**STATEMENT OF COMPUTATION OF  
MINIMUM CAPITAL REQUIREMENTS**

COMPANY NAME \_\_\_\_\_

LICENSE NO \_\_\_\_\_

AS OF DATE \_\_\_\_\_

**NET CAPITAL**

1	CURRENT ASSETS (Form FR1, Line 14)		
2	TOTAL LIABILITIES (Form FR1, Line 22)		
3	DEDUCTIONS FROM TOTAL LIABILITES SATISFACTORY SUBORDIANATED LOANS ADJUSTED LIABILITIES		
4	LINE 2 MINUS LINE 3		
5	NET CAPITAL (LINE 1 MINUS LINE 4)		

**CHARGES AGAINST NET CAPITAL**

A	10% OF STHE MARKET VALUE OF HEDGED INVESTMENTS		
B	25% OF THE MARKET VALUE OF UNHEDGED INVESTMENTS		
C	10% OF THE MARKET VALUE OF HEDGED OPEN CASH CONTRACTS		
D	25% OF THE MARKET VALUE OF UNHEDGED OPEN CASH CONTRACTS		
E	UNDERMARGINED CUSTOMERS' ACCOUNT		
11	DEFICIT ACCOUNTS		
12	TOTAL CHARGES (Add Lines 5 to 10)		

**NET CAPITAL COMPUTATION**

13	ADJUSTED NET CAPITAL (Line 5 minus Line 12)		
14	NET CAPITAL REQUIRED		
	A AMOUNT REQUIRED TO BE SEGREGATED (Form FR2, Line 6) This amount is subject to a 10% net capital factor		
	B ENTER 10% OF LINE A		
	C ENTER THE GREATER OF LINE 14B OR U S \$500,000		
15	EXCESS NET CAPITAL (Line 13 less Line 14C)		

## **MARKET SURVEILLANCE PROGRAM**

Bappebti as an independent agency will be responsible (among other tasks) to use a market surveillance program to maintain

### **COMPETITIVE MARKETS ORDERLY TRADING PUBLIC TRANSPARENT PRICES EQUITABLE TREATMENT TO ALL PARTICIPANTS**

The goals of market surveillance are to spot adverse situations in futures markets and to pursue appropriate remedial actions in coordination with the futures exchange to avoid disruption of the market. To accomplish these objective, a market surveillance program must determine when a trader's position in a futures market becomes so large relative to other factors that it is capable of causing prices to no longer accurately reflect legitimate supply and demand conditions. A surveillance program needs to collect, analyze and compare daily data concerning overall supply and demand conditions in the cash market, both spot and forward, cash and futures prices and price relationships, and the sizes of hedgers and speculators position in the futures markets. The market surveillance activities involve monitoring large trader's position, maintaining speculative limits for coffee and CPO and analyzing physical supply-demand data.

Futures contracts are traded for specific delivery months established by the exchange. Bappebti must concentrate its market surveillance analysis on contracts that are expiring because it is during contract expirations when the market prices are most vulnerable to manipulation through abuse of the delivery process. When price movements, not supported by supply and demand conditions, occur during contract expiration, the result may allow a trader to benefit from the situation at the expense of other participants. The delivery mechanism is intended to lead to, and normally results in convergence of cash and futures prices at contract expiration. However, if a trader attains a market dominant position, he may be able to control the delivery process, dictate the terms of liquidating open trades and cause a divergence of futures and spot cash prices. Bappebti will be alerted to possible disruption through its day to day analysis of cash prices, flat and basis, cash positions, futures positions and supply-demand data. Bappebti's first line of surveillance defense in the futures contract itself. Each proposed futures contract must be analyzed for its economic purpose, terms and conditions, and public interest concerns before it can be approved for trading.

### **APPROPRIATE CONTRACT ECONOMIC TERMS AND CONDITIONS ARE THE BEST PREVENTION AGAINST MARKET DISRUPTION**

For all futures contracts the market surveillance staff will monitor the daily activities of large traders, key price relationships and relevant supply and demand factors as a continuous review for potential market problems, Additionally surveillance staff must

prepare weekly surveillance summaries for each futures contract that is approaching its critical expiration period. Any potential problems must be reviewed immediately by the Bappebti senior staff and chairman. These reviews keep these individuals abreast of potential problems and significant market developments so they will be prepared to take prompt legal action as required by law.

The market surveillance staff will routinely review the market to detect situations that forewarn Bappebti of possible market problems. These situations are observed and if necessary verbal contacts are made with the futures brokers or traders who are significant participants in the market being examined. These verbal contacts may be for the purpose of asking questions, confirming reported market positions, alerting the brokers or traders as to Bappebti's concern for the situation, or warning them to conduct their trading responsibly. The "Jawboning" activity may be quite effective in resolving many potential problems at an early stage.

The exchange also must be required, as a provision for their licensing to maintain an effective market surveillance program. Further they must be required by regulation to serve as the first line of defense against market disruption.

The market surveillance process is not conducted exclusively at Bappebti. If a problem develops, it must be handled jointly by Bappebti and the affected exchange. Relevant surveillance information is exchanged and, when appropriate, corrective actions are coordinated. Bappebti should give the exchange the first opportunity to resolve the problem itself, either informally or through emergency action. If an exchange fails to take actions the Bappebti deems appropriate, Bappebti has powers under which it can order the exchange to take actions specified by Bappebti. Most issues will be resolved without the need to use emergency powers.

### **LARGE TRADER REPORTING SYSTEM**

A main goal of market surveillance is to detect an individual or group of traders that may attempt to control or manipulate the futures market, and thereby cause prices to inaccurately reflect supply and demand. To accomplish this goal, a market surveillance system must be able to track the relative cash and futures positions of significant traders and identify when the position of one or more traders is capable of creating price distortions.

The large trader reporting system may be the heart of Bappebti's surveillance system, as the staff will use this to collect and analyze data on all large trader positions in all commodities. Each day the staff must examine computer listings of large trader positions in actively traded markets, to identify positions that could pose the threat of manipulation. Reportable positions—a daily report of positions above 25 contracts in any one month of any commodity—will be collected daily for futures brokers and clearing house members. Clearing houses will also be required to provide daily positions each clearing member is carrying in each futures contract in each commodity.

Since traders may carry futures positions through more than one futures broker and since individuals sometimes control or have a financial interest in more than one account, Bappebtí must collect information that enables its surveillance staff to aggregate related accounts. Futures brokers must file FORM 102, which identifies each new account with reportable positions for each future. In addition, once his position reaches a reportable level, the trader is required to file a more detailed identification report a FORM 101, to further identify accounts and reveal any relationship that may exist with other accounts or traders.

Futures positions also must be analyzed in relation to the deliverable supply of individual commodities, to determine whether a position may have the potential to affect prices. For coffee and CPO the exchange must supply data on deliverable inventories of particular commodities in approved warehouses, providing a preliminary approximation of deliverable supply. These data do not, however, reveal actual ownership and availability of a particular commodity.

Hedgers who have reported on their status on FORM 101 may exceed the speculative limit controls. However these hedgers will be required to report their hedged futures trades and actual cash inventories and actual spot and forward cash contracts on a weekly FORM 104. Thus, in order to better assess the deliverable supply, Bappebtí may take action including

- ◆ Surveying the ownership of the physical commodity, in coordination with the exchange that must have daily records of deliverable supplies in approved delivery warehouses
- ◆ Special calls on large traders to determine quantities owned
- ◆ Surveying major long and short position holders to evaluate their intentions and capabilities regarding deliveries
- ◆ Interviewing with industry participants (who may or may not be participants in the particular futures contract) to assess the availability of the physical commodity in other sections of the cash markets

### **SPECULATIVE LIMIT CONTROLS**

Another element of the market surveillance program is the monitoring of compliance with Bappebtí or exchange speculative limit rules. These rules help prevent speculators from accumulating concentrations of contracts of a size sufficient to possibly disrupt a market. To monitor these limits, the market surveillance staff must review daily all large trader reports for potential violations. Although bona fide hedgers are exempt from speculative limits Bappebtí will require these hedgers to submit weekly reports of cash positions. A hedger is allowed to exceed its cash positions but only by the speculative limit amount.

**FORM 100**  
**STATEMENT OF REPORTING TRADER**

Every person who holds a reportable position must file a Form 100. If after one year from the filing date, you are still in a reportable position, you must file a new Form 100. This form is required by Bappesti regulation.

**PART A**

1 NAME OF REPORTING TRADER \_\_\_\_\_

2 STREET ADDRESS \_\_\_\_\_

3 CITY \_\_\_\_\_

4 PRINCIPAL BUSINESS OF THE REPORTING TRADER \_\_\_\_\_

5 IS THE REPORTING TRADER'S FUTURES TRADING ANY OF THE FOLLOWING

- A COMMODITY POOL PROGRAM
- B SPECULATIVE
- C HEDGING (if hedging complete part B)
- D OTHER (specify)

6 IS THE REPORTING TRADER REGISTERED WITH BAPPEBTI AS

- A FUTURES BROKER
- B COMMODITY POOL
- C COMMODITY TRADING ADVISOR
- D FUTURES TRADER

7 GIVE THE NAMES AND LOCATION OF ALL FUTURES BROKERS THROUGH WHICH THIS REPORTING TRADER NOW CARRIES ACCOUNTS

NAME \_\_\_\_\_  
ADDRESS \_\_\_\_\_

8 DOES THE REPORTING TRADER HAVE ANY ACCOUNTS OR CONTROL ANY OTHER FUTURES ACCOUNTS OR HAVE A FINANCIAL INTEREST IN ANY OTHER FUTURES ACCOUNTS \_\_\_\_\_, IF YES, ATTACH SPECIFIC INFORMATION

9 DOES THE REPORTING TRADER REPRESENT A FOREIGN GOVERNMENT OR ACT AS THE AGENT OF A FOREIGN GOVERNMENT \_\_\_\_\_, IF YES, ATTACH SPECIFIC INFORMATION

SIGNATURE \_\_\_\_\_ DATE \_\_\_\_\_

**FORM 100 – PART B**

**HEDGING OR COVERING RISK EXPOSURE**

<b>Futures or Option Contract Used</b>	<b>Cash Commodity(ies) Hedged Or Risk Exposure Covered</b>	<b>Marketing Occupations Associated With Hedging Uses</b>
		<input type="checkbox"/> (1) Producer/Feeder of livestock or poultry <input type="checkbox"/> (2) Other Producer <input type="checkbox"/> (3) Merchant or Dealer <input type="checkbox"/> (4) Processor <input type="checkbox"/> (5) End User/Consumer <input type="checkbox"/> (6) Swaps or Derivatives Dealer <input type="checkbox"/> Other (specify) _____
		<input type="checkbox"/> (1) Producer/Feeder of livestock or poultry <input type="checkbox"/> (2) Other Producer <input type="checkbox"/> (3) Merchant or Dealer <input type="checkbox"/> (4) Processor <input type="checkbox"/> (5) End User/Consumer <input type="checkbox"/> (6) Swaps or Derivatives Dealer <input type="checkbox"/> (7) Other (specify) _____
		<input type="checkbox"/> (1) Producer/Feeder of livestock or poultry <input type="checkbox"/> (2) Other Producer <input type="checkbox"/> (3) Merchant or Dealer <input type="checkbox"/> (4) Processor <input type="checkbox"/> (5) End User/Consumer <input type="checkbox"/> (6) Swaps or Derivatives Dealer <input type="checkbox"/> (7) Other (specify) _____



**FORM 104**  
**Weekly Statement of Cash Positions**  
**In Commodities**

DATE \_\_\_\_\_ BAPPEBTI CODE # \_\_\_\_\_

**PART 1 Fixed-price cash positions**

FUTURES MARKET USED FOR HEDGING	CASH COMMODITY HEDGED IN FUTURES	Long Cash			Short Cash
		(1) Stocks Owned	(2) Purchase Commitments	(3) Total Long	(4) Sale Commitments
COFFEE (in tons)	COFFEE				
	COFFEE PRODUCTS (in '000 bu Equiv )				
	OTHER				
	TOTAL				
CRUDE PALM OIL (in tons)	CRUDE PALM OIL				
	CRUDE PALM OIL PRODUCTS (in '000 bu Equiv )				
	OTHER				
	TOTAL				

PART II – Fixed-price cash positions for cross hedging

FUTURES MARKET USED FOR HEDGING	CASH COMMODITY (SPECIFY COMMODITY OR PRODUCT)	UNITS (Specify tons, ctw , lbs , bu , etc )	LONG CASH		SHORT CASH
			STOCKS OWNED (1)	PURCHASE COMMITMENTS (2)	SALE COMMITMENT S (3)

## **CHAPTER THREE**

### **Report on Proposed Bappebti Rules by Frederic Spindel**

#### **Background and Scope**

Contained in this chapter are an analysis and recommendations regarding proposed Government of Indonesia (GOI) regulations for supervision and monitoring of commodity futures trading. One of the Team's legal specialists reviewed draft regulations to be administered by Bappebti, the GOI agency that is to oversee such trading. The objective of this examination was to determine whether these regulations were consistent with the Commodity Futures Trading Law, No 32 (1997) (the "Law"), as well as with any draft exchange or clearinghouse rules available, and to suggest changes to remedy observed deficiencies in the regulatory scheme.

Two sets of proposed regulations were reviewed. The first was a Government Regulation Regarding the Execution of Commodity Futures Trading. This regulation was designed for adoption by GOI's Minister of Industry & Trade under which Bappebti operates. The second set was the rules to be promulgated by Bappebti itself. Under the Indonesian system, ministerial-level regulations delineate the framework for implementing enacted legislation, rules providing further detailed requirements are then approved by the responsible agency.

The proposed Bappebti Rules are discussed in this report. An evaluation of the proposed government regulation is contained in a separate report, which specifically addresses that Regulation's provisions. The two sets of regulatory requirements should be considered together to gain a proper perspective on the changes that the Project Team recommends.

#### **Comments and Recommendations**

Before proceeding with an analysis of specific provisions, it is important to underscore the context in which the proposed Bappebti rules were developed. The Rules consist of an English-language draft that was crafted for ICEB in July 1996 by a U.S. law firm and patterned in material respects on regulations of the U.S. Commodity Futures Trading Commission. A draft of the proposed Law was then available for reference. However, the Rules were prepared without the benefit of the Law as enacted, which was not put into effect until December 1997, or to the proposed Government Regulation, which was initially developed in early 1998.

Also, an electronic, screen-based, system for trading futures and options contracts has been selected by the Indonesian Futures Exchange ("IFE"), instead of a conventional trading floor where transactions are executed by the open-outcry method. The Bappebti

Rules, however, do not take into account the particular features offered by a computerized system. As a result, the regulatory requirements in these Rules are not tailored to such a regime. For this reason, revisions to a number of the sections in the Rules are necessary to harmonize them with the trading environment and the IFE rules governing the operations of the electronic market.

## **I Structural Defects**

The proposed Rules are divided into nine chapters, which deal with various substantive and procedural requirements, such as recordkeeping, licensing and obligations of market professionals. While this approach is generally satisfactory, the structure of certain of the chapters is believed to be unsuitable and should be replaced. In addition, the Rules fail to deal with several major functional areas within Bappebti's regulatory mandate. These matters are addressed in this Part I. Inadequacies in specific sections of the Rules are treated in Part II below.

*Chapter 7 - (Rules of Practice)* This chapter creates a framework for conducting adjudicatory-type proceedings whenever Bappebti seeks to impose sanctions for violations of law or where it is considering a denial, suspension or revocation of a license. The provisions in this chapter contemplate the service of a complaint and answer, hearings before an independent hearing officer, the calling of witnesses with right of cross examination, prohibitions on ex parte communications, the submission of briefs, and other formal procedures traditionally associated with proceedings before administrative agencies in the U.S. This form of decision-making is not consistent with the Indonesian model, and the Project Team believes that it would be inappropriate and ineffective to superimpose these kinds of procedures.

Under the Indonesian model, a person who is subject to an agency examination for possible violations or whose license application is being reviewed is afforded the opportunity to explain his position and offer pertinent information to the examiners, and then to progressively appear before higher levels of officials as the inquiry continues. A more detailed discussion of this process is provided in the Project Team's Report on Enforcement.

**Recommendation** In lieu of the provisions in Chapter 7, the proposed enforcement rules prepared by the Project Team, which are appended to the Report on Enforcement, should be incorporated. These rules delineate the manner in which Bappebti examinations are to be conducted and include references to a person's ability to submit information and explanation in opposition to adverse action proposed to be taken by Bappebti. To insure that these procedures are applicable to licensing, the enforcement rules should be modified to expressly indicate that they also encompass situations where Bappebti staff is evaluating whether to deny, suspend or revoke a license.

*Chapter 8 (Appeals from Exchange Disciplinary and Membership Actions)* - This chapter contains procedures under which Bappebti reviews disciplinary sanctions and adverse membership actions taken by the IFE against members of the Exchange or applicants.

for membership. Similar to the Rules of Practice in Chapter 7, these procedures contemplate a formalized process derived from the U.S. model, with pleadings, motions, evidentiary record, legal briefs, and orders. The Project Team believes that these provisions will be difficult for Bappebti to administer and are not mandated by the Law.

Under Article 5, clause O, of the Law, Bappebti is authorized to “examine” any objection submitted by a party to a decision of the Exchange or Clearing House, and to determine whether to certify or revoke it. An examination is understood as being an inquiry into the matter involved with no particular format to be followed. Thus, the Project Team is of the view that effective review of Exchange disciplinary and membership actions can be achieved more informally and in a manner in which Indonesians are more accustomed.

This would entail an obligation by the Exchange or Clearing House (“SRO”) to submit all exchange disciplinary rulings to Bappebti within a prescribed period after a final decision is rendered by the SRO. A member aggrieved by a decision would have the right to submit to Bappebti within a fixed period thereafter a written petition challenging the SRO’s action and explaining the basis for overturning it. Bappebti, through its staff, would then review the ruling and would have the discretion to ask the SRO and/or the aggrieved member or applicant to provide additional information and to appear at a conference to discuss the matter. A staff report, with recommendations, would then be presented to the Chairman who in turn could ask for further written statements or have the parties appear prior to determining to sustain, modify or set aside the SRO action. Since it is in the SRO’s province to sanction its members for misconduct and to decide the qualifications for membership, the rules should make clear that Bappebti will not disturb the SRO decision unless serious substantive or procedural deficiencies in the ruling are uncovered by its examination.

**Recommendation** The provisions in Chapter 8 of the proposed Bappebti Rules should be recast to reflect the above-described framework for Bappebti’s review of SRO actions against members. Set forth in Attachment A to this Report is a revised version of Chapter 8 of the Rules that incorporates the restructuring that is suggested by the Project Team.

Chapter 4 (Exchanges and Clearing Houses) - This chapter is limited to a group of provisions that impose duties of recordkeeping, audit, financial responsibility and reporting on the Exchange and Clearing House. Commentary on the adequacy of these sections is presented in Part II below. However, the Project Team is of the view that this chapter needs to be expanded in two fundamental respects. First, the concept of self-regulation by an Exchange and Clearing House of its members embraces a responsibility of the SRO to enforce its rules and to have programs in place to assure compliance by members. The omission of provisions dealing with these responsibilities creates a regulatory gap. In this regard, individual officials of the SRO as well as the SRO itself should be held accountable for failures to enforce regulatory standards.

Second, it is important to outline the mechanism for facilitating Bappebti's role in determining whether a change to SRO rules, including the terms of futures and options contracts to be traded on the Exchange, should be put into effect. Under Article 6, clauses G and H, of the Law and Article 84 of the proposed Government Regulation, that role entails review and approval of rule changes proposed by the SRO, or a directive from Bappebti that the SRO adopt or amend a rule. See Articles 4 and 28 of the proposed Government Regulation.

**Recommendation** The scope of Chapter 4 should encompass the following additional provisions:

- ◆ A section expressly mandating SRO enforcement of its rules and making the SRO and its officials subject to sanctions from Bappebti for any willful or negligent failure in such enforcement.
- ◆ A section requiring an SRO to have and use due diligence to implement an affirmative program to assure member compliance with rules. This program would include surveillance of market activity, examination of member records, and investigation of customer complaints and other possible violations of law, regulations and SRO rules.
- ◆ A section providing that any SRO application to Bappebti requesting an amendment to the SRO's rules should contain (i) the exact language of the change, (ii) an explanation of the reasons for and effect of the change, (iii) and a statement whether the change is substantive, administrative or deals with an emergency matter. In the case where it is considering whether to direct the SRO to adopt a rule, Bappebti shall notify the SRO of the text of and explanation for the rule. It would then afford the SRO 10 days to object before it would be able to order adoption of the rule. There would be an exception for an emergency rule which is one that Bappebti could direct be immediately put into effect. In the latter situation, the section would provide that the SRO may request Bappebti to lift the emergency rule, but that it remains operative unless Bappebti suspends it.

A section requiring that, if Bappebti finds that a rule amendment submitted by an SRO as an administrative rule is in fact a substantive rule, Bappebti shall give notice to the Exchange of that finding. In that event, if notice is given by Bappebti within 10 days of its submission, the rule shall not become effective at the end of that period. If Bappebti gives notice after the rule has already become effective, then such rule would be suspended pending Bappebti's further review of the rule.

Chapter 10 (Arbitration) - Under Article 6 of the Law, Bappebti is charged with establishing a dispute resolution facility for claims arising from commodity trading activities. In turn, the Government Regulation in Article 112 contemplates a mediation or consensus process to be then followed by arbitration. The Project Team's Report on the proposed Government Regulation suggests revisions to Article 112 so that market participants are legally bound to arbitrate claims by entering into pre-dispute arbitration agreements. Moreover, as discussed in the Project Team's Report on Arbitration,

procedural rules to govern the arbitration process are needed to guide persons desiring to utilize the arbitration forum

**Recommendation** A new Chapter 10 should be added to the Bappebti Rules to deal with arbitration and should incorporate the suggestions made in the Project Team's Report on Arbitration. In particular, this Chapter should provide that BANI be delegated to conduct arbitrations between customers and market professionals under BANI's existing rules of procedure or, alternatively, that BANI's rules be used as the pattern for a set of rules in Chapter 10 for conducting arbitrations under Bappebti's supervision. In either case, Chapter 10 should contain provisions suspending a market professional's license or a trader's right to trade in the event an arbitral award is not paid. With respect to appeals from member/member arbitrations decided under the auspices of the Exchange, a procedure similar to that proposed for review of Exchange disciplinary action in Chapter 8 should be considered.

## **II Specific Inadequacies**

Apart from the foregoing structural deficiencies in the Rules, a number of provisions were observed by the Project Team to be incomplete or warranting modification to enhance effectiveness. The results of the Team's analysis and the suggested changes are presented below.

### **Chapter 1 (Recordkeeping)**

*Section 1 01* This section mandates that books and records required to be kept under the Law and Bappebti Rules be maintained for five years and be readily accessible for two years. The records are to be open for inspection by Bappebti representatives. The provision leaves open whether other GOI agencies should also be accorded inspection rights.

It is believed that, given the sensitive nature of trading information, inspection powers should not be available to other GOI agencies as a matter of course. Rather, Bappebti's consent should be needed to enable another agency's personnel to inspect records.

Another concern is that there is no reference in this section to records required to be maintained pursuant to the proposed Government Regulation, even though that Regulation contains a number of articles imposing recordkeeping obligations. See, for example, Articles 85-90.

### **Recommendation**

- A Inspection authority should be limited to Bappebti representatives. This section should provide that other GOI agencies must obtain the Chairman of Bappebti's consent before accessing records.

- B The section should be revised so that the records-retention policy is applicable to records required by the proposed Government Regulation

*Section 1 02* This section is designed to allow records to be stored on media such as microfiche and optical disk It contemplates that handwritten records such as orders be kept for two years in paper record form and that the problem of preserving the integrity of existing records be addressed

This provision needs to be developed in a number of respects First, the Rules should make clear that optical disk storage includes data and information storage on both computer diskette and CD ROM Second, since trading on the Exchange will be through an electronic system and market professionals and participants will have terminal access to such a system there should be an express recognition in the Rules that computer-generated data and documents created through the system may be retained in that format Third, to deal with the threats of unauthorized destruction or alteration of information, this section should make such conduct a violation and require that entities responsible for maintaining records adopt adequate procedures for assuring both the physical and electronic security of information that is to be maintained

Among other things, the technology employed must be non-rewritable media and have write-verify capabilities in order to automatically verify and correct defects in information entered Disks or CDs should be removable and serialized, and have non-erasable time-date capability so that all information on the disk is recorded with a time and date of entry Entities using optical storage should also be required to have available to Bappebt representatives conducting an inspection of records the information needed for them to read, convert to hard copy and download such records

**Recommendation** Section 1 02 should be drafted to incorporate the concepts referred to above

*Section 1 03* Under this section, Futures Brokers are compelled to keep complete and systematic records of their business transactions This provisions appears to be the same substantively as Article 90(1) of the proposed Government Regulation, which applies to Futures Traders as well as Futures Brokers

**Recommendation** To prevent confusion over the governing standard, this section should either be eliminated or at least indicate that it represents a refinement of the mandates in Article 90(1)

*Section 1 05* This section provides that a written record be made for each order for an account and time stamped to within the nearest minute It appears to be similar to Article 91 of the proposed Government Regulation that requires that an order card be prepared and printed out As was noted in commenting on Article 91, in an electronic trading environment, a representative without using a handwritten order ticket may take a customer order This can be accomplished by directly entering the order information

into a desktop terminal, which will automatically record to the second the time at which the order is entered

Section 1 05 does not currently allow for this method of accepting orders. The provision also does not recognize that, under Article 52(1) the Law, orders may be accepted from customers only if they are in writing. Nor does it take into account that the proposed Government Regulation in Article 106 appears to allow satisfaction of this written order requirement where the Futures Broker records the telephone conversation through which an order is placed.

### **Recommendation**

- A Section 1 05 should expressly allow terminal order entry in lieu of a time-stamped handwritten order.
- B A requirement should be added that any written orders transmitted to a Futures Broker by a customer be time-stamped within one minute of its receipt and that in the case of a telephone-recorded order the recording system should have the capability of identifying the time of the call.

*Sections 1 06 & 1 11* These provisions require a Futures Broker to maintain floor orders and trading cards with respect to orders placed for execution on the floor of an exchange. Since IFE will have no trading floor and all orders on the Exchange will be executed electronically, there will be no need for floor orders or trading cards. In the case of futures traded on a foreign exchange, the Futures Broker will not have access to such trading records.

**Recommendation** Sections 1 06 and 1 11 should be deleted from the Rules.

*Section 1 07* Under this section, a Futures Broker must provide a written confirmation to a customer no later than the next trading day. There seems to be a discrepancy between this standard and the duties imposed on Brokers in the proposed Government Regulation. On the one hand, Article 92(2) requires confirmation of a customer's position arising from a transaction by midday of the day after execution of the trade. On the other hand, Article 106(3) states that a Broker must deliver a transaction report to a customer who placed an order within 2 working days. With a computerized trading system, reports of execution are communicated instantaneously to the terminal of the Futures Broker placing the order, usually with the capability of printing out a confirmation form showing price and other details of the trade for transmission to the customer. Accordingly, written confirmations for IFE trades can easily be sent out to customers on the very day of execution and certainly by midday of the next trading day.

**Recommendation** This section should be revised so that written confirmations of IFE trades are sent out to customers by midday the following day in conformity with Article 92(2). Futures Brokers should also be required to provide make reasonable efforts to provide verbal confirmation promptly after receipt of notification of execution but in no

event on the same day of the trade Foreign futures transactions should be confirmed no later than the following day

*Section 1 08* This section provides for the furnishing of monthly statements to customers and prescribes the content of those statements Although Article 92(3) of the proposed Government Regulation would appear to permit quarterly statements in certain cases, the monthly obligation exists even where there is no activity in the account

**Recommendation** This section should be amended to enable a Futures Broker to furnish a quarterly statement if there is no trading or other activity, such as cash deposits or withdrawals, during the quarter

### Chapter 2 (Licensing)

*Section 2 01* Pursuant to this section, applications for business licenses are to be made on a “Form1” to be filed with Bappebti together with a prescribed filing fee The provision states that it is for licensing of Futures Brokers, Pool Operators and Trading Advisors, but omits the category of Futures Trader

**Recommendation** Section 2 01 should cover the application for licensing as a Futures Trader and the instructions to Form 1 should be tailored to elicit relevant information needed by Bappebti to determine whether this license should be granted to an applicant In view of the fluctuation of the rupiah, the section should be revised so that the application fee can be set in accordance with a schedule established from time to time by the Chairman of Bappebti

*Section 2 02* Under this section, a Futures Broker application is to be accompanied by an audited financial statement not more than a year from the date of the application date and an unaudited statement for an interim period preceding the application date The financials must show compliance with net capital standards This approach is not consistent with Article 39(1)(d) of the proposed Government Regulation that requires an application to be accompanied by an audited balance sheet prepared no earlier than one month before the application is submitted

**Recommendation** This section should be conformed to the Government Regulation with respect to the financial statement called for Further, in conjunction with submission of the financial statement, this section should direct the applicant fill out a schedule reflecting the computation of adjusted net capital, showing non-allowed assets and the haircuts taken, in accord with Bappebti’s net capital requirements

*Section 2 04* Section 2 04 contemplates that, once a license is granted to conduct business as a market professional, the licensee continues to be licensed in that capacity absent revocation or withdrawal While a continuous licensing regime of this type is particularly valuable when dealing with a large number of licensees, Article 83(2) of the proposed Government Regulation has opted for the renewal of licenses every two

years. Given the relatively small number of licenses that are expected to be involved, this approach appears administratively feasible and will probably be beneficial in that Bappebti will be compelled to review a licensee's qualifications at the time of renewal.

**Recommendation** This section should be revised to conform to the two-year renewal requirement in the proposed Government Regulation.

*Section 2 06* This section prohibits any Futures Broker, Pool Operator and Trading Advisor from employing an unlicensed "Associated Person" or "Principal." Although this provision is critical as it imposes a responsibility on futures businesses to retain only those individuals who Bappebti has found qualified, the quoted terms are not defined in the Law or ministerial regulation. Both the Law and the proposed Government Regulation use the term "Representative" to refer to an individual associated with a Futures Broker, Pool Operator or Trading Advisor. In connection with Article 56 of the proposed Government Regulation, the Project Team has recommended that the concept of "Representative" be defined to encompass all individuals associated with a firm other than those acting in a clerical or administrative capacity. Under that definition, principals, who are persons deemed to control or supervise personnel at a firm, would be subject to licensing.

**Recommendation** References to Associated Persons and Principals should be deleted from this section and replaced by the term "Representative." Since these same terms are used in the remaining sections in Chapter 2 and in a number of sections in Chapter 3, a substitution of terms should be likewise made in these sections as well.

### Chapter 3 (Futures Brokers)

*Section 3 01* This section allows a Futures Broker to cross orders it has in hand from different customers at the market price where the orders could not be filled competitively on the market if the transaction is subsequently recorded and reported to the Exchange. Article 57(2)(b) of the Law, however, appears to forbid such a practice. Moreover, it is the Project Team's conviction that cross trades should not be permitted in an electronic trading environment. All orders without exception should be entered into the system. Since they will be logged sequentially according to time and price, orders will be fully transparent and those capable of execution will be automatically executed.

**Recommendation** An amendment should be made to this section prohibiting cross trades.

*Section 3 04* Under this section, prior to opening an account, a Futures Broker must deliver a Risk Disclosure Statement ("RDS") to the customer and obtain from the customer a signed and dated acknowledgement that the customer has received and understood the document. The content of the RDS is set out in Appendix A to the Rules, and is a form that deals with futures and options trading involving both domestic and foreign transactions.

Since Article 104 of the proposed Government Regulation already requires delivery and acknowledgement of an RDS, this section is redundant except insofar as it prescribes the content of the RDS to be delivered. Also, it is believed that the RDS form is unduly complicated by references to foreign markets and “off exchange” trading. Under the Law and proposed Government Regulation, no domestic futures and options trading can occur except on the IFE. In addition, foreign futures and options transactions are restricted only to foreign exchanges designated by Bappebti and may be offered only through Futures Brokers approved by the Chairman. Thus, an explanation of these other markets to customers interested in trading on the IFE appears irrelevant and distracts from an understanding of the risks the customer will encounter. Paragraph 2 of the RDS also leaves the impression that stop loss or stop limit orders may be available for trading on the Exchange. This is incorrect. The electronic trading system to be employed by IFE permits only limit, ‘fill or kill’ or orders accepting a bid or offer in the system to be entered. See IFE Rule 510.

### **Recommendation**

- A Language duplicative of Article 104 should be deleted
- B Consideration should be given to eliminating paragraphs 8, 9 and 12 from the RDS, which deal with foreign and off-exchange markets. Instead, the RDS should focus specifically on the risks of trading on the electronic market provided by IFE. A separate disclosure document geared to foreign trading could be provided only to those customers who seek to trade on exchanges outside Indonesia through Futures Brokers approved by Bappebti to handle such business.
- C Paragraph 3 of the RDS, addressing options risks, should add a point that, under Article 14(3) of the Law, a person who writes or grants options must secure a permit from Bappebti to do so. Moreover, in place of the discussion of partial payments of option premiums, a statement should be included indicating exactly how premiums are to be paid with respect to options to be traded on IFE.
- D Paragraph 2 of the RDS should be revised to state that stop loss and stop limit orders are unavailable for trading on IFE.

*Section 3 06* This section obligates a Futures Broker to collect margin on a gross basis for an omnibus account it carries for another Futures Broker or a foreign broker. While this is unobjectionable with regard to a foreign broker seeking to do business on the IFE, Section 3 06 is not consistent with Article 103(1) of the proposed Government Regulation, which proscribes one Futures Broker from having an account with another Futures broker. A principal purpose for having omnibus accounts is to enable a so-called introducing broker (“IB), who does not handle customer funds but only solicits and accepts orders, to have an arrangement with a member firm, which holds funds of the IB’s customers and enters their orders for execution. Since under the Law all Futures Brokers in Indonesia must be members of the IFE, introducing brokers are

presumably not authorized to operate and there appears no need at this early stage of the market's development to create a community of IBs to foster competition

Another concern is that neither Section 3 06 nor any other section in Chapter 3 addresses the amount of margin that is to be maintained for accounts and how it is set Article 51 of the Law and Article 105 of the proposed Government Regulation only go so far as to obligate the Futures Broker to collect margin from customers on trades and to forbid a Futures Broker from accepting an order without adequate margin

### **Recommendation**

- A Section 3 06 should be revised to conform to Article 103 of the proposed Government Regulation
- B There should be added to this section a paragraph providing that the Chairman of Bappebti shall issue a schedule from time to time setting minimum initial, maintenance (i.e. variation) and spread margins for futures contracts traded on the IFE after consultation with the directors of the IFE It should be made clear that the IFE and each Futures Broker are free to impose higher margins for all accounts carried or for certain accounts if such levels are believed appropriate by the Exchange or the Broker for its financial integrity

*Sections 3 07 & 3 10* Pursuant to these sections, a Futures Broker and its affiliates are prohibited from trading ahead of a customer's order Under this standard, a customer order that is executable at or near the market price must be entered before a similar order for a proprietary or affiliated account Representatives of Futures Brokers may not open accounts at other Futures Brokers to evade this requirement Moreover, an affiliated person of a Futures Broker cannot maintain an account at another Futures Broker unless the Broker with which he is affiliated consents and receives the affiliate's account statements on a regular basis from the Broker carrying the account

These limitations are sound deterrents against overreaching of customers However, there is a lack of clarity and consistency in the manner of their operation One problem is that the sections utilize the concept of "Affiliated Person" without indicating the meaning of that term Thus, it is unclear exactly which persons are subject to the rules Also, under Article 103(2) of the proposed Government Regulation, employees of a Futures Broker and their spouses may not have accounts to trade futures other than with the employing Broker No accommodation appears to have been made in the Bappebti Rules for this absolute bar

### **Recommendation**

- A Sections 3 07 and 3 10 should be revised to include a definition of "Affiliated Person " It is suggested that an Affiliated Person be described as a party who has an affiliation of the kind that is defined in Article 1, clause 9, of the Law

- B Section 3 10 should be revised to provide that Affiliated Persons who are Representatives or the spouses of Representatives of a Futures Broker are prohibited from maintaining accounts at another firm

*Section 3 14* Pursuant to Article 100 of the proposed Government Regulation, a Futures Broker is required to maintain adjusted net capital in an amount stipulated by Bappebti's Chairman To implement this requirement, a definition of net capital for this purpose must be provided In addition, guidelines need to be developed which identify the assets and liabilities of the Futures Broker that are to be included in and excluded from the calculation of adjusted net capital and the adjustments to the values of particular assets and liabilities that are to be considered Accepted international practice is to express adjusted net capital in terms of the greater of a fixed monetary amount or a percentage of customer-segregated funds with net capital meaning current assets less liabilities Restrictions are customarily imposed on withdrawals of equity contributions and repayment of subordinated loans that capitalize the Futures Broker

**Recommendation** A new Section 3 14 should be added to the Bappebti Rules to address net capital requirements For the basic standard, Rule 602 of the IFE's Rules can be used as a satisfactory model The new provision should indicate that the requirement is a minimum and that the Exchange and the Clearing House are authorized to set higher standards for their members if deemed appropriate With regard to the methodology of the calculation, the Project Team believes that that Section 3 14 should be patterned in a number of respect after Rule 1 17 of the U S Commodity Futures Trading Commission Although complex and containing a number of references that are inapposite to the Indonesian context, many of the provisions dealing with allowable assets, excludable liabilities, discounts on valuations and restrictions on capital withdrawals are pertinent and can be readily extracted for use in the Bappebti Rules It is suggested that Bappebti officials confer with the Project Team's legal consultants on the formulation of an acceptable rule

*Section 3 15* Bappebti is authorized by Article 6, clause M, of the Law to compel market professionals to correct or cease distributing misleading advertising In order to enable Bappebti to exercise its oversight of advertising activities, market professionals should be proscribed from disseminating marketing letters and other advertising that is untrue or misleading At the same time, Bappebti should be in a position to examine advertising materials prior to their use so it can prevent incorrect information from reaching members of the public

**Recommendation** A new Section 3 15 should be added to Chapter 3 to provide the following

- A Prohibit a Futures Broker from distributing inaccurate advertising materials Representations of individual examples of trading success or assurances of profit would be deemed false advertising
- B Require the Futures Broker to submit for review by Bappebti at least 10 days prior to use copies of any advertising materials

- C Require the Futures Broker to correct any advertising as directed by Bappebti or to refrain from its dissemination
- D Similar sections should be incorporated into Chapter 5 dealing with Pool Operators and Trading Advisors

#### Chapter 4 (Exchanges and Clearing Houses)

*Section 4 01* This section requires that the Exchange and Clearing House keep records of trades containing specified information about the transaction. Included is the identity of the buying or selling floor broker. Since there are no floor brokers associated with an electronic exchange, this reference is unnecessary. Moreover, it appears that Article 86 of the proposed Government Regulation contains a similar trade-recording obligation except that Section 4 01 also requires recording of information on transactions in the underlying commodity as well, such as in the case of a delivery.

**Recommendation** Consideration should be given to eliminating Section 4 01 as duplicative if Article 86 can be modified to include a reference to trade records for transactions in underlying commodities. Alternatively, Section 4 01 should be harmonized with Article 86 by use of similar terminology and the reference to floor brokers should be deleted.

*Sections 4 01 & 4 03* Under these two sections the Exchange is to maintain a price/change register and have procedures to record the time each of the steps involved in the execution of a transaction on the Exchange occurs. Since IFE will be employing an electronic system, the capability exists for a complete audit trail of a transaction to be created. Thus, any rule dealing with this matter should require the Exchange to generate and maintain records identifying the exact time orders are entered, executed or cancelled in the system. Members using handwritten office order tickets to take a customer order that is to be logged into the trading terminal should be required by Exchange rule to time-stamp the order within one minute of its receipt. Finally, the system should enable the Exchange to generate a detailed "price/trade" register as opposed to only a "price/change" register. The former offers substantially more information on the sequence and profile of trades occurring on the Exchange during the trading day.

**Recommendation** Sections 4 01 and 4 03 should be modified as discussed above to impose requirements on the Exchanger that are consonant with the computerized configuration of the trading system.

*Section 4 05* In this section, the Exchange is directed to set speculative position limits for contracts traded on the IFE and levels at which traders are to report their positions in the market. While this is unobjectionable, the section as drafted does not recognize that, pursuant to Article 58 of the Law, the limits on the number of contracts a speculator may hold is to be fixed by Bappebti. Likewise, Bappebti is the body that establishes reporting levels for traders, although the reports are channeled through the Exchange.

See Article 59 A further concern is that there is no explanation in the Rules of what constitutes a speculative as compared to a hedging position

### **Recommendation**

- A Section 4 05 should be amended to expressly state that the Chairman of Bappebti shall from time to time set speculative position and large trader reporting limits for contracts and that these limits will become effective on a specified date following notice to the Exchange and official public announcement
- B The section should also indicate that any speculative limits that the Exchange establishes in its rules will at a minimum be that prescribed by Bappebti's Chairman Similarly, any Exchange rule dealing with large trader reporting would need to set the level at which such reporting is triggered at no higher than that fixed by Bappebti
- C There should be incorporated a definition of bona fide hedging for the purpose of distinguishing such trading activity from speculative transactions subject to the position and reporting limits of this rule It is suggested that the definition of bona fide hedging in the IFE Rules is satisfactory for this purpose and should be placed into Section 4 05 A caveat should be added to the effect that, although a position may fit this definition, it will still be categorized as a speculative position unless the trader notifies the Exchange that it is a hedger in accordance with IFE Rule 625

*Section 4 06* This section mandates the Exchange to adopt rules for minimum financial and reporting requirement of members Here again, there is a need to make clear that any rules that the Exchange chooses to adopt must set a standard that is no less stringent than a particular requirement imposed by Bappebti directly on a market professional or participant

**Recommendation** This section should be amended to provide that any standards that have been adopted by Bappebti are the minimum that can be prescribed by Exchange rules in this area In particular a reference should be made to the minimum adjusted net capital for Futures Brokers in new Section 3 14

### *Chapter 5 (Pool Operators and Trading Advisors)*

*Sections 5 01 & 5 02* These sections deal with recordkeeping requirements for trading advisors and pool operators It appears that the records to be kept under these provisions are essentially the same as those called for under Articles 95(1), 96 and 97 of the proposed Government Regulation

**Recommendation** To avoid the possibility of misapprehension as to which set of rules are controlling, Sections 5 01 and 5 02 should be removed or alternatively, the cited Articles should be recast to delete itemization to particular records and refer to the Bappebti Rules as delineating the records to be maintained

*Section 5 03* This sections details the frequency and content of financial and other reports to be provided by a Pool Operator to pool participants. It implements the provisions of Articles 95(2) and 95(3) of the proposed Government Regulation and offers a comprehensive mechanism for dissemination of information regarding the ongoing operations and performance of the futures pool. Subsection (e), however, leaves open the time period to be covered by the reports by suggesting that, depending on the size of the pool, the Pool Operator would report to clients either monthly or quarterly. This size distinction is not recognized in the proposed Government Regulation in that Article 95(2) states that financial reports must be submitted to clients within 30 days after the end of each month.

It is the Project Team's opinion that monthly reporting, even for those pools with a modest amount of assets, will serve to deter potential abuses that would seriously undermine the integrity of the market at the initial stages of its development. Bappebti should be able to police these reports effectively since it is unlikely that many pools will be established at least at the outset.

**Recommendation** Subsection (e) of this section should be revised to require that the profit and loss statement and change of net asset report called for by Section 5 03 be provided to clients for each monthly period.

*Section 5 04* Under Article 110 of the proposed Government Regulation, it is a violation for a Pool Operator to solicit and accept funds for a pool unless the Pool Operator provides to the prospective clients pertinent information about the experience and qualifications of the Pool Operator, the planned operations of the pool, and the risks associated with futures trading. Bappebti is conferred with the authority to prescribe the form and content of the disclosure documents to be employed. In turn, Section 5 04 operates to implement Article 110 by outlining the information to be contained in a prospectus that is to be delivered to clients prior to receipt by the Pool Operator of funds for the pool.

For the most part the description of the disclosures that are to be made in the prospectus are acceptable. However certain omissions of information as well as one inconsistency were identified. With respect to the amending of the prospectus to keep it current, subsection (r) states that a Pool Operator may not use a disclosure document to solicit clients that is dated more than 9 months prior to its use. This is contrary to Article 110(2), which provides that a disclosure document is effective for a period of 6 months and must then be updated.

With regard to omitted information, although it is mentioned that a statement of risks should be included in the prospectus (see subsection (e)) there is no articulation of the types of risks that should be presented. The Project Team believes that, in addition to the inherent risks in commodity trading that are reflected in the RDS that is provided to customers of Futures Brokers, the special risks involved in an investment in a pool should be presented. For example, it should be explained that large net trading losses

would likely have a major negative impact on the net asset value of the pool and a participant's interest. Also proper for disclosure is that fact that, because of restrictions on redemption, a pool participant may be unable to withdraw from the pool to avoid incurring such losses. Furthermore, there is the risk that, due to the fees and expenses charged to the pool, a significant profit would need to be generated before the pool could break even and provide a return of initial investment.

Another area of deficiency is the absence of information on the business backgrounds of the principals of the Pool Operator and any Trading Advisor associated with managing the pool investments. There is also no summary of the contract governing the relationship with the custodian bank that is to hold the pool's funds or of the Futures Broker that is carrying the contracts acquired for the pool. In this regard, Articles 63 and 64 of the proposed Government Regulation require the contract with the custodian bank to be approved by Bappebti and to set forth the arrangements governing the rights of pool participants, fees and expenses, trading policy, redemption of interests, settlement of disputes and conditions for termination of the pool.

Other important information for consideration by a prospective client is the existence of pending litigation against the Pool Operator or other person associated with the pool and of the effect of taxation laws on distribution of pool profits. Section 5.04 does not provide for disclosures on these subjects.

#### **Recommendation**

- A Section 5.04 should be revised by modifying subsection (r) so that a Pool Operator prospectus must be updated within 6 months of its issuance,
- B Additional disclosures as discussed above should be itemized in this section for inclusion in the prospectus.

*Section 5.05* A Trading Advisor is prohibited under this section from accepting funds or property from a client for the purpose of purchasing and margining futures contracts (unless it is also a Futures Broker). This language is virtually identical to Article 109(1), which prohibits a Trading Advisor from collecting margin for a client's futures transactions. And Article 53(3) of the Law forbids acceptance of monies and commercial paper from a client. However, there is an exception in the Law for payments made to a Trading Advisor for rendering advisory services to the client. Although this exception is implicit in Section 5.05 in that it enjoins a Trading Advisor's receipt of funds only to purchase or margin a futures contract and not for compensation, there exists some lack of certainty in the operation of the section.

**Recommendation** Section 5.05 is redundant. Consideration should be given to eliminating it from the Rules. If it is retained, a clause should be added to allow Trading Advisors to accept client funds and property as compensation for services.

*Section 5.06* This section describes the information that is to be contained in a disclosure document that a Trading Advisor must deliver to a prospective client in

advance of entering into an agreement for advisory services. It operates to implement Article 109(2) of the proposed Government Regulation. That article requires that, in connection with the solicitation by a Trading Advisor, a prospective client is to receive information about the Trading Advisor's experience and qualifications and the risks involved in futures trading.

This section is sufficiently comprehensive to permit a prospective client to evaluate whether to enter into an agreement with a Trading Advisor. Nevertheless, as was the case with the prospectus for the Pool Operator, it would be of benefit if the disclosure document afforded notification of risks specifically arising from the advisory relationship. Among other things, there should be a warning that fees charged for managing or advising on an account could be substantial so that significant profits would need to be generated to avoid depletion of the assets in the account. The disclosure document should also contain language informing the prospective client that a Trading Advisor is forbidden from accepting funds from a client to trade futures contracts but that all funds should be placed directly with a Futures Broker.

The business background of the Trading Advisor and whether he is subject to pending litigation are material matters that should be included. Moreover, since under Article 109(5) of the Government Regulation, a Trading Advisor is not permitted to have discretionary authority over a client's account without the approval of Bappebti, the disclosure document should be required to state whether the Trading Advisor has been granted such approval and under what conditions.

With respect to disclosures regarding the Trading Advisor's past performance, a notice should be incorporated advising the prospective client that past performance is not necessarily indicative of future results and whether the Trading Advisor has previously directed trading in an account.

**Recommendation** The additional items of information discussed above should be identified in Section 5.06 for inclusion in the Trading Advisor disclosure document.

### Chapter 6 (Segregation)

*Section 6.01* This section provides that "Customer Funds" are to be segregated and separately accounted for. The quoted term, which is also used in succeeding sections of this Chapter, is not defined. To achieve the goal that commingling with the assets of a Futures Broker or Pool Operator does not occur, the concept of "Customer Funds" must cover not only monies but also securities and other property deposited by the customer or purchased with the customer's cash.

**Recommendation** The term "Customer Funds" should be defined to consist of cash, securities and other property held for a customer account.

### Chapter 9 (Bankruptcy)

This chapter and related appendices annexed to it outline extensive procedures for the conduct of business of an insolvent Futures Broker and the safeguarding, classification and distribution in kind and by way of liquidation of property held by such entity. These procedures are designed to operate within the framework of a general bankruptcy law of the type that exists in the U.S. In the second quarter of 1998, an interim bankruptcy law was enacted in Indonesia. A analysis of that law and a comparison between its provisions and Chapter 9 to determine whether the two schemes can be integrated with each other is beyond the scope of the Project Team's assignment. Specialized consulting expertise is required to evaluate what changes may be needed to harmonize the procedures in Chapter 9 with the Indonesian bankruptcy regime that is now in effect.

**Recommendation** Bappebti officials should undertake an evaluation of the procedures in Chapter 9 in the context of the Indonesian bankruptcy law with the assistance of a qualified expert in the area.

## CHAPTER FOUR

### Enforcement and Criminal Investigation

by

Thomas Goodbody

#### Enforcement

In 1997, Indonesia created the Commodity Futures Trading Law, Law No 32. The Law is to be administered by a new agency, to be known as Bappebti, within the Government of Indonesia's Ministry of Industry & Trade. As part of an overall regulatory scheme, the Law confers broad civil and criminal enforcement authority on Bappebti. This chapter accordingly covers enforcement matters and hearing procedures. It reflects a thorough review of the 1997 law, various draft regulations under that legislation, and the draft rules of the Indonesian Futures Exchange (IFE). Also contained are draft regulations and analysis of criminal investigative powers.

#### A Examinations Draft Regulations

Chapters IX and X of the Law set out Bappebti's law enforcement duties and powers. The Law envisions an administrative law enforcement program. Articles 66 - 67 of Chapter IX of the Law authorize Bappebti to conduct administrative investigations ("examinations"), implemented through a Government Regulation. Under Article 69, Bappebti is empowered to impose an array of administrative remedies against persons or organizations licensed by it which violate the Law or any implementing regulations.

The draft regulations accompanying this chapter are intended to allow Bappebti to conduct broad-ranging examinations while protecting the rights of the examinations' subjects and the integrity of the process itself. The draft is the result of extensive consultation with ICEB staff, and reflects their concern that the agency's examination powers be clear, flexible, and be administered fairly, while minimizing the opportunities for corruption or manipulation of the process. The draft also draws and expands on regulations developed by the BAPEPAM (the Indonesian SEC).

A major challenge facing Bappebti is the creation of an enforcement process that is, and appears to be, fair. The Law, to an American lawyer, conspicuously lacks "due process" protections, there is simply no hearing mechanism for enforcement matters in the Law. Yet virtually every person interviewed -- in and out of government -- stressed the importance of being "fair" in enforcement matters. For this reason, a mechanism that enables the subjects of enforcement activities to have a chance to defend themselves meaningfully is critical, particularly given the perception of many Indonesians that the government has historically been arbitrary and has favored the wealthy and well-connected. The draft regulations attempt to address this concern, both in the initial information-gathering ("examination") stage, and in the decision-making stages that follow.

Any enforcement program must have the authority on its own to conduct initial, informal inquiries into possible violations of the Law or implementing regulations, and for that reason the draft regulations allow the Bureau of Enforcement to conduct "informal inquiries" without the prior approval of the Chairman. The regulations contemplate that Bappebti's enforcement activities will be conducted under the general supervision of the Bureau, but that the Bureau may use other agency staff when necessary.

Even if Bappebti the Enforcement Bureau believes there is sufficient reason to invoke the agency's examination powers, the regulations require the approval of the Chairman to initiate an examination under Article 66. Article 66 confers substantial authority on Bappebti, and the approval of the Chairman is an important check to ensure that these powers are used appropriately, and that the resources of the agency are properly deployed.

Under the draft regulations, Bappebti initiates an examination by issuing a Letter of Assignment (Surat Tugas). This letter, which must be signed by the Chairman or his designee, notifies the subject of the examination of the reason for the inquiry and the subject's rights during the examination. The regulations provide that the staff's request for a Letter of Assignment must be reviewed by the agency's Bureau of Legal Counsel prior to its issuance. This review serves as a checkpoint to ensure that the Law and regulations are being applied appropriately and consistently and that the actions alleged by the Enforcement staff may in fact constitute violations of the Law or regulations. At this stage of an inquiry, however, the staff should have wide latitude to investigate possible violations, and the Legal Counsel's review should take this latitude into consideration.

The regulations do not require the Surat Tugas to give a detailed recitation of the suspected violations -- since after all the purpose of the examination is to find out the details -- but should give the subject general notice of the reasons for the examination. For example, the Letter might state that the examination is for the purpose of determining whether there has been a manipulation of a particular futures contract under Article 57(1) of the Law. Thus, the Letter is not intended to be a general warrant giving the staff unfettered latitude, but is expressly intended to limit its authority to the general subject matter specified. If additional authority proves necessary, the draft regulations provide that the staff can ask the Chairman to amend the Letter.

**Article 4** Article 4 of the regulations governs the conduct of an examination. At the suggestion of ICEB staff, the regulations try to protect the examiners from subsequent allegations of undue pressure or corruption by requiring that two or more officers be present at all on-site examinations. (For the same reason, Article 3F(b)(5) of the regulations require that the Surat Tugas to explain that only Bappebti, and *not* the examination staff, can resolve any dispute.) The regulation allows Bappebti to conduct examinations both on the examinee's business premises (with due regard for the examinee's on-going business) and off-site. It allows staff to review and copy examinee's books and records, and in extraordinary circumstances take temporary custody of such books and records. It allows staff to take witness statements (although

it does not require witnesses to give statements) For the protection of examination subjects, and to protect the integrity of the examination process, it gives affected parties the right to examine and dispute in writing the accuracy of all such statements, and requires that these disputes be included in the record of the exam

In all enforcement regimes, it is common for the subjects of an inquiry to complain about the fairness of the process, and sometimes to try to go over the heads of the investigators in an effort to short-circuit the inquiry Most times, these complaints are an effort to disrupt the inquiry, but occasionally have merit Because actual fairness, and the perception of fairness, are both critically important, Article 4J allows the examination subject or its representative to communicate with Bappebti's Chairman about any matter relating to the examination during the examination Such communications must be in writing, however, with copies of the communication to the staff This provision gives subjects an avenue to communicate with the Chairman, while at the same time preventing *ex parte* communications that exclude the staff This procedure should help preserve the integrity of the examination process by deterring efforts to manipulate it, while still giving the subject a way to raise matters of legitimate concern

**Article 5** Article 5 of the draft regulations provides for the confidentiality of on-going examinations, Bappebti except in extraordinary circumstances This is because examinations are inquiries into possible, not proven, violations of the Law and implementing regulations Premature disclosure of even the existence of an examination might unfairly damage the reputations of an examinee

**Article 6** Article 6 of the draft governs the Report of Examination The report is the key document in an examination, since it forms the basis for Bappebti decisions on enforcement matters The regulations thus require the officers responsible for the exam to prepare a written report that, at a minimum, includes

- ◆ A brief summary of the reasons for the examination and the results,
- ◆ A conclusion about whether any Law or regulation has been violated, including the legal and evidentiary basis for that conclusion,
- ◆ A discussion of the seriousness and public impact of any violation,
- ◆ Recommendations regarding administrative sanctions (if any) under Article 69 of the Law,
- ◆ Recommendations (if any) for further action (such as a criminal investigation or referral to another agency or the exchange)

The regulation next requires review and approval of the Report by the Head of the Bureau Then, the examinee, or any other person or organization for whom the Report recommends sanctions or other action, may review the Report, and if it agrees with it, sign If the examinee or other person disagrees with the Report, it may submit a separate written statement, with supporting documentation, to the agency If, after review, the Head of the Bureau deems it appropriate to proceed, the entire record (including the examinee's statement), together with a recommendation for action, will be forwarded to the Chairman

Article 6F of the draft regulations requires the agency's Legal Counsel to review all Reports and staff recommendations prior to any action by Bappebti. Legal review at this point in the process is important to ensure the legal and evidentiary sufficiency of any findings of violation in the Report and the appropriateness of any recommended sanctions, and to ensure that agency policy is appropriately and consistently applied. This second set of eyes makes it more likely that Bappebti's ultimate action will be fair and in the public interest. Until Bappebti develops its own legal expertise, it may wish to outsource legal review to private attorneys. Review is important because in the long run fairness and consistency help any enforcement program develop the credibility and legitimacy that makes it an effective instrument of public policy.

**Article 7** At this stage, the administrative record should be fully developed. Thus, Article 7 of the regulations allow Bappebti to impose sanctions after review of the Report. Any final action of the agency imposing sanctions shall be in the form of a written order signed by the Chairman and served on the parties subject to the order. The Order must specify the sanctions imposed or actions ordered, and explain the basis for its directives. This requirement forces Bappebti to articulate the basis for its action, informs the parties and the public of that basis. In turn, this supports the perception that Bappebti actions are fair and legitimate. The requirement of a written order also ensures that under the law Bappebti's action will be reviewable by the Civil Administrative Court.

While the draft regulations do not include a trial-type hearing procedure, Article 7D does allow the Chairman, upon request of the subject of an examination, to meet face-to-face with the subject or his representative to hear why sanctions should be mitigated or not imposed. Whether to allow this meeting is a matter left to the sole discretion of the Chairman, but it is expected that in most cases written statements under Article 6D will be sufficient. The Chairman has the discretion to hear from other persons in addition to the subject, a flexibility that is important when a decision involves an assessment of the credibility of contending points of view. The regulation requires that the examiners, the Head of the Enforcement Bureau, and the Bureau of Legal Counsel will attend any such meeting, both so all viewpoints will be represented at the meeting, and so the staff can help the Chairman evaluate the subject's presentation in making the final agency decision.

**Article 8** In mature enforcement programs, most matters are settled. There are a number of reasons for this, including the fact that regulatory agencies usually lack the resources to contest every matter, that few regulated persons wish to engage in protracted battle with their regulator, and that contested cases do not consistently yield sufficiently better results for either party to make a fight worthwhile. In Indonesia, the culture also encourages the conciliation of disputes. Article 8 of the draft regulations accordingly permit settlement of enforcement matters, through what the regulations call "Agreed Resolutions." Agreed Resolutions may be entered into at any time during the examination process, but are generally most appropriate after the staff has had a chance to investigate and assess the seriousness of any violations. The regulations allow the subject of an examination to request a meeting with the head of the

Enforcement Bureau, and -- prior to the imposition of administrative sanctions -- to submit written offers to resolve a dispute to Bappebti without waiving its right to contest the matter should the offer be rejected. Similarly, Article 8C provides that the examinee may submit a written settlement offer directly to the Chairman, but only after the completion of the Report of Examination. Thus, an examinee can bring an offer to settle before the Chairman even if it has been unable to reach agreement with Bappebti staff. The regulation provides that copies be provided to the Enforcement Bureau, and that the Head of the Bureau advise the Chairman of its views on the offer.

Article 8D requires that any offer to enter into an Agreed Resolution be reviewed by the agency's Bureau of Legal Counsel prior to any decision to accept or reject the offer. As with contested sanctions, this review helps ensure that Bappebti's actions will be legally sufficient and that agency policy is appropriately and consistently applied.

These structural paths to resolution should not be considered exclusive, as ICEB staff stressed during field work, settlements are desirable and should be encouraged at any reasonable point in the process.

### **Criminal Provisions**

The Law also contains criminal provisions. Part Two of Chapter X (Articles 71 - 76) make various violations of the Law either "violations" (which are less serious) or "crimes." Both have statutorily prescribed prison terms and/or fines. Article 68 gives designated Bappebti officials the authority to conduct criminal inquiries ("investigations") concerning futures activity. As in most regulatory regimes, criminal sanctions may be imposed in addition to administrative ones under the Law. For that reason, Article 9 of the draft regulations provides that Bappebti staff may initiate an investigation even after the conclusion of an examination.

### **Conclusion**

In summary, the draft regulations on examinations are an initial procedural roadmap. Their purpose is to describe Bappebti's investigative jurisdiction and powers, to ensure that examinations are duly authorized by the agency on the basis of legitimate information, to provide notice to the subjects of the nature of the examination and the subject's rights, and to provide guidance on the conduct and confidentiality of examinations. The draft also describes how Bappebti staff should report the results of examinations, and establishes a mechanism to settle disputes and impose agreed-upon sanctions when appropriate. In other words, the draft tries to establish a balance that protects the integrity of the enforcement process, gives due regard to the rights of examination subjects, while maintaining the flexibility and informality that any investigative process needs.

## *B The Opportunity to be Heard*

This Chapter does recommend a trial-type hearing procedure. In Indonesia there is no administrative procedures law or tradition involving a neutral fact-finder on which to model a culturally familiar process. Instead, a person faced with administrative sanctions is, if lucky, afforded a chance to meet with the staff of an agency to try to convince it not to take adverse action. For example, the head of enforcement at BAPEPAM explained that a target of a BAPEPAM investigation has the opportunity to meet with agency staff at several stages in an investigation, and at each stage gets to explain its side of the story. At each stage, he said, the agency assesses the evidence against the target, considers defenses, and evaluates possible sanctions. Only after this iterative process is complete is a recommendation for sanctions made to BAPEPAM's Chairman. After BAPEPAM imposes sanctions, an aggrieved party can appeal to the Civil Administrative Court, but that court's jurisdiction is appellate and hence its factual review is limited.

BAPEPAM considers these procedures fair -- and they may be -- and Bappebti officials agreed that similar procedures would allow the subjects of examinations to be heard fairly. In fact, the government officials interviewed valued highly the flexibility that this informality allows, even though they were simultaneously leery of the arbitrariness that it can permit. These officials understood that while this informality may work well in most instances, it also raises the possibility of the perception of unintentional inconsistencies or, worse, actual administrative arbitrariness. They understood that even a perception of unfairness can undermine the credibility and legitimacy of any law enforcement process.

BAPEPAM's informal procedures are nowhere enshrined in the agency's enabling law or its regulations, and instead seemingly depend on unwritten norms and the good will of the officials administering them. This is a deficiency that the draft Bappebti regulations avoid by incorporating this process into the regulations themselves. While the regulations apply to administrative enforcement proceedings, they could be adapted to the license application process as well. This chapter strongly recommends that whatever form the regulations ultimately take, they should formally give the subject of an enforcement inquiry (or license applicant) the opportunity to present its position to Bappebti prior to the imposition of sanctions or denial of a registration. The draft regulations build in several opportunities for these "hearings." In this way, Bappebti can become a leader in enhancing the credibility to the administrative regulatory process in Indonesia.

## *C Sanctions*

ICEB staff has no experience with either regulatory enforcement or criminal law enforcement. As a result, they are rightly concerned about how to determine when administrative sanctions are warranted, how to decide what sanctions are appropriate, and when to consider criminal action.

These determinations are never easy, even for experienced administrators operating in highly-evolved regulatory systems. How to measure what is an appropriate sanction in the case of a particular violation of the Law or underlying regulations, and how that sanction fits into an overall regulatory scheme, is an extraordinarily difficult challenge facing any new administrative agency. At Bappebti, the evolution of the judgment and experience that encourages good decisions in this area will have to develop over time.

Bappebti will, of course, have to start somewhere, and consider the three traditional purposes for regulatory sanctions when contemplating enforcement remedies. These are

- ◆ To punish wrongdoers,
- ◆ To deter others in the industry from engaging in illegal practices,
- ◆ To articulate and prescribe agency policy

Civil enforcement activity therefore serves not only a traditional law enforcement role, but also is an important tool of public policy by which the agency can announce what practices are illegal, and how seriously it views that illegality. The relation of administrative remedy to agency policy is traditionally viewed as a matter peculiarly within the agency's expertise, but is a concept with which ICEB personnel have little experience.

The Law gives Bappebti the authority to make considered judgments in enforcement matters. Article 69 allows Bappebti to impose a wide and flexible range of administrative sanctions, from written warnings to license revocation, on registrants who violate the Law or the implementing regulations. For example, the provision that allows Bappebti to issue a sanction "in the form of restriction of business activities" appears to permit the agency to issue orders similar to cease-and-desist orders, and to prohibit a licensee from particular activities for certain periods of time. At the same time, it does not require the imposition of a particular sanction in every case. This flexibility gives Bappebti the opportunity to adjust any sanctions to fit the circumstances of each case. But because the Law does not set any standards, it also raises the possibility that sanctions be applied arbitrarily.

There was discussion with ICEB staff about the wisdom of publishing a schedule of fines and sanctions to address this lack of standards. In fact, Chapter XII of draft ICEB regulations would try to establish a finely calibrated set of sanctions for particular violations, a regime that attracted ICEB staff because of its predictability and resistance to manipulation.

This Chapter, however, urges Bappebti to avoid a rigid schedule for several reasons. First, the gradation of administrative remedies in the Law plainly contemplates that Bappebti administer sanctions commensurate with the misconduct demonstrated.<sup>1</sup> Second, the agency has no experience with an enforcement program, and propriety and utility of any particular level of sanctions will, at this point, be simply a guess. Third,

---

<sup>1</sup> In contrast, the criminal sanctions in Articles 71-76 carefully limit the fines and prison terms that can be imposed.

there is the danger that the political nature of the regulation process will produce a schedule of sanctions that are either so harsh that the agency will be reluctant to apply them in particular cases, or will be set so low that they become an acceptable risk for registrants to run -- a "cost of doing business" Fourth, the establishment of a realistic schedule of fines is difficult in Indonesia's current economic climate, and so may become quickly outdated yet difficult to adjust in the future

This does not mean that Bappebti should operate in an entirely standardless fashion Article 7B sets forth a non-exhaustive list of factors that the agency should consider when imposing sanctions Bappebti may also wish to publish a schedule, or range, of intended sanctions (including monetary sanctions) for certain routine matters, such as late filings, while leaving itself more freedom in more serious cases

In addition, Bappebti should consider publishing a statement of its intended policy with respect to sanctions, describing, for example, how the factors set forth in Article 7B will be applied when issuing sanctions The considerations that enter into decisions about whether "the punishment fits the crime" include

- ◆ Seriousness of the violation Is the violation "technical" or does it involve fraud or other dishonesty?
- ◆ Was the conduct willful or unintentional? Was it a mistake?
- ◆ Is the violation pervasive in the industry or does the agency wish to make an important regulatory point (so that stringent sanctions may send a "signal" to the industry)?
- ◆ Is the violator an individual or a company? If an individual, did the organization "approve" of the misconduct? Does it reflect inexperience or lack of supervision?
- ◆ Is the violation a first-time or repeat violation? It may be appropriate to impose lighter sanctions if the law or regulation does not clearly spell out the violation Repeat violators should be dealt with more severely,
- ◆ Are the rules clear or is the violation unclear or a matter of first impression? If the violation involves a "novel" interpretation of the law, it may be appropriate to impose lighter sanctions,
- ◆ Was market integrity damaged by the violation? Were members of the public hurt?
- ◆ How much money was lost? Has the violator compensated the victims of the violation?
- ◆ Are there mitigating or extenuating circumstances?

This list is not meant to be exhaustive

Relation of remedy to policy is a matter that should remain peculiarly within the province of Bappebti It is the agency the law has entrusted to develop the expertise necessary to judge what sanctions best serve its regulatory agenda and protect the integrity of the new Indonesian futures markets It must be recognized, however, that it will take time

for Bappebti to develop the experience and judgment that allow the nuanced application of the factors listed above in the context of the Indonesian markets and culture

#### D Relations with the Industry and other Agencies

The Law contemplates that any futures exchange will be a self-regulating organization. Thus, in addition to Bappebti, the IFE will have an enforcement function. Its draft rules establish an elaborate enforcement regime for the exchange and its members. For example, the IFE rules would allow the exchange to discipline its own members and to order liquidation of non-members positions in certain cases. Under the rules, a Business Conduct or Trade Practices Committee conduct hearings and impose sanctions based on a majority vote. In theory, then, the exchange will form the first line of defense against misconduct in the futures industry, with Bappebti providing backup, filling gaps, dealing with off-exchange matters, and prosecuting the most serious matters. In fact, one of the challenges Bappebti and the IFE will face is creating the appropriate division of enforcement functions, especially since in the early stages of the market's development there is not likely to be a great deal of enforcement work.

ICEB officials have a tendency to view enforcement as a kind of specialized police work. There is, as noted above, little understanding of regulatory enforcement in the ICEB or with enforcement activity as an instrument of public policy. For example, ICEB staff said that its current plans were to send ten of its employees to a three-month long training course as criminal investigators (PPNS), which would empower Bappebti investigators to conduct criminal inquiries. It seems unlikely that a nascent futures industry will spawn enough criminal activity to justify this allocation of resources, although the training may be useful in teaching investigative techniques. Thus, while Bappebti should maintain its working relationship with the Jakarta police, liaisons with other regulatory agencies are probably more important in the long run.

In fact, the Law expects inter-agency cooperation. Article 77 requires the Bank of Indonesia (BI) and BAPEPAM to coordinate and consult with Bappebti "in line with their respective functions in the monitoring and supervising of the activities under the scope of their respective authorities, related to activities in the field of Futures Trading." What this mandate means in practice is unclear. In interviews, BI officials did not see a regulatory overlap at this time, especially since banks cannot speculate and can only to hedge exchange-rate and interest-rate risk and are therefore unlikely entrants in the new Indonesian futures markets. Since Indonesian banks are apparently allowed to operate broker/dealer type subsidiaries, however, there may be some overlap in the future. A similar jurisdictional overlap with BAPEPAM is also possible.

Discussions between Bappebti and BI officials generated agreement that the two agencies should implement Article 77 through a Memorandum of Understanding delineating their respective responsibilities. Such an MOU could include a protocol to facilitate BI response to Bappebti information requests, blanket approval of access to the bank accounts of entities licensed by Bappebti as a condition of registration, so that Bappebti will not have to get separate BI cooperation in every examination, include a

review of any futures accounts in BI examination protocols, and the development of regular staff contacts between the two agencies

A similar regime should be developed between Bappebti and BAPEPAM. In fact, cooperation between the two agencies could be especially fruitful, given that BAPEPAM's enforcement function is evolving at the same time as Bappebti's. There is much "learning by doing" for both agencies to do, and a sharing of their respective experiences could be highly useful.

### **Recommendations**

An effective regulatory enforcement program is important to the development of the futures industry in Indonesia. Market participants must believe that the marketplace is honest and that the rules will be enforced. At the same time, industry participants must believe that enforcement actions are brought objectively, and that the process gives the subjects of examinations a fair opportunity to defend themselves. To that end:

- A Bappebti should adopt regulations which regularize the examination process, protect the integrity of that process, afford subjects of examinations the chance to be heard and submit information in their defense, and encourage the settlement of disputes and imposition of sanctions. In this way, the enforcement process will provide the fairness and objectivity that allows it to develop credibility and support the evolution of a respected futures industry in Indonesia.
- B In cases where violations of the Law and implementing regulations are shown, Bappebti should allow itself time to develop the experience and judgment to levy sanctions commensurate with the violation. While it may be desirable to publish a range of sanctions for "routine" violations of the Law and regulations, Bappebti should avoid the publication of rigid schedule of sanctions, since these are difficult to administer fairly and could become a "cost of doing business" for unscrupulous industry members.
- C Bappebti should attempt to develop working relationships with regard to enforcement matters with the IFE and other regulatory agencies. All parties can learn from such exchanges and evolve an appropriate division of responsibilities over time.

## **Regulation of Futures Markets Examinations**

### **Article 1**

#### **General Provisions, Purpose of Examinations**

- A These Regulations govern Bappebti's conduct of examinations under Article 66 of Law No 32 of 1997 (the "Law"), and are promulgated under the authority contained in Article 67 of the Law
- B An examination is an inquiry by Bappebti into whether there has been or not a violation of the Law or the regulations under the Law has occurred Under its examination authority, Bappebti gathers the information it needs to determine whether administrative sanctions under Article 69 of the Law should be imposed, whether a criminal investigation under Article 68 should be initiated, or both
- C Bappebti may conduct an examination whenever it receives information from any source that tends to show that a violation of the Law or the regulations has occurred or is about to occur The determination as to whether to conduct an examination under the Law is matter solely within Bappebti's discretion
- D Examinations are to be conducted by civil servants who are officers of Bappebti and have the legal authority to conduct examinations under Article 66

### **Article 2**

#### **Informal Inquiries**

- A An informal inquiry is a process by which an officer or officers of Bappebti gather information to ascertain whether there has been a possible violation of the Law or regulations or whether an examination under Article 66 or an Investigation under Article 68 is warranted
- B With the approval of the Head of the Bureau of Enforcement, any officer or officers of Bappebti may conduct an informal inquiry
- C Officers of Bappebti may obtain information regarding potential violations from any source, including other Bureaus of Bappebti, customer complaints, newspaper articles, any commodities exchange, review of promotional materials, interviews, and confidential tips
- D An informal inquiry does not require prior approval of the Chairman, but when conducting an informal inquiry, Bappebti officers do not have the powers granted to them under Article 66 (2) of the law

**Article 3**  
**Initiation of Examinations under Article 66, Letters of Assignment**

- A Examinations are official inquiries to determine whether any person may have violated, or is violating, the Law or regulations, and is conducted under the authority contained in Article 66 and in accordance with these regulations
- B Only officers of Bappebti authorized to do so under the law may conduct examinations, although the officers may assisted by other Bappebti staff
- C Any examination under Article 66 must be approved in advance by the Chairman of Bappebti (or his designee) by execution of a Letter of Assignment (Surat Tugas)
- D Any request from Bappebti staff for the issuance of a Letter of Assignment must be reviewed by the Bureau of Legal Counsel prior to execution of the Letter by the Chairman After review, the Bureau will advise the Chairman of its views as to whether the letter should be issued
- E The Chairman may issue the Letter based on information provided by Bappebti staff
- F Any documents or other information provided to the Chairman by Bappebti staff in connection with the Chairman's determination to issue a Letter of Assignment shall remain confidential and not be released to any person
- G Letter of Assignment
  - (i) The Letter of Assignment institutes a formal examination under Article 66 of the Law, and notifies the subject of the examination of the basis for the examination and the subject's rights during the examination
  - (ii) The Letter shall include
    - (a) The identity of the Bappebti officers authorized to conduct the examination and a brief statement of their authority under the Law,
    - (b) The identity of the organization and persons that are subject to the examination,
    - (c) A brief statement of the scope of the examination and the suspected violations of the Law or regulations giving rise to the examination,
    - (d) A brief statement explaining the examinee's right to refuse examination (Surat Pernyataan Menolak Pemeriksaan), together with a warning that the failure to submit to an examination of by a Bappebti registrant is itself grounds for sanctions under the Law,
    - (e) A statement that only Bappebti, and not the officers conducting the examination, has the authority to resolve the examination,
    - (f) A brief statement explaining the examinee's right to be represented by legal counsel during the examination,
    - (g) A statement explaining the examinee's right to review the results of the examination, to submit statement to Bappebti explaining, questioning, or

refuting results of the examination, and to request a meeting with Bappebti after the conclusion of the examination to seek resolve any issues raised by the examination

- (iii) Bappebti may, upon approval by the Chairman, amend the Letter as it deems appropriate

#### **Article 4**

#### **Conduct of the Examination**

- A All examinations shall be conducted by officers of Bappebti in a fair and honest manner,
- B Two or more Bappebti officers shall be assigned to each examination. When an examination is being conducted on an examinee's business premises, at least two Bappebti officers shall be present at all times,
- C The examination may be conducted from the examiners' offices, at the examinees' place of business, or any other place deemed necessary by the examining officers to determine whether a violation has occurred,
- D Except in extraordinary circumstances, or with the permission of the examinee, an examination on an examinee's business premises shall be conducted during normal business hours, with due regard for the examinee's continuing business. An examination may continue from day-to-day, in Bappebti's sole discretion,
- E Bappebti may gather information from any source it deems appropriate, including the exchange and any third parties with knowledge of the matters under examination,
- F Bappebti may examine or make copies of any books or records or other documents or things (including computer records) belonging to or under the control of the examinee, or that relate to the matter under examination and are in the possession or control of a party under Bappebti's jurisdiction,
- G Bappebti may take such other steps as it deems necessary to preserve the integrity of any books, records, or other documents or things (including computer records), including taking temporary possession (not to exceed three business days) of any documents or things. If Bappebti removes any records from the examination site, it shall provide the examinee with a receipt for such records,
- H In connection with an examination, Bappebti may take a statement from any person suspected, directly or indirectly, of any conduct in violation of the Law or regulations, including employees of the suspected party. Statements may be taken in written or recorded form. Statements taken in recorded form may subsequently be transcribed.

- I All persons subject to examination by Bappebti have the right to review the Letter of Assignment, the right to be represented by legal counsel at all times during the examination, and to review a copy of any written or recorded statement provided to Bappebti in the course of the examination. If any person disputes, in whole or in part, to the accuracy of that person's statement taken by Bappebti during an examination, that person may provide Bappebti with detailed written description of that person's disagreement with any portion of the statement, which description shall be included in the record of the examination.
- J During the course of an examination, the subject of the examination or its representative may communicate with the Chairman on any matter relating to the examination. Such communications must be in writing, with copies of such communication to the Bappebti staff conducting the examination and the Head of the Bureau of Enforcement.

### **Article 5 Confidentiality of the Examination**

- A Bappebti will ordinarily keep confidential the existence of any examination, and any information, documents, or things gathered in connection with an examination until the conclusion of the examination.
- B At the conclusion of the examination, Bappebti may, in its sole discretion, disclose the existence of an examination, and any information gathered in connection with that examination.
- C In extraordinary circumstances, Bappebti may disclose the existence of an on-going examination, but only if Bappebti finds that the public interest will be served by such disclosure.

### **Article 6 Report of Examination**

- A A written Report of Examination will be prepared at the conclusion of all examinations by the Bappebti officers with principal responsibility for conducting the examination.
- B The Report shall include, but not be limited to, the following information:
  - (i) A brief summary of the reasons for the examination and the results,
  - (ii) A conclusion as to whether any violations of the Law or regulations thereunder have been found, and the legal and evidentiary basis for that conclusion,
  - (iii) A discussion of the seriousness of the violation, taking into consideration the severity, monetary loss, public policy impact, adverse effect on the integrity of the marketplace, pervasiveness or repeated nature of any violations, the cooperation of the subject of the examination, and any other relevant factors,

- (iv) Recommendations for appropriate of remedial actions (if any), including any administrative sanctions under Article 69 of the Law,
  - (v) Recommendations, if any, for further action,
- C The Bappebti examiners shall submit a copy of the Report for review to the Head of the Bureau in which the examiners are employed
- D Upon approval by the Head of the Bureau, the examiners shall make a copy of the Report available to the examinee and any other person or organization that the Report recommends be subject to administrative sanctions or other action. If the examinee, or other person or organization, agrees with the Report, its duly authorized representative shall sign the Report. If the examinee (or other person or organization) disagrees, in whole or in part, with the conclusions of the Report, it may submit a separate written statement explaining the reasons for its disagreement, together with any supporting documentation. This statement should include any information that the submitter believes explains or mitigates its conduct. Any such statement shall be made part of the record of the examination.
- E After review by the examinee, the Head of the Bureau will, if he deems it appropriate, forward the Report and a summary of any objections by the examinee, to the Chairman of Bappebti, together with a recommendation for any action to be taken by Bappebti.
- F Bappebti's Bureau of Legal Counsel shall review all Reports and recommendations prior to any action by Bappebti, and shall separately advise the Chairman of its views on the Report and recommendations. The results of this review, and any recommendations, shall be provided to the Chairman.

#### **Article 7**

#### **Imposition of Sanctions**

- A With the approval of the Chairman, Bappebti may take such action, including the imposition of administrative sanctions as authorized by Article 69, as in its discretion it deems appropriate.
- B In connection with the imposition of administrative sanctions, Bappebti shall consider the facts and circumstances giving rise to the violation, including but not limited to the following factors:
- (i) The seriousness of the violation, and whether the violation involves fraud or other dishonesty,
  - (ii) The willfulness of the violation,
  - (iii) Any previous violations by the person or entity to be sanctioned,
  - (iv) The effect of the violation on the integrity of the futures market,
  - (v) The pervasiveness of the violation, and whether the violation was an isolated incident or reflects a pattern of misconduct,
  - (vi) The monetary loss attributable to the violation,

- (vii) Damage to the public,
- (viii) The deterrent effect of the sanctions,
- (ix) The public policy effect of the sanctions,
- (x) Any mitigating or extenuating circumstances

- C Any administrative sanction or other directive mandated by Bappebti shall be set forth in a written order signed by the Chairman or the Chairman's designee. The order shall specify any sanctions imposed or actions ordered, together with the reasons therefore, and shall be promptly served upon all parties subject to the order. All orders shall be made available to the public.
- D Prior to the imposition of sanctions, the subject of an examination may request a meeting with the Chairman of Bappebti to explain why, in the subject's view, sanctions should be mitigated or not be imposed. The Chairman, in his sole discretion, may agree to hear the subject of the investigation, and from such other persons as the Chairman determines appropriate. The examiners who prepared the report, the Head of the Bureau of Enforcement, and the Bureau of Legal Counsel will attend any such meeting.
- E Any final order issued by Bappebti may be appealed to the Civil Administrative Court in accordance with law and the rules of that Court.

### **Article 8 Agreed Resolutions**

- A At any time during the course of an informal inquiry or Examination, any person may agree to resolve a matter with Bappebti by entering into an Agreed Resolution, including an agreement to any administrative sanctions under Article 69 of the Law and such other actions as the person may agree with Bappebti to undertake.
- B After completion of the Report of Examination, and at such other times as the Head of the Bappebti Bureau conducting the examination shall allow, an examinee or its representative may request a meeting with the Head of the Bureau to discuss the Report and a possible Agreed Resolution to any violations identified in the Report. At that time, the Head of the Bureau may, in his discretion, recommend to the Chairman that an Agreed Resolution be entered into by Bappebti.
- C At any time prior to the issuance of sanctions under Article 69 of the Law, an examinee or its representative may submit a written offer to the Head of the Bureau to enter into an Agreed Resolution (including an agreement to administrative sanctions) to any violations specified by Bappebti staff or in the Report of Examination. The Head of the Bureau shall present any such offer to the Chairman, together with a recommendation as to whether Bappebti should accept the offer.

- D At any time after completion of the Report of Examination, an examinee or its representative may submit a written offer to enter into an Agreed Resolution directly to the Chairman, with a copy to the Head of the Bureau. The Head of the Bureau shall advise the Chairman of its recommendation as to whether Bappebti should accept the offer.
- E Any offer to enter into an Agreed Resolution shall be reviewed by the Bureau of Legal Counsel prior to Bappebti's decision to accept or reject the offer. The Bureau shall recommend to the Chairman whether the offer should be accepted or rejected.
- F A written offer of Agreed Resolution is solely for the purpose of resolving matters raised by an examination. Any statement of fact or law contained in an offer of Agreed Resolution shall not be deemed a waiver of any right, admission of any fact, or consent to sanctions by the examinee, and shall not be used by Bappebti in any manner against the examinee or any other person.

## **Article 9 Further Investigation**

- A If, in Bappebti's sole determination, information developed in the course of the examination indicates that criminal conduct may have occurred, Bappebti may initiate an Investigation under Article 68 of the Law.
- B An examination and an Investigation may proceed simultaneously, and may employ the same Bappebti personnel.

### *Criminal Investigative Powers*

In addition to administrative sanctions, the Commodity Futures Trading Law of 1997 makes certain futures-related conduct violations of criminal law. Under Articles 71-75 of the Law, criminal violations include certain unlicensed futures activity, manipulations and bucketing, failure to maintain properly segregated accounts, dealing in futures transactions without proper licenses from Bappebti, assisting violations of the Law, and impeding a Bappebti examination or investigation. The more serious of these activities are crimes, while the less serious are violations, which carry shorter prison sentences and have lower fines than crimes.

Article 68(1) allows certain Bappebti officials with special authorization to conduct criminal investigations of violations of the futures Law. These "Civil Servant Officials" must receive special training in criminal investigative techniques—taught by the police in a course that runs several months. After training, these officials are empowered under Article 68(2) to

- ◆ Receive reports of suspected criminal activity,
- ◆ Initiate (and terminate) investigations into suspected criminal activity,
- ◆ Interview witnesses,
- ◆ Examine the suspect's futures-related books and records,

- ◆ Inspect premises suspected of being the location at which the possible crime took place, and to “confiscate” possible evidence,
- ◆ Request a bank to freeze the accounts of a suspect,
- ◆ Obtain help from other experts or other law enforcement agencies (Article 68(6)), as necessary
- ◆ Under Article 68(3), Bappebti may request the Minister of Finance to obtain information from the suspect’s bank, “in accord with Banking law and regulations ”

Under Article 68(4), the agency must report the commencement of any criminal investigation to the police. Bappebti does not have the authority to prosecute crimes itself, but must—pursuant to Indonesia’s criminal laws—report its findings to the Attorney General through the police. Nevertheless, its investigative powers in the futures context are very broad and potentially serious for its targets.

These powers reside within what is principally a regulatory agency, charged with overseeing the new Indonesian futures industry. While it may be efficient to include criminal law enforcement powers within the duties of an expert agency (BAPEPAM has similar powers), Bappebti’s focus should be on regulatory activity, not criminal law enforcement. ICEB officials indicated to the project team that they intended to send about ten agency staff through the police training that is the prerequisite to exercising criminal investigative powers. This may be good training, but the number of staff seems large for a small agency. Bappebti should be careful not to overemphasize criminal investigations, or to criminalize activity which might better be dealt with administrative sanctions.

Because criminal matters are so serious, this report recommends that Bappebti adopt regulations governing criminal investigations that encourage such investigations only when truly appropriate. Thus, Article 2B of the draft regulations require that no criminal investigation be instituted without the Chairman’s written approval, and upon a determination that criminal conduct is reasonably suspected and that a criminal investigation is in the public interest. The regulations also require prior consultation from Bappebti’s Legal Counsel. As with examinations, this review is a checkpoint to ensure that the Law is being applied appropriately and consistently. The determination is also intended to focus the agency on the appropriateness of a criminal investigation as opposed to, or in addition to, administrative sanctions. If the futures-related conduct is sufficiently serious to merit criminal prosecution, administrative sanctions will almost always be merited.

Article 3 of the draft regulations govern the conduct of the investigation under Article 68. The regulations follow the powers granted Bappebti by Article 68(2) of the Law, and generally parallel Article 4 of the draft regulations on examinations. Article 3C of the draft requires that evidence gathered during a criminal investigation be maintained separately, to avoid chain of custody disputes and to protect the integrity of the investigation. The regulations also allows Bappebti to “confiscate” certain evidence, as the Law allows, but confiscation is a serious action and this power should be used very

sparingly and only when necessary. The regulations also allow Bappebti to return seized records not confiscated at the conclusion of an investigation. The agency can also return "confiscated" records.

Criminal investigations, even more than regulatory examinations, have the potential to do great damage to their target -- even if ultimately no prosecution results. For that reason, Article 4 of the draft regulations provides that criminal investigations will almost always remain confidential during its pendency or after its conclusion if no criminal prosecution eventuates. The regulations do allow Bappebti to disclose the existence of an investigation when it finds that to do so is in the public interest. Disclosure will ordinarily be in connection with highly publicized cases when to do so will confirm what is already public knowledge.

Article 5 governs resolution of the investigation. Article 68(5) of the Law provides that Bappebti will give its findings to the Police Investigator, who will in turn submit those findings to the public prosecutor. This does not involve an evaluation of prosecutorial merit by the police, as the Law's "Elucidation" explains, the police are not expected to conduct another investigation -- they have been kept informed by Bappebti as the investigation proceeds. This reflects the fact that the Law assigns of futures regulation to Bappebti, the police are not to second-guess the agency.

Obviously, the initiation of a criminal investigation does not impel the conclusion that a criminal prosecution is warranted. Article 5A of the draft regulations makes it clear that Bappebti "may," but need not, submit a report recommending prosecution to the Attorney General. To make this entirely clear, the regulations also state in Article 5F that Bappebti may terminate a criminal investigation at any time with the approval of the Chairman.

The regulations provide that any report submitted to the prosecutor must first be reviewed by Bappebti's Legal Counsel and approved, in writing, by the Chairman. This process is intended to ensure that prosecution recommendations to the Attorney General are legally sound and consistent with agency regulatory policy.

Finally, Article 6 of the draft regulations clarifies that criminal investigations complement the agency's regulatory enforcement powers. First, information developed in criminal investigations may be used as the basis for administrative sanctions, since conduct serious enough to be prosecuted criminally will almost invariably merit administrative actions. Second, the regulations make it clear that Bappebti need not elect its remedies, and that the imposition of criminal or administrative sanctions does not preclude subsequent administrative or criminal action.

## **Regulation of Futures Markets Criminal Investigations**

### **Article 1 General Provisions**

- A These regulations govern Bappebti's conduct of suspected criminal violations of Law No 32 of 1997 (the "Law"), conducted pursuant to Article 68 of the Law
- B An investigation is an inquiry into whether or not there has been a criminal violation of any provision of Articles 71, 72, 73, 74 or 75 of the Law, and, if so, whether, pursuant to Article 68(5) of the Law, a report of investigative findings recommending criminal prosecution should be forwarded the Attorney General through the Police Investigator of the Republic of Indonesia
- C Bappebti may conduct an investigation into suspected criminal violations of the law whenever information is received by Civil Servant Officials authorized to receive reports or complaints under Article 68 which indicates that a violation of the criminal provisions of the Law may have occurred. Such information may come from any source, including members of the public, participants in the futures markets, other members of Bappebti's staff, or other agencies of the Indonesian government. Whether Bappebti conducts an investigation is a matter within its sole discretion, and receipt of such information does not require Bappebti conduct a criminal investigation
- D Bappebti may conduct investigations under Article 68 at any time, and any such investigation may be in addition to an examination of the same matter under Article 66 of the Law
- E Only Civil Servant Officials authorized as investigators under Article 68(1) of the Law may conduct investigations, although such Officials may receive assistance from experts employed within or outside Bappebti as the Chairman deems appropriate

### **Article 2 Initiation of Investigations**

- A No investigation under Article 68 may be initiated without prior written approval of the Chairman of Bappebti in the form of an Order signed by the Chairman
- B The Order shall state a finding by Bappebti that criminal conduct under the law is reasonably suspected and that an investigation is appropriate in the public interest. The Order shall designate those members of Bappebti's staff authorized to conduct the investigation

- C Any request by Bappebti staff to initiate an investigation shall be reviewed by the Bureau of Legal Counsel prior to the issuance of an Order
- D The Bappebti Civil Servant Official in charge of the investigation shall notify the Police Investigator of the Republic of Indonesia of the initiation of the investigation within five business days after the execution of the Order by the Chairman, and shall consult as necessary with the Police Investigator during the course of the investigation

### **Article 3**

#### **Conduct of the Investigation**

- A All investigations shall be conducted in accordance with Article 68 of the Law, other relevant provisions of law, and the Constitution of the Republic of Indonesia
- B The Civil Servant Officials authorized to conduct the investigation may
  - (i) receive reports or complaints of any activity which may constitute criminal conduct under the Law,
  - (ii) conduct an investigation into such reports or complaints,
  - (iii) investigate, interview, or examine any person, and request information and physical evidence from any such person,
  - (iv) examine the books and records required by Bappebti to be kept under the Law and regulations, and all other books, records, or documents (including computer records) reasonably related to suspected criminal violations of the Law,
  - (v) enter into any place reasonably suspected to contain evidence, books, records, documents or other physical evidence (including computer records) relating to suspected violations of the Law Except in extraordinary circumstances, such entry should be during normal business hours, and should be conducted with due regard for the ongoing business of any persons affected by the investigation,
  - (vi) take possession of any evidence the Civil Servant Official reasonably believes to be potential evidence of criminal violations under the Law If the Official takes possession of any potential evidence, the Official shall provide the person from whom the evidence is taken with a receipt describing with reasonable specificity the items taken,
  - (vii) request the Bank of Indonesia or any other financial institution to freeze the bank accounts of any party suspected of violating the Law Bappebti shall notify the person whose accounts are subject to the freeze of its request after the request has been granted,
  - (viii) request the assistance of other persons, including but not limited to other members of Bappebti's staff and other law enforcement agencies, in the conduct of the investigation, as Bappebti in its sole discretion may deem appropriate,
  - (ix) request approval from the Minister of Finance to obtain the bank records of any person or entity suspected of violating the Law, in accordance with Banking law and regulations

- C Any book, records, documents or other physical evidence taken into possession by Bappebti during an investigation shall be maintained separately from other agency records and safeguarded in a manner that ensures its integrity
- D Bappebti may, in its sole discretion, confiscate any book, record, documents or other physical evidence taken into possession during an investigation, if it deems such confiscation as necessary and in the interests of justice Bappebti shall notify the person or entity from whom the evidence is confiscated of its action
- E Bappebti may, at the conclusion of an investigation, return to the person or entity from which it was taken any book, record, document, or other physical evidence taken into its possession during the investigation and not confiscated

**Article 4**  
**Confidentiality of the Investigation**

- A Bappebti will ordinarily keep confidential the existence of any investigation, and any information, documents or other evidence gathered in connection with the investigation until the conclusion of the investigation
- B If, at the conclusion of the investigation, Bappebti does not recommend the criminal prosecution of any person for violations of the Law, it will not ordinarily disclose the existence of the investigation, or any information gathered in the course of the investigation, except as may be required by law
- C In extraordinary circumstances, Bappebti may disclose the existence of an on-going investigation if it finds that the public interest is served by disclosure

**Article 5**  
**Resolution of the Investigation**

- A At any time during the investigation, pursuant to Article 68(5), the Civil Servant Official authorized to conduct the investigation, may submit a report of the findings of the investigation through the Police Investigator to the Attorney General, in accordance with provisions of the Indonesian Criminal Code The report may recommend criminal prosecution of persons which the investigation finds have committed violations of any provisions of Article 71, 72, 73, 74, or 75 of the Law, and shall contain the legal and evidentiary basis for any recommendation
- B No report of findings may be submitted to the Attorney General without the prior written approval of the Chairman of Bappebti

- C Any report to be submitted to the Attorney General shall be reviewed by the Bureau of Legal Counsel prior to the approval of the Chairman and submission to the Attorney General
- D Bappebtı will not publicly disclose any report of findings submitted to the Attorney General
- E An investigation under Article 68 may be terminated at any time upon the written approval of the Chairman

**Article 6**  
**Sanctions, Further Action**

- A Information developed during an investigation may form the basis for administrative sanctions under Article 69, whether or not the Chairman of Bappebtı determines to submit a report of findings recommending criminal prosecution to the Attorney General
- B The imposition of administrative sanctions shall not prevent the criminal prosecution of any person under the Law
- C The imposition of criminal penalties upon any person under the Law shall not preclude the imposition of administrative sanctions under Article 69 of the Law