

The Implications of Corruption on Indonesia's Investment Climate Are Reviewed from the Theory of the Legal System and Business Ethics

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ABSTRACT: This study examines corruption as the main obstacle to investment competitiveness in Indonesia. Although investment has a crucial dual role for the economy and the Government has launched various regulatory reforms such as the Job Creation Act and the Online Single Submission (OSS) system, Indonesia still faces an institutional paradox and lags behind Singapore in attracting Foreign Direct Investment (FDI). This normative legal research analyzes the relationship between corruption and the investment climate through the lens of Lawrence M. Friedman's Legal System Theory and Business Ethics. The results of the study show that the root of the problem lies in the Legal Culture component which triggers the emergence of "stealth costs" and uncertainty for investors. Ethically, acts of corruption expressly violate the principles of Utilitarianism, Deontology, and John Rawls's Theory of Justice because they hinder the common good and create inequality of access. This study concludes that improving the investment climate is not enough just by adding new rules, but must focus on improving law enforcement behavior and optimal public services.

KEYWORDS: Corruption, Investment, Business Ethics

I. INTRODUCTION

According to Harrod-Domar's theory, investment activities have a very important dual role to advance a country's economy. First, investment functions like an injection of funds that directly increases the country's demand and revenue. This means that the easier it is for people to invest, the more money is circulating, and the more revenue the country generates. Second, investment helps build and increase working capital, such as new factories or machinery, so that the production capacity of the economy becomes larger. With these two functions, investment is simultaneously able to encourage an increase in public demand while increasing the country's ability to produce goods or services. Law Number 59 of 2024 concerning the National Long-Term Development Plan for 2025-20245 (RPJPN Law), with the Golden Indonesia Vision 2045, explicitly places increased investment as the main pillar of economic transformation, through downstreaming, equity, and competitiveness enhancement strategies. However, without adequate capital flows, the national ambition to achieve the status of a high-income country and realize the Golden Indonesia Vision 2045 will be difficult to achieve.

Reflecting on neighboring countries, other ASEAN countries for comparison, according to UN Trade and Development (UNCTAD) data, Indonesia is in second position as the country that has managed to attract Foreign Direct Investment (FDI) in 2024, and far behind Singapore which is in first place. Then followed by Vietnam which was in third place. This indicates that Vietnam with its various policies, has shown rapid development. The ASEAN region, with its increasingly integrated growth dynamics and single market, is a major competition ground for Indonesia in attracting global capital. Each member state strives to offer the best business climate, spur the speed of licensing, and ensure legal certainty.

FDI is an important driver for the progress of a country. Foreign investors are interested in investing because they see several key conditions, such as stable governance in the context of politics and security, the availability of natural resources and good labor, and open economic policies and financial systems. With this attraction, the government should be ready in all sectors to accelerate economic growth. Unfortunately, bringing large foreign investment into the country is often not as easy as expected, making it difficult to realize the full growth potential of FDI.

Indonesia, with the aim of inviting global investment, has launched a series of adaptive regulatory reforms, such as the *Omnibus Law* and the Online Single Submission (OSS) *licensing system*. The main goal of the Job Creation Law is to create the widest possible employment opportunities evenly throughout Indonesia, in order to ensure the people's right to a decent livelihood. This regulation includes four main pillars, namely: improving the investment ecosystem and business activities, improving the protection and welfare of workers, facilitating and protecting Cooperatives and Micro, Small, and Medium Enterprises (MSMEs), and increasing government investment and accelerating national strategic projects. Job creation is

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specifically encouraged through regulations on improving the investment ecosystem, which include regulations on simplifying business licensing, easier investment requirements, ease of doing business, support for research and innovation, land provision, and economic zone development. As a follow-up to the efforts to simplify business licensing, Government Regulation of the Republic of Indonesia Number 28 of 2025 concerning the Implementation of Risk-Based Business Licensing has regulated detailed steps to provide ease of service to business actors, ranging from registration, business license management, to the issuance of commercial and/or operational licenses. These steps can be done through the so-called Online Single Submission (OSS) licensing system.

If you look at the existing regulations, they are supported by facilities that support investment activities in Indonesia. Indonesia should be ready to become a destination for FDI. However, realization in the field is often not in line with the initial goal. Indonesia is faced with an institutional paradox, having huge market potential but lagging behind regional competitors such as Vietnam, Thailand, or even Malaysia, in terms of efficiency and investment attractiveness. This problem is inseparable from the problem of corruption in Indonesia. Widespread corrupt practices in the public and private sectors have led to inefficiencies in resource management and significantly eroded public trust in state institutions. This problem shows that when viewed on a business ethics scale, this is very worrying and bad. Corruption is generally manifested through the abuse of power for personal gain, including bribery, nepotism, and budget manipulation, which ultimately hinders the effectiveness of public policies. Although FDI inflows to developing countries are influenced by various macroeconomic factors such as production, employment, income, prices, and trade balances, the level of corruption in the host country is considered to be a very significant determinant of location and has a major impact on economic growth and general welfare. To increase FDI attractiveness. Regarding its impact on FDI, there are two perspectives that refer to corruption as an obstacle to FDI inflows. First, it is of the view that corruption increases costs and weakens transparency, property rights, and competition. Second, there is a positive view that corruption can facilitate FDI because it can be a way out of the complexity of weak systems and regulations.

Based on the above problems, what will be studied in this study is how the implications of corruption actions with the investment climate in Indonesia are reviewed from the theory of the legal system of Lawrence M Friedman. In addition, this study is to see the implications of acts of corruption when associated with business ethics in the context of investment.

II. METHODOLOGY

This writing is done using a type of normative legal writing or literature writing, which means that the focus is on analyzing legal rules and norms. By using a legal approach, a comparative approach, and a conceptual approach. The main source analyzed is the legal norms contained in the Law related to the investment climate in Indonesia and various other laws and regulations. This writing uses two types of primary legal materials, namely legally binding documents such as regulations, and records related to the Job Creation Law; Secondary legal materials, which are all forms of writing, scientific journals, and books whose function is to explain and clarify primary legal materials; and tertiary legal materials, as complementary legal materials obtained from *legal websites*.

III. RESULTS AND DISCUSSION

A. *The Implications of Corruption Reviewed from Lawrence M Friedman's Legal System Theory*

Acts of corruption are one of the ones responsible for investment policy issues in Indonesia. Because indirectly corruption has disrupted political stability. Political stability is a very important determinant for investment and development, because in the financial literature, capital inherently seeks a safe and stable environment. Countries facing political conflict are characterized by poor institutional and governance qualities and high uncertainty, thus encouraging investors to shift their capital to more attractive markets abroad.

According to François Valérian, Chairman of Transparency International, corruption is a growing threat globally. He emphasized that the impact of corruption goes far beyond just damaging development; Corruption is the root cause of the decline of democracy, increasing instability, and human rights violations. Therefore, Valerian calls for the international community and every country to make the eradication of corruption a top and long-term priority. This action is considered crucial to counter authoritarianism and ensure the creation of a peaceful, free and sustainable world. Based on the Corruption Perception Index (CPI), released by Transparency International, Indonesia in 2024 shows an improvement compared to the previous year. Indonesia scored 37 out of 100, placing it 99th out of a total of 180 countries surveyed. This score experienced a significant increase of 3 points from the CPI score in 2023 which was only 34 out of 100, where at that time Indonesia was ranked lower, which was ranked 115 out of 180 countries. This figure shows that Indonesia's figure is still far below Singapore in 3rd place, and even below Malaysia in 57th place. The relationship between corruption and the investment climate has indirectly caused a bad perception of the integrity of the public sector. The glaring GPA score gap between Indonesia and regional competitors is the most obvious indicator that explains why, despite Indonesia's natural resource potential, FDI flows often choose neighboring countries.

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In order to examine the root of the problem of corruption related to the investment climate in Indonesia, the author uses his analytical knife, namely Lawrence M Friedman's Legal System Theory. In his book entitled *The Legal System: A Social Science Perspective*, Lawrence M. Friedman, argues that the legal system can be comprehensively understood through the interaction of three components. The first component is the Legal Structure, which refers to formal institutions or institutions created to run the legal system, such as courts and other law enforcement agencies. This structure is responsible for regulating how legal materials are processed and ensuring that legal services run in an orderly manner. The second component is Legal Substance, which is the real result or output of the system. This substance is manifested in the form of applicable regulations, norms, and decisions, which are used by both the regulatory maker and the regulatory subject. The third crucial component is Legal Culture, which serves as a bridge that connects written rules with actual social behavior. This legal culture consists of values and attitudes that collectively affect the effectiveness of legal work. Friedman divides this legal culture into two aspects: internal legal culture, which is the values and attitudes of law enforcers, and external legal culture, which is the views and attitudes of the wider community towards the law. These three components must work in synergy with each other so that the desired legal system can be implemented properly.

In Indonesia, legal substance in the form of rules for the eradication of corruption already exists, namely in laws and regulations such as Law Number 30 of 2002 concerning the Eradication of Corruption Crimes (Corruption Law), along with derivative rules of the law, and other regulations under laws in various sectors. Seen in terms of legal structure, Indonesia already has an institution that specifically functions to eradicate corruption, namely the Corruption Eradication Commission (KPK) and other law enforcers. However, on the other hand, legal culture, which is also associated with Indonesia's corruption ranking in the world, shows a picture of a bad attitude, both in the application of the rule of law and the way law enforcement works.

From the description of the theory, the author argues that in improving the investment climate in Indonesia, it is not by making new rules with the premise of eradicating corruption. In fact, Indonesia can be called an overregulated country, because of the many rules in Indonesia. Talking about corruption is no longer talking about the substance of the law or the legal structure, but we are talking about the culture of law. Corruption seems to have become a hereditary culture among state officials. In the context of investment, corruption not only slows down the process, but also fundamentally changes the economic calculation and risk for investors. Licensing reforms mandated by the RPJPN, such as the simplification of OSS, are often stopped at the level of the implementing bureaucracy. This is where the phenomenon of so-called "stealth fees" arises, this term is described as a form of unofficial fees, illegal levies, or bribes that must be paid to expedite or even obtain approval or permission.

Corruption increases transaction fees and waiting times significantly, creating uncertainty that does not exist in cleaner competitor countries, such as Singapore or Malaysia. The lack of adequate services in Indonesia has a significant impact on the investment climate. This condition is the main factor that drives the reluctance of foreign investors to invest their capital in the country. In other words, the quality of service that is not optimal creates a less attractive environment, so that the potential for investment from abroad cannot be realized optimally.

B. The Implications of Corruption Reviewed from Business Ethics Theory

Business ethics specifically encompasses at least three main areas of activity. First, business ethics focuses on applying general ethical principles into specific business cases and practices, which will then result in ethical guidelines that are specific to the business world. Second, the scope of business ethics goes beyond just application; It also covers the realm of metaethics. In this context, business ethics questions whether ethical judgments imposed on individual behavior can be fairly applied to collective entities such as organizations or companies. Third, business ethics also highlights various basic assumptions about business activities themselves. Since business operates within the framework of an economic system, this field of business ethics must also evaluate and assess the morality of the economic system in general, and the economic system of a country in particular.

Business ethics can be understood as the application of universal ethical principles into the specific realm of human behavior, namely economic and business activities. These ethical principles form a systematic framework of thought called ethical theory. The existence of this ethical theory is needed to help a person make moral decisions that can be accounted for or withstand the test.

The three theories of business ethics used in reviewing this problem are the theory of Utilitarianism, Deontology, and the Theory of Justice from John Rawls.

1. Utilitarian Theories

The theory of utilitarianism, introduced by Jeremy Bentham, holds to the view that good is based on happiness or pleasure, while evil is defined as suffering or pain. Bentham taught that human actions are driven by the effort to achieve the maximum possible happiness and, to avoid suffering. In the context of law, the principle of Utilitarianism is used to judge the goodness or badness of an action or regulation based on its impact on happiness. Thus, the provisions of the legislation that are considered successful are those that are able to bring the greatest happiness. The main goal of the law according to this theory is to create the

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greatest happiness for the wider community. Bentham emphasized that individuals use the law as a means to achieve happiness, so the legal system functions solely as a tool to realize happiness for the entire society.

From the perspective of this theory, corruption is considered morally wrong because its impact on the investment climate causes losses that far exceed the utility or profits obtained. Corruption creates uncertainty, increases investment costs through bribery, and disrupts the allocation of resources so that investments tend to go to corrupt projects instead of the most efficient and beneficial ones in the public interest. Instead of investment and tax funds being used to improve the common welfare, for example through infrastructure development or good public services, the funds are diverted for the benefit of corrupt policymakers. Thus, corruption massively reduces the total happiness of society at large, hinders job creation, and undermines long-term economic growth, making it a practice that is expressly contrary to the main tenets of Utilitarianism.

2. Theory Deontology

According to this theory, what determines the good or bad of an action is the obligation itself. The philosophical basis of this theory was developed by Immanuel Kant, who argued that a new act is considered morally good if it is done solely because it must be done or is based on obligation. Furthermore, Kant states that good deeds must be based on the "Categorical Imperative". A Categorical Imperative is an absolute command that obliges us to act without depending on any terms or purpose (e.g., the loan item must be returned). Kant summed up the essence of the Categorical Imperative in every moral act with a short phrase: *Du sollst*, which means "thou shalt be taken for granted" or an absolute necessity.

From the perspective of this theory, Corruption in the investment climate expressly violates two main things. First, corruption violates the moral obligation to act according to a law that is considered universal. Second, corruption violates the principle of treating humanity of others as an end, not just a tool. When officials accept bribes or investors give bribes, they treat the system, the legal process, and even society as tools to achieve personal gain, rather than respecting them as moral subjects entitled to justice. Therefore, from the point of view of Deontology, corruption is considered to be clearly wrong because it is an absolute violation of moral duties and obligations, making its negative impact on the investment climate a consequence of actions that have been wrong from the beginning, not because of the consequences.

3. John Rawls's Theory of Justice

According to John Rawls in his book entitled *A Theory of Justice* (1971), the theory of justice is built on two main principles: *The Difference Principle* and *The Principle of Fair Equality of Opportunity*. The essence of the Difference Principle is that social and economic inequality is only permissible if the arrangement provides the greatest benefit to the most disadvantaged groups. Overall, Rawls's theory of justice is centered on efforts to maximize the independence of each individual, where restrictions on freedom can only be done for the sake of freedom itself. Second, this theory demands equality for all people in social life and in the use of wealth or social *goods*, with restrictions only allowed if they result in greater collective gains. Third, Rawls emphasizes the need for honest equality of opportunity for all parties, as well as the total elimination of inequality based on wealth or birth status.

From the perspective of this theory, corruption is considered very damaging to the investment climate and unethical. Corruption directly violates the Fair Opportunity Principle because it creates a system in which access to investments, contracts, and licensing is determined by bribery and connections, rather than on competence, meritocracy, or honesty. It removes equality of opportunity and perpetuates wealth-based inequality, contrary to Rawls's demand to abolish inequality caused by birth and wealth. Furthermore, corruption violates the Principle of Difference, which states that social and economic inequality should be governed in such a way as to benefit the most disadvantaged those who are most disadvantaged. Investment funds that are supposed to create infrastructure, jobs, and public services for the poor are actually diverted or misused by corruptors. Thus, corruption adds to the suffering of the most vulnerable groups, thus fundamentally contradicting the primary goal of Rawls's social justice to maximize the well-being of the most disadvantaged.

IV. CONCLUSIONS

Investment has a crucial dual role for the national economy, both as an injector of funds to increase state revenue and as a means of developing working capital to increase production capacity. Although the Government has launched regulatory reforms through the Job Creation Law and the OSS system, Indonesia still faces an institutional paradox where the realization of foreign investment (FDI) remains lagging behind Singapore and is beginning to be overshadowed by Vietnam's rapid development. Judging from Lawrence M. Friedman's Legal System Theory, the root of the problem of investment barriers in Indonesia does not lie in the substance or structure of the law, but in the aspect of *a bad* Legal Culture. Corruption, which has become a hereditary culture among officials, triggers the emergence of "stealth fees" and illegal levies that increase transaction fees and create uncertainty for investors. In terms of Business Ethics, corrupt practices in investment are considered a gross moral violation because they are contrary to the principles of Utilitarianism which prioritize the happiness of the wider community, violate absolute obligations in Deontological theory, and undermine the principle of fair opportunity in John Rawls' Theory of Justice. Policy implementation failures often occur at the regional level, especially in the procurement of goods and services sector, so

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risk-based licensing reform (OSS-RBA) is often stalled at the implementing bureaucratic level. Therefore, efforts to improve the investment climate are not enough just by adding new rules (*overregulation*), but must focus on improving law enforcement behavior and optimal public services in order to attract global capital interest.

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