INDONESIA

TRADE SUMMARY

The U.S. goods trade deficit with Indonesia was $7.8 billion in 2009, down $2.3 billion from 2008. U.S. goods exports in 2009 were $5.1 billion, down 9.5 percent from the previous year. Corresponding U.S. imports from Indonesia were $12.9 billion, down 18.1 percent. Indonesia is currently the 35th largest export market for U.S. goods.

U.S. exports of private commercial services (*i.e.*, excluding military and government) to Indonesia were $1.5 billion in 2008 (latest data available), and U.S. imports were $543 million. Sales of services in Indonesia by majority U.S.-owned affiliates were $2.2 billion in 2007 (latest data available), while sales of services in the United States by majority Indonesia-owned firms were $76 million.

The stock of U.S. foreign direct investment (FDI) in Indonesia was $17.9 billion in 2008 (latest data available), up from $17.7 billion in 2007. U.S. FDI in Indonesia is concentrated largely in the energy and mining sectors.

IMPORT POLICIES

Tariffs

In 2009, Indonesia changed applied tariffs for some products, including for chemical and milk products, for which rates increased. In 2008, Indonesia's simple average bound tariff, *i.e.*, the rate which generally cannot be exceeded under WTO rules, was 37 percent, while its simple average applied tariffs were around 8 percent. Most Indonesian tariffs are bound at 40 percent, although bound tariff levels exceed 40 percent or remain "unbound" on automobiles, iron, steel, and some chemical products. U.S. motorcycle exports remain severely restricted by the combined effect of a 60 percent tariff, a luxury tax of 75 percent, a 10 percent value added tax, and the prohibition of motorcycle traffic on Indonesia's highways.

In the agricultural sector, tariffs on more than 1,300 products have bindings at or above 40 percent. Tariffs on fresh potatoes, for instance, are bound at 50 percent, although the applied rate is 25 percent. Local agriculture interests continue to lobby the Indonesian government to increase tariff rates above bound WTO levels on sensitive agricultural products, such as sugar, soybeans, and corn.

Indonesia has extensive preferential trade relationships with other Asian countries. Under the ASEAN Free Trade Agreement, import duties from ASEAN countries are applied at zero percent to 5 percent, except for products included in an Exclusion List. In addition, Indonesia accords preferential access to its market to Australia, China, Japan, Korea, India, and New Zealand (under ASEAN free trade agreements) and to Japan (under a bilateral Economic Partnership Agreement).

Import Licensing

In 2009, the Indonesian government implemented sweeping new non-automatic import licensing procedures on a broad range of products, including electronics, household appliances, textiles and footwear, toys, and food and beverage products. The measure, known as Decree 56, includes a requirement for pre-shipment verification by designated surveyors at importers' expense and a restriction on imports to five designated ports and airports. The Indonesian government was considering extending these licensing provisions to additional products; however, it has informally limited application of the decree to "final consumer goods." The Indonesian government also appears to be exempting select registered importers from certain requirements of this decree. However, the approval process to qualify as a registered importer is opaque, ill-defined, and potentially discriminatory. The United States and other WTO Members have expressed concern about the decree and are seeking its withdrawal.

Since 2002, Indonesia has continued to maintain other additional non-automatic licensing requirements on textiles, clothing, and other "made-up goods" such as curtains and blankets, which limit market access for a wide range of products. Only approved local producers are authorized to import products covered by this regulation, and these products are permitted to be used only as inputs in domestic production, not for resale or transfer. Approval must be obtained for both the quantity and timing of imports. The United States continues to press Indonesia to eliminate these requirements.

In May 2008, Indonesia introduced new import restrictions for plantation white sugar. The United States is concerned that the new regulation will further limit sugar imports, which already are highly restricted as a result of existing regulations and has urged Indonesia to remove these restrictions.

Pharmaceutical Market Access

The United States continues to have serious concerns about barriers to entering Indonesia's pharmaceuticals market. Following a 2008 Health Ministry decree requiring foreign pharmaceutical companies operating in Indonesia to manufacture locally in order to get drug approvals, the Indonesian food and drug agency (BPOM) has been rejecting or delaying the approval of new applications for drug registrations by some companies, including wholesalers and distributors that do not have manufacturing operations in Indonesia. If these rules are not modified, some foreign firms may be forced to leave the market as their drug approvals, generally valid for two years, gradually expire. The United States and other WTO Members have repeatedly expressed their serious concern about this regulation, which effectively discriminates against companies that manufacture overseas. We will continue to urge Indonesia to resolve the issue so that the affected firms can continue to make their products available to the people of Indonesia.

Quantitative Restrictions

The Indonesian government requires an import permit from the Directorate General of Livestock Services for imports of animal-based food products. In approving import permits, the Indonesian government retains discretion to alter the quantity it allows to enter. U.S. industry estimates the annual trade impact of this restriction to be between $10 million and $25 million. The United States will continue to raise concerns about these practices with the Indonesian government.

Indonesia bans salt imports during the harvest season. It requires salt importers to be registered and to source locally. Indonesia also maintains a seasonal ban on imports of sugar.

Indonesia applies quantitative import limits to imported wines and distilled spirits. Only one registered importer, a state-owned enterprise, is authorized to import alcoholic beverages, with an annual quota set by the Ministries of Trade and Industry.

As a result of new mining legislation, mining firms operating in Indonesia will face new restrictions in exporting unprocessed ore. The legislation requires them to process ore locally in Indonesia before shipping it abroad. The United States will closely monitor implementation of the law to ensure that it does not constitute an export ban on raw materials.

Product Registration

Beginning in late 2008 and continuing throughout 2009, BPOM slowed its process of reviewing applications for the registration of food, beverage, health supplements and other products including cosmetics. Combined with an aggressive enforcement campaign in which large quantities of imported products were seized and destroyed, the process for registering products has become inefficient, burdensome, opaque, and costly to U.S. exporters. Some companies have discontinued or reduced sales to Indonesia as a result of BPOM's enforcement of this requirement.

Customs Barriers

U.S. firms continue to report that Indonesia's Customs Service uses a schedule of "check prices" rather than actual transaction prices to assess duties on food product imports as it committed to do under the WTO Customs Valuation Agreement. Customs makes a valuation assessment based on the perceived risk status of the importer and the average price of a same or similar product imported during the previous 90 days. In addition, the U.S. Government has received complaints from importers about costly delays in customs processing and requests for unofficial payments to customs officers.

Luxury Taxes

The luxury sales tax on 4,000cc sedans and 4x4 Jeeps or vans is 75 percent, compared with the luxury tax on automobiles with engine capacities of 1500cc or less, which ranges from 10 percent to 30 percent. Passenger cars with engine displacement less than 1500cc comprise 40 percent of the market, including a large group of vehicles predominantly produced in Indonesia that are taxed at a rate of 10 percent.

In addition to a 10 percent VAT and an import duty of 150 percent, Indonesia charges luxury taxes on imported distilled spirits of 40 percent to 75 percent. The combined effect of these measures, which produces an effective rate of protection of more than 200 percent, is to place imports at a significant disadvantage in Indonesia's market.

State Trading

In April 2008, the Indonesian government announced that the National Logistics Agency (BULOG) would have exclusive authority to import rice. This action was based on food security and price management considerations. Imports are not permitted before, during, and immediately after the main harvest period, effectively the first quarter of the year. Private firms can import rice for special purposes only, such as for seed and specialty rice, but they must obtain a special importer identification number issued by the Ministry of Agriculture.

GOVERNMENT PROCUREMENT

Indonesia grants special preferences to encourage domestic sourcing and to maximize the use of local content in government procurement. It also instructs government departments, institutes, and corporations to utilize domestic goods and services to the maximum extent feasible. In February 2009, the Minister of Industry issued a circular "recommending" that civil servants purchase domestic goods and services in their official capacities, as well as their private purchasing, in order to "improve domestic product usage." Foreign firms bidding on high value government sponsored projects report that they have been asked to purchase and export the equivalent value of selected Indonesian products. Indonesia is not a signatory to the WTO Agreement on Government Procurement.

INTELLECTUAL PROPERTY RIGHTS (IPR) PROTECTION

Indonesia was elevated to the Special 301 Priority Watch List in 2009 because of growing concerns about IPR protection and enforcement in Indonesia as well as new market access barriers on intellectual property products. In particular, U.S. companies have serious concerns that widespread optical disc piracy and counterfeiting of consumer goods, including pharmaceuticals, not only causes significant economic losses for rights holders, but also poses significant health and safety risks. Cable signal piracy and the illegal downloading of copyright works using mobile devices also remain pervasive. In addition, Indonesia has implemented policies that undermine the protection afforded by the country's IPR regime and thereby increase harm to U.S. rights holders. Two such policies – a regulation issued by the Ministry of Health preventing foreign pharmaceutical companies from registering drugs if they do not manufacture in Indonesia and a regulation issued by BPOM – could severely restrict the registration and availability in Indonesia of pharmaceutical products containing alcohol or ingredients of porcine (pork) origin, including vaccines and products delivered in gelatin capsules. The United States continues to raise these concerns with Indonesia and to urge Indonesia to strengthen its IPR protection and enforcement regime.

SERVICES BARRIERS

Indonesia maintains significant and far-reaching trade and investment barriers in many key services sectors.

Legal Services

Only Indonesian citizens may obtain a full license to practice as lawyers. Foreign lawyers are permitted only to work in Indonesia as "legal consultants" and must first obtain the approval of the Ministry of Justice and Human Rights. A foreign law firm seeking to enter the market must establish a relationship with a local firm.

Express Delivery and Logistics Services

In September 2009, the Indonesian legislature introduced new restrictions on postal services, broadly defined to include courier, express delivery, and other logistics services. The law requires that postal service providers be majority-owned by Indonesians and that foreign providers limit their activities to provincial capitals with international airports and seaports.

Health Services

Hospital services are mostly closed to foreign investment, though Indonesia does allow for up to 65 percent foreign ownership in hospital services in the cities of Medan and Surabaya. Indonesia also restricts foreign health care professionals from practicing in Indonesia. Foreign trained physicians are only allowed to supervise and perform procedures in the course of educating Indonesian physicians.

Distribution

Some U.S. direct selling companies raised concerns that Indonesia's market is generally closed to investment in the direct selling industry. Although Indonesia allows up to 100 percent foreign equity in the distribution and retail sectors, investors must enter into a "partnership agreement" with a small scale Indonesian enterprise.

Financial Services

Indonesia allows 99 percent foreign ownership in the banking sector. Financial service providers may not establish as a branch. In the insurance sector, the 2007 investment law introduced a new foreign equity cap of 80 percent for new investors.

Energy Services

In 2009, the Indonesian Ministry of Industry enacted a regulation requiring foreign bidders for energy services contracts to use a minimum of 35 percent domestic content in their operations. From the perspective of foreign energy services companies, such discriminatory policies severely undermine their ability to make successful bids on contracts and to make decisions about sourcing and personnel that would allow them to function efficiently and profitably in the Indonesian market. Foreign energy services companies that cannot document their compliance appear to be subject to substantial fines, even though it is unclear that Indonesia has the capacity to provide the level of domestic content required by the regulation.

Audit and Accounting Services

Foreign firms cannot practice under international firms' names, although terms such as "in association with" are permissible. Foreign accounting firms must operate through technical assistance arrangements with local firms. Foreign agents and auditors may act only as consultants and cannot sign audit reports. Foreign directors, managers, and technical experts/advisors, are allowed a maximum stay of two years, with a possible one-year extension. Licensed accountants must hold Indonesian citizenship. Auditors practicing in the capital markets are prohibited from delivering specified non-audit services such as consulting, bookkeeping, and information system design.

Film

A September 2009 law provides for screen quotas permitting no more than 60 percent of screen time for foreign films, unspecified import restrictions to achieve that quota, prohibitions against the dubbing of foreign films, and prohibitions against foreign companies distributing or exhibiting films. In December 2009, the Minister of Culture and Tourism announced its intention to re-issue a previously suspended regulation requiring all local and imported movies – both theatrical prints and home video copies – to be duplicated locally with penalties on exhibitors for failing to do so. The United States continues to work with Indonesia to try to address these concerns.

Construction, Architecture and Engineering

Foreign construction firms are only allowed to be subcontractors or advisors to local firms in areas where the government believes that a local firm is unable to do the work. In addition, for government financed projects, foreign companies must form joint ventures with local firms.

Telecommunications Services

Indonesia permits up to 65 percent foreign ownership in value added and mobile telecommunications services and up to 49 percent for fixed networks. While this foreign ownership level goes beyond Indonesia's current commitments in its WTO GATS schedule, the new limits on fixed services represent a step backward from recent practice where up to 95 percent ownership was permitted. A Ministry of Communications and Informatics decree issued in 2008 restricts the construction, management, and ownership of cell towers to domestic companies and would force existing investors to exit the market within two years. The United States has registered its serious concerns to Indonesia about the decree and is seeking its withdrawal.

Education

Indonesia's Law on Education Legal Entities does not allow FDI in higher education in the form of a limited liability company, contrary to the existing Investment Law. In addition, foreign educational personnel require permission from both the Ministry of Education and the Ministry of Manpower. The permission is granted on a case-by-case basis and is only given when there are no Indonesian instructors capable of filling the position.

INVESTMENT BARRIERS

Indonesia maintains significant and far-reaching foreign investment restrictions. Its investment climate continues to be characterized by legal uncertainty, economic nationalism, and disproportionate influence of business interests seeking control and ownership of existing enterprises and new market opportunities. Both through formal regulation and indirect guidance, foreign companies are compelled to do business with local partners and to purchase goods and services locally.

In an attempt to improve its foreign investment climate in 2007, Indonesia introduced a new investment law intended to provide improvements in transparency, as well as a range of investor protections, including non-discriminatory treatment, protection against expropriation, and recourse to international arbitration in disputes against the government. At the same time, however, the new law significantly increased the number of sectors in which foreign investment is restricted, and increased foreign equity limitations in sectors of interest to U.S. investors, including in telecommunications, pharmaceuticals, film and creative industries, and construction. An ongoing process of decentralization, intended to reduce burdensome bureaucratic procedures by moving decisions to provincial and district-level governments, has led to some improvements but has also resulted in new restrictive measures that appear to conflict with other national laws.

Indonesia continues to review the 2007 investment law and "negative list" of restricted sectors. Although Indonesian officials have in the past provided assurances that the more restrictive provisions of the investment law would apply only to new investments, Indonesia appears to allow retroactive application in practice. Moreover, despite the fact that one of the intended purposes of the new law is to enhance transparency, it is unclear whether the negative list represents the full range of sectors where investment restrictions apply. Several ministries, including the Ministry of Communications and Informatics, the Ministry of Health, and the Ministry of Culture and Tourism, have issued decrees that introduce additional new investment restrictions in their respective sectors. The United States continues to strongly urge Indonesia to enhance the transparency and openness of its investment regime, and to address specific problems and concerns of U.S. investors.

Pharmaceuticals

The United States has serious concerns about the deteriorating business climate in Indonesia's pharmaceutical sector. Although Indonesia's 2007 investment law grandfathered existing investments, Indonesian authorities are asserting that any changes in the shareholding capital or ownership structure of an existing company will trigger new foreign equity restrictions, thus requiring that foreign equity in firms be reduced to 75 percent and a domestic partner identified to acquire the remaining 25 percent.

Energy and Mining

Several regulatory changes have recently been introduced to increase government control in the energy and mining sectors and to generate higher royalties for the government.

Indonesia enacted a new mining law in December 2008, replacing a “Contract of Work” system with a system of licensing. The legislation creates new risks and burdens for investors. The new law subjects investments to unpredictable changes in tax and royalties policy and allows central and local governments to cancel licenses. Mining companies must give preference to local subcontractors and service companies and are required to process and smelt ore domestically. The new law also reintroduces divestment requirements that have led to investment disputes in the past. While not requiring the conversion of existing contracts to licenses, the new legislation mandates unspecified changes to existing contracts. The Indonesian government has indicated that it does not intend to honor contractually mandated extensions to contracts of work. To date, the only implementing regulations for the new law have been those mandating preferences for domestic subcontractors.

The Indonesian government also has attempted to unilaterally alter the terms of energy and mining contracts in its favor. In 2008, certain foreign coal purchasers saw their long term contracts nullified when the Energy and Mineral Resources Department ordered private Indonesian coal mining firms to renegotiate sales contracts with foreign buyers if the contracts involved long term fixed price arrangements and the sale prices were below a government-determined benchmark price. Indonesian coal mining firms have stopped shipments in cases where foreign buyers have been unwilling or unable to renegotiate their contracts. In addition, throughout the mining sector, companies have reported problems importing exploration and production equipment free of duties or VAT, as provided for in their contracts. Separately, the oil and gas regulator BP MIGAS has threatened to penalize oil and gas firms that do not meet arbitrary production goals.

Telecommunications

In 2009, the Indonesian government enacted more onerous local content requirements in the telecommunications sector. In October 2009, the Ministry of Communications and Informatics announced a new decree requiring all telecommunications operators to expend a minimum of 40 percent of their total capital expenditures for network development on locally sourced components or services. In July 2009, the same ministry issued a decree imposing local content requirements on operating and capital expenditures of 30 percent to 50 percent in the wireless broadband sector. The United States continues to press Indonesian to address its concerns about the decrees.

OTHER BARRIERS

The Indonesian government and in particular the Corruption Eradication Commission, which coordinates anti-corruption efforts and has the authority to investigate and prosecute high level corruption cases, continues to address the widespread corruption problem in the country. Still, foreign companies continue to report corruption-related difficulties, including demands for unwarranted fees to obtain required permits or licenses, to expedite processes, or to influence government awards of contracts and concessions. Indonesian courts have a reputation for being inefficient and corrupt, creating serious problems for companies drawn into disputes with local partners and threatening the viability of U.S.-invested enterprises.

U.S. industry reports that illegal logging activity in Indonesia results in lost trade opportunities for U.S. producers in Indonesia and third country markets. In addition, the illegal activity results in lost revenue to the Indonesian government as well as significant environmental damage. Indonesia recognizes the seriousness of the issue and is taking steps to address it, including by working with the United States under the auspices of a 2006 Memorandum of Understanding on Combating Illegal Logging and Associated Trade. The United States and Indonesia meet regularly in the context of a bilateral working group and last year took an important step in expanding our cooperation by co-convening a first-ever regional dialogue to explore regional solutions to the illegal logging problem with other Asia-Pacific countries. A second meeting of the regional dialogue is planned for 2010.