INDONESIA

TRADE SUMMARY

U.S. goods exports in 2013 were $9.1 billion, up 13.6 percent from the previous year. Corresponding U.S. imports from Indonesia were $18.9 billion, up 4.9 percent. The U.S. goods trade deficit with Indonesia was $9.8 billion in 2013, down $211 million from 2012. Indonesia is currently the 33rd largest export market for U.S. goods.

U.S. exports of private commercial services (*i.e.*, excluding military and government) to Indonesia were $2.1 billion in 2012 (latest data available), and U.S. imports were $476 million. Sales of services in Indonesia by majority U.S.-owned affiliates were $3.2 billion in 2011 (latest data available), while sales of services in the United States by majority Indonesia-owned firms were $87 million.

The stock of U.S. foreign direct investment (FDI) in Indonesia was $13.5 billion in 2012 (latest data available), up from $12.0 billion in 2011. U.S. FDI in Indonesia is primarily concentrated in the mining sector.

IMPORT POLICIES

In recent years, Indonesia has enacted numerous regulations on imports that have increased the burden for U.S. exporters. Import licensing procedures and permit requirements, product labeling requirements, pre-shipment inspection requirements, local content and domestic manufacturing requirements, and quantitative import restrictions impede U.S. exports. Numerous other measures have been adopted or are being considered in the context of draft legislation, including new food law, trade law, industry law, and quarantine law. In 2013, Indonesia intensified domestic discussions of a revised Negative Investment List. The Indonesian government has increasingly adopted such measures as it pursues the objective of self-sufficiency. These measures are also being adopted as Indonesia reduces tariffs to implement its preferential trade agreements with countries such as China, Australia, Japan, South Korea, New Zealand, and India. The United States will continue to press Indonesia to resolve U.S. concerns regarding these measures.

In August 2013, Indonesia announced a package of policy measures to increase exports, reduce imports, and bolster investment. In December, the Ministry of Finance increased the income tax on imports from 2.5 percent to 7.5 percent for over 500 tariff lines, largely affecting consumer goods.

Tariffs

In 2012, Indonesia's average most-favored-nation applied tariff was seven percent. Indonesia periodically changes its applied rates. In December 2011, the Ministry of Finance increased applied import duties for designated grain and oilseed products from zero percent to five percent. In August 2012, the Ministry of Finance reduced import duties on soybeans from five percent to zero percent through the end of 2012 to counter rising international soybean prices. The import duty on soybeans returned to five percent in January 2013 but was reduced to zero again in October 2013 in response to soybean price increases. In 2009, 2010, and 2011, Indonesia increased its applied tariff rates for a range of imported goods that compete with locally manufactured products, including electronic products, electrical and non-electrical milling machines, chemicals, cosmetics, medicines, iron wire and wire nails, and a range of agricultural products including milk products, animal or vegetable oils, fruit juices, coffee, and tea.

Indonesia's simple average bound tariff of 37 percent is much higher than its average applied tariff. 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. 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 20 percent. The high bound tariff rates, combined with unexpected changes in applied rates, create uncertainty for foreign companies seeking to enter the Indonesian market

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 2010, Indonesia converted its applied tariff on imported distilled spirits from 150 percent *ad valorem* to 125,000 rupiah (approximately $15) per liter.

Indonesia has extensive preferential trade relationships with other countries. Under the ASEAN Free Trade Agreement, duties on imports from ASEAN countries generally range from zero percent to 5 percent, except for products specified on exclusion lists. Indonesia also provides preferential market access to Australia, China, Japan, Korea, India, Pakistan, and New Zealand under regional ASEAN agreements and to Japan under a bilateral agreement. In accordance with the ASEAN-China FTA, in August 2012, Indonesia increased the number of goods from China receiving duty-free access to 10,012 tariff lines. Indonesia is currently negotiating bilateral agreements with Iran, India, Australia, New Zealand, South Korea, and the European Free Trade Association. In addition, Indonesia is studying potential FTAs with Chile, Turkey, Tunisia, Mexico, South Africa, and Egypt. Indonesia is also participating in negotiations for the Regional Comprehensive Economic Partnership, which includes the ten ASEAN members and six additional countries (Australia, China, India, Japan, Korea, and New Zealand).

Indonesia imposes a progressive export tax on cocoa and palm oil exports. The cocoa export tax rate ranges from a minimum of 5 percent to a maximum of 15 percent and is calculated based on a monthly average of export prices. The minimum palm oil export tax rate is 2 percent, and the maximum rate is 22.5 percent. The Indonesian government also imposes export taxes on mineral ores and is considering imposing export taxes on other products, including coconut, base metals, and coal.

Luxury Taxes

Luxury goods (defined as goods not considered necessities), imported or locally produced, may be subject to a luxury tax of up to 200 percent, although the current range is 10 percent to 75 percent for goods listed in the implementing regulations as subject to the luxury tax. In May 2013, Indonesia introduced regulation GR-41, which lowers the Luxury Goods Sales Tax base rates for automobiles that meet certain environmental requirements. This tax is now 75 percent for motor vehicles using advanced diesel/petrol engine technology, dual petrol gas engines, biofuel engines, or hybrid technology, and with fuel consumption of 20 km/liter to 28 km/liter; 50 percent for those same motor vehicles with fuel consumption of more than 28 km/liter; and zero percent for motor vehicles under the government's Low Carbon Emission programs that have spark ignition under 1,200 cc or compression ignition under 1,500 cc (excluding sedans and station wagons).

Although Indonesia has eliminated its luxury tax on imported distilled spirits, the current excise tax regime imposes higher excise taxes on imported spirits than on domestic spirits.

Import Licensing

Indonesian importers must comply with numerous and overlapping import licensing requirements that impede access to Indonesia's market. Under Ministry of Trade Decree 27/MDAG/PER/5/2012 as amended by Decree 59/MDAG/PER/9/2012, all importers are required to obtain an import license as importers of goods for further distribution or for their own manufacturing, but not for both. However, companies that operate under an import license for their own manufacturing are allowed to import finished products provided they are market test products or complementary goods. The decrees also require companies to demonstrate a "special relationship" with the foreign company. The "special relationship" must be consularized by the Indonesian Embassy located in the country in which the foreign company is located. Only then may the companies import products from more than one section of the HS tariff code.

In addition, the Indonesian government requires non-automatic import licensing procedures on a broad range of products, including electronics, household appliances, textiles and footwear, toys, food and beverage products, and cosmetics. The measure, originally known as Decree 56 in 2009, has been extended twice by the Ministry of Trade, most recently in December 2012 through Ministry of Trade Regulation 83/M-DAG/PER/12/2012. Regulation 83/2012 will remain in effect until December 31, 2015. The decree also requires pre-shipment verification by designated companies (known in Indonesia as "surveyors") at the importers' expense and limits the entry of imports to designated ports and airports. Indonesia informally limits application of the decree to "final consumer goods." While the Indonesian government appears to exempt selected registered importers from certain requirements of this decree, the approval process to qualify as a registered importer is opaque, ill-defined, and potentially discriminatory. The United States continues to seek withdrawal of the measure.

Ministry of Trade Regulation 82 of 2012, as amended by Regulation 38 of 2013, and Ministry of Industry Regulation 108, in effect since January 2013, impose burdensome import licensing requirements for cell phones, handheld computers, and tablets and may prevent U.S. hardware companies from becoming importers of record. Under Regulation 82, importers of cell phones, laptop computers, and tablets can no longer sell directly to retailers or consumers. In addition, importers must have at least three years experience and must use at least three distributors to qualify for a Ministry of Trade importer license. In addition, Regulation 38 requires an importer to commit to establish an "industry" within 3 years of obtaining its import permit. Under Regulation 108, an importer must provide product identification numbers for each imported item in order to receive a Ministry of Industry importer license. Companies are unable to provide identification numbers months in advance and, as such, may need to apply for both licenses on a per shipment basis.

Indonesia maintains 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, and these products are permitted for use 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.

Import Licensing for Agricultural Products

Import licensing requirements also apply to horticultural products. In August 2013, Indonesia adopted two ministerial regulations on the importation of horticultural products. These regulations are Ministry of Agriculture Regulation 86/2013 (replacing Regulation No 47/2013, 60/2012, and 3/2012) and Ministry of Trade Regulation 47/2013 (amending Regulation No 16/2013, which replaced regulations No. 60/2012 and 30/2012). The regulations require Indonesian importers to obtain three permits in order to import

horticultural products: (1) a Registered Importer (RI) and/or a Producer Importer (PI) designation from the Ministry of Trade; (2) an Import Recommendation of Horticultural Products (RIPH) from the Ministry of Agriculture; and (3) an Import Approval (SPI) from the Ministry of Trade. Additionally, before applying for recognition as an RI or PI, an importer must obtain an Importer Identification Number (General or Producer) and must prove that it has met certain criteria.

RIPHs and Import Approvals are issued on a biannual basis and are valid for one six-month semester. RIPHs specify, *inter alia*, the product name, HS code, country of origin, manufacturing location (for industrial materials), and entry point for all horticultural products the applicant wishes to import. After securing an RIPH, an importer must obtain an Import Approval from the Ministry of Trade before importing horticultural products. An Import Approval specifies the total quantity of a horticultural product (by tariff classification) that an importer may import during the period for which the Approval is valid. Importers cannot amend existing Import Approvals or apply for additional ones outside the application window. Furthermore, importers must import at least 80 percent of the quantity specified on their Import Approval, or risk losing the right to import in the future.

Indonesia adopted similar rules for the importation of animals and animal products in August and September 2013. Ministry of Agriculture regulation 84/2013 (replacing regulations 50/PERMENTAN/OT.140/9/2011 and 63/PERMENTAN/OT.140/6/2013) and Ministry of Trade regulation 46/2013 (replacing regulation 22/M-DAG/PER/5/2013) require importers, in order to import animals or animal products, to obtain: (1) a RI-Animal and Animal Product determination from the Ministry of Trade; (2) a Recommendation from the Ministry of Agriculture; and (3) an Import Approval from the Ministry of Trade. Additionally, to obtain an RI determination, the importer must be certified as a business establishment, possess a trading license and importer identification number, and meet other requirements.

Recommendations and Import Approvals for animals and animal products are issued quarterly. Recommendations may be valid for up to the remainder of the current year, and SPIs are valid for a fixed term of three months. The Directorate of Veterinary Public Health and Postharvest issues Recommendations, and importers may apply for SPIs only after obtaining a Recommendation for a given product. Recommendations specify, *inter alia*, the name, tariff category, entry point, country of origin, and intended use (which the regulations limit to certain sectors) of the product(s) to be imported. Import approvals specify the quantity of each product that may be imported. Importers must demonstrate actual importation of at least 80 percent of the quantity specified in their Approval from the previous year or risk losing their RI designation.

Similar to the prior import regulations, the new import regulations restrict the import of poultry and poultry products. The regulations governing animals and animal products maintain a positive list of products that may be imported, with the proper permits. The regulations provide for the import of fresh or frozen poultry (chicken, turkey, or duck) carcasses but not for the import of poultry parts, resulting, in effect, in a ban on the import of poultry parts. Additionally, although the regulations provide for the import of whole chicken carcasses, in practice, Indonesia does not issue import permits covering this product.

The licensing regimes for horticultural products and animals and animal products have significant trade restrictive effects on imports and the United States has repeatedly raised its concerns with Indonesia bilaterally and at the WTO. Indonesia failed to address these concerns. As a result, in January 2013, the United States requested consultations with Indonesia under the WTO's dispute settlement procedures, challenging the regimes' consistency with Indonesia's WTO obligations. After the consultations failed to resolve the concerns, the United States requested establishment of a WTO dispute settlement panel to address them, and a panel was established in April 2013. In August 2013, New Zealand joined the

dispute by filing its own request for consultations to address Indonesia's measures. At the same time, the United States filed a revised consultations request to address recent modifications to Indonesia's measures and to facilitate coordination with co-complainant New Zealand. The United States and New Zealand held consultations with Indonesia in September 2013.

Additional import licensing and registration requirements apply to other agricultural products, including animal and animal products, sugar, and dairy.

Pharmaceutical Market Access

The United States continues to have serious concerns about barriers to Indonesia's market for pharmaceutical products. Ministry of Health Decree No. 1010/MENKES/PER/XI/2008 requires foreign pharmaceutical companies either to manufacture locally or to entrust another company that is already registered as a manufacturer in Indonesia to obtain drug approvals on its behalf. Among its requirements, Decree 1010 mandates local manufacturing in Indonesia of all pharmaceutical products that are five years past patent expiration. It also contains a technology transfer requirement. A subsequent pair of regulations, Regulation 1799 and BPOM's (Indonesian Food and Drug Regulatory Agency) updated regulation on drug registration (most recently revised in Regulation 27 of 2013), provides additional information about the application of the local manufacturing requirements and lays out several exceptions to local manufacturing and technology transfer requirements. In September 2012, Indonesia issued Presidential Regulation 76/2012, granting compulsory licensing for nine HIV/AIDS and Hepatitis B treatment drugs. The United States will continue to monitor the implementation of these regulations.

A bill on *halal* certification has been under discussion in the Indonesian Parliament for several years and would require mandatory *halal* certification of pharmaceuticals as well as other products. The United States will continue to monitor the status of this proposed bill, including the potential impact on access to affected products.

Indonesia begins implementation of universal health care coverage (UHC) in January 2014. Routine purchases of pharmaceuticals and medical devices covered under UHC must be made from electronic catalogs developed by the Ministry of Health. There are reportedly few products from U.S. companies included in the Ministry of Health's electronic catalogs. U.S. companies will thus be restricted to competing for sales of their products primarily in the reimbursement (private insurance) market. The United States will continue to follow this issue.

Quantitative Restrictions

Indonesia removed quantitative restrictions on most agricultural products in August 2013 (MOA regulations 84/2013, 86/2013 and MOT regulations 46/2013 and 47/2013). Under current regulations, an importer is required on SPI applications made to the Ministry of Trade to request a quantity of product that the importer will be permitted to import. The Indonesian government has stated that it will approve any quantity requested, with the caveat that an importer must import at least 80 percent of the approved amount or lose the right to import in the future.

The Indonesian government also stated that the import of many agricultural products, including meat and some horticultural products, will be subject to a target price system, whereby imports will be permitted as long as domestic prices are above a set target price. In the event that prices fall below a set target price, the government reserves the right to stop ("postpone") imports.

While the removal of quantitative restrictions is a welcome change, the new system has not yet been tested, and the Indonesian government has not yet demonstrated how the new SPIs and RIPHs will be

issued. Exporters have expressed concern that if imports are permitted on a quarterly basis for animal products, the limited validity of SPIs (three months) will prevent the United States from shipping to Indonesia or drive up costs. Importers have also reported that the SPI and RIPH application process lacks transparency and that many parts of the application system did not function during the two-week period that the application window was open in late 2013.

Indonesia imposes an "unofficial" restriction on corn imports. Unofficially, since 2012, only feed millers can import corn. They must apply for an import permit from the Ministry of Agriculture. The import permit will specify the volume of corn that can be imported. The volume will be set based on the level of domestic feed production.

Indonesia bans salt imports during the harvest season. It requires salt importers to be registered and to purchase domestic supplies as well as imports. Indonesia also maintains a seasonal ban on imports of sugar, in addition to limiting the annual quantity of sugar imports based on domestic production and consumption forecasts. In late 2011, Indonesia banned exports of raw and semi-processed rattan. This ban remains in effect.

Indonesia applies quantitative limits on the importation of wines and distilled spirits. Companies seeking to import these products must apply to be designated as registered importers authorized to import alcoholic beverages, with an annual company-specific quota set by the Ministry of Trade.

Mining firms operating in Indonesia may not export unprocessed ore unless they have the Indonesian government's prior approval to do so *via* a contract of work or plans to build a smelter in Indonesia to process that ore. A 2009 mining law requires companies to process ore locally before shipping it abroad. Although scheduled to enter into force in 2014, Indonesia started implementing the law in 2012, by imposing an export tax of 20 percent on exports of mineral ores. A Supreme Court ruling made public in January 2013, which struck down the unprocessed ore export ban provisions of the Ministry of Energy and Mineral Resources regulation, and a subsequent Ministry promise to continue the ban, has further confused the situation. Foreign and domestic mining companies operating in Indonesia are concerned that a complete export ban would severely limit or stop operations. On January 12, 2014, Indonesia implemented the ban on unprocessed exports of mineral ores, including on nickel and bauxite. However for six mineral ores, including copper, Indonesia will allow export of mineral ore subject to a progressive export tax that will increase every six months through the end of 2016. For instance, for copper, the export tax is 25 percent in the first half of 2014 and will increase to 60 percent in the second half of 2016. U.S. companies have expressed concern that this export tax effectively functions as a ban. The United States will continue to raise concerns on this issue with the Indonesian government.

Indonesia also effectively bans the export of steel scrap.

Product Registration

Beginning in late 2008 and continuing through 2013, Indonesia's food and drug agency (BPOM) slowed its process for reviewing applications for the registration of processed foods, beverages, and other products, including health supplements. Although BPOM reportedly has improved the efficiency of its product registration system, such as through the implementation in early 2013 of an e-registration system for low-risk products, concerns remain about proposed changes to the registration requirements and submission process that would further complicate the process. The United States will continue to monitor developments in this area.

Customs Barriers

U.S. firms continue to report that Indonesian customs relies on a schedule of reference prices to assess duties on some imports, rather than using actual transactions as required by the WTO Agreement on Customs Valuation. Indonesian 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 late 2010, Indonesian customs changed its methodology for assessing import duties on motion pictures from import duties "per meter" to a calculation based on royalties, significantly increasing duties payable. Following a disruption in trade, and as a result of bilateral consultations between the U.S. and Indonesian Governments, the Ministry of Finance adopted a new specific tariff based on a "per minute" calculation rather than royalties. The Finance Ministry also changed the application of its value-added tax on movie imports. Overall, the incidence of duties and taxes under the current system continues to be higher than it was in 2010, though trade has resumed.

In 2013, Indonesian issued Finance Regulation No. 51/2013, which provides tax incentives for foreign investors and labor intensive industries that decide to re-invest in Indonesia. In January 2012, the Ministry of Agriculture announced that, in order to comply with priorities set by the Ministry of Trade, the port of Jakarta and several other major ports would be closed to horticulture imports beginning in March 2012. More than 90 percent of Indonesian imports of U.S. fresh fruits and vegetables (more than $200 million annually) move through the port of Jakarta, Tanjung Priok, and are destined for the Jakarta market. Despite this announcement, since June 2012, U.S. horticulture exports were able to continue using Tanjung Priok port as a result of the U.S.-country recognition status, approved by the Ministry of Agriculture. Australia, New Zealand, and Canada have also been allowed to continue using Tanjung Priok. In January 2013, the Ministry of Agriculture renewed the U.S.-country recognition status.

State Trading

In April 2008, Indonesia granted the National Logistics Agency (BULOG) exclusive authority to import standard unbroken rice. Indonesia cited "food security" (with the Indonesian government separately detailing its aspirations for food self-sufficiency) and price management considerations as the principle objectives of the authorization. BULOG is not allowed to import rice before, during, or immediately after the main harvest period (January/February annually). This requirement effectively prohibits any rice imports during the first quarter of the year. Private firms are only allowed to import broken rice for processing and specialty rice varieties, such as basmati, jasmine, and sushi rice for retail or food service. Importers of broken and specialty rice must obtain a special importer identification number from 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. Presidential Regulation 54/2010 requires procuring entities to seek to maximize local content in procurement, use foreign components only when necessary, and designate foreign contractors as subcontractors to local companies. Presidential Regulation 2/2009 stipulates that all state administrations should "optimize" the use of domestic goods and services and give price preferences for domestic goods and providers. Ministry of Industry Regulation 15/2011 provides for the creation of an Accelerated Use of Local Product National Team to optimize local product use in the procurement of goods and services.

Indonesia's 2012 Defense Law mandates priority for local materials and components and requires defense agencies to use locally produced defense and security goods and services whenever available. In addition, when an Indonesian government entity procures from a foreign defense supplier due to lack of availability from an Indonesian supplier, there is a requirement for trade balancing, incorporation of local content, and/or offset production. The amount of domestic value or local content required will increase over the succeeding five years. Initially, the domestic value required is 35 percent of the total contract value and will increase by 10 percent every year for the subsequent 5 years, after which 85 percent of the value should be compensated by trade balancing, incorporation of local content or offset production. The implementing regulations for the 2012 Defense Law have yet to be finalized, but U.S. defense firms already meet existing informal Indonesian government policy requiring 35 percent of the contract value of defense procurements to be sourced domestically. Contractors reportedly will be able meet the new formalized requirement through various methods, including co-production, joint ventures, buybacks, knowledge transfer, and training.

In 2012, Indonesia became an observer to the WTO Committee on Government Procurement.

INTELLECTUAL PROPERTY RIGHTS PROTECTION

Indonesia remained on the Priority Watch List in the 2013 Special 301 report. Key concerns in Indonesia include continuing widespread copyright piracy and trademark counterfeiting, an inadequate number of criminal prosecutions, and non-deterrent penalties for those who are convicted. U.S. industry reports that one of its most significant frustrations remains the nontransparent and non-deterrent court system, which also impedes the ability of rights holders to obtain information about cases directly affecting their interests. Further, law enforcement and customs officials lack *ex officio* investigation and seizure authority, limiting their ability to enforce IPR laws effectively without a specific complaint from rights holders. As such, rates of physical counterfeiting and piracy, as well as online piracy, are extremely high (an estimated 86 percent of business software is unlicensed) while piracy rates at malls and in the retail sector are also high. Furthermore, counterfeiting activity extends to counterfeit products that present serious risks to human health and safety, such as counterfeit pharmaceutical products. Enforcement efforts are insufficient to keep pace with broad-based piracy and counterfeiting in Indonesia. The Indonesian government is in the process of amending intellectual property laws, including with respect to copyrights, industrial designs, trademarks, and patents. The United States has engaged the Indonesian government during the legislative process, and works with the Indonesian government to develop a mutually agreed Intellectual Property Action Plan to address deficiencies in IPR protection and enforcement, public education and outreach.

SERVICES BARRIERS

Legal Services

Only Indonesian citizens may be licensed as lawyers in Indonesia. Foreign lawyers may only work in Indonesia as "legal consultants" with the approval of the Ministry of Justice and Human Rights. A foreign law firm seeking to enter the market must establish a partnership with a local firm.

Express Delivery and Logistics Services

In September 2009, the Indonesian legislature passed a law with restrictions on the provision of postal services, broadly defined to include courier, express delivery, and other logistics services. The law requires that postal service suppliers be majority-owned by Indonesians and that foreign suppliers limit their activities to provincial capitals with international airports and seaports. Implementing Regulation No. 15/2013 under the law, issued in March 2013, states that only an Indonesian legal entity can apply for

a license and any foreign ownership of a company offering postal services be limited to a maximum 49 percent.

Health Services

Changes to the negative list of foreign investment restrictions in 2010 allow for 67 percent foreign ownership of private specialist hospitals in all regions of Indonesia, in contrast to the previous regulation which limited foreign investors to the cities of Medan and Surabaya. However, foreign ownership is prohibited for health research centers, private maternity hospitals, and general or public hospitals.

Most foreign healthcare professionals may act only as consultants/trainers to Indonesian healthcare professionals. Although the Doctors Practice Law 29/2004 and Minister of Health Regulation No. 512/2007 allow foreign doctors to practice in Indonesia, a 2004 technical note by Indonesia's Investment Coordinating Board banned foreign doctors from practicing in Indonesia, creating uncertainty in the market. In practice, it is nearly impossible for foreign doctors to obtain a license due to strong opposition from the Indonesian Doctors Association.

Financial Services

Nonbank financial service suppliers may do business in Indonesia as a joint venture or be partly owned by foreigners but cannot operate in Indonesia as a branch of a foreign entity. A single entity, either foreign or Indonesian, may own no more than 40 percent of an Indonesian bank. Bank Indonesia may grant exceptions and allow for greater than 40 percent ownership of Indonesian banks in certain cases. In the insurance sector, the 2007 Investment Law limits foreign equity to 80 percent for new investors. In December 2013, Bank Indonesia adopted a new regulation No. 15/49/DPKL restricting foreign ownership in private credit reporting firms to 49 percent.

Energy Services

Article 79 of Presidential Regulation No. 35/2004, which regulates contractor activities in the upstream oil and gas sector, provides that contractors must “prioritize” the use of domestic services, including energy-related services, as well as technologies, and engineering and design capabilities (see below).

Maritime Cabotage

Indonesia’s 2010 Law No. 17 on Shipping requires all vessels operating in Indonesian waters to be Indonesian flagged. Indonesian law further limits foreign ownership of Indonesian-flagged vessels to 49 percent. However, the Indonesian shipbuilding industry does not have the capacity to build the variety of specialty ships its economy requires and is unlikely to have such capacity in the near to medium term. Full implementation of the law would be particularly problematic for foreign investors in Indonesia’s energy and telecommunications sector, which would no longer be permitted to bring in the sophisticated rigs and specialized vessels needed to develop large upstream projects. In response to concerns raised by the United States and others, the Ministry of Transportation issued Regulation No. 48/2011 allowing certain classes of non-transportation vessels to be eligible for a three-month renewable waiver from the domestic flagged-vessel requirements when there is no suitable Indonesian-flagged vessel available. The three-month waivers are often not long enough to cover the duration of a project and they were scheduled to begin phasing out in December 2012. The Indonesian government reports that it plans to move to one-month waivers, which would further add to investor uncertainty and regulatory burden, but so far it has continued to grant three-month waivers. The United States will continue to press Indonesia on this issue.

Audit and Accounting Services

Foreign public accounting firms must be affiliated with a local public accounting firm to conduct business in Indonesia. A foreign accounting firm must use the name of its local affiliate in addition to the foreign firm's name in presentations and disclosures. Indonesia allows a maximum of 10 percent foreign national staff for each level of management in the affiliated local accounting firm. Foreign accountants can operate in the country if they have a license from the Ministry of Finance and are a member of the Indonesian Institute of Certified Public Accountants. In affiliated accounting firms, the ratio of foreign audit signing partners to local signing partners cannot exceed one to four.

Film

A September 2009 Law on Film imposed a 60 percent local content requirement for local exhibitors and included the authority to implement unspecified import restrictions to achieve that quota, prohibitions against the dubbing of foreign films, and prohibitions against foreign companies distributing or exhibiting films. The law also restricted vertical integration across segments of the film industry but that restriction has not been implemented fully to date.

The temporary postponement of a 2008 regulation requiring all local and imported movies, both theatrical prints and home video copies, to be replicated locally, with penalties on exhibitors for failing to do so, was replaced by consecutive one-year suspensions issued by the Minister of Culture and Tourism. In November 2013, Tourism and Creative Economy Minister Pangestu issued a decree suspending implementation until January 1, 2015. The United States continues to advocate for the permanent suspension and repeal of this regulation.

Construction, Architecture, and Engineering

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

Education

Indonesia limits foreign investment in primary, secondary, and tertiary educational institutions through special licenses. Foreign investment in non-formal education is limited to 49 percent. Law 12/2012 on Higher Education liberalizes the tertiary education sector and allows foreign universities to operate in Indonesia if they are accredited in their country of origin, collaborate with local universities, are non-profit, support national interests, and prioritize the appointment of Indonesian citizens as faculty and staff. In order for a foreign national to provide educational services, he or she must be authorized by the Ministry of Education and the Ministry of Manpower. Authorization is granted on a case-by-case basis and only when there are no Indonesian instructors capable of filling the position.

Franchising

In 2012 and 2013, Indonesia's Ministry of Trade made three major regulatory changes in the franchising sector that threaten to have a significant chilling impact on future operations of foreign franchisors. In August 2012, Indonesia promulgated Ministry Regulation No. 53/2012, which establishes a local content requirement obliging an Indonesian franchisee to source 80 percent of its equipment and inventory domestically, unless a waiver is granted. While implementing rules remain vague, this sourcing requirement could have a significant negative impact in the development of new franchising agreements

in Indonesia. This new requirement is not expected to be fully enforced against existing licensed franchisees until 2017.

In October 2012, the Ministry of Trade issued regulation 68/2012 restricting the number of outlets that can be owned by a modern retail franchisee, such as supermarkets, to 150 before they must sub-franchise a portion of additional units to another local sub-franchisee. In February 2013, the Ministry of Trade issued regulation 7/2013 restricting the number of outlets that can be owned by food and beverage franchisee to 250. Under these regulations, companies have five years to come into compliance. These requirements could force some major U.S. and other foreign firms to divest a large number of outlets. It remains unclear when enforcement of this regulation will commence.

In December 2013, the Ministry of Trade issued a new regulation 70/2013, building on the localization requirements of the above regulations requiring modern retail establishments, such as shopping centers, minimarkets, and hypermarkets, to sell 80 percent domestic product within two years of the implementation of the regulation in June 2014. The regulation also limits modern retail establishments to sell a maximum of 15 percent of their stock as private label products and retailers must comply within two years of the regulation's implementation.

INVESTMENT BARRIERS

Indonesia's investment climate continues to be characterized by legal uncertainty, economic nationalism, and the disproportionate influence of local business interests. Indonesian government requirements often compel foreign companies to do business with local partners and to purchase goods and services locally.

Indonesia's 2007 Investment Law significantly increased the number of sectors in which foreign investment is restricted and increased foreign equity limitations in sectors such as telecommunications, pharmaceuticals, film and creative industries, and construction. Pursuant to presidential regulation, Indonesia continues to review the Investment Law and its "negative list" of restricted sectors. The most recent revisions to the list, in 2010, increased restrictions in sectors such as delivery services, while foreclosing foreign investment entirely in others, such as with respect to telecommunications towers (resulting in some firms being forced to exit the market). While the ongoing process of transferring investment-related decisions from central to provincial and district governments has helped reduce some burdensome bureaucratic procedures, the process has also led to inconsistencies between national and regional or local laws.

In 2010, the Indonesian legislature introduced a new horticulture law which reduced permissible foreign equity in horticulture-related business activities from 95 percent to 30 percent.

In 2013, Indonesia continued to consider revisions to the negative list. In late December, a revised list was sent to the president for approval. The revised list appears to contain limited easing of restrictions in a few sectors, including pharmaceuticals, while increasing restrictions in other areas, including distribution and logistics. The revised list also appears to retain the 30 percent restriction in horticulture-related business activities previously contained in the 2010 Horticulture Law.

Energy and Mining

Over the past several years, the Indonesian government has introduced regulatory changes to increase government control and local content levels in the energy and mining sectors.. The regulatory changes have raised costs for foreign businesses and raised questions about the sanctity of contracts already in force with the Indonesian government.

In the oil and gas sector for example, Government Regulation 79, signed in December 2010, allows the Indonesian government to change the terms of certain existing production sharing contracts, while eliminating the tax deductibility of certain expenses, changing the terms and criteria for cost recovery, and placing limits on allowable costs for goods, services, and salaries. Criminalization of the civil production sharing contract added to uncertainty in 2013, as U.S. company contractors and employees were convicted, fined, and imprisoned for doing work that was approved and defended in court by relevant government regulators.

Article 79 of Presidential Regulation No. 35/2004, which regulates contractor activities in the upstream oil and gas sector, provides that contractors must "prioritize" the use of domestic services, including energy-related services, as well as domestic technologies, and engineering and design capabilities. Foreign energy and energy services companies have noted that these local preference policies severely undermine their ability to make successful contract bids and decisions about sourcing and personnel that are necessary to efficiently and profitably operate in the Indonesian market. Indonesia's implementation of its local preference and local content policies in this sector is also becoming more restrictive.

In 2011, Indonesia's oil and gas regulator tightened rules relating to how such content is measured with respect to oil and gas projects. Once fully implemented, the new criteria are intended to achieve an average of 91 percent local content by 2025, up from 61 percent in 2012. Moreover, under the new rules, the goods and services of companies without majority Indonesian shareholding can no longer qualify as "local" content. As a result, foreign energy service companies have been placed at a disadvantage *vis-à-vis* majority Indonesian-owned companies, which can more easily meet local content requirements, but are often less able to meet the technical requirements of a project, often complicating and delaying project tendering processes.

The Indonesian House of Representatives continues to pressure the oil and gas regulator to maintain or increase the local content requirements, leading to increased uncertainty in the market. The United States will continue to monitor developments in this area.

In 2013, the Indonesian government initiated taxation of oil and gas exploration companies in the form of a land tax on all the area in an exploration block regardless of the size of the actual area used for exploration. It also instituted a similar tax on the subsea area of an offshore exploration block and began charging taxes on all equipment and buildings used in exploration.

In 2013, upstream oil and gas regulator SKK Migas, through policy PTK 51 of 2013, began delaying indefinitely cost recovery reimbursement to oil and gas companies with whom disputes arise with respect to reimbursement amounts. At the same time, the Indonesian government increased pressure on oil and gas companies to repatriate export earnings into Indonesian state-owned banks, per Bank of Indonesia Regulation 13 of 2011 as amended by Regulation 14 of 2012, subjecting such earnings to Indonesian banking law and regulations despite production sharing contract language allowing companies to retain such earnings abroad.

A new regulation promulgated by the Ministry of Energy and Mineral Resources in 2013, Regulation 31/2013, also limits the amount of time expatriates can work in Indonesia's oil and gas sector to four years and sets an age limit of those expatriates at 55 years old, requirements that U.S. companies believe will significantly affect staffing patterns and technical capacity if implemented.

Indonesia's 2009 Mining Law replaced a system based on contracts between a company and the central government with one based on licenses issued by local agencies. The law and its implementing regulations impose onerous requirements on companies doing business in this sector, including local content requirements, domestic demand requirements, and a requirement to process raw materials in

Indonesia prior to export. Because the mining licenses are subject to future regulatory, permitting, and tax changes, they provide significantly less certainty than the contract of work system. However, the Indonesian government is requiring companies with contracts of work to renegotiate those existing contracts in order to increase government royalty rates, increase local content requirements, require domestic smelting of minerals, decrease the size of mining areas, and make other changes that significantly alter the economic potential of these projects. The law's implementing regulations also reduced foreign ownership in the sector (to 49 percent within 10 years of the start of production). The United States will continue to press Indonesia on this range of issues.

Telecommunications

Telecommunications providers face myriad investment restrictions. Foreign ownership is capped at 65 percent for suppliers of value-added and mobile telecommunications services and 49 percent for suppliers of fixed network services. While these ownership limitations are higher than those required of Indonesia pursuant to its GATS commitments, the ownership limitation on suppliers of fixed services represents a step backward from past practice, where up to 95 percent ownership was previously allowed.

Regulations signed by the President in November 2012 to implement the 2008 Electronic Transactions Law may require companies operating in Indonesia to build or hire data and disaster recovery centers inside Indonesia. Further draft implementing regulations under consideration define "service providers" broadly such that the regulation would cover almost all online transactions, creating a significant hurdle to companies seeking to do business in Indonesia. The U.S. Government continues to engage the Indonesian government on this issue.

U.S. stakeholders have raised concerns about a spate of local content requirements in the telecommunications sector. Recent Ministry of Communication and Information Technology regulations, Regulation 07/2009 and Regulation 19/2011, require that equipment used in wireless broadband services should contain local content of at least 30 percent for subscriber stations and 40 percent for base stations, and that all wireless equipment should contain 50 percent local content within 5 years. Indonesian telecommunication operators are also required, pursuant to Decree 41/2009, to expend a minimum of 50 percent of their total capital expenditures for network development on locally sourced components or services.

OTHER BARRIERS

Although the Indonesian government and the Corruption Eradication Commission continue to investigate and prosecute high-profile corruption cases, many investors consider corruption a significant barrier to doing business in Indonesia. Other barriers to trade and investment include poor coordination within government, the slow pace for land acquisition for infrastructure development projects, poor enforcement of contracts, an uncertain regulatory and legal framework, and lack of transparency in the development of laws and regulations. U.S. companies seeking legal relief in contract disputes have reported that they are often forced to litigate spurious counterclaims.