INDONESIA

TRADE SUMMARY

The U.S. goods trade deficit with Indonesia was $11.7 billion in 2011, up $2.2 billion from 2010. U.S. goods exports in 2011 were $7.4 billion, up 6.7 percent from the previous year. Corresponding U.S. imports from Indonesia were $19.1 billion, up 16.0 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 $1.6 billion in 2010 (latest data available), and U.S. imports were $413 million. Sales of services in Indonesia by majority U.S.-owned affiliates were $3.2 billion in 2009 (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 $15.5 billion in 2010 (latest data available), down from $15.6 billion in 2009. U.S. FDI in Indonesia is primarily concentrated in the nonbank holding companies and mining sectors.

IMPORT POLICIES

In recent years, Indonesia has introduced numerous new regulations affecting imports, significantly increasing the complexity of accessing the Indonesian market. In addition to tariffs, import requirements include import licensing and permit requirements, product labeling requirements, pre-shipment inspection requirements, local content and domestic manufacturing requirements, and quantitative import restrictions. Numerous other measures are being considered in the context of draft legislation, including deliberations over a new trade law, as the Indonesian government pursues self-sufficiency objectives and seeks to offset the reduction in tariff protection during the implementation of preferential trade agreements with China, Australia, Japan, South Korea, New Zealand, India, and other bilateral and regional partners. The United States will continue to press Indonesia to resolve U.S. concerns regarding these new measures and to encourage Indonesia to maintain an open and transparent trade regime.

Tariffs

In 2011, 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. This change will be applied to wheat and soybean imports. In 2010 and 2009, similar increases in applied rates were implemented for a range of goods that compete with locally manufactured products, including chemicals, electronic products, electrical and non-electrical milling machines, 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, with the applied rate at 20 percent. The large gap between bound and applied rates, combined with seemingly arbitrary changes in applied rates, creates uncertainty for foreign companies seeking to enter the Indonesian market.

U.S. exporters report that a reduction in Indonesia's tariffs could increase market access opportunities in agricultural and manufactured goods. For companies operating in the restaurant sector, the reduction or elimination of tariffs on a wide range of products including beef pepperoni, mozzarella cheese, cooking appliances, cookware, and beverage systems could result in increased U.S. exports. 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 ($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 five percent, except for products specified on exclusion lists. Indonesia also provides preferential market access to Australia, China, Japan, Korea, India, and New Zealand (under regional ASEAN agreements) and to Japan (under a bilateral agreement). Indonesia is currently negotiating bilateral agreements with Iran, India, Pakistan, Australia, and European Free Trade Association countries, and undertaking joint studies on potential FTAs with Chile, Turkey, South Korea, Tunisia, and Egypt.

Indonesia imposes an export tax of 5 percent on cocoa exports and an export tax of 15 percent on palm oil exports. The Indonesian government is considering the imposition of export taxes on other products, including base metals and coal.

Import Licensing

Exporters to Indonesia must comply with numerous and overlapping import licensing requirements that create confusion for traders. In 2009, the Indonesian government implemented a sweeping regulation imposing 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, was extended by Ministry of Trade Regulation 57/M-DAG/PER/12/2010 in December 2010, and it will remain in effect until December 31, 2012. The extended decree includes additional products under the scope of the licensing restrictions, including cosmetics, while retaining a requirement for pre-shipment verification by designated surveyors at importers' expense and a restriction that limits entry of imports to a limited number of designated ports and airports. The Indonesian government was considering extending these licensing provisions to additional products; however, for the time being, 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. Still, the approval process to qualify as a registered importer is opaque, ill-defined, and potentially discriminatory. The United States continues to seek its withdrawal.

Ministry of Trade Regulation No. 45/M-DAG/PER/9/2009, as amended and clarified by Regulation No.17/M-DAG/PER/3/2010, introduced a requirement that companies can only import goods for further distribution or for their own manufacturing, but not for both. Under these regulations, companies are permitted only one kind of license, and those that need both kinds of licenses need to separate into manufacturing and trading businesses. Effective January 1, 2011 in Regulation No. 39/M-DAG/PER/10/2010, Indonesia introduced a new kind of importer license, called a PI License, which permits companies to import certain finished products not used in the production process provided such imports support the development of the company's business in Indonesia. The rationale for this policy is unclear, though importers have expressed concern that it is intended to restrict imports and make them more expensive. Under these regulations, companies must submit import realization reports to the Ministry of Trade on a quarterly basis; if they do not, or if the information is found to be incorrect or inconsistent with the licenses granted, the import license may be revoked.

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 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.

Additional burdensome product-specific import licensing and registration requirements apply to agricultural products, including beef, 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 to manufacture locally or entrust a company already registered as a manufacturer in Indonesia, a potential competitor, to obtain drug approvals for them. Under this policy, foreign companies can be barred from the Indonesian market even if they are market leaders in globally recognized good manufacturing and distribution practices and provide high quality pharmaceutical products to Indonesian patients. Among its requirements, Decree 1010 requires local manufacturing in Indonesia of all pharmaceutical products that are five years past patent expiration. It also contains a technology transfer requirement. A subsequent regulation, Regulation 1799, provided additional information about the application of the local manufacturing requirement, but the regulatory environment remains opaque and uncertain. The Indonesian government had pledged to issue, before the end of 2011, a questions and answers document to further clarify the remaining questions of pharmaceutical companies about the trade and investment restrictions affecting pharmaceutical products, but has not yet done so.

A bill on *halal* certification, currently under discussion in Indonesian Parliament, may require mandatory *halal* certification of pharmaceuticals as well as other products. Such a policy could have significant adverse consequences on U.S. and other foreign companies as well as Indonesian patients.

Quantitative Restrictions

Indonesia maintains quantitative restrictions, particularly on imports of agricultural products such as beef, where annual import quantities are determined by Indonesian agencies in nontransparent processes. The U.S. Government has raised strong concerns over these issues and will continue to seek to address these issues with the Indonesian government.

For animal-based products, a new import permit process is being introduced. The Ministry of Trade issues permits for the import and export of animals and animal products after receiving a recommendation approval from the Directorate General of Livestock and Animal Health Service of the Ministry of Agriculture per Ministry of Trade regulation No. 24/M-DAG/PER/9/2011 and Ministry of Agriculture regulation No. 50/PERMENTAN/OT.140/ 9/2011 dated September 7, 2011. The Ministry of the Economy also plays a key role in the process, particularly in setting national and importer specific allocations. Both regulations were put into effect on October 1, 2011. These regulations now effectively ban imports of any chicken product, including whole birds and mechanically deboned meat. U.S. industry estimates the annual trade impact of this restriction to be between $75 million and $100 million.

A draft regulation has been prepared that would introduce an import quota system on imports of fresh and processed fruits and vegetables, a category of commodities which exceeded $200 million last year.

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.

Indonesia applies quantitative limits to imported wines and distilled spirits. Companies can now apply to be designated as registered importers authorized to import alcoholic beverages with an annual quota set by the Ministry of Trade.

Mining firms operating in Indonesia may not export unprocessed ore. Under the mining law, companies are required to process ore locally before shipping it abroad. The policy is intended to support the expansion of value-added activities, including the smelting industry.

In late 2011, Indonesia banned exports of raw and semi-processed rattan.

Product Registration

Beginning in late 2008 and continuing through 2011, Indonesia's food and drug agency (BPOM) slowed its process of reviewing applications for the registration of food, beverages, and other products, including health supplements. Combined with announced plans to implement an onerous Indonesian language labeling requirement, the process for registering products has become increasingly burdensome, opaque, and costly to U.S. exporters. Some companies have discontinued or reduced sales to Indonesia as a result of the manner in which BPOM is implementing this requirement.

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 transaction prices. 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, vastly increasing duties payable. Following a disruption in trade and 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 is higher than it was in 2010, though trade has resumed.

The Ministry of Agriculture has announced that, in order to comply with priorities set by the Ministry of Trade, the port of Jakarta and several other major ports will be closed to horticulture exports to Indonesia, 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 Jakarta port, Tanjung Priok, destined for the Jakarta market. The U.S. and other foreign governments continue to press Indonesia to suspend this measure.

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. The luxury 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. The luxury tax on motorcycles with the cylinder capacity of 250cc up to 500cc is 60 percent.

State Trading

In April 2008, the Indonesian government announced that the National Logistics Agency would have exclusive authority to import rice. In doing so, Indonesia cited 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 processing 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. 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 sub-contractors 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 Decree 15/2011 provides for the creation of an Accelerated Use of Local Product National Team to optimize local product use in goods or services procurement. 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 if they are awarded the contract.

Indonesia is not a signatory to the WTO Agreement on Government Procurement.

INTELLECTUAL PROPERTY RIGHTS PROTECTION

Indonesia remained on the Priority Watch List in the 2011 Special 301 Report. Key issues 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, shielding rights holders from information about cases directly affecting their interests. Rates of physical counterfeiting and piracy and piracy over the Internet are extremely high (an estimated 87 percent of business software was unlicensed in 2010) while piracy rates at malls and in the retail sector are even higher. Enforcement efforts were insufficient to keep pace with broad-based piracy and counterfeiting in Indonesia, including with respect to counterfeit pharmaceutical products.

SERVICES BARRIERS

Indonesia maintains significant and far-reaching trade and investment barriers in many key services sectors. The United States will continue to press Indonesia to address its concerns on these issues.

Legal Services

Only Indonesian citizens may be licensed as lawyers in Indonesia. Foreign lawyers may only work in Indonesia as "legal consultants" upon 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 introduced a new 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 providers be majority-owned by Indonesians and that foreign providers limit their activities to provincial capitals with international airports and seaports. The Ministry of Communication and Informatics has said that joint ventures will be able to service cities with international airports and seaports, as well as supporting economic areas of provincial capitals with international airports and seaports. However, there are no legal instruments providing such treatment. The United States will continue to press Indonesia on this issue.

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.

Under Doctors' Practice Law No. 29/2004 and Regulation of Minister of Health No. 512/2007, foreign doctors should be permitted to practice in Indonesia, but the situation is unclear because a 2004 technical note from Indonesia's Investment Coordinating Board (BKPM) bans foreign doctors from practicing in Indonesia. In practice, it is nearly impossible to obtain a license due to strong opposition from the Indonesian Doctors' Association. Most foreign healthcare professionals act only as consultants and trainers for Indonesian healthcare professionals.

Financial Services

Financial service providers may not establish as a branch. In the insurance sector, the 2007 Investment Law limits foreign equity to 80 percent for new investors.

Energy Services

In 2011, Indonesia's upstream oil and gas regulator, BP MIGAS, increased local content requirements from 35 percent to 51 percent, even though it is unclear whether Indonesia has the capacity to supply the level of domestic content required by the regulation. Foreign energy and energy services companies, while supportive of the concept of building capacity within the domestic oil and gas industry, state that their operations already support thousands of local businesses, and are concerned that these local preference 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. BP MIGAS is under pressure from the Indonesian Parliament to maintain or increase the local content requirements and is considering further revisions.

Cabotage

Indonesia's 2010 shipping law requires all vessels operating in Indonesia's waters to be flagged domestically and manned by Indonesian crews, and cabotage regulations would have applied that law to all offshore activities beginning May 2011. Implementation of such a requirement would be a particular problem for foreign investors in Indonesia's energy sector, which will no longer be permitted to bring in the sophisticated rigs and specialized equipment needed to develop large upstream projects. As a result of widespread expressions of concern, the Ministry of Transportation issued Regulation No. 22/2011 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. Exceptions included drill rigs, seismic vessels, and other vessels unique to the oil and gas industry, as well as cable-laying ships. These exceptions delay implementation of a broad-based local content effort, but are time limited and scheduled to phase out over the next few years.

Audit and Accounting Services

Foreign public accounting firms must be affiliated with a local public accounting firm to conduct business in Indonesia. Foreign accounting firms must use the name of its local affiliate in addition to the foreign firm's name in presentation and disclosure. 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 Indonesia Institute of Certified Public Accountant. 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 includes a 60 percent local content requirement for local exhibitors, 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 restricts vertical integration across segments of the film industry, which could have unintended consequences in reducing business efficiency and in making the market a less attractive destination for foreign investment.

In January 2010, following concerns raised by the United States, the Minister of Culture and Tourism issued a two year 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. A subsequent deferral, until December 31, 2012, was signed by Minister Pangestu in early 2012. The United States continues to advocate for the permanent suspension 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 government-financed projects, foreign companies must form joint ventures with local firms.

Education

Indonesia's Law on Education Legal Entities does not allow foreign investment in higher education in the form of a limited liability company, in conflict with provisions of the existing Investment Law. In addition, in order for foreign nationals to provide educational services they 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.

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 local business interests seeking control and ownership of both existing enterprises and new market opportunities. Foreign companies are compelled to do business with local partners and to purchase goods and services locally.

In an attempt to improve its investment climate, Indonesia in 2007 introduced a new Investment Law intended to improve transparency and provide a range of improved protections for foreign investors including non-discriminatory treatment, protection against expropriation, and recourse to international arbitration in the event of a dispute with 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. These sectors include telecommunications, pharmaceuticals, film and creative industries, and construction. An ongoing process of decentralization, which is intended to reduce burdensome bureaucratic procedures by moving investment-related decisions to provincial and district level governments, has led to some improvements but has also resulted in new restrictive measures that conflict with national laws.

Indonesia continues to review the 2007 Investment Law and its negative list of restricted sectors.

Presidential Regulation 36/2010, signed by President Yudhoyono on May 25, 2010, issued long-awaited changes to the negative list providing legal clarifications in conjunction with limited liberalization. The clarifications include issues relating to retroactive implementation of the list, and promise a continuous review of closed sectors for increased market access. The revisions include modest changes to investment limits in individual sectors, such as construction, health care, film technical services, and electricity generation. The revisions also increase restrictions in some sectors, however, such as postal services and the telecommunications tower sector, which is now closed to foreign investment.

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.

Energy and Mining

Over the past several years, sweeping regulatory changes have been introduced to increase government control in the energy and mining sectors and to generate higher royalties for the government. The changes increase the cost of doing business and reduce the attractiveness of foreign investment in Indonesia's energy sector. They also raise questions about the sanctity of contracts signed with the Indonesian government.

Mandatory changes in contract terms remain a serious concern in the oil and gas sector. Government Regulation 79, signed in December 2010, changes the terms of existing production sharing contracts and alters the fiscal climate for new investment. It removes certain expenses from tax deductibility, changes the terms and criteria for cost recovery, and places limits on allowable costs for goods, services, and salaries.

Indonesia's 2009 Mining Law replaced the "contract of work" system with a licensing system. The law and its implementing regulations impose onerous requirements on companies doing business in this sector, including local content requirements, domestic demand requirements, a requirement to process raw materials in Indonesia prior to export, and a requirement that foreign license holders divest a 20 percent stake to Indonesian investors after five years of production. The law also reduces the maximum mine work area, diminishing a mining company's ability to fully recover any resource it discovers. Many companies operating in the sector are being called to renegotiate existing contracts, including provisions related to the validity or duration of the contract period, the size of the concession area, and the amount of royalty paid to the Indonesian government.

Telecommunications

Telecommunications providers face myriad investment restrictions. Foreign ownership of up to 65 percent is generally permitted for suppliers of value-added and mobile telecommunications services and up to 49 percent for suppliers of fixed networks. Foreign ownership of up 95 percent is allowed for suppliers of certain data communication system services, and foreign firms have obtained licenses in this sector. While these ownership limitations are higher than Indonesia's current GATS commitments require, the ownership limitation on suppliers of fixed services represents a step backward from past practice, which allowed up to 95 percent ownership.

A Ministry of Communications and Informatics decree issued in 2008 closed the construction, management, and ownership of cell towers to foreign investment. Some foreign firms were forced to exit the market. The Ministry is currently drafting regulations that will require telecommunications companies operating in Indonesia to build data and disaster recovery centers inside the country. If implemented, that requirement would create a significant hurdle to companies seeking to do business in Indonesia.

The Ministry of Communications and Informatics issued two decrees in 2009 requiring telecommunications operators to source significant percentages of their capital and operating expenditures from domestic suppliers.

OTHER BARRIERS

Other barriers to trade and investment include corruption, poor coordination across government ministries, the slow rate of 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. While the Indonesian government and the Corruption Eradication Commission continue to investigate and prosecute high-profile corruption cases, corrupt business practices are endemic and considered by many investors to be an inherent cost of doing business in Indonesia. Corruption can influence the development of regulations as well as government awards of contracts and concessions, while weak rule-of-law institutions, including the judiciary, often mean that U.S. companies seeking legal relief in contract disputes are forced to litigate spurious counterclaims. Regulatory uncertainty, amplified by decentralization and its concomitant multiple layers of bureaucracy, is driven primarily by contradictory laws and regulations, as well as overlapping jurisdictions across government agencies and ministries.