INDONESIA

TRADE SUMMARY

The U.S. goods trade deficit with Indonesia was $10.3 billion in 2006, an increase of $1.4 billion from $9.0 billion in 2005. U.S. goods exports in 2006 were $3.1 billion, up 0.8 percent from the previous year. Corresponding U.S. imports from Indonesia were $13.4 billion, up 11.6 percent. Indonesia is currently the 40th largest export market for U.S. goods.

U.S. exports of private commercial services (i.e., excluding military and government) to Indonesia were $1.2 billion in 2005 (latest data available), and U.S. imports were $348 million. Sales of services in Indonesia by majority U.S.-owned affiliates were not available in 2004 ($1.1 billion in 2003) (latest data available), while sales of services in the United States by majority Indonesia-owned firms were $21 million in 2004.

The stock of U.S. foreign direct investment (FDI) in Indonesia was $9.9 billion in 2005 (latest data available). U.S. FDI in Indonesia is concentrated largely in the mining, and non-bank holding companies sectors.

The United States and Indonesia concluded a bilateral Trade and Investment Framework Agreement (TIFA) in 1996. In recent years, the United States and Indonesia have held regular meetings under the TIFA. The United States has used the TIFA to discuss and seek resolution of many issues that threaten to inhibit bilateral trade and investment. The United States- Indonesia TIFA is a component in the Enterprise for ASEAN Initiative, which was launched by President Bush in October 2002.

OVERVIEW

Since taking office on October 20, 2004, President Yudhoyono, Indonesia's first directly-elected leader, has pursued plans to improve Indonesia's business climate and regional competitiveness; attract greater foreign and domestic investment, especially in infrastructure and export sectors; and generate high-quality job growth needed for sustained economic development. An October 18, 2005 Presidential Decree established an interagency Indonesian National Trade Negotiation Team, with the Coordinating Minister for the Economy and the Minister of Trade as its chair and deputy chair, respectively. This team has the overarching goal of improving coordination of Indonesian government strategies and positions in trade dialogues and negotiations. Early in the Yudhoyono Administration, Minister of Trade Mari Pangestu announced a comprehensive trade policy review aimed at dismantling protectionist measures of previous administrations, rationalizing and harmonizing tariffs, and gradually removing bans and quotas and lowering tariffs. As part of this review, Indonesia's Team Tariff, an interagency body responsible for reviewing tariff and non-tariff measures, announced in December 2004 and January 2006 the completion of each of the two phases of a comprehensive Tariff Harmonization Program.

President Yudhoyono's program to improve Indonesia's business climate and competitiveness seeks to address concerns over the wide range of business problems some United States industry encounters in Indonesia, including the lack of contract enforceability, arbitrary and inconsistent interpretation and enforcement of laws, the absence of a transparent and predictable regulatory environment, irregularities in government procurement tenders, poor infrastructure, labor market rigidities, discriminatory taxation, and ineffective enforcement of intellectual property rights. These business problems cause uncertainty, which combined with widespread corruption, and an unreliable judicial system, hinders commercial dealings in

Indonesia. The Yudhoyono Administration has focused its reform agenda first on revising Indonesia's investment, tax, customs and labor laws; undertaking an effective anti-corruption campaign; and laying the foundation for judicial and civil service reform. On March 2, 2006 the Indonesian government announced an "Investment Climate Improvement Package" containing 85 regulatory and institutional reforms it planned to take in 2006 to improve the investment climate. The package focused on five areas: general investment policies; customs, excise and duties policies; taxation; labor; and small and medium enterprises (SMEs). Indonesia also announced on February 17, 2006, an ambitious infrastructure policy reform package. However, much of the reform agenda has yet to be implemented.

President Yudhoyono continues to make progress in his multi-faceted anti-corruption program. He placed reformers in key positions, such as the chiefs of the tax and customs offices in April 2006. The national budgets for 2006 and 2007 provided additional resources to government agencies engaged in anti-corruption efforts including the Attorney General's Office. Meanwhile, anti-corruption institutions are active and growing in significance and donor assistance to improve public sector performance is robust.

Other priorities for Indonesia in 2006 were continuing recovery and reconstruction efforts following the massive loss of life and destruction from the December 26, 2004 earthquake and tsunami in Aceh and Nias and May 27 earthquake in Jogjakarta and Central Java. Indonesia's economy demonstrated impressive resilience following October 2005 reductions in government fuel subsidies and monetary policy tightening in response to a budget and currency crisis brought on by record world fuel prices. By mid-2006, consumption showed signs of recovery, inflation was on the decline, and Bank Indonesia (central bank) began lowering interest rates. Meanwhile, high world commodity prices contributed to record exports and foreign reserves, enabling Indonesia in October 2006 to complete payment of its IMF program four years ahead of schedule. Investment also showed some signs of recovery with the improving macro-economic environment, but remains well below pre-financial crisis levels.

The United States and Indonesia reenergized Trade and Investment Framework Agreement (TIFA) talks in 2005, and continue to hold regular productive meetings to discuss outstanding trade concerns and to explore areas for future cooperation. The Indonesian government generally has adhered to its long-term trade liberalization program, and the Yudhoyono Administration has actively pursued greater access to global markets through bilateral, regional and multilateral agreements. Indonesia fully implemented the first stage of its commitments under the ASEAN Free Trade Agreement (AFTA) on schedule in 2002, and has been active in ASEAN's efforts to pursue free trade agreements with China, Japan, South Korea, India, Australia and New Zealand.

IMPORT POLICIES

Tariffs

In the late 1980s, Indonesia began long-term trade reform to wean the economy away from its dependence on the petroleum sector and to increase Indonesia's industrial competitiveness. In the early 1990s, it began a series of annual deregulation packages designed to gradually lower applied tariff rates, convert non-tariff barriers into tariffs, and remove restrictions on foreign investment. By January 2003, about 70 percent of Indonesia's tariff lines were assessed import duties ranging between zero percent and 5 percent. Indonesia's unweighted applied tariff average is 6.9 percent, compared to 20 percent in 1994. Indonesia's average WTO bound rate is 37.1 percent.

The Indonesian government released a new tariff reduction package in January 2004. The new tariff book categorizes tariffs into International Non-ASEAN Tariffs and ASEAN Tariffs. Most Non-ASEAN tariffs fall into 0 percent, 5 percent, and 10 percent tiers, except for sensitive items such as automotive goods

and alcohol. ASEAN tariffs fall into three tiers, 0 percent, 2.5 percent, and 5 percent, for all goods covered by the AFTA.

In December 2004, Team Tariff announced the results of the first phase of its Tariff Harmonization Program (THP) with new rates that went into effect on January 1, 2005. This first phase covered 1,964 tariff lines with actual changes to 239 lines: 96 tariff increases and 143 tariff reductions. Of particular note are tariff increases for agricultural (rice, fish, chicken quarters, mangos, carrots, mandarin oranges and flowers) and ceramic products and tariff decreases for some mining related products. In January 2006, Team Tariff announced the results of the second and final phase of the THP. Of 9,209 tariff lines reviewed, Indonesia made changes to 800, lowering 635 tariffs and increasing 165. Most Indonesian tariffs are bound at 40 percent. Products for which tariff bindings exceed 40 percent or which remain unbound include automobiles, iron, steel, and some chemical products. In the agricultural sector, 1,341 tariff lines have bindings at or above 40 percent, including the most sensitive and heavily protected sectors. In the current WTO Doha negotiations, Indonesia, as leader of the G-33, has been advocating special products exemptions from tariff reductions for rice, sugar, soybeans, and corn.

Since late 1999, rice imports have been subject to a specific tariff of 430 rupiah per kilogram (5.1 cents per kilogram or approximately 30 percent on an *ad valorem* basis). In 2004, the Indonesian government instituted bans on imports of rice, sugar and salt, and in 2005, Indonesia increased import duties on corn and soybeans from zero percent to 5 percent and 10 percent, respectively. Local agriculture interests continue to lobby the government to increase tariff rates above the levels bound in the WTO on sensitive agricultural products, such as sugar, soybeans and corn. However, the Minister of Trade is conducting a comprehensive trade policy review that remained ongoing as of March 2007, which may address these tariffs.

Non-Tariff Barriers

During the Soeharto era, the National Logistics Agency (Bulog), had a monopoly on importing and distributing major bulk food commodities, such as wheat, rice, sugar, and soybeans, but it now has the status of a state-owned enterprise with responsibility for maintaining stocks for distribution to military and low-income families, and for managing the country's rice stabilization program. Bulog has floated the idea of again becoming a state trading enterprise with monopoly import rights for some products, but the Indonesian government has not taken action on this proposal. Bulog is no longer entitled to draw on Bank Indonesia credit lines, a privilege it long enjoyed under the Soeharto regime, and must use commercial credit and pay import duties. In conjunction with the minimization of Bulog's authority and role, some designated private companies are now permitted to import rice, wheat, wheat flour, soybeans, garlic, and sugar.

The Indonesian government continues to maintain a ban on imports of chicken parts originally imposed in September 2000 by the Directorate General of Livestock Services in the Ministry of Agriculture (MOA). The U.S. Government has raised concerns about this issue, but the MOA continues to insist on the necessity to assure consumers that imports are *halal* (produced in accordance with Islamic practices). U.S. imports comply with Indonesia's established requirements for *halal* certification, and several ministries have unsuccessfully sought to repeal the ban. U.S. industry estimates the value of lost trade from this ban at roughly $10 million per year.

Indonesia's government also imposes *de facto* quantitative restrictions on imports of meat and poultry products by requiring an Importer Letter of Recommendation. In approving requests for such letters, the Indonesian government can arbitrarily alter the quantity allowed to enter, raising concerns that these

Letters of Recommendation are being used to limit imports. U.S. industry estimates the annual trade impact of this restriction to be between $10 million and $25 million.

Following the June 2005 finding in the United States of a single case of Bovine Spongiform Encephalopathy (BSE), Indonesia's MOA banned imports of U.S. meat and other ruminant products on July 1, 2005. The MOA has yet to inform the United States what information it will need to reinstate this trade, nor would it be ready to reconsider U.S. beef imports. U.S. beef exports had been growing rapidly and approached a record $15 million in 2005 prior to imposition of the import ban. Recent movement to allow meat and bone meal (MBM) imports from the United States on a company by company basis following on site inspection by the MOA has provided very limited access.

The Indonesian government has imposed a rice import ban since February 2004, which was only eased somewhat in November 2005, when the Ministry of Trade issued import permits to Bulog allowing for imports of about 70,000 tons of rice, and again in September 2006 when imports of 210,000 tons were authorized. However, these decisions met with sharp criticism from other ministries, producer groups, and Members of Parliament. Minister of Trade Pangestu, in February 2007, announced that Indonesia was relaxing the ban on rice imports in 2007 due to a late rains and a poor harvest, but that this did not indicate an outright end to the ban on rice imports. Historically, the United States has not made significant commercial sales of rice to Indonesia; most shipments have occurred through the P.L. 480 Title I concessional loan program.

In June 2004, the Ministry of Trade banned the importation of salt during the harvest season from July through the end of each year. Under the regulations, salt importing companies must be registered and source 50 percent of their raw materials locally. A September 2004 Ministry of Trade decree allows five companies to import sugar. It also states that the Ministry of Trade decides which companies can import sugar and how much.

In May 2005, Indonesia issued a proposed regulation, Decree 37, which imposed new requirements for fresh fruit and vegetable imports. The proposal inaccurately reflected the presence of fruit flies in the United States. Although the United States corrected this information in its August 2005 response to the proposed regulation, Decree 37 became effective on March 27, 2006 without modification of the U.S. pest status. The final regulation requires imports of fruit fly host commodities to originate from fruit fly free areas or to be treated as a condition of entry. Eleven U.S. fruit exports were affected by Decree 37, including apples and grapes. Indonesia is the seventh-largest market for U.S. apples worth over $20 million in 2005. In December 2006, following a Ministry of Agriculture inspection visit, Indonesia declared California as a pest free area for the Mediterranean fruit fly for grapes, opening the way to renewed grape exports. The United States will continue to press Indonesia to permit resumption of U.S. fruit exports on the basis of sound science and in conformance with international sanitary and phytosanitary standards.

Quantitative import limits apply to wines and distilled spirits. In addition to the regular import duty of 170 percent, a 10 percent VAT and 35 percent luxury tax, the Indonesian government restricts imports of alcoholic beverages to three registered importers, including one state-owned enterprise.

The U.S. Government has received reports that Indonesia's Customs Service uses a schedule of arbitrary "check prices" rather than actual transaction prices on importation documents to assess duties on food product imports. Indonesian Customs officials defend this practice by arguing it combats under-invoicing. They claim that 80 percent of all Customs applications, electronic or paper, are accepted without extraordinary review. Importers are notified, however, when an application appears to be suspicious and, if the matter is still not resolved, Customs makes an assessment based on an average of

the price of the same or a similar product imported during the previous 90 days. Indonesian Customs, however, does not publicize this methodology or a current list of such reference prices. As a result, although most food product import tariffs remain at 5 percent, the effective level of duties can be much higher. For example, industry estimates that application of arbitrary check prices adds up to $2,000 per shipment of U.S. table grapes to Indonesia, leading to an estimated annual loss of around $3.5 million per year in potential trade for this product alone. The U.S. Government also has received many complaints from importers about costly delays and requests for unofficial payments from a number of companies importing goods through Indonesian ports.

Parliament approved an amended Customs Law on October 18 that cuts red tape for importers and exporters and imposes stiffer sanctions on smugglers. It establishes a code of ethics for customs officers and a set of penalties and incentives to punish corrupt behavior and reward good performance. The United States will press for active enforcement of this law.

Import Licensing

The Indonesian government continues to reduce the number of products subject to import restrictions and special licensing requirements. Currently, 141 tariff lines are subject to import licensing restrictions, down from 1,112 tariff lines in 1990. Alcoholic beverages, lubricants, explosives, and certain dangerous chemical compounds, among other items, are subject to these requirements.

In March 2002, the Minister of Industry and Trade issued a decree on Special Importer Identification Code Numbers (NPIK). This decree requires importers of certain product categories to apply for a special importer identity card, without which products can be detained at port. These goods include: corn, rice, soybeans, sugar, textile and related products, shoes, electronics and toys.

On October 23, 2002, the Minister of Industry and Trade issued a decree concerning Textile Import Arrangements. Only companies that have production facilities using imported fabrics as inputs for finished products, such as garments or furniture, may obtain import licenses. The United States has raised concerns that the import licensing requirements restrict and distort trade and has recommended that the decree be rescinded. The Indonesian government insists the regulations are designed to help curb smuggling from neighboring countries.

STANDARDS, TESTING, LABELING AND CERTIFICATION

In July 2000, the Indonesian government implemented the Consumer Protection Law of 1998 by requiring registration of imported food products. Importers must apply for a registration number from the Agency for Drug and Food Control (BPOM). According to U.S. importers, these requirements have proven to be overly complex, time consuming, and costly.

BPOM tests imported food products although implementation of this requirement is not yet complete and enforcement is inconsistent. Some U.S. producers have expressed concerns that the extremely detailed information on product ingredients and processing they must provide may require them to reveal proprietary business information leading some of them to discontinue sales in Indonesia. If fully implemented the annual level of trade adversely affected by this requirement is estimated by U.S. industry at between $10 million and $25 million.

Beginning January 2001, Indonesia’s regulations required labels identifying food containing "genetically engineered" ingredients and "irradiated" ingredients. However, the Indonesian government has not implemented these new requirements because it has yet to establish minimum threshold-presence levels.

U.S. industry estimates that the new regulation could affect sales of approximately $411 million annually in soybeans and soybean meal from the United States. The U.S. Government is closely monitoring this issue.

GOVERNMENT PROCUREMENT

Indonesia is not a signatory to the WTO Agreement on Government Procurement. In 2004, Indonesia issued a Presidential Decree on government procurement aimed at simplifying procedures and increasing efficiency and transparency in the procurement process. However, the new rules grant some special preferences to encourage domestic sourcing and call for the maximization of local content in government projects, regardless of their source of funding. According to the Decree, foreign companies are eligible to bid on government contracts as part of a joint partnership or as a subcontractor to a domestic firm, and permissible foreign participation increased from $1 million to $5 million. Nevertheless, regional decentralization may introduce additional barriers as local and provincial governments adopt their own procurement rules.

Bilateral or multilateral donors finance many large government contracts and often impose special procurement requirements. For large, government-funded projects, international competitive bidding practices must be followed. The Indonesian government seeks concessional financing for most procurement projects. Since late 1999, the Indonesian government has conducted audits of the state-owned electricity company (PLN), the state oil and gas company (Pertamina), and the State Logistics Agency (Bulog), and identified serious irregularities in their procurement. However, no legal action has been taken with respect to these irregularities.

Foreign firms bidding on high value government-sponsored projects have been asked to purchase and export the equivalent value in selected Indonesian products. Government departments, institutes, and corporations are expected to utilize domestic goods and services to the maximum extent feasible, with the exception of foreign aid-financed procurement of goods and services. State-owned enterprises that publicly offer shares through the stock exchange are exempted from government procurement regulations.

EXPORT SUBSIDIES

In 2004, the Indonesian government ended several credit programs that offered subsidized loans to agriculture and small and medium sized businesses to support exports.

INTELLECTUAL PROPERTY RIGHTS (IPR) PROTECTION

IPR protection and enforcement remains a serious concern in Indonesia, where widespread optical disc piracy and counterfeiting of consumer goods, including automotive parts and pharmaceuticals, cost U.S. firms and the Indonesian government hundreds of millions of dollars in lost revenues and pose serious health and safety concerns for Indonesians. Indonesia has made some progress in the past couple of years, and recent increased Indonesian commitment to IPR protection and enforcement led the U.S. Government on November 6, 2006, to improve Indonesia's Special 301 standing to Watch List.

Copyrights

Indonesia's copyright law came into force in July 2003. The law contains a number of important provisions long sought by U.S. and Indonesian copyright holders, including provision for the issuance of an implementing regulation on optical disks (OD), criminal penalties for end-user piracy, and the ability of rights holders to seek civil injunctions against pirates. An OD regulation became effective in April

2005. The Ministry of Industry leads an interagency OD factory monitoring team that has registered 27 factories and begun unannounced inspections with some support from local intellectual property industry associations. The success of the monitoring team's efforts will depend on its ability to conduct more robust and unannounced inspections on a regular basis and Indonesia's ability to effectively sanction factories and their management involved in piracy.

The Copyright Law establishes rights to license, produce, rent or broadcast audiovisual, cinematographic, and computer software. It also provides protections for neighboring rights in sound recordings and for the producers of phonograms. It stipulates a 50-year term of protection for many copyrighted works.

The Indonesian government regularly consults with copyright holders and associations. In recent years, movies on high-quality pirated DVDs have become increasingly available alongside video compact disks (VCDs). Following a December 2005 directive by Indonesia National Police (INP) Chief Sutanto, police stepped up with increased and sustained IPR enforcement activities, particularly against pirate OD vendors, distributors and factories. The Jakarta and Surabaya police were particularly active, seizing and destroying millions of illegal ODs, arresting hundreds of suspects, and seizing or sealing illegal burners and OD production lines. These activities, however, have yet to result in a significant increase in prosecutions and deterrent fines or custodial sentences, or the permanent impoundment or destruction of large scale production equipment used to manufacture pirated products. While recent police enforcement activities have resulted in some decrease in the quantity and availability of pirated ODs, the rate of piracy in Indonesia remains high, undermining the sale and rental of legitimate products. According to U.S. industry estimates, total losses from copyright piracy in Indonesia during 2005 were above $200 million.

Patents

Indonesia enacted its Patent Law on August 1, 2001. The law consolidated three previous laws covering patents, and established an independent commission to rule on patent disputes and appeals. The law transferred jurisdiction over IPR civil cases to the Commercial Court from the District Court, and raised the maximum fine for patent violations to Rp 500 million ($60,000). The term of protection remains 20 years with a possible two-year extension. A patent is subject to cancellation only in the event the patent holder fails to pay annual fees within specified periods. Unauthorized use of a product or process invention that is the subject of a pending application constitutes patent infringement.

Despite these measures, Indonesia continues to suffer from a lack of effective enforcement of patent rights. The patent law does not address some of the weaknesses that concern foreign rights holders. Chief among these is the requirement that an inventor must physically produce a product or utilize a process in Indonesia in order to obtain a patent for the product or process.

Trademarks

Indonesia enacted its trademark law on August 1, 2001. The law raised the maximum fine for criminal trademark violations to Rp 1 billion ($120,000), and slightly reduced the maximum possible prison term. The Indonesian government justified this move by claiming that financial penalties were a greater deterrent to IPR violators than imprisonment. Foreign rights holders, arguing that most IPR cases never result in the maximum sentence, had pushed for minimum sentencing guidelines rather than higher fines.

The trademark law provides for the determination of trademark rights by priority of registration, rather than by priority of commercial use. The law also provides for the protection of well-known marks, but offers no administrative procedures or legal grounds under which legitimate owners of well-known marks can cancel pre-existing registrations. Currently, the only avenue for challenging existing trademark

registrations in Indonesia is through the courts, an often-burdensome undertaking that must be initiated within five years from the date of the disputed registration. Faster processing (within 180 days) of trademark cases by the Commercial Courts has provided relief to some trademark holders. However, industry representatives are seeking additional injunctions by the courts, especially in cases where a lower court eventually invalidates a false trademark registration.

SERVICES BARRIERS

Despite relaxation of some restrictions, trade barriers to services continue to exist in many sectors.

Legal Services

A few local law firms currently dominate the legal market, and foreign law firms cannot operate directly in Indonesia. A foreign law firm seeking to enter the market must establish a relationship with a local firm. Only Indonesian citizens with a degree from an Indonesian legal facility or other recognized institution may practice as lawyers. Foreign lawyers can only work in Indonesia as "legal consultants" and must first obtain the approval of the Ministry of Justice and Human Rights.

Distribution

In 1998-99, Indonesia liberalized portions of the distribution services sector under the terms of its agreements with the IMF. The Indonesian government eliminated restrictive marketing arrangements for cement, paper, plywood, cloves and other spices. Indonesia allows up to 100 percent foreign equity in the distribution and retail sectors, with the condition that the investor enter into a “partnership agreement” with a small-scale Indonesian enterprise. This partnership agreement need not involve an equity stake in the project.

In the energy sector, Indonesia passed an Oil and Gas Law in November 2001 to deregulate the downstream oil and gas sectors, which includes refining, distribution, storage and retail activities. Under the law, the state oil and gas company Pertamina was converted into a limited liability company (Regulation No. 31/2003) and ended its public service obligation (PSO) two years after passage of the law. The law also stipulates the formation of a new Oil and Gas Downstream Business Regulating Board (Badan Pengatur Kegiatan Usaha Hilir Migas, or BPH Migas) that effectively took control of Pertamina’s former regulatory function over the downstream industry. Although the day-to-day activities of the board must still be defined through implementing regulations, BPH Migas is an independent government institution that reports directly to the President. Its primary functions include regulating the supply and distribution of oil fuel, allocating sufficient fuel oil to meet national fuel oil reserves, stipulating conditions on fuel oil transportation and storage, setting tariffs for natural gas pipeline use, setting the price of natural gas for households and small consumers, and regulating the transmission and distribution of natural gas. The downstream sector is further regulated with President Regulation No. 46/2004 on Oil and Gas Downstream Activities, issued October 14, 2004, which outlines the general procedures, activities and licenses for downstream activities.

In October 2005, Shell was the first private investor to open a non-Pertamina retail fuel station in Indonesia. About 25 local and international investors, including Malaysia’s national oil and gas company Petronas, are reported to have obtained initial licenses for downstream operation.

Financial Services

Indonesia allows 99 percent foreign ownership of domestic banks. In October 2006, BI launched a new banking policy package consisting of 11 regulations. The two-fold aim of the package is to expand the banks' role in the financing of development and to promote consolidation of small banks, which create a supervisory burden while generating little economic activity. (More than 40 of Indonesia's 131 banks have capital of less than $11 million.) The new rules ease lending limits and minimum capital requirements for sound commercial banks. The "single presence policy," will require banks with the same owner to consolidate their presence. They must submit a restructuring plan to BI by December 2007 and report quarterly starting January 2008. The restructuring is be completed by December 2010. To promote banks' intermediary function, the regulatory package relaxes the Legal Lending Limit and creates more flexibility for banks to respond to financing needs in the real sector.

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. Licensed accountants must hold Indonesian citizenship.

Audio-Visual

Indonesia bans all foreign investment in media businesses, including cinema construction or operation, video distribution and broadcast services. Foreign investment is prohibited in broadcast and media sectors, including the film industry (film making, film technical service providers and movie house operations). Foreign investment in the provision of radio and television broadcasting services, radio and television broadcasting subscription services and media print information services also are prohibited.

Construction, Architecture and Engineering

Foreign consultants working under government contract are subject to government billing rates. Foreign construction firms are only permitted 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 has recently made progress in making the telecommunications playing field more transparent and competitive in all but basic services delivery. Foreign investors face few impediments to entering the Indonesian value-added telecommunications market.

Indonesia formed a telecommunications regulatory body in July 2004 to improve transparency in regulation development and dispute resolution. To date, this body has been largely inactive and the Ministry of Communication and Information has been more effective in pushing through sector reforms.

The provisions of Indonesia's Telecommunications Law 36, which came into force in 2000, have guided reforms to end monopolies and open basic telecommunications services to majority foreign ownership. Telecommunications Law 36 lays out goals that exceed many of the modest commitments Indonesia agreed to under the WTO Basic Telecommunications Agreement (maximum foreign investment limit of 35 percent for telecommunications services companies) and the WTO Pro-Competition Annex in 1997

(transparent regulatory procedures, nondiscriminatory licensing, and competitive safeguards for companies operating in Indonesian markets).

In 2002, subsequent implementing regulations for Telecommunications Law 36 established conditions for a new policy of duopoly and accelerated reforms. The government ended the exclusive rights of PT Telkom for domestic long distance service and local fixed-line service in August 2003 and of PT Indosat and Satelindo for international calling service in 2003. Instead, PT Telkom and PT Indosat were established as Indonesia's only full service providers, a move that ensured PT Indosat's survival in the face of increasing competition from Voice Over Internet Protocol (VOIP) services. Since 2002, however, PT Telkom has focused most investment in the value-added cellular market and added very few new lines to remote areas. Although homes and businesses in Indonesia that are wired can enjoy world class telecommunications services by combing services of different providers, only 5 percent of homes have even basic connectivity.

Furthermore, Indonesia allows PT Telkom to charge interconnection fees to both domestic and foreign competitors that renders it almost impossible for other operators to offer service in any but the major metropolitan centers. As a result, most of the major operators (Including PT Indosat) do not have significant foot-print into outlying areas in the same fashion as PT Telkom, simply because they could not be in a position to offer affordable services when interconnection to PT Telkom's vast network reach is required.

Telecommunications Law 36 removed previous requirements that prospective foreign investors partner or enter into a revenue-sharing arrangement with a state-owned enterprise. In January 2002, to attract investors, the government committed to raise telephone tariffs each year for three years to achieve market levels. Popular resistance, however, prevented the second round of price increases in 2003. Indonesia has undertaken partial privatization of its telecommunications companies. In July 2002, government ownership of PT Telkom was reduced to 51 percent, after a public offering of 3.1 percent. In December the same year, the government reduced its ownership of PT Indosat to 15 percent, after it sold 41.9 percent to Singapore Technologies Telemedia.

INVESTMENT BARRIERS

The Yudhoyono Administration has made improving Indonesia's investment climate a priority and has focused its reform agenda first on revising investment, tax, customs and labor laws; undertaking an effective anti-corruption campaign; and laying the foundation for judicial and civil service reform.

A World Bank study found that it takes 97 days on average to establish a business in Indonesia. FDI declined sharply after the 1997-98 financial crisis, but realized foreign investments topped $8.9 billion in 2005, a sign that investor confidence is on the mend. Indonesian government approvals for investment proposals reached $10.4 billion in 2004, compared to $14.3 billion in 2003 and $9.9 billion in 2002.

Indonesia blocks or restricts foreign investment in some sectors. These restricted sectors are included in the "negative list." The most recent list of restricted sectors, issued in August 2000, opened some sectors, including certain medical services, but other sectors remain closed, such as casino and gaming facilities, air traffic and marine vessel certification and classification systems, and radio frequencies. Various infrastructure sectors and the airline, medical services, marine and fisheries, industrial, and other trade sectors are open to investment subject to joint venture or other conditions.

On January 1, 2001, Indonesia began to implement a large-scale decentralization of authority and budget control from the central government to the provincial and district-level governments. Differences of

opinion between the central and local governments about which level of government has authority on certain issues have increased uncertainty among foreign investors. In many areas, despite being contrary to Indonesian law, local governments have instituted trade distorting, revenue-raising measures

In an effort to help alleviate this problem, under proposed revisions to the law, local governments would be granted the authority to tax based upon a "positive" list indicating affirmative local authority, rather than a "negative" list indicating areas where the central government retains authority.

Decentralization has complicated government efforts to improve Indonesia's investment climate and reduce burdensome bureaucratic procedures and other requirements on foreign investors. Indonesian law provides for both 100-percent foreign ownership of direct investment and joint ventures with a minimum Indonesian equity of 5 percent. Currently, Indonesia's Investment Coordinating Board (BKPM) and other relevant agencies in certain sectors must approve proposed foreign investments, but under the new proposed Investment Law being debated in Parliament, Indonesia would move from an investment approval to an investment registration system and BKPM's new mission would be investment promotion. The proposed new investment law do is to provide greater clarity on which sectors are closed and which sectors are open to foreign investment.

In an effort to speed up implementation of proposed reforms, Indonesia on March 2 announced an Investment Climate Improvement Package containing 85 regulatory and institutional reforms it plans to take in 2006 to improve the investment climate. The package focuses on five areas -- general investment policies; customs, excise and duties policies; taxation; labor; and small and medium enterprises -- and specifically calls for revisions to the investment, labor, tax and customs laws. Following a number of delays, Indonesia's Parliament is not expected to pass Indonesia's proposed investment law or tax law amendments until mid-2007. In response to labor demonstrations in April and May 2006, Indonesia decided to indefinitely postpone plans to revise the country's labor laws.

ELECTRONIC COMMERCE

Despite the proliferation of Internet service providers in recent years, several factors hinder the growth of electronic commerce in Indonesia. These include the lack of a clear policy in support of an open telecommunications infrastructure, monopoly provision of fixed landline service by PT Telkom, a low level of computer ownership by both businesses and individuals, lack of funding and weak IPR protection. U.S. industry has identified the lack of a legal framework for ensuring security of online transactions as a particularly significant impediment. The Indonesian government completed drafting of cyber crime and electronic transactions legislation in September 2005 and the measures are currently being debated in the legislature.

OTHER BARRIERS

Transparency

Foreign companies continue to experience problems with corruption in Indonesia. Companies have expressed concern about demands for unwarranted fees to obtain required permits or licenses, and government awards of contracts and concessions based on personal relationships. Legal uncertainty is also a frequent complaint, and courts at several levels are perceived as inefficient and corrupt. The central government is pushing for improvements. The President is urging state-owned enterprises to improve management performance and reduce corruption. Tax administration is undergoing real change with a modernization team committed to reform under a new Director General. New leadership in customs is also seeking to improve services and efficiency. These are part of broader Ministry of Finance

reforms which include improving capital markets supervision, debt management, budget and expenditure planning and internal controls. Reform in other areas such as the non-bank financial sector such as pensions and insurance, however, remains slow.

Indonesia has empowered several corruption-fighting bodies. The Corruption Elimination Commission (KPK) dramatically ramped up its activity since it set up operations in 2004. In 2004 it conducted 17 pre-investigations, 1 investigation and began 2 prosecutions: in 2005, it had 31 pre-investigations, 19 investigations and 17 cases being prosecuted. The Special Court of Corruption, domiciled in the District Court of Central Jakarta but with jurisdiction over all of Indonesia, handles all anti-corruption cases initiated or taken over by the KPK. The Attorney General's Office announced in August 2006 the formation of a "reform team" to improve prosecutor performance. President Yudhoyono created a Police Commission in June 2006 to advise him on police-related issues. He named three anti-corruption "champions" in August 2006: Attorney General Abdul Rahman Saleh, National Police Chief General Sutanto, and KPK Deputy Chairman Erry Riyana Hardjapmengkas. A Presidential Working Unit to improve public services and policy implementation was also formed in November 2006. An "Interagency Corruption Eradication Team") has been active in investigation and prosecution of public corruption including of several high-ranking officials. In addition, Indonesia ratified the United Nations Convention Against Corruption in March 2006 and passed new whistleblower protection legislation in August 2006.

Many challenges remain and Indonesia's commitment to reform is attracting robust donor assistance. The U.S. Millennium Challenge Corporation provided a $55 million grant for Indonesia's "Threshold Country Plan" in October 2006. The two-year plan has a strong anti-corruption component including judicial reform, increased enforcement capabilities to fight money laundering, prosecution of cases of public corruption, and reduction of opportunities for corruption through the modernization of public procurement systems. Donor organizations from Europe, Japan, Australia and the United States are providing grants, technical expertise and training for Indonesian institutions. The World Bank and the Asian Development Bank programs remain robust to help improve all types of public sector performance.

Automotive Policies

The maximum tariff on automobiles is 80 percent. Tariffs on passenger car kits imported for assembly range from 25 percent to 50 percent, depending on engine size. Tariffs on non-passenger car kits are a uniform 25 percent. Tariffs on automotive components and parts imported for local assembly of passenger cars and minivans are a uniform rate of 15 percent. Imports of motor vehicles are no longer restricted to registered importers or sole agents of foreign automakers, but are open to any licensed general importer. U.S. motorcycle manufacturers remain concerned about the high tariff of 60 percent (25 percent on knockdown kits), the luxury tax of 75 percent, as well as the prohibition on motorcycle traffic on tollways as barriers to the Indonesian market.

The luxury sales tax on 4,000 cc sedans and 4x4 Jeeps or vans is 75 percent. The luxury tax on automobiles with engine capacity of under 1500 cc ranges from 10 to 30 percent. The luxury tax on automobiles with engine capacity between 1,500 cc and 3,000 cc ranges from 20 percent to 40 percent, depending on the size of the engine and body style of the vehicle. In 2006, a dramatic increase in fuel prices, which took effect in October 2005 led to a significant shift in motor vehicle sales to vehicles with engine displacement below 1500 cc Forty percent of the market is made up of passenger cars with engine displacement under 1500 cc, with the MPV type vehicles accounting for 35 percent. These MPV type vehicles, predominantly produced in Indonesia, have a luxury tax of 10 percent.