INDONESIA

TRADE SUMMARY

The U.S. trade deficit with Indonesia was $8.1 billion in 2004, an increase of $1.1 billion from $7.0 billion in 2003. U.S. goods exports in 2004 were $2.7 billion, up 6.1 percent from the previous year. Corresponding U.S. imports from Indonesia were $10.8 billion, up 13.6 percent. Indonesia is currently the 39th largest export market for U.S. goods.

U.S. exports of private commercial services (i.e., excluding military and government) to Indonesia were $1.1 billion in 2003 (latest data available), and U.S. imports were $278 million.

The stock of U.S. foreign direct investment (FDI) in Indonesia in 2003 was $10.4 billion, up from $10.3 billion in 2002. U.S. FDI in Indonesia is concentrated largely in the mining, utilities, and manufacturing sectors.

OVERVIEW

Although Indonesia's economy weathered the 2002 global economic slowdown relatively well, the country still has not fully recovered from the effects of the 1997-98 financial crisis. The government of former President Megawati Soekarnoputri maintained a measure of political stability during its tenure, despite an ongoing conflict with separatists in the gas-rich province of Aceh. In 2004, Indonesians elected a new President, Susilo Bambang Yudhoyono, who took office in October pledging fundamental reform as part of his "100-Day Plan." President Yudhoyono has announced an ambitious economic reform program that focuses on reducing poverty by raising Indonesia's GDP growth rate, eliminating corruption, and improving the business climate. The earthquake and tsunami that struck Sumatra and the Indian Ocean region on December 26, 2004, left over 150,000 dead in Indonesia alone and caused incalculable human suffering as well as losses in property and infrastructure. As of the end of 2004, it was unclear what effect this natural disaster would have on Indonesia's economy and President Yudhoyono's reform plans.

The Indonesian government generally has adhered to its long-term trade liberalization program, although some backsliding occurred under the Megawati administration between 2002 and 2004. Indonesia fully implemented the final stage of its commitments under the ASEAN Free Trade Agreement (AFTA) on schedule on January 1, 2002. However, during its tenure, the Megawati administration expressed reservations about the pace of liberalization within AFTA, and noted an interest in pursuing emergency exit clauses from AFTA commitments in general.

Indonesia has a mixed record in the WTO. In the current Doha multilateral negotiations, Indonesia continues to advocate special product exemptions for rice, sugar, soybeans, and corn. 2002 textile regulations favor domestic textile fabrics over imports, and we have raised our concerns in the WTO. However, in 2003 the government used WTO-compliant mechanisms, like safeguards, as an alternative to protectionist measures.

Indonesia's garment sector suffers from poor capital investment and low productivity. Some observers predict the industry may lose half of its four percent world market share following the expiration of the Multi Fiber Agreement at the end of 2004.

The new Yudhoyono administration has pledged to reassert Indonesia within multilateral trade organizations like the WTO, APEC and ASEAN. The new government has also committed itself to improving Indonesia's trade competitiveness by streamlining bureaucracy, improving competitiveness, and rectifying ill-conceived policies of the past.

Indonesia's relationship with the International Monetary Fund (IMF) provided the framework for the country's economic policies since November 1997. IMF-supported economic reforms helped stabilize the macro economy, restructure the financial sector, and reinforce policies of trade and investment liberalization. Indonesia concluded its IMF program at the end of 2003.

President Yudhoyono has proposed creating an economy characterized by efficient resource allocation, open markets and free trade, the protection of property rights, and a stronger rule of law that is applied transparently and free from corruption and that diffuses knowledge broadly. He has also proposed increasing Indonesia's competitiveness in priority sectors including: electronics, textiles, automotive, fisheries, wood-based and rubber-based industries, as well as key service sectors such as air travel, tourism, health care and electronic commerce, and small- and medium-sized businesses. The economic goals expressed by President Yudhoyono touch on U.S. industry's continuing concerns over the wide range of business problems it encounters in Indonesia, including the lack of contract enforceability, discriminatory taxation, the absence of a transparent and predictable regulatory environment, arbitrary and inconsistent interpretation and enforcement of laws, irregularities in government procurement tenders, and ineffective enforcement of intellectual property rights. These business problems cause great uncertainty, which combined with widespread corruption, an ineffective judicial system, non-existent credit reporting, and underdeveloped capital markets, hinders commercial dealings in Indonesia.

IMPORT POLICIES

Tariffs

As of January 2003, about 70 percent of Indonesia's tariff lines were assessed import duties ranging between zero percent and five percent. Indonesia's unweighted tariff average is 7.3 percent, compared to 20 percent in 1994.

In the late 1980s the Indonesian government began long-term trade reform to wean the economy away from its dependence on oil and gas 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. The January 11, 2001, tariff reduction package cut five percentage points on 1,279 tariff lines. The majority, 769 lines, had tariff rates reduced to 10 percent or below. Effective January 1, 2002, Indonesia, along with the other five original ASEAN members, implemented the final phase of the ASEAN Free Trade Agreement (AFTA). Indonesia has reduced tariffs for all products included in its original commitment (7,206 tariff lines) to five percent or less for products of at least 65 percent ASEAN origin. The 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 ASEAN Free Trade Agreement (AFTA).

In the Uruguay Round market access negotiations, Indonesia committed to bind 94.6 percent of its tariff schedule; most 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. Indonesia committed to remove import surcharges on items bound in the Uruguay Round by the year 2005, and had done so by the end of 1996. In accordance with the WTO Agreement on Agriculture, Indonesia agreed to eliminate non-tariff barriers on agricultural products, and replace them with tariffs. 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 has been advocating special products exemptions from tariff reductions for rice, sugar, soybeans, and corn.

Beginning in 2002 and intensifying through 2004, domestic agricultural interests put pressure on the Indonesian government for protection from international competition. However, with some notable exceptions, the Indonesian government has resisted such pressure. 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. 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 Yudhoyono administration has announced plans for a review of all rules and regulations related to imports and exports and business licensing. The stated intention of the review is to identify and rectify onerous bureaucracy and ill-conceived trade policies.

Non-Tariff Barriers

Since 1997, Indonesia has dismantled many formal non-tariff barriers. In September 1998, the Indonesian government sharply curtailed the role of the National Logistics Agency (Bulog), which had a monopoly on importing and distributing major bulk food commodities, such as wheat, rice, sugar, and soybeans. Bulog now maintains 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. The agency 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. The U.S. government has raised concerns about this issue, but the Ministry of Agriculture 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 ("Surat Rekomendasi Importir"). In approving requests for such letters the 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.

The government imposed a rice import ban in February 2004 just prior to the rice harvest season (February - May). The ban is supposed to be in effect one month before and two months after the planting season. The Ministry of Agriculture, however, requested that the ban be extended through the end of 2004. Meanwhile, U.S. rice exports increased from $5 million in 2001 to $18.5 million in 2002. Most of these exports were linked to two P.L. 480 Title I concessional loan programs in each respective year. Although the Indonesian government rejected the program for 2003, U.S. rice exports reached $16.3 million (mostly for humanitarian purposes), 12.2 percent lower than in 2002.

In June 2004, the Ministry of Trade banned the importation of salt during the harvest season from July through the end of the year. Under the regulations, salt importing companies must be registered and source 50 percent of their raw materials locally. A September 2004 Ministry of Industry and 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.

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 for assessing duties on food product imports. While Indonesia’s government officials defend this practice on the basis of combating under-invoicing, they do not publicize the list or the methods used to arrive at those prices. As a result, although most food product import tariffs remain at five percent, the effective level of duties can be much higher.

Other quantitative 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, Indonesia's government restricts imports of alcoholic beverages to three registered importers, including one state-owned enterprise.

Import Licensing

Indonesia's government has continued 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 to use imported fabrics as inputs for finished products, such as garments or furniture, may obtain import licenses. The United States has raised serious concerns that the import licensing requirements severely restrict and distort trade. Indonesia's government insists the regulations are designed to help curb smuggling. The U.S. Government has recommended that the decree be rescinded.

STANDARDS, TESTING, LABELING AND CERTIFICATION

In July 2000, the Indonesian government began to implement 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). After complaints from Indonesian importers and retailers of overly complex, time consuming, and costly requirements, BPOM drafted revised procedures that would simplify the process. However, those draft regulations have stalled in the President's Office without approval or further comment.

All imported food products must be tested by BPOM. Fees for such testing range from Rp 50,000 ($6.00) to Rp 2.5 million ($300) per item, and between Rp 1 million ($120) to Rp 10 million ($1200) per product. Some U.S. producers have expressed concerns that the extremely detailed information on product ingredients and processing they must provide may infringe upon proprietary business information. This has led some U.S. exporters to discontinue sales.

However, the government has not fully implemented these regulations, and enforcement is weak and inconsistent. 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.

Indonesia's government also has been gradually implementing a strict food labeling law that requires labels written only in the Indonesian language on all consumer products. Labels may not include any other languages. U.S. companies, which generally design labels to accommodate several export markets (often in several languages), have concerns about this requirement because it makes it cost ineffective to export smaller volume products. However, as of December 2004, the government had not issued implementing rules or enforced the food labeling requirement. The United States is closely monitoring this situation.

Beginning January 2001, Indonesia's regulations required labels identifying food containing "genetically engineered" ingredients and "irradiated" ingredients. However, the 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 United States is closely monitoring the situation.

GOVERNMENT PROCUREMENT

Indonesia is not a party to the WTO Government Procurement Agreement (GPA). Indonesia's government procurement regime is governed by a number of overlapping laws, regulations, and presidential decrees. Most important is a presidential decree issued in February 2000, which updated the Law on Government Procurement of 1994. The decree simplified procurement procedures and enhanced transparency, but also granted special preferences to domestic sourcing. In addition, Construction Law 14/1999 governs procurement of civil engineering services and related consulting services. Regional decentralization also 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), which identified serious irregularities in procurement. However, no legal action has been taken.

Foreign firms bidding on high value government-sponsored construction or procurement 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 goods and services procurement projects. State-owned enterprises that publicly offer shares through the stock exchange are exempted from government procurement regulations. The new oil and gas upstream authority, BP Migas, regulates the import of all materials used by the oil and gas sector.

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

The United States placed Indonesia on the "Priority Watch List" again in 2004, due to continued weak IPR enforcement. Previous Special 301 Annual Reviews in 2003, 2002 and 2001 identified a range of IPR concerns, including rampant software, audio, video disk and book piracy; pharmaceutical patent infringement; counterfeiting; trade secret protection; data protection; apparel trademark counterfeiting; an inconsistent and corrupt law enforcement regime; and an ineffective judicial system. The lack of effective IPR protection and enforcement are major disincentives to foreign investment in Indonesia, particularly in high technology sectors.

The government agency responsible for IPR legislation, the Ministry of Justice Directorate General for Intellectual Property Rights, works closely with industry groups. However, prosecution of violators has been difficult due to inadequate police action, prosecutor and judge unfamiliarity with the new law, as well as the Indonesian public's limited understanding of the importance of IPR protection, and rampant corruption. In 2001, the Indonesian judiciary began consideration of certain IPR cases in the Commercial Courts. In a landmark case that year, a U.S. software company won a civil suit against five retailers for selling computers bundled with pirated software. In their first two years, the Commercial Courts have concluded over 150 cases. Nonetheless, U.S. companies often find the Indonesian court system unpredictable in practice and ineffective in punishing violators. Industry representatives say the vast majority of criminal prosecutions must be dropped due to poor evidence documentation and maintenance, as well as widespread corruption within the justice system. The few cases that are concluded by the courts often result in minimum sentences and/or fines being imposed which are not sufficient to act as a deterrent.

Indonesia is a member of the WIPO and has acceded to numerous international conventions on IPR. These include the Paris Convention for the Protection of Industrial Property, the Berne Convention for the Protection of Literary and Artistic Works, the WIPO Copyright Treaty, the Patent Cooperation Treaty, the Trademark Law Treaty, the Nice Agreement for the International Classification of Unclassified Goods and Services, and the Strasbourg Agreement Concerning International Patent Classification. Despite well-publicized raids on pirate operations in the last few years, industry sources report that Indonesia ranks very poorly when compared to its peers in ASEAN in its record for payment of IPR royalties.

Copyrights

The new copyright law came into force in July 2003, one year after it passed Parliament. 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 rightholders to seek civil injunctions against pirates. President Megawati signed the OD regulation into law in October 2004. The outgoing Minister of Industry and Trade issued two ministerial decrees required to implement the OD regulation. These new regulations include a six-month transition grace period and will become effective in April 2005.

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, meeting TRIPS Agreement requirements. A 1989 copyright agreement between the United States and Indonesia extends national treatment for copyright protection to works created by citizens of each country.

The government's enforcement of copyrights is uneven, although it periodically intensifies actions against copyright piracy and officials regularly consult with copyright holders and associations. However, piracy of video compact disks in Indonesia is widespread, undermining the sale and rental of legitimate products. Periodic raids result in the seizure of sizable caches of pirated OD products. However, none of these cases has resulted in meaningful penalties or permanent impoundment or destruction of equipment used to manufacture pirated products. In recent years, movies on high-quality pirated digital video disks (DVDs) have become increasingly available alongside video compact disks (VCDs). According to U.S. industry estimates, total losses from copyright piracy in Indonesia during 2002 were nearly $260 million, the last year for which consolidated losses are available.

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, a lack of effective enforcement of patent rights continues. The patent law does not correct some of the weaknesses that concern foreign rights holders. Chief among these is the requirement that an inventor must produce a product or utilize a process in Indonesia to obtain a patent for the product or process. The standard for excluding inventions contrary to the public interest from patentability appears broader than the standards enumerated in the TRIPS Agreement.

Trademarks

Indonesia enacted its trademark law on August 1, 2001. The trademark law consolidated three prior laws enacted over 20 years. The law raised the maximum fine for trademark violations to Rp 1 billion ($120,000) and slightly reduced the maximum possible prison term. The 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. Indonesia's trademark officials' requirement that all trademark modifications be registered raises concerns under the TRIPS Agreement and the Paris Convention. 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 benefited some trademark holders. However, industry representatives had hoped courts additionally would use injunctions, especially in cases where a lower court eventually invalidates a false trademark registration.

SERVICES BARRIERS

Despite relaxation of some restrictions, particularly in the financial services sector, 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. In order to practice legally, lawyers must hold Indonesian citizenship and a degree from an Indonesian legal facility or other recognized institution. Foreign lawyers can only work in Indonesia as "legal consultants" and must first obtain the approval of the Ministry of Justice and Human Rights. A foreign law firm seeking to enter the market must establish a relationship with a local firm.

Distribution

In 1998-99, Indonesia liberalized portions of the distribution services sector under terms of its agreements with the IMF. The Indonesian government eliminated restrictive marketing arrangements for cement, paper, plywood, cloves and other spices. Indonesia has opened the wholesale and retail trade sectors to foreign investment. Since 1998, it has allowed 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. The film sector is not covered by this regulation. There is a ban on all foreign investment in media businesses, including cinema construction or operation, video distribution and broadcast services. Presidential decrees issued in July and August 2000 prohibit foreign investment in broadcast and media sectors, including the film industry (film making, film technical service providers and movie house operations). The decrees also prohibit foreign investment in the provision of radio and television broadcasting services, radio and television broadcasting subscription services and media print information services.

In October 2001, Indonesia passed a new Oil and Gas Law to deregulate downstream activities. Presidential Decree 86/2002 and Government Regulation 67/2002 establish a new Oil and Gas Downstream Business Regulating Board (Badan Pengatur Kegiatan Usaha Hilir Migas, or BPH Migas) to control downstream activities. Although the day-to-day activities of the board must still be defined through implementing regulations, BPH Migas will be 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.

Financial, Accounting and Banking Services

Under the WTO Financial Services Agreement, Indonesia committed to allow 100 percent foreign ownership for non-bank financial services companies that are publicly listed, including insurance and securities firms. Indonesia also guarantees the access of existing financial services firms in its market. It lifted restrictions on branching and sub-branching for joint venture banks and foreign branches in 1998.

Paid-in capital requirements are twice as high for multi-finance companies with foreign partners than for domestic multi-finance companies. However, in November 1998, Parliament passed amendments to the 1992 banking law that allow 100 percent foreign ownership of Indonesian banks. All insurance policies in Indonesia must be purchased from either domestic or joint venture companies unless specific coverage is unavailable in Indonesia or if the insured is a wholly foreign-owned entity. Under an Insurance Industry Association rule, supported within the GOI, Insurance companies are required to purchase a percentage of their reinsurance for earthquake coverage (5 percent for West Java and Jakarta and 25 percent elsewhere) from the local firm MAIPARK. There is discussion about soon expanding that requirement to coverage of floods.

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 prohibits foreign film and videotape distributors from establishing branches or subsidiaries. Under the Film Law, provision of importation and distribution services is limited to wholly-owned Indonesian companies. The film law contains a screen quota that gives priority to the showing of local Indonesian language films. However, this has not proven to be a serious barrier as few local films have been produced in recent years.

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

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. Telecom 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 Telecom 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. The requirement for a foreign satellite operator to have an Indonesian partner, however, perpetuates inefficiency, raises costs to Indonesian consumers, and constitutes a serious trade barrier. Indonesia also formed a telecommunications regulatory body in July 2004 to improve transparency in regulation development and dispute resolution.

Telecom 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 privatizations of its telecommunication 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.

Despite the autonomous liberalization that Indonesia has implemented, the government has yet to submit a revised telecommunications offer in the Doha Development negotiations in the WTO.

INVESTMENT BARRIERS

Indonesia's investment climate is poor. The World Economic Forum's 2003 competitiveness rankings scored Indonesia 97th of 102 countries. Foreign direct investment (FDI) has declined steeply since the 1997-98 financial crisis and in the last few years the numbers have been inflated by the inclusion of state-owned firms that were partially privatized. Government approvals for investment proposals reached $14.6 billion in 2003, $9.8 billion in 2002, an adjusted $9 billion in 2001, and $16 billion in 2000. Investment proposals from Asia, North American and Europe - traditionally large investors - declined from 2002. Most of this investment is never realized.

On January 1, 2001, Indonesia began to implement a large-scale decentralization of authority and budget from the central government to the provincial and district-level governments. Differences of opinion between the central and local governments about which has authority on certain issues has added to the level of uncertainty facing foreign investors. In many areas, even though contrary to law, local governments have instituted revenue-raising measures ("retribusi"), which are trade-distorting.

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 FDI projects and joint ventures with a minimum Indonesian equity of five percent. Currently, BKPM and other relevant agencies in certain sectors must approve proposed foreign investments, but under the proposed law, BKPM would be responsible for approvals in all sectors, including licenses, tax incentives, and business registrations. The Government is considering proposing a revised investment law to Parliament in 2005 that would streamline foreign investment approval procedures.

Indonesia blocks or restricts foreign investment in some sectors in addition to those service sectors mentioned above. These restricted sectors are described in the "negative list." The most recent version, issued in August 2000, is based on Presidential decree 96, which opened some sectors, particularly certain medical services, to foreign investment. The negative list restricts foreign investment in industries producing marijuana, certain environmentally harmful chemicals, chemical weapons, and alcoholic drinks, and it closes to foreign investment casino and gambling facilities, air traffic and marine vessel certification and classification systems, and radio frequencies. However, various infrastructure, airline, medical services, marine and fisheries, industrial, and other trade sectors are open to investment subject to joint venture or other conditions.

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. Indonesia's government expects to complete drafting of cyber crime and electronic transactions legislation in early 2005.

OTHER BARRIERS

Transparency

President Yudhoyono has stated repeatedly that eliminating corruption will be one of his Administration's top priorities. Nonetheless, a lack of transparency and widespread corruption are significant problems for companies doing business in Indonesia. Corruption was endemic under the former Soeharto regime, and still remains an enormous problem for foreign companies. These companies are concerned about demands for irregular fees to obtain required permits or licenses, government awards of contracts and concessions based on personal relations, and an often arbitrary legal system.

Many laws passed since late 1997 have established new institutions and agencies to respond to popular demands to address corruption, collusion, and nepotism, but poor implementation has undermined that effectiveness. Indonesia's government established stiffer penalties for corruption as well as an independent commission to investigate and audit the wealth of senior government officials. In December 2003, the government also established an Anti-Corruption Commission.

Automotive Policies

On June 24, 1999, the Indonesian government announced a major revision of its national automotive policies in order to rely on market forces to foster a more efficient and globally competitive automotive industry. The new policy eliminated extensive tariff and tax incentives for local content. The Indonesian government reduced the maximum tariff on automobiles from 200 percent to 80 percent. Tariffs on passenger car kits imported for assembly, which had ranged from zero percent to 65 percent, were reduced to 25 percent, 35 percent, 40 percent, or 50 percent depending on engine size. Tariffs on non-passenger car kits were reduced to a uniform 25 percent. Tariffs on auto components and parts imported for local assembly of passenger cars and minivans were changed to 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 are concerned about the high tariff of 60 percent (25 percent on knockdown kits), the luxury tax of 75 percent, and the prohibition on motorcycle traffic on tollways as barriers to the Indonesian market.

In December 2000, Indonesia's government restructured the way luxury sales taxes are imposed on motor vehicles. The luxury sales tax on 4,000cc sedans and 4x4 Jeeps or vans was raised from 50 percent to 75 percent. The luxury tax on automobiles with engine capacity between 1,500cc and 3,000cc was increased from 15 percent to between 20 percent to 40 percent, depending on the size of the engine. This decision had a significant negative impact on the market since 65 percent of the market share belongs to automobiles with engine sizes between 1,500cc and 3,000cc.