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In 1996, the U.S. trade deficit with Indonesia was approximately $4.2 billion, an increase of $167 million from the U.S. trade deficit of nearly $4.1 billion in 1995. U.S. merchandise exports to Indonesia were approximately $4.0 billion, an increase of $609 million (18.2 percent) from the level of U.S. exports to Indonesia in 1995. Indonesia was the United States' twenty-eighth largest export market in 1996. U.S. imports from Indonesia were slightly more than $8.2 billion in 1996, an increase of $776 million (10.4 percent) from the level of imports in 1995.

The stock of U.S. foreign direct investment (FDI) in Indonesia in 1995 was about $7.1 billion, an increase of 44.3 percent from the level of U.S. FDI in 1994. U.S. FDI in Indonesia is concentrated largely in the petroleum and manufacturing sectors.

IMPORT POLICIES

In recent years, Indonesia has liberalized its trade regime and has taken a number of important steps to reduce protection. Since 1996, the Indonesian Government has issued deregulation packages that have reduced overall tariff levels, simplified the tariff structure, removed restrictions, replaced non-tariff barriers with more transparent tariffs, and encouraged foreign and domestic private investment. The most recent of these packages were issued in January and June 1996.

Tariffs

Indonesia's applied tariff rates range from 5 to 30 percent. A major exception to this range is the 170 percent duty applied to all imported distilled spirits. In May 1995, the Indonesian Government unveiled a comprehensive tariff-reduction package covering roughly two thirds of all traded goods, designed to reduce most tariffs to under 5 percent by 2003. The package stipulated that all tariff items with a rate of 20 percent or less would be reduced to no greater than 5 percent by 2000, and items with rates of more than 20 percent would be reduced to no more than 20 percent by 1998, and 10 percent by 2003. However, some products in the automotive, chemical, metal, and agriculture sectors were excluded. This tariff reform generally extends Indonesia's commitments under the Association of Southeast Asian Nations (ASEAN) Free Trade Area (AFTA) on an MFN basis.

The deregulation packages announced in January and June 1996 advanced some of this tariff reform. The January 1996 package included a consolidation of the tariff code, reducing the total number of tariff lines by 22 percent, to a total of 7,284. This package also lowered tariffs on 428 items, primarily capital equipment, raw materials, and intermediate goods used by export industries. The June package detailed a schedule of tariff reductions on 1,497 items and eliminated import surcharges on a number of goods, although on 80 tariff lines the surcharge amount was folded into the tariff. The June 1996 package also contained immediate tariff reductions on 385 categories of capital goods. With the June package, Indonesia's average unweighted tariff is 12.2 percent, down from nearly 20 percent in 1994. In the Uruguay

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Round market access negotiations, Indonesia committed to bind 94.6 percent of its tariff items, mostly at ceiling bindings of 40 percent. Exceptions to the 40 percent binding include automobiles, iron, steel, and some chemical products. In accordance with the WTO Agreement on Agriculture, Indonesia has agreed to tariffy its non-tariff barriers on agricultural products. Some of the exceptions to the 40 percent tariff bindings are still heavily protected. For example, when the Indonesian Government lifted the import ban on completely built-up cars in 1993, the ban was replaced with duties of up to 200 percent and import surcharges of 100 percent. The import levies were decreased in a subsequent deregulation package, but tariffs of up to 125 percent are still compounded by import surcharges of up to 75 percent on completely built-up models. Indonesia has committed to remove import surcharges on items bound in the Uruguay Round by the year 2005. The pioneer auto program (see also "Investment Barriers") provides tax- and duty-free treatment for one designated company which uses a unique Indonesian-owned trademark.

All processed goods are subject to a 10 percent value-added tax. A luxury tax ranging from 20 percent to 35 percent is also levied on certain products.

Quantitative Restrictions

Many major bulk food commodities, such as wheat, rice, sugar, and soybeans, are subject to non-tariff barriers. The sole importer is the National Logistics Agency (BULOG), a state trading entity. Prices of these commodities are often higher than world market prices; sugar and soybean prices are about 40 percent higher than import parity prices. Rice and wheat flour prices are currently fairly close to world market prices. Other agricultural products are subject to local purchase requirements. Effective April 1, 1996, the government lifted the requirement that 20 percent of all soybean meal used by feedmills be purchased domestically, but a similar restriction remains in place for milk products. Under Uruguay Round commitments, dairy product protection must be phased out by 2003.

Import Licensing

The government continues to reduce the number of items subject to import restrictions and special licensing requirements. As a result of the January 1996 reform package, 203 tariff lines still remain subject to restrictive import licenses, down from 261 in 1994 and 1,112 lines in 1990. The January package reduced restrictions on imports of 23 tariff lines, including seven categories of steel products.

For goods that continue to be regulated, the following import license categories exist (number of affected tariff codes provided in parentheses): registered importers -- alcoholic beverages (27), milk products (7), hand tools (6); producing importers -- soy meal (4), salt (2), artificial sweeteners (3), propylene granules (2), iron and steel products (7), engines and pumps (5), tractors (3), knocked-down electronic keyboards (1), and scrap materials (57); approved importers/sole agents -- motor vehicles (47); BULOG -- garlic (2), wheat (3), rice (4), flour (3), soybeans (2), sugar (7); state oil company PERTAMINA -- lube oil (3); clove marketing board -- cloves (2); PT Dahana -- explosives (4). In accordance with Indonesia's WTO commitments, the non-tariff barriers on items not controlled by state trading agencies will be removed over a ten-year period.

STANDARDS, TESTING, LABELING, AND CERTIFICATION

In May 1990, the Indonesian Government issued a decree that states that the Department of Health must decide within one year of receipt of an application whether to grant registration for new foreign pharmaceutical products. In practice, registration can take much longer, although companies report the process is slowly improving. Foreign pharmaceutical firms have complained that copied products sometimes become available on the local market before their products are registered.

New maximum pesticide residues (MRLs) for all food commodities were announced in August 1996. These MRLs are largely consistent with the international CODEX standards. However, the government has not yet announced the details on exporter obligations to ensure that the MRLs are not exceeded. The United States has commented on the unworkability of Indonesia's WTO notification that shipment-by-shipment certification would be required.

The Indonesian Government also introduced a new broadly based food law in November 1996 and now is in the process of drafting implementing regulations. Early indications of the plans for these regulations has caused concern among U.S. and other exporters, particularly about how issues such as labeling (including "halal" certifications), product expiration, and advertising will be handled.

GOVERNMENT PROCUREMENT

In 1994, the government enacted a new procurement law to regulate government procurement practices and to strengthen the procurement-oversight process. Most large government contracts are financed by bilateral or multilateral donors each of which imposes its own procurement requirements. For large, government-funded projects, international competitive bidding practices must be followed. The government seeks concessional financing, which includes a 3.5 percent interest rate, a 25-year repayment period, and a 7-year grace period.

Some projects do proceed on less concessional terms. Foreign firms bidding on certain government-sponsored construction or procurement projects may be asked to purchase and export the equivalent in selected Indonesian products, but this rarely occurs. Government departments and institutes and state and regional government corporations are expected to utilize domestic goods and services to the maximum extent feasible, but this is not mandatory for foreign-aid-financed goods and services procurement. State-owned enterprises that have offered shares to the public through the stock exchange are exempted from government procurement regulations.

Foreign joint ventures are not eligible to tender for government pharmaceuticals procurement. The requirement that doctors employed in government institutions prescribe only listed generic drugs also prevents the procurement of foreign pharmaceutical products. Foreign companies are generally prohibited from competing in the generic drug market.

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EXPORT SUBSIDIES

As part of its June 1996 deregulation package, the Indonesian Government extended rediscount facilities for "special exporters" in certain industries, namely textiles and textile products, shoes, electronics, timber and rattan products, and leather goods. Eligible exporters may sell their export letters of credit or other instruments to the central bank, Bank Indonesia (BI), through foreign exchange banks. BI rediscounts the export drafts at SIBOR for special exporters and SIBOR plus one for general exporters. Through a decree issued on December 31, 1996, the Indonesian Government extended this rediscount facility to exporters of crude palm oil and its derivatives and pulp and paper products, as well as to "special suppliers" to the special exporters. BI also announced that it will rediscount in U.S. dollars, in addition to rupiah.

Companies producing 65 percent for export may apply for restitution of import duties paid on inputs that are subsequently re-exported in a finished form. Import-duty exemptions may also be granted for all capital equipment, machinery, and raw materials needed for the initial investment. Companies located in bonded or export-processing zones pay no duty until the portion of production destined for the domestic market is released, at which time duty is owed only on that portion.

LACK OF INTELLECTUAL PROPERTY PROTECTION

Although Indonesia is making progress in this area, it still provides inadequate intellectual property protection for patents, trademarks, copyrights, trade secrets, industrial designs, and integrated circuit layout designs. Under the "Special 301" provisions of the 1988 Omnibus Trade and Competitiveness Act, the U.S. Trade Representative raised Indonesia to the "priority watch list" in 1996, from the "watch list" where it had been since 1989. The Indonesian Government often responds to U.S. companies that raise specific complaints about pirated goods and trademark abuse, but the court system can be capricious, and punishment of pirates of protected intellectual property is very rare. New patent, trademark, and copyright laws, which were submitted to the Indonesian Parliament in December 1996, are designed to bring Indonesia's laws into compliance with the WTO Agreement on Trade-Related Aspects of Intellectual Property Rights. It is hoped that the laws will address many of the remaining legal deficiencies that pose problems for companies but it is unclear at this time whether they will.

Patents

Indonesia's first patent law went into effect on August 1, 1991. Several areas of concern remain, including compulsory licensing provisions, a relatively short term of protection (14 years), and a provision allowing the import of certain patented raw materials. In addition, concerns remain regarding Indonesia’s law and regulations on local working requirements and patent cancellation. Finally, the 1989 Indonesia patent law offers no "pipeline" protection. When enacted, the new patent law may address many of these concerns.

Trademarks

The April 1993 trademark law provides for determination of trademark rights by registration rather than by first use. The law provides for protection for well-known marks but offers no procedures or grounds for owners of well-known marks to clear the trademark register of existing registrations infringing on well-known marks. Currently, the only avenue for challenging existing trademark registrations in Indonesia is to bring a court challenge. Cancellation must be sought within five years from the date of registration. But U.S. companies have found it difficult to protect their well-known marks, since the judicial process can be very time consuming and unreliable. Injunctive relief apparently is not provided, even when a lower court invalidates false trademark registrations. The new trademark law may enhance protection by providing for administrative cancellation of registrations competing with well-known marks.

Copyrights

In 1987, Indonesia enacted amendments to its copyright law which generally brought it closer to conformity with international standards for copyright protection. A bilateral copyright agreement between the United States and Indonesia that went into effect in August 1989 extended national treatment to each other's copyrighted works. The Indonesian Government has demonstrated that it wants to stop copyright piracy and that it is willing to work with copyright holders toward this end. There is good enforcement of the ban on pirated audio and video cassettes and textbooks, but efforts to combat software piracy are still at an early stage. In 1996, rampant piracy of video compact disks (VCDs) developed in Indonesia. This is disrupting the market for cinemas, as well as sale and rental markets for videos and laser disks. Enforcement efforts targeting pirated VCDs have just begun.

New Technologies and Trade Secrets

Biotechnology and integrated circuit layout designs are not protected under Indonesian intellectual property laws. The government is in the process of preparing laws on trade secrets, industrial designs, and integrated circuits.

Indonesia is a member of the World Intellectual Property Organization (WIPO) and is a party to the substantive provisions of the 1934 London Text of the Paris Convention for the Protection of Industrial Property. Indonesia withdrew from the Berne Convention for the Protection of Literary and Artistic Works in 1959.

SERVICES BARRIERS

Despite some loosening of restrictions, particularly in the financial sector, services trade barriers to entry continue to exist in many sectors. Foreign accounting firms must operate through technical assistance arrangements with local firms, and citizenship is a requirement for licensing as an accountant. Foreign agents and auditors may act only as consultants and cannot sign audit reports. Foreign law firms cannot establish a practice in Indonesia, and graduation from an Indonesian legal faculty or an institution recognized as the equivalent is a requirement to be admitted to the bar. Foreign consulting engineers can only operate by forming a joint-venture with local partners in Indonesia.

Distribution

Distribution in the domestic market remains quite restricted. The June 1996 deregulation package included a first step in opening the distribution sector to majority foreign investment by allowing foreign firms with plants in Indonesia to import and sell complementary goods from affiliated companies. Majority-owned foreign plants may also sell their own products down to the wholesale level. An Indonesian agent or distributor must be employed for wholesale distribution if the foreign company does not manufacture in Indonesia. All retail distribution and sales must be handled by Indonesian firms or individuals.

A number of U.S. companies have expressed concern that existing restrictions increase costs and impede their ability to effectively market and service their products in Indonesia. Analysis has also shown that distribution barriers in Indonesia (which are more stringent than virtually anywhere else in ASEAN) reduce the efficiency of the Indonesian economy and increase prices for Indonesian consumers.

Financial Services

Insurance: In 1988, Indonesia opened several insurance subsectors to foreign participation. All foreign investment must be made through joint ventures; the minimum Indonesian ownership is 20 percent. Foreign joint ventures in the insurance sector must be capitalized at up to five times the level of domestic operations. In ongoing WTO negotiations in financial services, Indonesia has offered to phase out the differential in this capital requirement over time.

In January 1992, the Indonesian Parliament approved a framework law on insurance. The law stipulates that the insured individual is free to choose his or her insurer except in the case of social insurance programs. The Workers Social Security Act of 1992 states that only state-owned enterprises may carry out the Act's social insurance program.

All insurance in Indonesia must be purchased from either a domestic or joint venture company. The only exceptions are for unavailability of coverage in Indonesia and total foreign ownership of the insured entity.

Banking: Any new foreign bank must be a joint venture between an Indonesian bank and a foreign bank from a country that offers reciprocity; the Indonesian partner must supply at least 15 percent of the capital. The capital requirement for new joint venture banks is now about $49 million, twice the requirement for domestic banks. However, the Central Bank has issued a regulation that requires all foreign exchange banks, whether 100 percent domestic or foreign joint ventures, to raise their capital to $66 million by the year 2001.

Securities: Foreign securities firms may only enter the Indonesian securities market in a joint venture with an Indonesian firm; the Indonesian partner must have at least 15 percent equity participation. Foreign joint venture firms are also subject to discriminatory capital requirements: to obtain a license as a securities broker/dealer, underwriter/broker/dealer, or investment manager, paid-in capital required for a foreign joint venture is twice that for a local firm.

Motion Picture Market Access

Indonesia prohibits foreign film and videotape distributors from establishing branches or subsidiaries. All importation and distribution is restricted by the film law to 100 percent Indonesian-owned companies. Importation and in-country distribution of U.S. films must be handled through a single organization, the

European and American Film Importers' Association (AIFEA). Annual import quotas apply to foreign films and videotapes. Duties, taxes, licensing, and other necessary payments also act as barriers to the film industry.

Telecommunications Services

In the recently concluded WTO negotiations on basic telecommunications services, Indonesia made commitments for some basic telecom services. These commitments limit the number of operators allowed for certain services, such as the provision of domestic and international satellite and international telex/ telegraph services, which is limited to a duopoly, subject to future government review. PT Telkom has exclusive rights to provide long-distance service. Indonesia also imposes a limit of 35 percent on foreign ownership in the telecommunications sector. Indonesia has adopted the reference paper on regulatory principles.

INVESTMENT BARRIERS

The Indonesian Government is committed to increasing foreign investment and to reducing burdensome bureaucratic procedures and substantive requirements for foreign investors. The most substantial measure taken in this regard, was in June 1994, when the government dropped initial foreign-equity requirements and sharply reduced divestiture requirements. Indonesian law provides for both 100 percent direct-foreign-investment projects and joint ventures with a minimum Indonesian equity of 5 percent. In addition, the government opened several previously restricted sectors to foreign investment, including harbors, electricity generation, telecommunications, shipping, airlines, railways, roads, and water supply. Some sectors remain restricted or closed to foreign investment and are implemented through a “negative list.” These include retail trade, television and radio broadcasting, aircraft manufacture, logging, and wood processing.

In general, foreign capital investment is primarily governed by the foreign capital investment law, as well as by presidential and ministerial decrees. The Capital Investment Coordinating Board (BKPM) and other relevant agencies must approve all proposed foreign-manufacturing investments in Indonesia. Investment in petroleum extraction, mining, forestry, telecommunications, and banking is covered by specific laws and regulations and handled by relevant technical agencies. Joint ventures with a majority Indonesian share, or in which Indonesians own 45 percent of shares and in which at least 20 percent of total stock is sold through the Indonesian stock market, are treated as domestic companies for certain purposes. This includes the ability to borrow short-term working capital in rupiah from state banks.

Despite the central government's plans to reduce red tape, regional license requirements and other levies can also make investing difficult. Every foreign investment project requires presidential approval. In practice, this means that the approval of investment applications can be delayed for indeterminate periods of time.

In 1996, the Indonesian Government issued a regulation under which tax exemptions may be provided to certain companies. This "tax holiday" was apparently created to attract large investments which Indonesia believes it is losing to other countries in the region with better tax incentives. In October 1996, the government formed an interdepartmental team to develop criteria under which companies could qualify for this exemption, but as of January 1997, the team had not yet completed its work.

Pioneer Auto Program

In February 1996, Indonesia's president issued a decree modifying the existing, WTO-inconsistent auto policy to grant tax and tariff exemptions to wholly owned Indonesian companies that use a unique Indonesian-owned trademark. Only one company, PT Timor Putra Nasional, was designated under the program to be exempt from the payment of any tariffs and luxury taxes if it increased the share of local content in the vehicles it produced over a three-year period. In June 1996, the government conferred further benefits on PT Timor by issuing a decree allowing the company to import from Korea, tax- and duty-free, up to 45,000 units of the "pioneer" car, during the first year of operation. The United States, Japan, and the EU have each requested formal consultations with Indonesia under the WTO Dispute Settlement Understanding to address their concerns with Indonesia's auto program.

OTHER BARRIERS

Indonesia's wood products sector remains heavily protected. Earlier government prohibitions on the export of raw rattan, logs, and timber were replaced with prohibitively high export taxes in May 1992. High export taxes on sawn timber have been in place since 1989. The Indonesian Government's practices in the wood industry have acted as obstacles not only to entry into the Indonesian market but also into the third-country markets such as Japan and Europe where U.S. finished and processed wood products compete with Indonesian products.

Some companies benefit from restrictive licensing regulations that severely inhibit competition in a number of areas in the domestic economy such as cement, fertilizer, and household gas.