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# **An Evaluation of the Need for Selected Trade Facilitation Measures in Indonesia: Implications for the WTO Negotiations on Trade Facilitation**

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## *Executive Summary*

As a member of WTO, Indonesia has been involved in the discussions of the WTO Negotiating Group on Trade Facilitation (NGTF). This study aims to examine the current situation of trade facilitation in Indonesia, as well to assess the needs and priorities of various measures related to the trade facilitation negotiations.

Trade activities have been the engine of growth since the period of economic liberalization and trade reform in the 1980s and 1990s. As part of past and on-going reforms, Indonesia has implemented various trade facilitation measures currently discussed in the WTO TF negotiation. However, the degree of implementation of those measures needs significant improvement in order to provide simplified and harmonized procedures related to trade.

In relation to GATT Article X, most government agencies have launched various efforts to disseminate trade-related regulations and procedures. However, as there is no specific guideline for publication of relevant regulations, policy towards dissemination is sporadic. New regulations are not communicated well to stakeholders, while no formal mechanism is available that allow traders to provide comments and suggestions regarding trade rules and regulations. The exploratory private sector survey conducted as part of this study reveals that measures regarding publication of relevant regulations are of highest priority for trade facilitation improvement. Another utmost concern related to Article X is the need for certainty and uniformity in how trade procedures are implemented, which relates to the improvement of the integrity of officials.

The government of Indonesia introduced a number of programs in order to improve trade facilitation measures related to GATT Article VIII. This study shows that more simplified and automated trade procedures and required documentations are among the measures perceived as highest priority for improvement in trade facilitation. While formal fees and charges for services related to trade procedures are perceived to be quite reasonable, the existence of rampant illegal charges need to be addressed as it erodes Indonesian products' competitiveness. With regards to GATT Article V, Indonesia recognizes special treatment for goods in transit and exempts them from import duties payment and submission of importation or exportation documents.

Recognizing the current situation of trade facilitation in Indonesia, the government might need a relatively long timeframe of implementation for some of the measures under discussion at the NGTF (e.g., advance ruling facilities) so as to prepare necessary institutions and administrative arrangements. Capacity building may be particularly important for implementation of measures to improve coordination among authorities responsible for trade activities. External technical assistance that has more flexibility to act across different agencies will accelerate the government's program to improve coordination. Technical assistance might also be needed to develop an information system for traders and other stakeholders to learn about trade procedures and regulations.

While it is important to account for the technical aspects of trade facilitation and Indonesia's implementation capacity when negotiating at the NGTF, improvement in trade facilitation can be expected to bring significant benefits to Indonesia's trade

performance and the economy as a whole. Successful negotiation on trade facilitation at the WTO, including binding commitments on selected trade facilitation measures, will support the already on-going unilateral efforts for the improvement of trade related procedures and system.

## *Introduction*

During the last three decades, Indonesia has taken various important actions to open its market and liberalize its trade regime. Indonesia's trade policies have shifted from the import substitution strategy and agricultural protection regime in the 1970s and early 1980s to trade liberalization in the late 1980s. Since then, international trade activities have become important components in Indonesia's economy. Both exports and imports values have increased substantially, while the structure of exports has also changed dramatically.

Trade activities have been the engine of growth during the period of economic liberalization in 1980s and 1990s. The growth of exports and imports has been generally higher than overall economic growth at around 7 percent annually. Even in 1998, when overall economic growth declined by more than 13 percent, trade sectors, especially exports, still grew by more than 10 percent. Specifically targeted reforms to promote exports together with a sound macroeconomic management produced the on-going exports boom from the mid-1980s.

Drivers of liberalization in the early 1980s came from both internal and external conditions. The end of the oil boom in the early 1980s forced the Indonesian government to launch various strategies to diversify the economic base away from oil, using general export incentives and undertaking a substantive program of structural reforms. Numerous non-tariff barriers were abolished while tariffs were drastically reduced, especially those applied to imported input for export-oriented industries, while investment deregulations were introduced to support trade. In addition to the internal condition, Indonesia's active participation in several regional trade agreements and economic cooperation schemes, such as APEC and AFTA, as well as the multilateral ones, led to further liberalization in the first half of the 1990s.

The current average tariff rate of 6.9% is much lower than the average tariff rate in the mid-1980s, which reached 28%. Various other unilateral measures, such as customs deregulation and abolishment of various trade licenses, were introduced at the end of the 1980s to further liberalize and facilitate trade activities and to encourage non-oil exports. The development of the trade infrastructure was also a government priority. Several ports were equipped with modern logistic and transport facilities to make trade activities easier. However, the availability and quality of trade infrastructure, as well as exports and imports procedures, are still the main obstacles for further development in the trade sectors. The high cost of transportation and port services, together with lengthy and complicated trade procedures, contributed significantly to the non-competitiveness of Indonesian products during the time of crisis. Trade infrastructure bottlenecks and unsupportive trade procedures weakened Indonesia's trade performance and earlier competitiveness gained from trade liberalization.

This paper discusses the trade facilitation situation in Indonesia with regards to the WTO Trade Facilitation Agreement. Section 2 presents the development of trade facilitation initiatives that have so far taken place. Section 3 evaluates the current state of trade facilitation in Indonesia with regards to various measures currently discussed by the WTO Negotiating Group on Trade Facilitation (NGTF). Section 4 presents the result of a field survey conducted to provide insight on the needs and priorities of private sectors

towards the provision of trade facilitation in Indonesia. Section 5 discusses several implications of current trade facilitation situation in Indonesia and its possible position in the WTO negotiation. The final section presents concluding remarks.

## *1. Trade Facilitation in Indonesia*

### *1.1. Review of Literature*

While trade facilitation frequently refers to all measures that can be taken to facilitate and ease trade flows, there is no standard formal definition of trade facilitation. In a broader sense of the term, trade facilitation can be defined as any action intended to reduce transaction costs which affect the international movement of goods, services, investments and people. In this sense, the term covers all types of non-tariff measures to trade such as technical standard, sanitary and phytosanitary (SPS) and environmental-related regulation, as well as other domestic business climate related regulations and all types of infrastructure issues. In a narrow sense, the scope of trade facilitation is generally limited to customs procedures and related formalities involved in the movement of goods.

Several studies show that improvement on trade facilitation could lead to substantial economic gains. Wilson, Mann, and Otsuki (2003), suggest that raising capacity in broad measures related trade facilitation, such as customs, regulations and infrastructure across whole countries, could increase world trade by approximately \$377 billion dollars. Other studies that mostly try to evaluate the benefit of certain actions in facilitating trade also reveal significant benefit of those measures<sup>1</sup>.

As one founding member of APEC, Indonesia has committed to take several actions under the APEC trade facilitation framework, which has an objective of reducing transactions costs by 5 percent by 2006 through introduction of trade facilitation measures<sup>2</sup>. On the movement of goods, the APEC Trade Facilitation Action Plan identifies 11 main measures to be implemented by member countries in order to achieve the overall objective. Of all 65 actions and measures Indonesia has committed to improve, 50 of them are now under implementation. In terms of trade related procedures, Indonesia agreed to implement 39 actions, 30 of which have been implemented to improve trade procedures<sup>3</sup>.

Indonesia has also been actively involved in various initiatives to improve trade-related procedures under ASEAN's Customs Procedures agreement. While commitment to improve trade-related procedures and facilitate intra-ASEAN trade has been introduced since 1983 by commencing an ASEAN Customs Code of Conduct, the need to provide such facilitation gained importance in the view of the ASEAN Free Trade Area. Since 1997, ASEAN member countries, including Indonesia, agreed to carry out various efforts in order to harmonize trade procedures under the program called ASEAN Policy and Implementation Work Program (PIWP). The harmonization of tariff classification applied in all ASEAN countries is among the fifteen elements of PIWP. The next main agenda of customs cooperation in ASEAN is the creation of an ASEAN Single Window, which will

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<sup>1</sup> See for example APEC Report on paperless trading (2001) that estimate application of the method will reduce up to 15% transaction cost of imported items.

<sup>2</sup> APEC Economic Committee, 2004

<sup>3</sup> APEC Individual Action Plan for Indonesia, 2004

require the establishment of national single window systems in each member country. Indonesia is now preparing to set up a single window system at national level.

As a WTO member, Indonesia acknowledged various attempts to facilitate trade under the General Agreement on Tariffs and Trade (GATT). At this multilateral level, WTO recognizes trade facilitation as “the simplification and harmonization of international trade procedures” covering the “activities, practices and formalities involved in collecting, presenting, communicating and processing data required for the movement of goods in international trade”. WTO discussion on trade facilitation focuses on improvement and implementation of Articles V, VIII and X of GATT 1994.

### ***1.2. Major government initiatives and institutions involved***

The story of Indonesia’s trade performance cannot be separated from several major trade reforms that have taken place during the last two decades. Besides the elimination of several trade restrictions and the reduction of tariff barriers, the reforms also covered various measures of trade facilitation aiming to simplify export and import procedures.

Indonesia’s trade procedures underwent various significant alterations to respond to the needs of more dynamic trade activities. The first significant reform program came into effect in April 1985 when the government of Indonesia decided to hand over trade procedures and formalities to a Swiss Company, *Société Générale de Surveillance* (SGS). Allowing the company to conduct pre-shipment inspection (PSI) for imported goods at the point of origin sidelined the customs agency. This policy was introduced to simplify and streamline import procedures.

Pre-shipment inspection provided various functions. The main function was to ensure that the quantity and the price of goods to be imported were compliant with the associated documents and invoices. Additionally, PSI also provided other services, such as verification of the origin of goods, data collection and other related trade procedures. These procedures and formalities, such as valuation of imported goods and assessment of duties as well as direct payments of duties through financial banks, were conducted in a more efficient way than the previous arrangement, and reduced the chance for bribery or side payments for import clearance.

The success story of PSI procedures led the government to continue implementing

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