

WTO, REGIONAL AND BILATERAL TRADE LIBERALIZATION: IT'S IMPLICATION FOR INDONESIA

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I. Introduction

Foreign economic policy is now and has long been a strategic instrument used by great powers in their dealings with one another.¹ The practice of international trade among nations are no more than uses of foreign economic policy to realize goals other than solely those of maximizing the economic welfare of nations or interest groups. Rather, foreign economic policy is a tool by which governments can (and often do) pursue non-economic ends.²

The purpose of this Paper is to assess the implication of Indonesia's foreign economic policy, as reflected in the membership of the country in the multilateral as well as regional trading arrangement, and the involvement of the country as a third party in the USA – Singapore FTA bilateral trade relationship. This Paper is structured as follows. Part II provides information necessary to understand the legal and institutional framework for multilateral trade liberalization in Indonesia. Part III examines the implementation of the rights and the duties as consequences of the country membership in the WTO. Part IV takes into account of the brief history as a background of the establishment of the ASEAN Free Trade Area/AFTA. Part V describes the legal and institutional framework for regional trade liberalization in Indonesia. Finally, part VI delves deeper into the implication of two existing free trade frameworks in the vicinity area –regional and bilateral free trade agreements—for Indonesia.

I argue that the frozen Doha Round has been displayed in a temporary shift away from multilateral trading system, and lead the way into the increasing intra-regional, inter-regional or bilateral trade relationships; however, each of this trade liberalization is only resulted in positive implication if its outcome is trade creation, not trade diversion. Since the establishment of AFTA has not been improved specialization among its member countries, and the formation of the FTA has been failed to increase the comparative advantage among its members, in order to increase the benefit from the trade cooperation as well as to decrease the tension among the member countries, the regional free trade agreement should be extended into a

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¹ See Lars S. Skalnes, *Politics, Markets, and Grand Strategy: Foreign Economic Policies as Strategic Instruments 1* (2000).

² See *id.* at p. 10.

broader free trade agreement not only between AFTA and its main trading partners (e.g. USA, China, or Japan), but also between AFTA and other regional trading arrangement (NAFTA, or EU); however, the just trade cooperation among countries should not established base on a charity, in an asymmetric relationship. It should be founded stand on equality among its parties. The economic attainment opportunities of AFTA members should not be sacrificed by the political consideration in the establishment of ASEAN.

II. Legal and Institutional Framework for Multilateral Trade Liberalization in Indonesia

Indonesia ratified The Agreement Establishing the World Trade Organization (WTO) in November 2, 1994 by the Law No. 7/1994. The country has in principle been adopted a quite liberal foreign trade regime and taken a number of important steps to reduce protection. Up to date there is no import tariff exceeded Indonesia bound rates as stated on Indonesia Schedule of Commitment under WTO Agreements.³ As of January 2002, 67.4 percent of Indonesia's tariff lines were assessed import duties ranging between zero and five percent. Indonesia's average un-weighted tariff is 7.3 percent, compared to 20 percent in 1994, before the country membership in the WTO.

The applied tariff on all food products are zero since 1999, except the rice imports are subject to a specific tariff of 430 rupiah per kilogram (approximately 30 percent at an exchange rate of US\$ 1 = Rp 10,000),⁴ import duties on raw sugar are 20 percent and refined sugar 25 percent.⁵ In sum, Indonesia has liberalized its trade regime by issuing periodic deregulation packages that have incrementally reduced overall tariff level, simplified the tariff structure, remove restrictions, and replaced non-tariff barrier with more transparent tariff. Indonesia committed to remove import surcharges on items bound in the Uruguay Round by the year 2005.

Although there is a complain among several WTO members that Indonesia's applied tariff rates tend to be substantially lower than that it bound rates and the gap has widened since 1998 as a result of scheduled tariff cuts, this

³ WTO Trade Policy Review of Indonesia: Replies to Questions Raised by Argentina, 27 and 30 June 2003, p.1.

⁴ Rice is a strategic food commodity in Indonesia. Since poor people spends most of their income for food, the increase of 33% rice price in the country in the period of February 2005 to March 2006 drags more than 3.1 millions peoples into poverty, increases the poverty level from 15.97% (3,95 millions peoples) to 17.75% (30.05 millions peoples). See, *World Bank East Asia up Date November 2006*, The World Bank: 2006.

⁵ In December 27, 2002, the Coordination Meeting of the Ministries on Economic Affairs decided to impose a specific tariff of 510 rupiah per kilogram of imported rice.

Agus Brotosusilo: WTO, Regional and Bilateral Trade Liberalization

tendency shows Indonesia's seriousness to fulfill its commitment to trade liberalization in line with the WTO spirit.

There is growing a concern among the businessperson regarding the enforcement of the trade laws since the promulgation of the Law No.22/1999 and the Law No.25/1999 on Decentralization and Regional Autonomy. On January 1, 2001, Indonesia began to implement a large-scale decentralization of authority and finances from the central government to the province and district level governments. Since many of the technical guidelines related to these decentralization and autonomy laws have not yet been drafted, some regions have attempted their own interpretation on these two laws, and have then drafted their own local regulations based on their interpretation.⁶ Some of local regulations resulted in unnecessary trade barriers.⁷

Indonesia promulgated the free trade zones provisions by the Law No.3/1970. The Law followed by several Laws that specify free trade zones in a specific area, among others the Law No.10/1985, the Law No.36/2000, and the Law No.37/2000 that stated Sabang area and its port as a free trade zones.

Environmental requirement in Indonesian law has been imposed on imported product such as CFC material, pesticides, methyl bromide and hazardous waste disposal.⁸

In 1999, Indonesia promulgated The Law No.5/1999 regarding the Prohibition of Monopoly Practices and Unfair Competition, however, there are complains among several Businessperson that unsatisfied by the performance of Komisi Pengawas Persaingan Usaha/KPPU (the Oversight Commission for the Business Competition), due to the lack of expertise among some of its members. The lack of expertise among the member of

⁶ See Agus Brotosusilo: Rancangan Akademik Undang-undang Tentang Lalu Lintas Barang dan Jasa di Dalam Negeri (Indonesian Domestic Trade in Goods and Services Law: An Academic Draft). A Paper presented for Seminar on Domestic Trade in Goods and Services Law. Faculty of Law - University of Indonesia, in cooperation with the Ministry of Industry and Trade, Jakarta, March 1, 2002, p.4. Ryaas Rasyid, former Ministry of Internal Affairs and Local Autonomy, the drafter of the Law No.22/1999 and the Law No.25/1999 on Decentralization and Regional Autonomy is in opinion that the implementation of the Law No.22/1999 and the Law No.25/1999 on Decentralization and Regional Autonomy should be supported by hundreds of Government and Presidential Decree. He affirmed that for Government affairs only the local governments need more than 190 Presidential Decree for their guidance.

⁷ USAID, Partnership for Economic Growth, and Departemen Perindustrian dan Perdagangan RI. *Domestic Trade, Decentralization and Globalization: conference Papers*. Jakarta, USAID, Partnership for Economic Growth in cooperation with Departemen Perindustrian dan Perdagangan RI, 2001.

⁸ WTO Trade Policy Review of Indonesia: Replies to Questions Raised by Brazil, 27 and 30 June 2003, p.11.

KPPU was the result of the improper recruitment that more political-laden than expertise-base consideration.⁹

In the same year, Indonesia enacted the Law No. 30/1999 on Arbitration that provides for non-discriminatory trade disputes resolution through international bodies or through local bodies in conformity with international law. Indonesia also adopted the Convention on the Recognition and Enforcement of Foreign Arbitral Award, 1958 (The New York Convention) by Presidential Decree No. 34/1984.

III. Multilateral Trade Liberalization in Indonesia¹⁰

A. Supports for Multilateral Trade Liberalization

1. Government Support

The support for trade liberalization from the government is relatively strong in Indonesia. Indonesia not only has been liberalized its trade regime, but the country also taken a number of important steps to reduce protection. There are several high level Government officials that recognize the importance of international trade and foreign investment. The government not only has been created an environment generally supportive of liberalized trade --such as lowering tariffs and reduces non-tariff trade barriers--, but it also has been issued reform decrees that stipulate the reduction of taxes, tariffs and quantitative restrictions on exports and imports. The Indonesia government continues to reduce the number of products subject to import restrictions and special requirement. 1412 tariff lines are now subject to import licensing, reduced from 261 tariff lines in 1994 and 1,112 in 1990. Alcoholic beverages, lubrications, and explosives, and certain dangerous chemicals compound continue to be subject to special import licensing regulations.

The government not only actively seeks to improve the participation of the country in multilateral trade agreements, but also to include the country into the regional trade agreement (e.g. ASEAN Free Trade Area/AFTA). The government actively seeks to enforce liberalization provisions of existing multilateral as well as regional trade agreements.

⁹ See "Research on Business Actors' Awareness on the Enforcement of the Competition Law and Awareness on the New Commission", an Executive Summary, pp. 52-53. The research conducted by USAID, Georgetown University, PEG, Partnership for Business Competition, and Pusat Studi Hukum & Kebijakan Indonesia, Jakarta, 2000.

¹⁰ Most of the information in this part is base on a research conducted by Agus Brotosusilo, Riyatno, Yetty K. Dewi and Rudy, in August 2003. The research is a part of "Commercial Legal and Institutional Reform (CLIR) Assessment", cooperation between Graduate Program in Law - University of Indonesia and USAID.

2. Improvement of Laws

In order to reduce the legal uncertainty in the country, Indonesian government actively seeks to improve transparency. The government offices provides copies of laws, regulations, instructions, application forms and similar subsidiary instruments readily available to the business community or other end user, however, the community complained that there is no one-stop information-centre publicly accessible to look for regulations issued by the government.

The government providing the business community with a meaningful notice and an opportunity to comment on draft laws or legislative amendments affecting trade. It is also providing the community with meaningful notice of and opportunity to comment on draft implementing regulations. Regarding formal mechanisms for soliciting input from the business and professional community for formulating and amending trade policy, there are still complaints from some business community that the government does not represent their interests when it creates regulations with respect to their sectors.

3. Private Sectors

Indonesia not only has a very promising economic opportunity (abundance natural resources, prospective market), but also rest on a very high level political stability (the 3rd biggest democratic country in the world), however, the country has been suffered from legal uncertainty. The business and professional communities in Indonesia perceive the legal and regulatory environment generally to be confusing, especially because there are many regional regulations, which sometimes overlap with the previous-centralized regulations applied. There is also regulations-inconsistency (contradictory) not only in the decision making of the regulations but also in interpreting them within the ministries. The communities are in opinion that major laws and regulations not only tend to be difficult to predict, but also lack of consistency in interpretation and enforcement. In addition, major laws and regulations tend to be lack of transparency for end users.

Most of the business and professional communities perceived the law and regulations issued by the government to be relatively not really precise in that they can be generally read and understood by a business person (or any other end user), and provide adequate indication of what is required there under. Most of the communities perceived that the law and regulations issued by the government to be relatively not complete in that they address the main needs of the business community and do not contain significant gaps. Since many of the regulations are not in detail, it is not uncommon that it creates many interpretations.

Most of them perceived that the law and regulations issued by the government to be relatively not responsive to their needs as reflected in "favorable" (pro-business) policy measure. The communities generally feel that they do not have a meaningful role to play in shaping policy reform in area of trade. This phenomenon is reflected in the fact that they already tried to give some inputs to the government in shaping policy reform especially in trade area, however, up to date there is not much improvement as a result of this effort.

The business and professional communities generally feel that the state is not really effectively meeting basic needs for legal reform in the area of trade because most of the legal reform seems as the result of the pressure given by the International society, such as IMF, and World Bank.

4. Demand for Effective Implementing Institutions

The existence of effective implementing institution is crucial in order to realize the goal of foreign economic policy to maximize the economic welfare of the nation. In Indonesia, both business community as well as officials of implementing institutions affirmed the existence of one or more high level government officials with responsibility for implementation champion the cause of more efficient and effective provision of services by the implementing institution.¹¹ The business community and officials of implementing institutions confirmed that several international lending institutions (e.g.: UNDP, ADB, World Bank) and donor agencies (e.g.: USAID, CIDA) have instituted assistance programs with the government to upgrade and improve the implementing institution, however, the assistance programs is not always meet their actual needs. Basically, the donor agencies hesitate to assist Indonesia in the skill that improves the ability of the country to improve its active participation in the WTO, especially if the skill led to increases the competitiveness of the country.

Professional associations, trade organizations and special interest groups that favor liberalized trade in the country actively pressure the implementing institution more actively than protectionist groups to apply the laws in a manner favoring their positions. In addition, the business community stated that in service areas where the implementing institutions are weak, the private sectors offers competing or replacement services to fill the gap.

Despite most of business community perceive that they are well represented by trade and special interest groups, however, they fell that their aspiration is often not accommodated by government, neither in trade policy-making nor in multilateral as well as regional trade negotiation (WTO, APEC and AFTA).

¹¹ The last Indonesia Trade Policy Review by the WTO was conducted at 27 and 30 June, 2003.

5. The Effectiveness of Implementing Institutions

The effectiveness of the implementing institution mostly depends on the quality of the person in charge in the institutions. The Indonesian officials of implementing institution stated that the institution actively utilize an internal plan. The officials affirm that the implementing institution provides a written basis for all decisions made based on existing, published law. They also confirmed that the implementing institution makes all regulations, forms, applications and other important documents and information's available to the end users. In contrary, most of business community confirmed the opposite opinion.

Despite the officials of implementing institution not only confirmed that the institution actively utilizes a system of accountability, but they also affirmed that the institution actively utilize a feedback mechanism, however, most of business community affirmed the opposite notion.

6. The Role of Private Sectors

Some of the Indonesian business community confirmed that the provision of services and execution of functions is not satisfactory because the implementing institution supplies services are not transparent. In contrary, the other business community confirmed that the provision of services and execution of functions is satisfactory because the implementing institution supplies services are non-discretionary.

The business community confirmed that the provision of services and execution of functions is not satisfactory because the implementing institution supplies services are discriminatory. The community also confirmed that the provision of services and execution of functions is not satisfactory because the implementing institution supplies services are at unreasonable price.

The end-users of the implementing institution fell that they do not have adequate opportunities to provide feedback to the institution on its performance. The general business and professional communities consider decisions made by the implementing institution to be unpredictable. The general communities consider decisions made by the implementing institution to be not appropriate under existing law. Not only they are considering decisions made by the implementing institution to be not understandable, but also the general business and professional communities consider decisions made by the implementing institution to be not supportive of liberalized trade.

Persons of the private sector stated that they do not create supporting

institutions as needed to provide services required for effective trade and a trade environment in the area of professional associations. The persons stated that they do not create supporting institutions as needed to provide services required for effective trade and a trade environment in the area of specialized services. They also stated that they do not create supporting institutions as needed to provide services required for effective trade and a trade environment in the area of trade and special interest group.

The business community generally considers the supporting institutions for subject matter area to be not adequate in facilitating or supporting the implementation of the framework law in terms of number of institutions. The community considers the supporting institutions for subject matter area to be not adequate in facilitating or supporting the implementation of the framework law in terms of quality of institutions. There is no sufficient mass of private sector associations supports free-market trade principles to counterbalance protectionist groups.

The role of the Indonesian business community in the trade law reform is really ambiguous. Despite byword they always emphasize the demand for legal reform in order to improve the business climate, however, most of the national top level businesspersons reject the challenge to join in the legal reform struggle, even if just participate as a respondent to the research on the related field.

Since the structure of Indonesian economic has been characterized by conglomeration and highly corrupt, collusive, and nepotistic practices, joint into the legal reform does not seem as the best choice for the opportunistic businesspersons. The more highly the level of corrupt, collusive, and nepotistic business climate, the easier for the opportunistic rent seeking businesspersons to get the profit in the shortest time. Up to date, more than last three decades Indonesian economic strongly influenced by the habit of the corrupt, collusive, and nepotistic action. Among the action, the most destructive practice is the collusion between the high rankings of the government officers with the top level of the businesspersons. This collusion practice has been lead into to the catastrophic multi-dimensional crisis in the country.

7. Abolition of non-tariff barriers

Since 1997, Indonesia has dismantled many formal non-tariff barriers. In September 1998, the Indonesia Government sharply curtailed the role of the National Logistics Agency (BULOG), which had been the sole importer and distributor of major food commodities, such as wheat, sugar, rice, and soybeans. BULOG is now an independent body with the responsibility of maintaining stocks for distribution to military and low-income families and

managing the country's rice stabilization program. BULOG is no longer entitled to use credit liquidity from the central bank.¹²

The remaining quantitative limits apply to wines and distilled spirits. The Government of Indonesia restricts import of alcoholic beverages to three-registered importer, including one state-owned enterprise. The import duty for the product is 170 percent, a 10 percent VAT and 35 percent luxury tax. These restrictions are imposing in order to protect the Indonesian people from moral hazards.

The Indonesia government continues to reduce the number of products subject to import restrictions and special requirement. 1412 tariff lines are now subject to import licensing, reduced from 261 tariff lines in 1994 and 1,112 in 1990. Alcoholic beverages, lubrications, and explosives, and certain dangerous chemicals compound continue to be subject to special import licensing regulations.

As a notable exception, though the Government of Indonesia does not impose an imports banning of chickens in the whole form however, the country continues to maintain a ban on imports of chicken parts, which the Directorate General of Livestock Service imposed in September 2000. Despite the efforts of several ministries to repeal the ban, the Ministry of Agriculture continues to insist that it is necessary to assure consumers that imports are halal (produced in accordance with Islamic practices).¹³

In the services sectors, even though there are relaxation of some restrictions, however, services trade barriers to entry continue to exist in many sectors, e.g.: legal services, distribution, financial-accounting and banking services, audio-visual, construction-architecture and engineering, and telecommunications services.

Standardization is not an instrument of non-tariff barrier to trade in Indonesia. Most of Indonesian standards are voluntary, and only several are mandatory. Most of the mandatory standardization has done into effect due to health, security, environment and safety reasons among others iron, helm, passenger car tire, fertilizers, fortified flours, iodized salt, and sealed water drinking. As a comparison, not mention the US Bio-terrorism Act of 2002 or the similar instrument of 2003 European Food Safety Legislation, traditionally in the USA standardization is utilizes as an instrument of non-tariff barrier to trade. In the country there are more than 2700 State and Municipal authorities require particular safety certifications for product sold or installed

¹² US Foreign Trade Barriers, 2002: Indonesia, p. 187.

¹³ The US system of Halal certification was reviewed by an Indonesia team in 2000, but since then, Indonesia frequently experienced that the non-halal chicken parts have entered the local market. See: WTO Trade Policy Review of Indonesia: Replies to Questions Rose by USA, 27 and 30 June 2003.

within their jurisdictions. The problem of excessive reliance on mandatory certification in the USA, contrary to the background of an international trend towards deregulation or the minimizing of third party intervention in the regulatory process, experienced by the country due to the continued reliance on third party conformity assessment procedure for many industrial products.¹⁴

Since January 2001, Indonesia regulations required labels identifying food containing "Genetically Engineered" ingredients and "Irradiated" ingredients. However, as of January 2002, implementation is pending until the government determines a threshold-presence level. If the government chooses to enforce strictly the regulation, import of approximately \$210 million in soybeans and soybean meal would be affected.¹⁵

8. Trade Defense Instruments

In 1995 Indonesia enacted the Anti-dumping and countervailing duty provisions by the Law No.10/1995. Indonesia Antidumping Committee (KADI) has conducted its investigation in accordance with Article VI-GATT 1994. Since 1996, KADI had imposed a definite measure on 12 cases and 13 cases terminated for various reasons.

The Government of Indonesia enacted the safeguard provisions by Presidential Decree number 84 dated 6 December 2003 regarding the Safeguard of the Domestic Industry Against the impact of Increased Imports. The safeguard provisions is supported by the Decree of Minister of Industry and Trade of the Republic of Indonesia No. 84/MPP/Kep/2/2003 dated 17 February 2003 establishing the Committee of Trade Remedy of Indonesia or Komite Pengamanan Perdagangan Indonesia (KPPI), and Decree of Minister of Industry and Trade of Indonesia No. 85/MPP/Kep/2/2003 dated 17 February 2003 laying down Procedures and Requirements of Application for Investigation with respect to Safeguarding Domestic Industry from an Increase Import. This supporting legislation lays down the institutional frameworks required. KPPI had imposed a safeguard action on import of ceramic tableware in May 5, 2005;¹⁶ however, the action has been criticized as a "non WTO consistent".¹⁷

¹⁴ Report on United States Barriers to Trade and Investment, European Commission, Brussels, July 2001, p.19.

¹⁵ US Foreign Trade Barriers, 2002: Indonesia, p. 190.

¹⁶ The safeguard action has been taken on import of ceramic tableware originating from China, Hongkong, India, South Korean, Singapore, Japan, Taiwan, Thailand, Italy, Great Britain, Malaysia, USA, Germany, Australia, and French.

¹⁷ Agus Brotosusilo: Globalisasi Ekonomi dan Perdagangan Internasional: Studi Tentang Kesiapan Hukum Indonesia Melindungi Produksi Dalam Negeri Melalui Undang-Undang Anti Dumping dan Safeguard (Economic Globalization and International Trade: Research on the Preparedness of Indonesian Law to Protect the Domestic Industries Through Safeguards and Anti-dumping Law), Fakultas Hukum Universitas Indonesia, Dissertation, 2006.

B. Implementing Institutions

1. Organization

Traditionally, the institution responsible for implementation of laws relating to trade (on goods) is the Ministry of Industry and Trade. Since the WTO Agreements expands the scope of the trade, not only limited to Agreement on Trade in Goods, but also covers: General Agreement on Trade in Services; Agreements on Trade-Related Intellectual Property Rights; and Agreement on Trade-Related Investment Measure, the membership of Indonesia in the WTO resulted in division of power among several ministries and institution responsible for implementation of the WTO agreements. The Ministry of Justice is responsible for the implementation of Agreements on Trade-Related Intellectual Property Rights; The Ministry of Finance and Indonesian Central Bank are responsible for the implementation of General Agreement on Trade in Services; and State Ministry of Investment is responsible for the implementation of Agreement on Trade-Related Investment Measure. However, the Presidential Decree No.102/2001 clearly defines mandate to the Ministry of Industry and Trade as an institution responsible for implementation of laws relating to trade. The internal regulations and operating procedures are set forth in the Ministry of Trade Decree No.86/MPP/2001. The officials of the Ministry stated that the Ministry of Trade has a sufficient authority, mandate, funding, internal regulations, operating procedures, an active staff, and development program to carry out its mandate. In contrary, respondents from the Chamber of Commerce as well as Business Associations affirmed the opposite answers for sufficiency of funding, and an active staff and development program to carry out its mandate.

Despite the officials of the implementing institution affirmed the adoption of "customer-oriented" approach by the institution, however, the contrary answers between the implementing institution and most of business community reveal again regarding the general consistency in understanding the implementing institutions role and functions among the government and the end user.

Based on the Law No.22/1999 and the Law No.25/1999 on Decentralization and Regional Autonomy the roles and functions of the implementing institutions are sufficiently decentralized to enable users throughout the country to have reasonable access. In addition, the Ministry of Trade has an active, current web site, at least for the purpose of monitoring and disseminating the dynamics of the daily price of major food commodities through out the country.

2. Operations

The implementing institution, through Indonesia representative in the WTO, actively monitors level of compliance with the terms of WTO accession

requirement and other trade agreement. The institution also actively pursues increased compliance with trade agreements. The Ministry of trade also maintains active contacts with counterpart organizations in other countries to ensure compliance with international standards.

Most of business community stated that the implementing institution does not distribute (or make available for a nominal fee) copies of all procedures, relevant laws, government regulations, fee schedules and other information governing trade and related activities.

The business community affirmed that Indonesia has no a special unit established mechanism to provide protection for private sector enterprises from unfair trade practices through enforcement of defensive instruments. The country also has no a special unit enforces the laws in a non-discretionary, non-discriminatory, consistent and transparent manner even when decisions will result in a negative impact on domestic enterprises. The private sector business does not generally consider the special unit to provide satisfactory protection from unfair trade practices.

Most of business community stated that the implementing institution does not provide import and export licenses transparently in accordance with published standard. The community also affirmed that to obtain import and export licenses are not free of bribes or other inappropriate rent-seeking behavior.

C. Supporting Institution

1. Government entities

Custom office as the supporting institution in international trade has clearly defined mandate to implement the trade laws (Act No. 10 Year 1995 on Custom). The office not only has sufficient professional and administrative staffing to carry out its mandate, but also it has sufficient authority and support to carry out its mandate, including clear policy statements and support from the government. The office has detailed internal regulations and operating procedures and an active staff training and development program utilizing appropriate training materials, guidebooks or procedural manuals to improve staff competency and service. But some customs officers affirmed that the office does not have sufficient funding through state budget, fees collected, or a combination of both to maintain its equipment and services.

The custom service interprets and applies custom laws uniformly throughout the territory. It is provided at general explanation of the Act No. 10 Year 1995 on Custom. The office has implemented a risk profiling system in which less than 50% of shipments are inspected and proceeding delay for overland shipments through land border posts averages less than 2 hours. The

customs office main operations have been computerized and networked. It applies a "customer-oriented" approach to fulfilling its mandate; however, most of the staffs do not have international inspection certificates.

Among the government, the Custom Service and end users, there is general consistency in understanding the Custom Service's role and functions. The Custom Service has an active, current web site, including contact information, trade legislation and policy papers, and other relevant materials.

2. Courts

Most of business community affirmed that the Courts and other relevant administrative bodies in adjudicate disputes involving foreign investor neither without regard to the nationality or residence of the litigant, nor in accordance with clear, published laws, regulations, and standard. The community also confirmed that the Court does not consistently adjudicate appeals from administrative decisions in a transparent, impartial manner. They also concluded that the Court does not make decisions regarding trade issues independently, since it is not uncommon that inappropriate political pressure or non-judicial considerations determines the decisions.

A pervasive lack of transparency and widespread corruption are significant problems for company doing business in Indonesia. Many of the new laws passed since late 1997 have established new institutions and agencies to respond to popular demands to deal with corrupt, collusive, and nepotistic practices. Law No.28/1999 established stiffer penalties for corruption and an independent commission to investigate and audit the wealth of senior government officials. Law No.31/1999 established an Anti-Corruption Commission. The press has reported a number of high profile corruption cases from the last 5 (five) Presidential Administrations; however, to date, few individuals have been prosecuted and of those, even fewer convicted. In sum, the Judiciary System is often arbitrarily.¹⁸ In some of the international trade dispute cases, the courts decisions influenced by the 'non-judicial' factors.

3. Professional Association

There are no specialized groups of lawyers' association dedicated to trade law issues except the Indonesian Capital Market Lawyer Association. Lawyers generally do not examine trade law issues and promote better understanding of market-oriented trade policy since there are no many lawyers who really understand about the international trade issues.

¹⁸ US Foreign Trade Barriers, 2002: Indonesia, p. 196.

4. Specialized Services

Inspection services are provided on a reasonable cost basis to importers and exporters. Despite most of the official are not yet internationally accredited, however, the inspection services is using international standard in the inspection and certification.

Sufficient facilities are maintained at land border posts to conduct on-site health, safety, and environmental inspections. There is also a well-developed industry of freight forwarders and customs brokers in the country.

Importer and exporters are generally not satisfied with the quantity, quality, and cost of bond warehouses and warehouse service. While the price is not reasonable, the safety in warehouses is questioned, and the services are not professional. When goods belong to Importer and exporter in warehouses lost, warehouses deny to responsible for the lost, that's why the importer and exporter are not satisfied with the quality of services.

Government provide trade forms (customs document, bills of lading, certification), which are printed and readily available locally, or when they use freight forwarders services, freight forwarders will provide trade forms for exporters and importers. Experienced local consultants and service providers are available to assist with trade mission, marketing and other trade promotion activities.

Local financial institutions offer trade finance to domestic importers and exporters on reasonable terms through the letter of credit facility that commonly used by business communities in international trade. Local insurance agencies provide insurance on imports and exports at reasonable commercial rates in accordance with international standards. Every general insurance company in Indonesia provides the Marine Cargo Insurance. This type of insurance will cover risks of the goods imported to or exported from Indonesia. Most of the Indonesian insurance companies have been using and regulating its business practices in accordance to the International Insurance Standard governed by the London market at Lloyd's, England.

IV. Historical Background of The Establishment of the ASEAN Free Trade Area/AFTA

Asean Free Trade Agreement/AFTA has been established based on Tokyo Round enabling clause, not founded on Article XXIV: 8 (b) of the General Agreement on Tariffs and Trade.¹⁹

¹⁹ Article XXIV: 8 (b) of the General Agreement on Tariffs and Trade stipulated:

"A free trade area shall be understood to mean a group of two or more customs territories in which the duties and other restrictive regulations of commerce ... are eliminated on substantially all the trade between the constituent territories in products

The formation of free trade agreements among regions differ considerably with respect to their objectives, country composition and scope.²⁰ The objectives of the RTAs reflected the motivation behind the formation, which are various from the commercial (EU-Mexico FTA), economic (Australia-New Zealand Closer Economic Relations Agreement), strategic (EU), political economy (EU-Mercosur and EU-Chile negotiations) perspectives, or combination of these factors (NAFTA).²¹ AFTA was created in order to strengthen the political ties among the ASEAN members. The trade agreement was not purely based on economic consideration, since UNSP comtrade database shows that most of the AFTA members merchandise trade is similar, not only in kind of commodities, but also in export destination.

The embryo of AFTA was the trade cooperation agreement among the original member of ASEAN to establish the ASEAN Preferential Trading Arrangements/PTA, sign in Manila on February 24, 1977. The cooperation was improved by the Protocol on Improvements on Extension of Tariff Preferences under the ASEAN Preferential Trading Arrangements/PTA, sign in Manila on December 15, 1987.²² The PTA was based on Tokyo Round enabling clause, which allow the GATT members to create a preferential trading arrangement.²³

AFTA was established by Singapore Declaration of 1992 on January 22, 1992 by 6 (six) original member of ASEAN (Brunei Darussalam, Indonesia, Malaysia, Philippine, Singapore, and Thailand).²⁴ The declaration applied the Common Effective Preferential Tariff (CEPT) Scheme on 15 products,²⁵ and extended to non-processed agriculture product. According to the scheme the import duty for the products will be reduced to 0 – 5 % within 7-10 years, not 15 years as the normal tariff reduction.

originating in such territories.”

²⁰ See Gary P. Sampson and Stephen Wollcock, ed.: *Regionalism, Multilateralism, and Economic Integration: The Recent Experience*. United Nations University Press, Tokyo, 2003, p. 10.

²¹ Ibid., p11.

²². *Interpretative Notes to the Agreement on the CEPT Scheme for the AFTA, Article 1: Definition*.

²³ Paul J. Davidson, *the Legal Framework for International Economic Relations*. Singapore: Institute of Southeast Asian Studies, Heng Mui Keng Terrace Pasir Panjang, 1997., p. 84.

²⁴. *Fourth ASEAN Summit, Singapore, 27-28 January 1992, Documentation: Annex I*.

²⁵ The product covered in the scheme are: vegetable oil; cement; chemicals; pharmaceuticals; fertilizer; plastics; rubber products; leather products; pulp; textiles; ceramic and glass products; gems and jewelry; cooper cathodes; electronics; and wooden and rattan furniture.

Based on the 36th ASEAN Economic Minister (AEM) 3-5 September 2004 agreement tariff reduction, the import duty for 98.62% of 6 (six) initial ASEAN member's (Indonesia, Thailand, Brunei Darussalam, Malaysia, Filipina, and Singapura) total products covered by CEPT-AFTA was deducted into 0% - 5%. In reality, the implementation of AFTA often conflicts with the national interest of each member. It put the high cost investment of Malaysian automotive manufacture "Proton" into crucial dilemma, since the product unable to reach the ASEAN market not only because some of the AFTA member countries produce a more competitive –in price as well as in quality-- products, but also due to the tariff peak has been retained by some AFTA members on this sector. Philippine cancelled its commitment to liberalize its petrol-chemicals. Indonesia in the September 2004 propose to include sugar –formerly in the "normal track" category--, into highly sensitive list (HSL) category, however, the proposal strongly opposed by Thailand, since most of Indonesia sugar has been imported from the country.

V. Legal and Institutional Framework for Regional Trade Liberalization in Indonesia

In 1995 the Government of Indonesia signs the Protocol to Amend the Agreement on the Common Effective Preferential Tariff (CEPT) Scheme for the ASEAN Free Trade Area (AFTA) by the Presidential Decree No. 85/1995.

Indonesia also fully implemented the final stage of its commitments under the ASEAN Free Trade Agreement (AFTA); however, the country has expressed its reservations about the pace of liberalization within AFTA, which is much more liberal than WTO Agreements (WTO Plus).²⁶ As an illustration, on services sector in ASEAN there is a principle of "GATS Plus" which means the commitments under ASEAN should be more liberal than under the WTO. In general, Indonesia commitments under ASEAN Framework Agreements on Services (AFAS) consist of widening and deepening of existing commitments under WTO.²⁷

In January 1, 2002, Indonesia implemented the final phase of the ASEAN Free Trade Area (AFTA). Indonesia has reduced tariff for all products included in its original commitment (7,286 tariff lines) to five percent or less for product of at least 65 percent ASEAN origin.

²⁶ Wollcock describes WTO-plus as an RTA which applies non-discrimination principle beyond the obligations undertaken in the WTO. He stresses that RTAs may create regional preferences if they do not extend non discrimination (most favoured nation and national treatment) to third countries. See Stephen Wollcock: "A Framework for Assessing Regional Trade Agreements: WTO-plus", in Gary P. Sampson and Stephen Wollcock, ed.: *Regionalism, Multilateralism, and Economic Integration: The Recent Experience*. United Nations University Press, Tokyo, 2003, p. 19.

²⁷ WTO Trade Policy Review of Indonesia: Replies to Questions Raised by Argentina, 27 and 30 June 2003.

VI. Regional and Bilateral Trade Liberalization And it's Implication for Indonesia

The frozen Doha Round has been displayed in a shift away from multilateral trading system, and lead the way into the increasing regional or bilateral trade relationships, however, regional or bilateral trade liberalization is only resulted in positive implication if its outcome is trade creation, not trade diversion. The regional as well as bilateral trade arrangement can be acts as building blocks for the multilateral trade liberalization if resulted in trade creation. On the contrary, the regional or bilateral trade arrangement acts as a stumbling blocks for the multilateral trade liberalization if resulted in trade diversion.

The trade creation most likely to occur in the trade among countries which are complementary, however, UNSP comtrade database shows that most of the AFTA members merchandise trade are similar, not only in kind of commodities, but also in export destination. Since the establishment of AFTA has not been improved specialization among its member countries, the formation of the FTA has been failed to increase the comparative advantage among its members. The database also has been shown that the flow of trade among ASEAN countries since the establishment of AFTA in 1992 to date has not shown any significant increase, as shown in table 1.

Table 1: Indonesia Export to ASEAN

| Ekspor-Impor | | | | |
|--|-----------------|-----------------|------------------|-----------------|
| Tabel 1 | | | | |
| Pangsa Pasar Ekspor Produk Indonesia | | | | |
| di Beberapa Negara ASEAN (Dalam persen) | | | | |
| Tahun | Malaysia | Filipina | Singapura | Thailand |
| 1999 | 2,7 | 2,1 | na* | 2,2 |
| 2000 | 2,8 | 2,1 | na | 2,1 |
| 2001 | 3,1 | 2,4 | na | 2,2 |
| 2002 | 3,2 | 2,2 | na | 2,4 |
| 2003 | 3,6 | 2,3 | 6,1 | 2,3 |
| 2004 | 4,0 | 2,3 | 5,6 | 2,5 |
| 2005 | 3,8 | 2,3 | 5,2 | 2,6 |

*na = data tidak tersedia
sumber: Database PBB, diolah

Source: UNSP, Comtrade Database, adjusted by P. J. Sadewa, 2006.

If it is the case, this phenomenon means that the existence of AFTA has been maintained base on non-economical consideration. AFTA has been sustained in order to support the continuance of ASEAN. The dilemma among the AFTA

members is whether the trade-off is worthy enough for each of its individual country. The answer is lying in the foundation of AFTA, which is established not based on Article XXIV: 8 (b) of the General Agreement on Tariffs and Trade, but founded on Tokyo Round enabling clause. The Tokyo Round enabling clause stipulated that the PTA only applies among the developing countries.

Miss-application of the PTA to the developed countries will lead into injustice: it is benefiting the more developed member country at the expense of the developing member countries. This phenomena has been experienced among the AFTA members, since some of the country GNP per capita is more than US\$ 25,000.00 (e.g. Singapore), while the other member GNP per capita is only around US\$ 1,000.00 (e.g. Indonesia).

The detrimental effect for Indonesia has been increased as implication of the bilateral USA-Singapore FTA. The trading goods flow from Indonesia to Singapore increases dramatically, either trough legal transaction, or mostly by illegal trading. It was estimated that Indonesia experienced a total loss of approximately US\$ 8 billion on smuggling of tin from Bangka and Belitung islands alone.

The inclusion of Indonesian islands (Batam and Bintan) in the Integrated Sourcing Initiative/ISI as a part of USA-Singapore FTA has been benefited Singaporean firm operating in Singapore to take advantage of the complementarities between Singapore and Indonesia. Singapore officials went to great lengths to describe the ISI as not just good for Singapore, but for all the countries in ASEAN.²⁸ John Coyle stated that these arguments were partly aimed at deflecting criticism from ASEAN countries--many of which were not pleased when news of the U.S.-Singapore FTA was announced.²⁹ No doubt, the ISI makes firms in Singapore more competitive. By outsourcing labor-intensive production to Batam and Bintan (or any other suitable location) and then exporting to the United States without paying any administrative costs of proving origin, these firms are better equipped to compete in the U.S. marketplace.³⁰

The ISI has been benefited U.S. multinational corporations/MNCs with operations in Singapore to capture the existing complementarities within the Growth Triangle (Singapore, Indonesia, and Malaysia) and to eliminate extra red tape, fees, and paperwork.³¹ Ambassador Zoellick has said that the ISI is intended to provide a degree of economic assistance to Indonesia because of U.S. concerns about "economic stability in a world where we're concerned

²⁸ Singapore Minister for Trade and Industry George Yeo, Remarks at a Press Conference at Venture Manufacturing Plant in Bintan Industrial Estate.

²⁹ Telephone interview by John Coyle with anonymous USTR official (Nov. 14, 2003).

³⁰ See Singapore Minister for Trade and Industry George Yeo, Connections: Singapore and Indonesia Link Up with New Gas Pipeline (Radio Singapore International Broadcast, Aug. 14, 2003), <http://www.rsi.com.sg/english/connections/view/20030814131752/1/html>

³¹ Telephone interview by John Coyle with anonymous USTR official (Nov. 14, 2003).

Agus Brotosusilo: WTO, Regional and Bilateral Trade Liberalization

about security and terrorist threats."³² In his view, the ISI represents a "creative" attempt to "try to help the Indonesians" economically and in so doing help prevent "failed states, broken societies, [and] extreme poverty In which the seeds of terrorism can grow."³³

The ISI permits non-signatory third countries (especially Indonesia) to take advantage of certain provisions of the U.S.-Singapore FTA.³⁴ However, not only the Vienna Convention on the Law of Treaties (Vienna Convention), but also the General Agreement on Tariffs and Trade (GATT) limit the ability of states to use rules of origin to benefit third states. Article 34 of The Vienna convention on the Law of Treaties (Vienna Convention)³⁵ establishes the principle that, for a bilateral treaty to create "rights or obligations" on the part of a third state, that state must consent to their imposition,³⁶ however, there is not even a reference to third countries in a generic sense in the text of either of US-Singapore FTA documents; Article 3.2 of the Free Trade Agreement simply states that "[e]ach Party shall provide that a good listed in Annex 3B is an originating good when imported into its territory from the territory of the other Party."³⁷ John Coley identifies the first question on the arrangement is whether Article 3.2, when read in conjunction with the various public statements made by officials from the United States and Singapore identifying Indonesia as the primary intended beneficiary of the ISI, is sufficient to confer upon Indonesia a right to benefit from the ISI. The second question is whether, if a right has been conferred, Indonesia has a viable remedy if it is violated. The ICJ held that France's high-ranking officials oral statements pledging to refrain from nuclear testing in the Pacific were binding because France intended that they be so.³⁸ By contrast, it is highly doubtful that any of the high-ranking officials in the United States or Singapore intended to assume a binding obligation (the flipside, after all, of conferring a right) to Indonesia by virtue of their public statements. They

³² U.S. Trade Representative Robert Zoellick, Address to the U.S. Asia Pacific Council Symposium, Apr. 24, 2003.

³³ Peter Hartcher, U.S. Links Free Trade to Global Security, *Australian Fin. Rev.*, Nov. 15, 2002, at 28, LEXIS, Nexis Library, News Group File (quoting Ambassador Zoellick).

³⁴ Products covered by the ISI include all those listed in Annex 3B of the Agreement and include semiconductors, computers, telecom equipment, cell phones, cordless phones, optical fibre cables, photocopying equipment, medical instruments, and a range of other high-tech products. See U.S.-Singapore Free Trade Agreement, *supra* note 5, Annex 3B; United States-Singapore Free Trade Agreement Implementation Act, Pub. L. No. 108-78, 117 Stat. 948 (2003). Only Congress can add items to this list.

³⁵ Vienna Convention on the Law of Treaties, May 23, 1969, arts. 34- 38, 1155 U.N.T.S. 331, 341 reprinted in 8 I.L.M. 679, 693-94 (1969).

³⁶ *Ibid.* art. 34, 1155 U.N.T.S. at 341 ("A treaty does not create either obligations or rights for a third State without its consent.").

³⁷ U.S.-Singapore Free Trade Agreement, *supra* note 5, art. 3.2(1).

³⁸ See *Nuclear Tests (Austl. v. Fr.)*, 1974 I.C.J. 253, 267 (Dec. 20), at 269-70.

expressed a desire that the ISI benefit Indonesia, but this is very different from expressing an intention that Indonesia has a right to benefit.

Coley argues that Article XXIV of the GATT--which permits the creation of free trade areas and customs unions generally--does not authorize bilateral treaty partners to use rules of origin to confer benefits upon third states, thereby imposing a significant constraint upon the ability of states to use rules of origin to realize non-economic goals.³⁹ He stresses that the ISI mechanism chosen for permitting the continued exploitation of the Indonesian cheap labor through rules of origin regime.⁴⁰ In sum, Indonesia possibility to take advantage of certain provisions of the U.S.-Singapore FTA is not even a right without remedy. It is no more than one-side charity, from the richer to the poorer country.

Basically, the just trade cooperation among countries should not established base on a charity. It should be founded stand on equality. So, it is more justifiable to establish the US-ASEAN FTA in ASEAN area, or to create a wider scope trade arrangement: NAFTA-ASEAN FTA, not exclusively limited to the US-Singapore FTA.

Conclusion

Considering the nature of AFTA members merchandise trade and the members export destination, most of AFTA member countries are competitor, not complementary to each other. Since the establishment of AFTA has not been improved specialization among its member countries, and the formation of the FTA has been failed to increase the comparative advantage among its members, in order to increase the benefit from the trade cooperation as well as to decrease the tension among the member countries, I propose that the regional free trade agreement should be extended into a broader free trade agreement not only between AFTA and its main trading partners (e.g. USA, China, or Japan), but also between AFTA and other regional trading arrangement (NAFTA, or EU); however, the just trade cooperation among countries should not established base on a charity, in an asymmetric relationship. It should be founded stand on equality among its parties. The prospect for economic attainment of AFTA members should not be sacrificed by the political consideration in the establishment of ASEAN. The exclusive agreement between any AFTA member and its main trading partner will lead into injustice: it is only benefiting the exclusive member country of AFTA at the expense of the rest member countries.

³⁹ John Coyle: Rules of Origin as Instruments of Foreign Economic Policy: An Analysis of the Integrated Sourcing Initiative in the US - Singapore Free Trade Agreement. Yale Journal of International Law, Vol. 29, 2004, pp. 545 - 580.

⁴⁰ Ibid.