



# TWO NEIGHBOURS, PARTNERS IN PROSPERITY

**Indonesia-Australia Business Partnership Group  
Submission towards the IA-CEPA**

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# FOREWORD

Indonesia. Australia. Two very different neighbours. Culturally, socially, economically, historically ... *different*. But in terms of resources, skills and assets, the two neighbours have such complementarity and, such compatible advantages that can be pressed in to service to deliver mutual benefits. With the slowing of global economic growth, and the economic transitions of both economies, as well as new opportunities presented by new megatrends in global trade and investment, both countries need to look to each other to make the most of the opportunities and jointly create new ones. Together, they are capable of creating an engine for growth of trade and investment with ASEAN, greater Asia and the world beyond. Together, they can be a shining example of new models of economic partnership.

Those are the obvious opportunities for an Indonesia-Australia Comprehensive Economic Partnership Agreement (IA-CEPA) to address, to the fullest extent possible. The IA-CEPA must create an environment to enable business from Indonesia and Australia to trade, invest and cooperate. If business does well, it also has the power to do good by creating new jobs and new wealth and by underpinning inclusive economic growth and higher standards of living. The IA-CEPA must embrace innovation to create a special and unique agreement between Indonesia and Australia. It must create an environment of preferential treatment for investors, exporters and business collaborators while empowering the vulnerable in both countries.

In doing so, a good place to begin is to identify opportunities for trade, investment and collaboration and then to ask why tariffs or barriers exists between the two countries. What would be the impact if there were none? Can the long list be erased over specified and realistic timeframes? How can exporters of goods and services be encouraged to invest in-market, to raise local standards, build capacity and levels of security in sector after sector? How can we avoid any future unintended interventions and impacts? What kind of protection, adjustments and capacity-building need to be implemented for the weak and vulnerable sectors? Governments are requested to approach these matters on a scientific basis.

The IA-CEPA must be opportunities-driven, seeking to create a bilateral environment in which business can thrive. By also recognising and responding to the strengths and



weaknesses of each country's economic assets, IA-CEPA can achieve a fair balance of risk and reward for all parties, in both countries. Recognising the different stages of development and capacities of business in each economy, IA-CEPA will include capacity-building that will help to address imbalances and enable adjustment. Capacity-building and preferential arrangements tailored to the opportunities and impediments in each country, across economies and by sector will facilitate business engagement. Without such tailored approaches to overcoming market failure and removing impediments, it is unlikely that the current level of business engagement will change significantly.

To achieve such a unique CEPA, both sides have to approach the negotiations with generosity and goodwill. The result will boost levels of trust and confidence, essential for continued success. With both large businesses and SMEs engaged, real people-to-people contact will change the relationship between the two neighbours.

The IA-BPG stands ready to continue assisting the negotiators and both governments during negotiation and implementation of the IA-CEPA. The following pages detail the features that the IA-BPG is advocating for the IA-CEPA.



## EXECUTIVE SUMMARY

The Indonesia-Australia Business Partnership Group (IA-BPG) welcomes and supports the creation of the Indonesia-Australia Comprehensive Economic Partnership Agreement (IA-CEPA). IA-BPG strongly believes that IA-CEPA should be a unique agreement, with a unique approach. It should avoid being a routine negotiation framed from the perspective of two opposing parties making concessions to reach a final agreement. It should turn traditional approaches to Free Trade Agreements (FTAs) on their head, and begin by identifying areas of potential and opportunity – it should seek to develop momentum by creating a ‘buzz’ generated from early outcomes, both in trade liberalisation and in initiatives designed to build the economic relationship. It should seek to deliver fast, demonstrable benefits and create its own momentum, recognition and support from businesses in both economies. It should implement President Widodo’s commitment to cut government regulations by 50% and take a common sense approach to trade and investment issues. It should be dynamic and responsive to the needs of business and the demands of the market. It should boldly go where no FTA has gone before.

As its name suggests, this bilateral agreement is expected to be a “21st Century agreement” which comprehensively covers a wide range of issues including and beyond trade and investment. The agreement should seek to build extensive links between the business sectors of both countries – to create closer relationships, increased trade and mutual prosperity. In a joint statement in March 2016, former Trade Minister Thomas Lembong and Minister for Trade, Tourism and Investment Steven Ciobo reiterated the bilateral support for a CEPA stating that “a successful Agreement would serve as a new platform toward a modern and dynamic economic partnership that reflects the strong bonds between the two countries”.

In going beyond traditional FTAs, the features of the IA-CEPA should include progressive removal of all trade barriers and facilitation of two-way trade in goods and services, plus investment. Technical and regulatory barriers to trade should be removed as much as possible while inhibitors to two-way investment should be eliminated. Rules and standards, including mutual recognition or harmonisation of qualifications should be aligned and simplified before being approved and implemented by both countries. Movement of skilled persons should be facilitated to meet market demand. Market failure should be overcome by providing information on market opportunities, on doing business in each economy and facilitation of business-to-business contact. Cross border cooperation to access global value chains is a key opportunity and incentive for business. And, last but not least, the importance of capacity building, including training and improving governmental procedures, is highlighted as a key element for success.

As the nature of the global and regional economy is changing, Indonesia and Australia have undergone substantial economic transformations. Australia is transforming from mining investment and extraction, plus agriculture and manufacturing, to a more diverse economy underpinned by services, knowledge and technology. Australia's economy is now geared more toward global value chains, having been globally competitive in producing primary products, in niche manufactures, in key services and in education and research. As these changes unfold, however, the nation faces challenges in balancing development, especially in the northern region. More critically, Australia's population is ageing, which changes the structure and nature of the workforce.

Indonesia, on the other hand, is moving away from relying on primary industries towards manufacturing and services, more so because of the effects of the demographic dividend and urbanisation. This transformation, however, requires substantial investments and exports, rather than relying on domestic consumption, which in turn needs significant change in the public and private sector, both at the national and regional level. In that context, exports and economic growth will be driven by investments that are needed to build connectivity in the archipelago through modern infrastructure, to develop human capital through improvement in health and education, and to spark innovation and creativity through technology development.

The two nations have very complementary needs and strengths and can achieve much more for their economies and peoples by working closely together than separately.

While the vision of increased prosperity through bilateral trade is shared by the governments and business communities of both countries, IA-BPG has identified a number of impediments which hamper the achievement of that goal. This report, based on an analysis of the existing economic relationship between Australia and Indonesia, strongly supports the conclusion that these two economies are complementary in many respects, that there are vast areas of potential for economic partnership, and that the two neighbouring countries can truly succeed together in a global market.

Beyond identifying impediments to greater economic engagement, the report identifies particular sectors where significant opportunities for economic growth may exist, and includes a number of recommendations for steps which can be taken towards achieving the stated goal of becoming partners in prosperity.

The IA-BPG was first formed in 2012, and compiled a report on the potential benefits of an IA-CEPA and included a set of recommendations. In 2016, governments of both countries restated their support for a bilateral agreement which addresses the unique economic relationship between the two neighbouring countries. The IA-BPG was reconstituted and discussions and consultations towards the IA-CEPA were formally reactivated. The IA-BPG process of broad-based consultations with businesses and member associations through individual interviews, workshops and written submissions has been hailed as the 'gold standard' for private sector engagement in the preliminary stages of a bilateral trade negotiation of this type. Following on from this solid base of stakeholder engagement, the group reiterates that the IA-CEPA should be a dynamic agreement with in-built mechanisms to monitor and adapt its performance. An ongoing business advisory and consultation mechanism should be established to ensure a continued business-to-business engagement and broader continuing stakeholder engagement.

## ISSUES AND IMPEDIMENTS TO TRADE AND INVESTMENT

Cooperation between the business sectors of the two countries continues to be hampered by remaining tariffs, trade regulations and procedures, technical barriers to trade, trade restrictions (including import quotas and licensing), barriers to movement of people, and restrictions on foreign direct investment. All of these substantial impediments must be addressed by IA-CEPA. Building upon the provisions and schedules in AANZFTA, and adapting provisions of other trade agreements, IA-CEPA should aim to remove remaining tariffs and barriers to trade for all goods and services as soon as possible and make a commitment to not impose further tariffs or barriers. Although necessary to protect consumers, trade regulations should facilitate rather than hinder trade, and they should provide clarity and certainty to business on technical requirements and costs.

Similarly, in tackling these impediments, while recognising that standards may be applied to maintain product quality or public safety, IA-CEPA must strive for a clear framework for aligning standards, qualifications and requirements. Additionally, a robust framework to address trade restrictions is necessary to achieve beneficial outcomes, ensure consumer protection and to initiate capacity building for skills and governance.

In an agreement such as this, people are key to unlocking the potential and complementarities in the two economies. Therefore, clarity, simplicity and transparency, to ensure that skills and labour demands are able to be met in a timely and efficient way, are essential. Finally, governments of both countries should support and facilitate business to target and activate investments that create the most value for the economy – i.e. those that are able to generate employment and stimulate productivity.

In addition, achieving the desired goals and outcomes of IA-CEPA may require serious consideration from the wider public and private sectors over more subtle impediments. First, *limited communication and exchange of information* has hampered businesses in pursuing opportunities, and this will require a common platform for accessing trade information and discussing policies, as well as capacity building for SMEs to tap into these resources. Second, *financing and access to capital* is critical for the cooperation as both countries rely on foreign investment, and to facilitate this it is necessary for the regulators to synchronise the rules and promote simultaneous operation for financial services companies, and for the companies to link seamlessly and connect to business.

Third, *gaps in infrastructure and logistics* are glaring, which will require significant investments – including through Public Private Partnerships (PPP), streamlining customs protocols, and connecting the transportation network of both countries. Fourth, *fostering small- and medium-enterprises* is imperative for a successful cooperation, and this will entail educating SMEs on the benefits of trade liberalisation, heeding their concerns, and promoting participation in bilateral trade and global value chains.

## STRATEGIC MODELS FOR PARTNERSHIP

In facilitating cooperation, IA-BPG aspires to the creation of integrated industries that are responsive to global markets, which utilise robust two-way investment, strengthened by knowledge-sharing and technology collaboration, as well as more targeted Aid for Trade, and linking services sector investments with capacity building. Hurdles remain, however, and overcoming them requires, first, *preferential treatment*, where IA-CEPA provides each country with preferential status for trade and investment, and that operates over and above other preferential arrangements. Second, taking

advantage of *Indonesia's Special Economic Zones (SEZ)*, where investments and collaborations are unrestricted by regulations applied elsewhere.

IA-BPG identified six specific sectors where significant potential exists for cross-border economic engagement and where benefits may be realised within a relatively rapid time-frame.

1. **Expanding tourism and enhancing hospitality** which will require liberalising visa requirements and movement of natural persons, as well as enhanced skills and training through skills exchange programs.
2. **Securing domestic food availability and participating in global food supply** through development of joint, integrated, two-way supply chains, facilitating bilateral preferential treatment, implementing joint research and capacity-building and tackling issues of differing food standards.
3. **Developing human capital through cooperation in technical and advanced education and training** to be achieved by opening the education sector to foreign investment, encouraging greater university engagement in joint research and degree programs, and facilitating MNP for education purposes.
4. **Improving health and quality of life by encouraging exchange programs** in healthcare, facilitating investment and movement of people in the healthcare industry, aligning qualifications and capacity building for healthcare professionals.
5. **Accelerating connectivity in digital economy, e-commerce and creative industry** by emphasising free flow of information while respecting security concerns and creating an environment that supports free-flow of investment in e-commerce and technology in the digital sector, especially for SME startups in this sector.
6. **Facilitating opportunities in infrastructure and energy** by removing restrictions, easing regulations on foreign workers and encouraging Public-Private Partnerships. Significant opportunities are presented by developing innovations in renewable energy sources and global energy integration systems to supply power to the Indonesian grid and regional communities which lack connectivity to reliable sources of electricity. Around a quarter of Indonesia's population, over 60 million people, currently do not have access to electricity.



# RECOMMENDATIONS FOR IA-CEPA NEGOTIATIONS

## CROSS-CUTTING MEASURES TO OVERCOME IMPEDIMENTS

Recognising that Australia and Indonesia are already partners in the AANZFTA free trade agreement along with current negotiations for RCEP and Indonesia's desire to join the TPP, the IA-BPG partners noticed a number of common themes which if considered appropriately, could address concerns and opportunities for multiple sectors through cross-cutting actions or initiatives, to enhance our bilateral relationship.

The recommendations the IA-BPG has identified in line with these cross-cutting themes include:

1. Accelerate tariff reductions to be faster than the time frames set in AANZFTA.
2. Accelerate removal of product quotas.
3. Apply consistent capital thresholds for all business.
4. Progressively remove limits to equity holdings in listed or private businesses held by nationals or companies from the IA-CEPA partners provided this meets the national interest test as overseen by the foreign investment review boards or equivalent against transparent criteria.
5. Allow full and free movement of skilled people across our common border.
6. Provide mutual recognition of educational and skill levels against international standards.
7. Encourage improved mutual cultural and linguistic understanding through wider inclusion in school curricula.
8. To the extent possible, aim measures at facilitating cooperation and collaboration to access global value chains and service provision.
9. Build a harmonised, borderless system for conduct and regulation of e-commerce based on global standards.
10. Remove foreign currency policies that inhibit business from fully engaging with global markets and from conducting cross-border AUD-IDR transactions except for monetary stability measures.

11. Create a consistent set of fees and levies domestically applied to imported goods and services that are WTO compliant and transparent.
12. Foster closer cooperation in skills development through education, training and professional development.
13. Build and strengthen administrative and regulatory institutions and their understanding of each other's policies, regulations and negotiation and dispute resolution norms through better Indonesia-Australia linkages and capacity-building.
14. Introduce strong, business-facilitative competition policy to encourage development of markets, efficient allocation of resources and markets that participants trust.
15. Provide information on business opportunities and on doing business in each economy, and facilitate business-to-business linkages and supply chain development.
16. Tailor development assistance to facilitate these recommendations and provide the capacity for Indonesia to implement rapid economic development.
17. Encourage greater B-to-B engagement in both countries. Chambers of Commerce and Business Councils could be the drivers of this by encouraging their members to foster closer relationships with counterparts.
18. Engage a broader set of stakeholders, beyond just business communities, including media, civil society, universities and local government institutions to generate awareness and involvement in IA-CEPA.
19. Encourage ongoing review and liberalisation of the Negative Investment List in Indonesia and further liberalisation of access to the services sector in Australia.
20. Foster *inclusive* economic growth, as a principle of IA-CEPA, which contributes to sustained poverty reduction, ensures equality of opportunity for regional areas, women and minority groups – and is essential for a successful growth strategy.
21. Encourage digitisation of trade-related practices and increased trust in the online environment through an e-commerce chapter.
22. Establish a framework of on-going monitoring to evaluate and improve the performance of the IA-CEPA as a dynamic and growing process – this could include the establishment of an on-going IA-BPG.

## RECOMMENDATIONS BY TOPIC

### 1. ECONOMIC COOPERATION

#### a. *Exchange of Information*

- i. Promote transparent and seamless regulatory processes based on international standards with a better application of the rule of law and a well-resourced and independent regulatory structure.
- ii. Develop accessible and transparent information about regulations, standards and certification required for market entry and how these can be met.
- iii. Provide information to investors in Australia and Indonesia to help make them more aware of the direct and indirect business benefits of investing in order to drive greater investment relations.

- iv. Establish an amalgam of national, regional and local government initiatives, coupled with private sector contact, to provide information on markets and doing business, and encourage market access.
- v. Develop sectoral direct communication platforms to bridge information and interaction gap between the two countries.
- vi. Disseminate information and raise awareness about the IA-CEPA within the SME community to encourage greater engagement of SMEs in both countries.

### **b. Capacity Building**

- i. Significantly increase capacity in vocational education and training (VET) in Indonesia through expanding and developing Vocational High School (SMKs) and polytechnic networks, including more polytechnic lecturers, building competency standards, industry engagement, VET quality, international VET partnerships and staff exchange and creating centres of excellence in each of Indonesia's major cities.
- ii. Australia should consider not only technical assistance at a scientific level but also deeper engagement by actual primary producers to assist in the development of Indonesia's agricultural industries to meet the standards required for entry to the Australian system.
- iii. Promote education cooperation, which includes standards on education curricula, teacher competencies, research and development agenda, and internship opportunities.
- iv. Promote cooperation to boost mutual competencies in branding, product innovation, research and development.
- v. Provide greater support to business people and public servants of the two countries to learn Bahasa Indonesia – and vice versa for those in Indonesia to learn English.
- vi. Include a program that establishes a capacity-building and export facilitation activity to support exporters of Indonesian agricultural products.
- vii. Ongoing support for improvements to economic governance in Indonesia.
- viii. Develop a business capacity building program about FTAs and how to utilise them in conjunction with exchange of information about business opportunities.
- ix. Assist businesses to understand the existing available mechanisms for international B-to-B dispute resolution.

### **c. Trade Facilitation**

- i. Centralise approvals for the exploitation of natural resources in Indonesia by the national government or competent regional authority using consistent and transparent decision criteria.
- ii. Encourage governments to support micro-economic reform designed to improve the productivity and competitiveness of industry.
- iii. Establish customs pre-inspection facilities in strategic locations to further benefit bilateral supply chains and to avoid inefficiency with the aim of providing reciprocal service levels.
- iv. Establish a joint Industry-Government monitoring and consultation mechanism regarding new or enhanced food regulations.

- v. Encourage greater collaboration between quarantine agencies of both countries to avoid double quarantine processes.
- vi. Emphasise cooperation and a sensible approach to health, safety and quality standards across the partner economies to support trade.
- vii. Propose the establishment of sectoral research centres within Indonesian universities, and research collaborations with Australian universities.
- viii. Establish a Trade Facilitation Centre of Excellence to address impediments to trade in the context of both bilateral and multilateral relations.
- ix. Remove barriers to infrastructure cooperation between businesses in Indonesia and Australia.
- x. Encourage reform of cabotage regulations in Australia and Indonesia for sea and air to reduce costs to businesses, consumers and facilitate greater trade.

## 2. TRADE IN GOODS

- i. Further reduce or eliminate tariffs to offer better prices and improve consumer choice and reassurance of product availability.
- ii. Accelerate the tariff reduction schedule beyond AANZFTA in the IA-CEPA for freer trade cooperation, especially for Indonesian tariff lines on agricultural products and Australian tariff lines on textiles and textile products.
- iii. Environmental goods and services should be free of tariff and trade restrictions.
- iv. Technical requirements and import procedures should be in accordance with international best practice, be transparent and not act as non-tariff barriers to trade.
- v. Harmonise and/or recognise standards and certification measures in IA-CEPA such as health, safety and quality standards, SVLK (the Indonesian Timber Legality Verification System), and Halal certification across the partner economies.
- vi. Create duty-free, quota-free, two-way access for food products and agricultural products.
- vii. Remove all barriers and restrictive regulations, on:
  - a. Goods imports that are not related to health and safety
  - b. Export activities
  - c. The implementation of caps or quotas on import permits
- viii. Facilitate preferential treatment between both countries for trade in food products.
- ix. Adopt similar Codex Alimentarius standards as much as possible to tackle issues of differing standards.
- x. Expand the red meat and cattle partnership, and apply a similar approach to other sectors of mutual interest such as grains, seafood and horticultural products.
- xi. Support the Rules of Origin and procedures system used within AANZFTA (ASEAN supported) inclusive of the First Protocol amendments but also seek to simplify administration with the objective to facilitate ease of use and economies of scale for business, in particular SMEs.

### 3. TRADE IN SERVICES

- i. Establish approaches which are in accordance with international best practices, transparent and do not act as restrictions to services.
- ii. Facilitate greater access to the services sectors of both countries.
- iii. Establish more flexible arrangements on commercial presence of foreign services providers.
- iv. Remove any restrictions on data flows and reconsider restrictions on server locations.
- v. Progressively remove the service-related barriers in the following areas:
  - a. Professional practice and establishment of service businesses
  - b. Foreign investment and service provision
  - c. Natural resource development
- vi. The IA-BPG recommends ongoing review and liberalisation of the Negative Investment List in Indonesia and further liberalisation of access to the services sector in Australia.
- vii. Restrictions on movement of people is another major impediment to growth in services trade and investment. As this position paper advocates elsewhere, easier movement of people is a key to the success of the IA-CEPA.

### 4. INVESTMENT

- i. Relaxing Indonesia's FDI regulations is seen as key to knowledge and technology transfer.
- ii. Australian Foreign Investment Review Board (FIRB) thresholds for review of investments in agriculture should be similar to the thresholds applied for investments from other countries, such as the US.
- iii. FIRB thresholds for other classes of investment should similarly be benchmarked against those in other trade agreements.
- iv. Progressively remove or lift all two-way barriers and restrictions to investment in the following:
  - a. Investment in land, production facilities such as feedlots, processing facilities such as abattoirs, flour mills, food processing and consumer good manufacturing, distribution and marketing chains
  - b. Export restrictions on products
  - c. The establishment of investment in educational institutions and the delivery of education (vocational and higher education) for people involved in the complete food supply chain (paddock to plate)
  - d. Foreign equity and service provision
  - e. The establishment of natural resource development services industry
- v. Stakeholders have identified the following sectors as being in need of foreign investment and capacity-building, which presents significant opportunities for Australian investors. IA-CEPA should include provisions for all levels of government to

work with business to facilitate the necessary exchange of information to help match investors with potential business partners in sectors such as, but not limited to:

- a. Coffee
- b. Sugar
- c. Cotton
- d. Cattle breeding
- e. Palm Oil
- f. Fisheries
- g. Grains
- h. Cocoa
- i. Minerals processing facilities (smelters, refineries)
- j. Coal Bed Methane
- k. Energy efficient lighting
- l. Digital economy and creative industry

IA-BPG recommends that the model of the red meat and cattle partnership could be deployed to assist industry engagement to advance mutual cooperation in each of these sectors.

- vi. Encourage creation of an Indonesia-Australia PPP Centre, which would help fulfil Indonesia's need for high quality design, structuring and documentation of projects on offer. Such a centre working closely with BKPM would streamline investment and workflow in this crucial sector.
- vii. Find mechanisms to ensure Australian involvement in PPP projects without having to go through international competitive tender requirements. G-to-G platforms such as an MoU on a specific infrastructure project should be established.
- viii. Remain open to accepting unsolicited bids for regional development and infrastructure projects from the private sector willing to invest in projects they have identified unilaterally.
- ix. Open energy sector to foreign investment in all classes of infrastructure.
- x. Open up opportunities for investment in hospitals and healthcare facilities.

## 5. MOVEMENT OF PEOPLE

- i. Mutual recognition of qualifications and certification by both countries to facilitate trade in services and movement of skilled workers.
- ii. Encourage freer movement of skilled people between the two countries. Encourage employment of skilled Indonesians and Australians in both countries.
- iii. Encourage alternative solutions for short-term migrant workers with limited English proficiency, for example by providing "forepersons with a high-level of English supervising work groups" similar to a system which operates in New Zealand for fruit pickers and packers.
- iv. Remove two-way barriers for the movement of skilled workers in the following areas:
  - a. Production agriculture, science, food processing and supply chain logistics
  - b. Agricultural sector to allow for training and working in both economies to facilitate skills development and transfer
  - c. Standard setting, certification and assessment

- d. Mining, energy, engineering and environmental management personnel
  - e. Skills development, training and technology transfer in the mining, energy, engineering and environmental management fields
  - f. Technical, vocational and higher education and training, including English language teachers.
- v. Mutual skills recognition, including developing training between professional associations or vocational schools and the possibility of establishing a joint committee or institution to facilitate initiatives in the field of education.
  - vi. Simplification of work permits for lecturers, teachers and researchers, and more relaxed visa provisions for students.
  - vii. Create a special visa category under IA-CEPA to facilitate service sector movement of skilled people.
  - viii. Implement more relaxed restrictions on temporary entry and work permits for professional and skilled personnel between Australia and Indonesia and vice versa.
  - ix. Establish visa regulations in the tourism sector to attract Australians to invest, reside, retire or take advantage of aged care facilities to be developed in Indonesia.
  - x. Harmonise arrangements for business visas for both Australia and Indonesia, including Visa on Arrival for Indonesians seeking business visas equivalent to that offered by Indonesia to Australian travellers, and easy-to-obtain multi-entry business visas for Australians entering Indonesia.
  - xi. Provide greater flexibility of visa options to facilitate greater tourism between both countries. Note: Indonesia has applied 30-day visa-free entry mechanism for Australians and Australia has the applied option to apply for a three-year multi-entry visitor visa. However, more can be achieved.
  - xii. Further develop the skills and training offered through the Skills Exchange program between Indonesia and Australia to develop human resources and skilled hospitality personnel in tourism sector.

## 6. E-COMMERCE

- i. Adopt trade rules that foster confidence in the on-line environment and limit the ability to put up roadblocks to such trade in the future. In particular the IA-CEPA will need to adopt rules that enable information flows and reconsider prohibition on data localisation, allow the cross-border provision of services, encourage the growth of online businesses, make it easy for SMEs and users to get online, and enable the usage of simple online payment systems.
- ii. Building a harmonised, borderless system for conduct and regulation of e-commerce
- iii. Consider training and capacity-building requirements for both governments and business to utilise e-commerce.
- iv. As a principle, the IA-CEPA should support the free-flow of information while respecting personal information security concerns as much as possible. Governments should not seek to create treaty terms where contract law is sufficient.

- v. Create an environment that supports industries in the digital economy sector, especially SMEs, by allowing freer flow of investment and people and progressively removing any remaining foreign ownership restrictions in digital sector.
- vi. Encourage a joint working group in establishing an Indonesia Australia digital economy sectoral convergence.

## 7. EDUCATION

The IA-CEPA and allied projects should include measures to encourage universities to work more closely together in teaching, learning and research, including joint degree programs and joint research activities and centres. As well, the IA-CEPA should include:

- i. Provisions for opening the university sector for foreign investments.
- ii. Provisions for opening the training sector to allow for resourcing of much-increased school to university transition programs.
- iii. Provisions for cooperation and capacity-building in the VET sector to enable it to better train skilled workers to international standards.
- iv. Provisions for movement of skilled people to undertake research and conduct teaching.

## 8. OPPORTUNITIES FOR EARLY OUTCOMES

Refocusing Australia's aid effort to assist to advance the following series of projects would assist to build confidence and advance the aims of the IA-CEPA while negotiations are conducted. Examples of such projects are listed below:

- i. Collaborations on the opportunities and challenges of electricity generation and supply including cross border electricity supply and markets.
- ii. Collaborative efforts to improve the opportunities in both countries for global tourism.
- iii. Banking and financial services opportunities and challenges including best practice digital economy issues.
- iv. Improving transport links between Northern Australia and Indonesia.
- v. Language and cultural orientation programs.
- vi. Open two-way Customs Pre-Inspection Services.
- vii. Establish a Trade Facilitation Centre of Excellence.
- viii. A Mining Equipment Technology and Services (METS) sector working group.
- ix. Indonesia-Australia Centre of Excellence for the grains industry.
- x. Revised visa categories to improve two way movement of people in all categories.
- xi. Develop a 'Food Plan 2030'.
- xii. Establish an Indonesia-Australia Agribusiness Leaders Network.
- xiii. Implement a specific IA-CEPA Standards Harmonisation Action Plan.
- xiv. A PPP Centre to facilitate bilateral infrastructure projects.



## Chapter 1

# BUSINESS EXPECTATIONS FOR A SPECIAL AND UNIQUE AGREEMENT

## CONTINUING TO BUILD UPON A STRONG FOUNDATION

### ➤ **BRINGING BUSINESS TOGETHER**

In March 2016, the Indonesian and Australian governments formally reactivated discussions to establish an Indonesia-Australia Comprehensive Economic Partnership Agreement (IA-CEPA). With the reactivation, the Indonesia-Australia Business Partnership Group (IA-BPG) was also reconstituted as an advisory body to provide business insight on issues relating to the framing of such an agreement. In 2012, the membership of IA-BPG consisted of the Indonesian Chamber of Commerce and Industry (KADIN), the Australian Chamber of Commerce and Industry (ACCI), Indonesia-Australia Business Council (IABC), and Australia-Indonesia Business Council (AIBC). In 2016, the IA-BPG expanded its membership to include the Employers' Association of Indonesia (APINDO) and the Australian Industry Group (Ai Group) to ensure an even broader representation of business stakeholders in the consultation process.

The role of the IA-BPG is to:

- examine the current trade, investment and economic cooperation profile between the two countries;
- identify economy-wide and sectoral trade and investment opportunities in both countries, as well as how economic cooperation could narrow the development gap between the two countries;
- identify impediments to increasing two-way trade and investment, and to developing greater economic interaction, including the scope for both countries to cooperate to facilitate access to third markets, as well as facilitating increased participation in global value chains;
- assess ways in which increased trade and investment will enhance inclusive and sustainable economic growth, and enable these benefits to be distributed widely through both economies, including to small and medium business and regional areas;

- propose mechanisms and actions to eliminate or mitigate impediments, and facilitate widespread distribution of the benefits of enhanced economic integration;
- make recommendations on the content of the IA-CEPA and its negotiation and implementation; and
- strengthen the understanding and partnership between Indonesian and Australian business communities and contribute to the development of an effective private and public sector dialogue.

In preparing this position paper, the IA-BPG, through its member organisations, has consulted extensively with the business sector in both countries. IA-BPG hopes that it has laid the groundwork for ongoing business engagement as negotiations on the IA-CEPA progress, and most importantly, for much greater bilateral trade, investment and business collaboration in the future.

### ➤ **BEYOND BUSINESS AS USUAL**

From the outset, it was always intended that the IA-CEPA should go well beyond a traditional free trade agreement (FTA), and that it should constitute a comprehensive strategic partnership encompassing trade in goods and services, investment, economic cooperation (including capacity building) and cross-cutting issues such as movement of natural persons. It is also the opinion of the IA-BPG that the negotiations should address a number of other important and substantive issues such as electronic commerce, competition policy, government procurement, intellectual property rights, environment and labour, as well as institutional and framework provisions (transparency, general provisions and exceptions, institutional provisions, dispute settlement procedures and final provisions).

ACCI, KADIN, APINDO, Ai Group, IABC and AIBC support the concept and vision of the IA-CEPA. The business sector believes that there are many opportunities for partnerships that can be developed between Indonesia and Australia and therefore create the potential for a truly comprehensive agreement which encompasses all aspects of the economic relationship between the two countries, and goes far beyond what has been achieved in other FTAs to date. The IA-CEPA represents a unique opportunity to create a strategic partnership between two nations; aimed at generating joint prosperity and success in the global economy.

Importantly, the IA-BPG believes that negotiations should be opportunities-driven, seeking to identify areas of economic potential, and agreeing on measures that will facilitate business to maximise opportunities by working together. A key theme of the agreement, and its implementation, will be facilitation of business linkages. Hence, just as the IA-CEPA will be different to and more far-reaching than traditional trade agreements, so too should the negotiations. The usual 'defensive' and 'offensive' modes of negotiation should be supplanted by seeking to maximise opportunities.

The IA-BPG is heartened to note that a similar sentiment is expressed by the leadership of the two countries. The joint statement by both governments in March 2016 underlines the strong political will to go beyond traditional free trade agreements to develop a 21<sup>st</sup> Century agreement. The IA-CEPA will be a platform for a new, visionary partnership that is broader, more advanced, modern, and facilitative than a traditional FTA in all aspects of the economic relationship, as well as capacity building. The former Minister of Trade of the Republic of

Indonesia, Thomas Lembong and the Minister of Trade and Investment of Australia, Steven Ciobo MP agreed that IA-CEPA will proceed on the basis of the core principles that:

- both sides will strive to ensure the final agreement is high quality and as comprehensive as possible, covering trade in goods and services, investment and economic cooperation, and that it is balanced and delivers mutual benefits; and
- the final agreement should build upon the existing multilateral and regional agreements as well as negotiations between Indonesia and Australia.<sup>1</sup>

The two ministers further stated that “a successful Agreement would serve as a new platform toward a modern and dynamic economic partnership that reflects the strong bonds between the two countries.”

### ➤ **GOING BEYOND OTHER AGREEMENTS**

Indonesia and Australia are parties to a number of agreements and economic partnerships that reflect a trend toward a freer trade environment and global economic integration. Indonesia and Australia are parties to the ASEAN-Australia New Zealand Free Trade Agreement (AANZFTA) which provides the basis for more liberalised trade between Indonesia and Australia, as well as the rest of ASEAN and New Zealand. Australia provides preferential access to goods from Indonesia, as a developing country, through Australian System of Tariff Preferences (ASTP), ASTP is currently under review and has potential to be enhanced for Indonesia. Despite its availability this appears to remain underutilised and needs to be promoted more in Indonesia. It has potential for Indonesian exporters to make greater use of it.

ASEAN is also heading towards a more liberalised and integrated economy. The ASEAN Economic Community (AEC) is founded on four pillars contained in the AEC blueprint of achieving a single market and production base, a highly competitive economic region, a region of equitable economic development, and a region fully integrated into the global economy by 2015.

More broadly, since the initial discussions on IA-CEPA in 2012, two further ‘mega-regional’ trade agreements have emerged. The Regional Comprehensive Economic Partnership (RCEP) is an economic partnership between the ASEAN bloc and its Plus-Six partners with which it has Free Trade Agreements, namely: China, Japan, South Korea, Australia, New Zealand, and India. It focuses on integrating the economies of the ASEAN-Plus-Six members, and, as an ASEAN-led regional framework, is guided by ‘the ASEAN Way’ which is more consensus-oriented, accommodative and flexible in achieving common goals. RCEP is currently under active negotiation and is expected to be completed in 2017. IA-CEPA negotiations should not wait for RCEP outcomes or be overly guided by them, as the outcomes are uncertain and in any case are unlikely to be as progressive as both governments and IA-BPG wish for IA-CEPA.

The Trans-Pacific Partnership (TPP), on the other hand, is a “21<sup>st</sup> century trade agreement” involving 12 developed and developing country members on the Pacific Rim. Negotiations were concluded in November 2015 and member countries are undergoing their internal ratification processes. Australia is a member of TPP and Indonesia has announced its ambition to join the partnership.

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<sup>1</sup> Joint Statement by the Minister of Trade of the Republic of Indonesia and the Minister of Trade and Investment of Australia on the Reactivation of negotiations on and Indonesia-Australia Comprehensive Economic Partnership Agreement (IA-CEPA), Canberra, 16 March 2016.

Further, Asia-Pacific Economic Cooperation (APEC) is a forum of 21 Pacific Rim member economies which promotes free trade and economic reform throughout the Asia-Pacific region, and includes both Indonesia and Australia as members. Both countries are also members of the World Trade Organisation (WTO) and the G20.

Each of these global and regional frameworks provides important references for shaping and developing IA-CEPA. They also create the challenge for IA-CEPA to go beyond, what is already available under their existing and potential agreements.

The concept of the IA-CEPA is undoubtedly complementary to the AEC, ASEAN, AANZFTA, APEC and WTO and APEC agendas. The final agreement must also be complementary to, and support, these agreements. The characteristics of the AEC provide benchmarks for both the AANZFTA and IA-CEPA to provide significant opportunities for the IA-CEPA to leverage the rapid progress towards ASEAN economic integration.

### ➤ **FOCUS ON SERVICES**

Services are going to play an increasingly important role in both the Indonesian and Australian economies as they transform. Services is both a key sector, encompassing many industry classifications, and a sector that is vital to all facets of the two economies, enabling competitiveness and transfer of knowledge and technology. Given the growing role of services in the Indonesian and Australian economies in enabling other sectors, in bilateral trade and investment, and in accessing global value chains, services need particular attention in the IA-CEPA.

For Indonesia, services will be vital to meeting the needs of the growing middle class, in supporting efficient primary and secondary industry, in enabling participation in global supply chains, and in transforming and growing the economy. For Australia, services are similarly important domestically, while they are playing an increasingly important role in exports.

Despite their importance domestically, and in bilateral trade and global supply chains, services are unnecessarily restricted by both Indonesia and Australia. This harms both economies. In the following chapter, this position paper identifies specific barriers to services trade and investment and recommendations to overcome them.

The Indonesia Services Dialogue Council Policy Recommendation 2015 report<sup>2</sup> sets out the implications of restrictions on Logistic Services, Distribution Services, Energy Services, ICT Services and e-Commerce. The Policy Recommendations report provides an excellent prescription for policy change in these sectors as well as others. In particular the report recommends review of the Negative Investment List to unlock the sub-optimal growth of services sector.

The Negative Investment List is also the most often cited regulatory instrument of concern to foreign investors in services. While the list was extensively modified earlier in 2016 to make some sectors more open to majority foreign investment, many sectors remain effectively closed, or significantly restricted to investors, which understandably seek control over their investment. Moreover, while the Negative Investment List may have opened up in several sectors, other regulations have gone the other way, effectively negating the more open provisions of the list.

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<sup>2</sup> <http://isd-indonesia.org/wp-content/uploads/2015/10/Indonesia-Services-Dialogue-Policy-Recommendation-Yose-Rizal-Damuri.pdf>

The Australian Services Roundtable has made recommendations<sup>3</sup> for Australian domestic and trade policy changes in its numerous submissions to governments. These include a review of barriers to investment such as state based professional licensing and currency restrictions and payment systems.

## RECOMMENDATIONS

- The IA-BPG recommends ongoing review and liberalisation of the Negative Investment List in Indonesia and further liberalisation of access to the services sector in Australia.
- Restrictions on movement of people is another major impediment to growth in services trade and investment. As this position paper advocates elsewhere, easier movement of people is a key to the success of the IA-CEPA.

### ➤ **DELIVERING ECONOMIC ASPIRATIONS**

#### ***Potential of Indonesia-Australia Economic Relationship***

In preparing this position paper the IA-BPG commissioned an analytical study of economic relations between Australia and Indonesia by Dr. Kiki Verico of the Faculty of Economics and Business at University of Indonesia. The study, included as Appendix 1, provides a detailed academic analysis of the economic relationship between Australia and Indonesia – including the historical and socio-political links between the two countries, trends in trade, commerce and economic growth. It provides extensive background material and context, providing a wide range of economic data, statistics and indicators. It concludes that, while the economies of the two countries exhibit significant differences, those differences are complementary and provide potential for significant *additional* growth as a result of concluding a comprehensive economic partnership agreement.

Assuming a closer economic relationship, such as that envisaged in the IA-CEPA, the report predicts greater economic growth for Indonesia and Australia. On that basis the report predicts that:

- Indonesia's long-term economic growth is predicted to increase from 5% (1999-2014) to 7.4% (2016-2030).
- Australia's long-term economic growth is predicted to increase from 3.1% (1999-2014) to 3.6% (2016-2030).
- Indonesia's GNI per capita is predicted to reach US\$10,385 by 2030 from US\$3,573 in 2015.
- Australia's GNI per capita is predicted to reach US\$118,648 by 2030 from US\$60,070 in 2015.
- Per capita income in Indonesia will triple over the next 15 years, while Australia's will almost double.

<sup>3</sup> <http://australianservicesroundtable.com.au/>

Indonesia and Australia are the two largest economies in the Southeast Asia/Oceania region. Together, they would be the ninth largest economy in the world. Indonesia is one of the fastest growing economies in the developing world (over the past decade it was third only to China and India in annual GDP growth), while Australia is the fastest growing OECD economy.

The bilateral trade and investment performance of the two economies greatly underperforms their potential, despite Indonesia and Australia being neighbours and despite their economic complementarities. The two economies are different in structure, typically reflecting their development status. Comparative and competitive advantages are different. Business and institutional cultures and capabilities are different. Business in each nation poorly understands opportunities in the other nation and how to do business there. Trust and confidence are, in general, low.

Nevertheless, and indeed in part due to differences, strong complementarities exist between the two economies. With complementary patterns of consumption, production, technologies and skills between Indonesia and Australia, and with the synergies that exist between the economies, there are lucrative opportunities for partnership to enhance economies in ways that either nation cannot do on its own. Building on existing agreements, the IA-CEPA is needed to provide an innovative framework for building a strong, lasting economic partnership.

Of all of Indonesia's and Australia's relationships, an economic partnership between them has the greatest potential for transformational change in bilateral ties. For Indonesia, Australia can work to meet crucial needs spanning agriculture to tourism, infrastructure to e-commerce to support Indonesia's economic growth and global trade connections. For Australia, Indonesia can open new avenues for growth using human resources, natural assets and the AEC as a springboard into Asia and the world beyond. When there is greater trade and investment, more partnerships and more people-to-people contact, the relationship will change for the better to one of mutual respect and greater cooperation towards achieving shared goals.

### ***IA-CEPA Basic Features***

The IA-BPG supports the concept of an IA-CEPA that is much broader than an FTA. The IA-CEPA should also reflect more advanced commitments than the ASEAN-Australia New Zealand Free Trade Agreement (AANZFTA) and at least the commitments of other FTAs that Indonesia and/or Australia have agreed with other nations. The IA-CEPA will lay the foundations for a comprehensive partnership between Indonesia and Australia that facilitates much greater trade, investment and joint business activity, utilising joint efforts between governments, relevant organisations, businesses and educational institutions as well as capacity building in areas that will have a strategic impact on bilateral economic relations. The free flow of raw materials and partially manufactured goods, capital and services will also enable economically efficient production chains to facilitate access to global markets and supply chains beyond our mutual borders.

The basic features of IA-CEPA as identified and recommended jointly by the business communities of Indonesia and Australia are as follows:

1. Further liberalisation of two-way trade in goods through faster tariff reductions and no or very limited exclusions (that need to be WTO consistent), and lowering of at-the-border and behind-the-border barriers, such as quotas and bans (with remaining measures needing to be WTO-consistent), to enable producers in both countries to

access both markets and in the process gain experience for jointly accessing other markets.

2. Liberalisation of two-way trade in services, including reduction of restrictive regulation, and enabling movement of natural persons to enable service providers in each country to access the other market and satisfy demands for services, knowledge and technology, enhancing providers' capacity and quality, and improving customer experience.
3. Investment facilitation in all sectors through more effective provision of investment information, actively encouraging two-way investment, promotion and reduction or removal of investment restrictions to increase economic activity in both economies.
4. Alignment and simplification of rules, including mutual recognition of technical standards for goods and services, professional qualifications, standards and classification of goods for customs purposes that will improve trade facilitation.
5. Facilitating movement of skilled persons to Indonesia and Australia, and seasonal workers to Australia, and capacity building for less skilled workers including in-market experience and improved language skills, to increase the pool of available people to support mutual economic development.
6. Value chain integration by cross-border cooperation to identify market opportunities and business synergies, leverage comparative and competitive advantages, improve access to internal markets and participate in global supply chains.
7. Ongoing capacity building to improve government policy and procedures, build institutional capacity, lift skill levels, facilitate bilateral business opportunities, improve two-way cultural and language skills and understanding, and boost farm production and food security
8. Digitisation of trade-related practices and increased trust in the online environment through an e-commerce chapter.
9. Facilitating trade in Environmental goods and services through identification of joint opportunities, and lowering of barriers to trade, investment and movement of people.
10. Promoting the development of Small Medium Enterprises SMEs by fostering cooperation and investments between SMEs in both Indonesia and Australia.
11. Seeking mechanisms that facilitate *regional* business development in addition to business in the current economic centres of both countries.
12. Establishing new institutional mechanisms to monitor and facilitate the implementation of IA-CEPA.

### **Key Characteristics of the IA-CEPA**

The Indonesian and Australian business communities agree that the IA-CEPA should be characterised by the following:

#### **1. Economic cooperation.**

The primacy of economic cooperation in the IA-CEPA over standard free trade agreements has been emphasised throughout the IA-BPG's deliberations. The potential gains from strategic cooperation between both countries' private sectors and governments are enormous, especially in cross-border value integration along the value chain of the economic

and business processes. The fact that both economies are essentially complementary in terms of resources and capabilities has made the case even more compelling. The economic analysis commissioned by IA-BPG (Appendix 1) found that “Indonesia and Australia both produce products that the other needs, providing an excellent opportunity for each of them to build strong trade relations”. And further, Indonesia’s abundance of unskilled labour, complements Australia’s relatively small, but highly skilled workforce. Australia’s development assistance program will be both a key economic cooperation mechanism in itself and an enabler of private sector economic cooperation between the two countries. The program should be aimed at building economic capacity and facilitating development of markets and value chains for both partners.

**2. *IA-CEPA as a dynamic and growing process.***

IA-CEPA should be a living process, a work in progress that needs consistent implementation, monitoring and evaluation as well as improvement over time. It is therefore required that an ongoing process of business input, including some form of permanent framework needs to be established between the two countries’ governments and private sectors to oversee the transformation and progress.

**3. *Fostering inclusive growth in both countries.***

Inclusiveness encompasses equity, equality of opportunity, and support in market and employment transitions. Inclusive growth should contribute to sustained poverty reduction allowing people to participate in and benefit from economic growth. This is essential item for a successful growth strategy that should be a key feature in the IA-CEPA. Equality of opportunity in terms of gender impacts and geographic spread of the opportunities and benefits, access to markets, resources, and unbiased regulatory environment for businesses and individuals should also be emphasised. Inclusive growth also implies a longer term perspective with regards to the targeted impacts to be achieved.

**4. *Continuous engagement with stakeholders.***

The IA-CEPA is expected to have a broad and far-reaching impact on both economies. This will require a transformation strategy that will facilitate and encourage changes within the business sector, especially SMEs. Continuous engagement with business communities in both countries is needed to ensure high awareness and buy-in. The IA-CEPA should also be practical, providing immediate outcomes through short term actions and solutions, and yet maintain a long-term aim and vision. The IA-BPG and its member organisations can continue to facilitate engagement of business during IA-CEPA implementation and be a conduit for feedback and measurement of impact.

**5. *Include measures to tackle the information shortage, and market failure, and facilitate business linkages.***

Businesses from both countries identified a lack of available information regarding business and trade opportunities in both markets. This lack of information – and even misinformation – is a major hindrance to the increase of trade and investment cooperation. While a significant business relationship already exists between the two countries, business stakeholders feel that this represents a narrow base and that much would be gained from organised and systematic business information sharing and awareness-raising in both countries. Even with better information on markets and doing business, the business relationship may continue to underperform due to longstanding negative perceptions and even lack of trust between businesses and between business and government. Therefore, aside from, measures creating a greater systematic exchange of information, the IA-CEPA

should provide funding for trade and investment promotion, and include mechanisms that will facilitate building relationships of trust leading to stronger B-to-B and B-to-G linkages.

### ***Business Involvement and Stakeholder Engagement in IA-CEPA***

The establishment of the IA-BPG and the resulting consultation and discussions between business associations in Indonesia and Australia represents a unique and ground-breaking approach to stakeholder involvement in a G-to-G negotiation process such as the IA-CEPA. The IA-BPG process has enabled business communities from both countries to voice their opinions to shape the economic and trade relationships that Indonesia and Australia are trying to build.

Following the approach taken by the IA-BPG in 2012 – that is, a consultative process which sought input from all business stakeholders – in preparing the current submission, the associations which make up the IA-BPG invited each of their constituent members to provide input, opinions, recommendations, or other suggestions through interviews, written submissions and workshops. Whereas in 2012 IA-CEPA was a relatively new concept, in the intervening period general awareness about the negotiation has increased, leading to better understanding of the concept and hence more extensive inputs to the IA-BPG process. More details on the process of seeking input from the private sector and other stakeholders are contained in the annex of this report.

Nevertheless, although this position paper reflects the broadly held position of Indonesian and Australian business, it is not possible for the paper to reflect the views of business on every aspect of the IA-CEPA.

As negotiations proceed between the two governments, business will need ongoing opportunities to provide input, particularly on the sectoral detail of the IA-CEPA, as well as on cross-sectoral and economic cooperation matters.

In addition, the IA-BPG points out that the process is almost as important as the outcome, in that the recent and ongoing consultations will be important in informing business about opportunities and in overcoming information deficits and market failure.

Further, as noted above, the IA-BPG believes that the IA-CEPA should be a dynamic agreement that can be adapted over time. In this context, the IA-BPG recommends the following to be established during the IA-CEPA negotiations:

- ***Continuing Business to Business Engagement.***  
Initiatives such as the IA-BPG should become a model for business associations from both countries to engage with each other to discuss and identify opportunities for cooperation. Chambers of Commerce and Business Councils could be the drivers in both countries and encourage their members to foster closer relationships with their counterparts in Indonesia or Australia. Businesses from both countries need to start looking at the significant opportunities that can be achieved by working together. Business to business engagement is also an efficient way to overcome the current market failure.
- ***Broader Stakeholder Engagement.***  
The IA-BPG also concludes that stakeholder engagement should not be limited to businesses only. IA-CEPA should include provisions for engaging with a broader set of stakeholders that can have a significant impact on the upcoming IA-CEPA. This should include the media, civil society, universities and local government institutions. Engagement with these stakeholder

groups in both countries is needed to ensure high awareness and buy-in. As an example, there is a general cynicism towards FTAs, CEPAs and an open economy in Indonesia. Meanwhile in Australia there are some community concerns about FTAs, plus negative and out-dated views about Indonesia that inhibit cooperation. This will need to be tackled strategically through stakeholder engagement activities. Engagement with the mass media is important considering its capacity to influence public opinion. False perceptions on both sides are in many ways fed by the media.

▪ ***Establishment of Ongoing Business Engagement***

The IA-BPG commends the commitment of the Department of Foreign Affairs and Trade (Australia) and the Ministry of Trade (Indonesia) to accommodate mechanisms to involve business and seek their input. The IA-BPG recommends that an ongoing process of business input, including a government-business group be established to oversee the implementation, monitoring and further development of the IA-CEPA. The IA-BPG suggests the committee should consist of representatives from the business community, sector experts and other stakeholder representatives (including academics) from both countries who will further discuss in detail how to activate the opportunities and address issues raised in this paper and by others. In line with the intention to make the IA-CEPA a living process, the ongoing IA-BPG will continue to provide input and suggestions on the IA-CEPA negotiation process and its application.



## Chapter 2

# ADDRESSING IMPEDIMENTS TO TRADE, INVESTMENT AND ECONOMIC COOPERATION

Despite recent trade liberalisation, a range of impediments to greater trade and investment flows between Indonesia and Australia – and to business collaboration – still exist.

During consultations and IA-BPG discussions, the business sectors from Indonesia and Australia, as drivers of trade and investment, drew on their knowledge and experience to provide insight into what are perceived to be the main obstacles to a stronger trade and investment relationship between the two countries.

Recommendations and expectations for the IA-CEPA expressed during consultations formed a starting point for the IA-BPG in devising this paper. As discussed above, an ongoing stakeholder engagement process is an essential element in drawing advice from a wide range of stakeholders and to develop the key pillars and sectoral and cross-sectoral detail of the IA-CEPA.

Despite the opportunities to develop comprehensive partnerships in many sectors between Indonesia and Australia, and despite their obvious benefits, the following section outlines several issues that continue to hamper trade and investment between the two countries.

## TRADE AND INVESTMENT BARRIERS

A more open and free flow of goods and services, with a high realisation of investment should be the main goals of the IA-CEPA according to business communities. This cannot be achieved if trade and investment barriers remain in place. The IA-CEPA should also contain a commitment that neither country will impose further trade restrictions in future, including for trade in new kinds of goods and services. Barriers to trade and investment as identified by business stakeholders are as follows:

## ➤ **REMAINING TARIFFS**

As noted in the IA-CEPA position paper of 2012, stakeholders in both countries have pointed to remaining tariff barriers as a significant impediment to trade. As the IA-CEPA is expected to be complementary to the provisions of AANZFTA, IA-BPG seeks to accelerate the AANZFTA commitment to phase-out and ultimately remove tariffs, including tariffs on products which have, so far, remained exempt from AANZFTA. According to AANZFTA's tariff elimination schedule, Australia has committed to 100% elimination of tariffs by 2020 while Indonesia has committed to eliminating 93.2% of overall tariffs by 2025. A quarter of Australian goods trade currently faces Indonesian tariffs, while as discussed below, trade in some goods where Indonesia has a competitive advantage (eg, textiles, clothing and footwear) still faces substantial tariffs in Australia.

The IA-BPG recommends the accelerated removal of all tariffs, as rapidly as possible. This will improve consumer choice and reduce costs of inputs by manufacturers, as well as assisting integration of value chains.

Indonesia has reduced but not eliminated tariffs on a range of agricultural and agribusiness products, including live cattle, certain categories of mutton and lamb, frozen pork, processed seafood, several dairy products, and some fresh and processed fruit and vegetables. A number of sensitive agricultural products such as rice, sugar, wine and spirits are also excluded from Indonesia's AANZFTA tariff reduction commitments, therefore some products continue to be subject to high tariffs. The Indonesian government is of the view that rice and sugar are staple agricultural commodities that need to be regulated and monitored considering the high consumption rates of those products and to protect local farmers. While the need to protect local farmers can be recognised, IA-CEPA should ensure that tariffs applied to Australia are reduced as much as possible and are at the same level as those applied to other countries. For example, Australian sugar exporters raise concerns relating to disadvantages arising from the ASEAN Trade in Goods Agreement (ATIGA) which provides lower tariffs and thus favours sugar imports from countries such as Thailand. There must be a reduction in tariffs on Australian sugar imports at least to a level equivalent to that applied to Thailand.<sup>4</sup>

On the other hand, Australia has already eliminated tariffs on most agricultural products but is applying a slower phasing out of tariffs on several lines of products, especially in manufacturing until 2020. Some tariff lines on textiles and textile products in Australia remain, and will only be phased out completely by 2020. For example, woven fabric textiles; wool carpet; terry towelling, and cotton knitted and crocheted fabrics will still be subject to tariffs until 2019. As for apparel and clothing accessories, a 15% tariff is applied and will be gradually reduced to 10% in 2019. Although the annual quantity of Indonesian textile exports remains limited, Indonesian textile businesses submit that, under IA-CEPA, textile exports to Australia should be made completely tariff-free or that they should receive a special tariff rate. Currently, there are only two tariff-free textile products, that is HS 52 (Garment Knitting) and HS 62 (Garment Non-Knitting).<sup>5</sup> While Indonesia already receives preferential treatment under the Australian System of Tariff Preferences (ASTP), eliminating these tariffs more rapidly will open up opportunities for Indonesian textile and clothing producers to compete with Chinese products in the Australian market. The current review of ASTP could recommend much larger concessions for Indonesia,

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<sup>4</sup> Submission from Australian Sugar Industry Alliance.

<sup>5</sup> Interview with the Indonesian Textile Industries Association (API).

but as stated, the preference of the IA-BPG is for faster removal of tariffs under IA-CEPA. Additionally, in the agricultural sector, Indonesian stakeholders seek the elimination of import tariffs on cocoa products.<sup>6</sup>

A complete removal of tariffs on manufactured goods would maximise consumer choice and enable producers to have greater access to raw or semi-finished materials and improve their competitiveness in the global market.

## ➤ **TRADE REGULATIONS AND PROCEDURES**

Complicated regulations and procedures often hamper the free movement of goods and services. Regulations are often overlapping and unclear, causing delays to business processes. Indonesian and Australian businesses stated their need for comprehensive guidance on trade regulations and market opportunities. Such guidance would help boost efficiency and productivity of conducting business in the respective countries as well as avoiding unnecessary complaints about trade between the two countries.

For Indonesian businesses, clearer guidance on import requirements into the Australian market is needed. Indonesian stakeholders have commented that lengthy delays are encountered when exporting goods such as handicrafts and coffee to Australia due to customs and quarantine processes.<sup>7</sup> Businesses have therefore voiced their preference for simplified procedures which will lower costs, increase certainty of outcomes and avoid double quarantine processes. Many Indonesian stakeholders believe that these procedures are intended to impede the entry of Indonesian goods to the Australian market, especially considering that the same goods are accepted more easily into the United States or European markets. Negative perceptions of this kind should be addressed by the IA-CEPA by making it facilitative and providing mechanisms which assist Indonesian exporters to enter the Australian market - including detailed information on how to meet usual quarantine provisions.

The Indonesian tobacco sector has pointed to Australia's plain packaging policy for tobacco products as a barrier to trade, and contends that there is insufficient scientific evidence to support the mandatory use of plain packaging. Indonesia, with several other countries including the Dominican Republic, Cuba, Ukraine and Honduras, have protested against Australian plain packaging policies arguing that the policy breaches Australia's international trade obligations with regard to intellectual property rights, in particular trademarks and geographical indications.<sup>8</sup> In the context of IA-CEPA, policies should be avoided by first having sound scientific basis before being enacted.

Just as Indonesian businesses have expressed concerns about regulatory difficulties in trade with Australia, so too have Australian businesses have voiced concerns about complicated and opaque regulations and procedures applied to trade in Indonesia. IA-BPG recognises that Indonesian Government is striving to remove certain trade obstacles by revising related regulations (eg, regulations on the importation of animal and animal products). Indonesia is progressively improving its trade and investment environments, but IA-BPG appreciates that such actions are taken with careful assessment, considering Indonesia has been paying special attention on its

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<sup>6</sup> Submission from Indonesian Cocoa Association (ASKINDO).

<sup>7</sup> Submission from Association of Exporters and Producers of Indonesian Handicraft (ASEPHI). Interview with Association of Indonesian Coffee Exporters and Industries (AEKI).

<sup>8</sup> Interview with Indonesia Tobacco Community Alliance (AMTI).

micro, small, and medium-sized enterprises (MSMEs) and preparing itself for global free trade era.

As was the case when IA-BPG prepared its 2012 report, Australian businesses still face complicated procedures in exporting food and food products into the Indonesian market. All imported products must be registered with the Indonesian National Agency for Drug and Food Control (BPOM) to obtain ML numbers, which takes 6 to 18 months to complete. Australian goods also require Halal certification from the Indonesian Council of Ulama (MUI) and must comply with Indonesian National Standards (SNI) certified by the Indonesian National Standardization Agency (BSN). Compliance with this suite of regulations is perceived as being complex, difficult and unclear by Australian business entities. Comprehensive and authoritative guidance in navigating these bureaucratic requirements is essential for achieving better trade outcomes for both countries.

Protective policies and regulations are still applied in the services sectors of both countries. For example, Australian doctors will find it difficult to operate in Indonesia despite the country's high demand for world-class health treatment, as will Indonesian doctors who would like to gain experience in Australia. The restrictions also limit the ability of Australian doctors to do on-the-job training in Indonesia. There is a need for cooperation with Australia in training, particularly for doctors who are in dire need for professional capacity building out of Jabodetabek and Java island and inland rural areas. The regulations should be relaxed to facilitate this.

Other professional services also deal with the same problems that hinder cooperation in this sector creating hurdles for transfer of knowledge, technology and best practices. Common understanding on what are considered acceptable qualifications for workers between Indonesia and Australia is also needed – as Australia's definition of "skilled" workers is based on possessing a recognised qualification.<sup>9</sup>

## RECOMMENDATIONS

- Establish a consultation forum to provide guidance on trade regulations and market opportunities particularly as they apply to professional services. Such guidance would help boost efficiency and productivity of conducting business in the respective countries, and enhance capacity.

### ➤ TECHNICAL BARRIERS TO TRADE

Technical barriers to trade, such as SPS<sup>10</sup> measures, mandatory registration requirements, or certifications, applied in Indonesia and Australia often hinder trade and investment. According to stakeholders, both Indonesia and Australia apply complicated standards and certifications processes which limit the free movement of products.

<sup>9</sup> Indonesia-Australia Business Partnership Group, "Position Paper: on Considerations towards the Indonesia-Australia Comprehensive Economic Partnership Agreement," 2012.

<sup>10</sup> Sanitary and Phytosanitary.

Overall, the IA-CEPA should seek to have Indonesia and Australia can work together harmonising on standards and regulations – for example, improved regulatory coherence between them, cooperative mechanisms, and mutual recognition.

### ***Sanitary and Phytosanitary Standards***

In Australia, high SPS<sup>11</sup> standards and quarantine requirements are not readily understood or complied with by Indonesian producers due to both capacity issues and costing pressures.<sup>12</sup> For Indonesian producers, the US and EU markets are considered more sizeable and attractive, making efforts to meet required US and EU standards worthwhile, compared to what they see as a small market in Australia by comparison. However, Indonesian businesses are baffled that these standards are often not recognised by Australian authorities. While many are unconvinced that the extra efforts and costs required to meet Australian SPS measures are commercially feasible, they expect that products already meeting international standards as applied in the US or the EU should also be accepted in Australia.

For example, Indonesian coffee products, which usually accepted worldwide, find it difficult to enter the Australian market due to the Australian high standards.<sup>13</sup>

The IA-BPG notes that the Thailand Australia FTA enables easier export of fruit to Australia, and includes cooperation to help Thai exporters meet SPS requirements. The IA-CEPA should include a program within the Economic Cooperation stream that establishes a capacity-building and export facilitation activity to support exporters of Indonesian agricultural products.

### ***Quarantine***

Quarantine agencies also need to collaborate in order to avoid double quarantine processes. For example, the Indonesian government requires imported cotton plants to be quarantined to prevent spread of disease. Similarly, the Australian government requires quarantining of cotton plants prior to export. This is seen as inefficient and hampers the supply of cotton. Quarantine mechanisms must protect the unique environments of both countries and be based on scientific rigour and risk-based analysis. However, it should not impede otherwise justified trade flows that may lead to inefficiency and higher production costs.

### ***Harmonising Standards***

Harmonising or aligning international standards has been identified as one area which will significantly facilitate trade; and progress has already been made in this area. The Indonesian National Standardization Agency (BSN) and Standards Australia (SA) have already commenced work on formulating an IA-CEPA Standards Harmonization Action Plan.<sup>14</sup> In this Action Plan, SA

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<sup>11</sup> SPS measures are applied to protect human, animal and plant life or health from risks arising from the introduction and spread of pests and diseases and from risks arising from additives, toxins and contaminants in foods and foodstuff.

<sup>12</sup> Interviews with Association of Indonesian Peppers Exporters (AELI), the North Sumatera chapter of Indonesian Association of Employers (APINDO Sumut), the East Nusa Tenggara chapter of Indonesian Association of Employers (APINDO NTT), the Association of Exporters and Producers of Indonesian Handicraft (ASEPHI), the Indonesian Fish Cannery Association (APIKI), the Association of Indonesian Soft Drinks Manufactures (ASRIM), the Indonesian Cosmetic Producers Association (PPA-Kosmetika).

<sup>13</sup> Submission from Association of Indonesian Coffee Exporters and Industries (AEKI)

<sup>14</sup> Submission from Standards Australia Ltd.

and BSN will collaborate to develop and align joint standards with the aim of reducing unnecessary costs stemming from different standards and regulations.

SA is well placed to provide technical expertise and capacity building support to BSN through an economic cooperation program to support the implementation of Standards, Technical Regulations and Conformity Assessment Procedures (STRACAP) provisions in the IA-CEPA. SA's actions include joint planning of activities, development of a Voluntary Action Plan for the adoption of international standards, and the implementation of a specific IA-CEPA Standards Harmonization Action Plan.

With regard to harmonisation of standards, the IA-BPG notes that significant differences may exist across various sectors in the complexity and length of time required to implement this process. Hence, priority sectors most in need of harmonisation should first be identified by both governments through consultation with business associations. Food and beverage, agriculture and labor are three high priority sectors.

The Indonesian plastic industry also emphasises that HDPE (High Density Polyethylene) which is currently not accepted in Australia, is normally accepted in other markets globally.<sup>15</sup>

### ***Halal Certification***

Halal certification has also been raised as a potential obstacle to trade which could be addressed by a coordinated approach. Currently, Australian processed food entering the Indonesian market must be certified as halal by the Indonesian Ulama Council (MUI). Establishing a joint body which could certify products as halal for the Australian, Indonesian and third-country markets could significantly address inefficiencies and uncertainty which currently exist in this area. Addressing this issue would lead to greater efficiency for exporters, which translates to greater access, choice and lower costs for consumers.<sup>16</sup> The end outcome should be one that supports trade and at the same time meets the larger objectives underpinning the new halal standards.

The BPG notes that the issue of halal certification is more complex than it may appear, as there remain differences between the halal certification requirements between Moslem countries which act as an impediment to the mutual recognition of halal standards.

### ***Alignment of Qualifications***

A further technical barrier to trade which should be addressed by IA-CEPA is the standardisation or alignment of qualifications for workers in the services sector. Indonesian stakeholders expressed difficulty in meeting specific sectoral standards applied in Australia. Indonesian professionals with qualifications in the mining and insurance sectors are relatively well-placed to enter the Australian market. However, qualifications of skilled workers such as nurses or caregivers are generally not recognised in Australia.

Stakeholders have therefore expressed the hope that an IA-CEPA can address this by providing capacity building to facilitate the entry of services sector workers into both markets. For example, Indonesian electrical engineers have expressed a need for further capacity building, training and skills enhancement to facilitate the certification necessary to access the Australian market.<sup>17</sup> Meanwhile, it is difficult for Australians to enter the Indonesian services market as

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<sup>15</sup> Submission from Indonesian Olefin Aromatic and Plastic Industry Association (INApLas).

<sup>16</sup> Submission from Meat and Livestock Australia.

<sup>17</sup> Interview with the Association of Indonesian Electrical and Mechanical Contractors (AKLI).

medical doctors or legal practitioners, although Australian lawyers may practice in Indonesian law firms with certain restrictions.

### ➤ **TRADE RESTRICTIONS SUCH AS IMPORT QUOTAS AND LICENSING**

In agriculture and agribusiness, Indonesia imposes import quotas and restrictions on beef and live cattle imports intended to protect domestic beef producers, and promote a long-term plan to achieve beef self-sufficiency. A recent decree imposes a restrictive weight limit on live cattle imports of 350 kg per consignment. Quantitative restrictions on the number of live cattle import permits are also imposed, and beef/offal import permits are also managed with import volumes being adjusted on an ad-hoc basis. Indonesia also currently enforces a ban on offal products and there is no agreed specific certification for the import of Australian rendered edible animal fats and oil, such as tallow, into the Indonesian market.<sup>18</sup> In terms of licensing, Australian stakeholders submit that procedures for administering import permits lack transparency and certainty. There is also concern that Indonesia's current ban on offal products cannot be justified on a food safety or halal certification basis.

Stakeholders from the meat and livestock sector therefore recommend that the IA-CEPA address the removal of these non-tariff measures which adversely impact industry's ability to provide consistency and certainty of supply.

In the agriculture sector, the Indonesian business people ask for Indonesian government consideration to eliminate import restrictions for canned fish products and refined sugar. Although this suggestion is initially expressed by the Indonesian side, this may impact the bilateral supply chain. Australian supply is needed to provide Indonesian demand of both fresh fish for the canned fish industry and refined sugar for the soft drink industry.<sup>19</sup>

In the mining and energy sector, the Indonesian government recently imposed a ban on exports of raw minerals, in an effort to secure domestic supply and boost development of the domestic downstream industry. The 2009 Indonesian Mining Law stipulated a complete export ban of unprocessed mining commodities to take effect in 2014, with progressive steps to reduce large-scale exports that are perceived as a threat to the country's energy security. Due to low commodity prices, Indonesia later issued governmental and ministerial regulations in 2014 extending the deadline to 2017 for companies with a demonstrated commitment to establishing processing facilities.

The Indonesian government is not expected to relax the provisions of the law although the Indonesian Mining Law is scheduled for revision in 2016. Regarding foreign investment, the current law still requires that mining services must be provided by Indonesian companies where available. Foreign mining services companies may only operate under special conditions where national providers are considered to be unable to provide the necessary services.

In manufacturing, some goods, such as plastics, medicines, alcohol and lubricants amongst others are subject to restrictions such as special licences and/or limited import volumes to Indonesia. The government issues these policies in order to protect up-stream industry and also consumers from low quality hazardous materials. Evaluation of these policies has taken place

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<sup>18</sup> Submission from Meat and Livestock Australia.

<sup>19</sup> Interview with Indonesian Fish Cannery Association (APIKI) and the Association of Indonesian Soft Drink Manufacturers (ASRIM).

based on discussions with upstream and downstream industry. If restrictions and special licences continue to be applied it will be difficult for Australia to obtain certain raw materials from Indonesia, for example restrictions on wood exports by Indonesian government to favour Indonesian downstream industries in manufacturing.

Restrictions can also be found in Australia where the government applies strict regulations on pharmaceutical and botanical products which represent an impediment to Indonesian herbal medicine companies acquiring supplies from Australia. Still related to manufacturing, some in Australian business have called for anti-dumping measures for paper products to protect local industry.

IA-BPG recognises that dumping and accusations of dumping can negatively impact on the bilateral relationship. While the rules around Anti-Dumping are technically administered by the WTO, we believe that in the interests of the bilateral relationship there should be ongoing cooperation to ensure that local industry, importers, exporters and customers have confidence in both the process and the decisions of the respective Anti-Dumping authorities. With any regulatory scheme, it is essential that governments receive regular updates from industry to ensure that the system continues to be effective in a dynamic business environment and provides industry with timely, consistent and transparent decisions.

In the services sector, protective regulations exist particularly in regard to the provision of professional services in Indonesia. Very tight entry controls and restrictions on business operations are considered discriminatory in professional services in Indonesia, and cover accountants, lawyers, architects, engineers, banking and healthcare professionals. Under current Indonesian regulations commercial presence of foreign services providers is not permitted without engaging local partners. In Indonesia, foreign lawyers may not exceed 20% of the proportion of lawyers in a firm and no more than five foreign lawyers per firm are allowed.

### ➤ **BARRIERS TO TEMPORARY ENTRY OF SKILLED PROFESSIONALS AND SEASONAL WORKERS**

Remaining and persistent impediments on trade are not limited to barriers to trade in goods and services. Impediments on the temporary entry of skilled professionals and seasonal workers also represent a significant obstacle to increased trade and economic engagement. In the context of the IA-CEPA negotiations, the movement of such workers is considered a key element to developing a fairer – not limited to freer – movement of skilled people. More importantly, without better conditions for movement of people, the IA-CEPA will not deliver on its full potential, as accessing the necessary skilled labour and human resources is key to success.

Issues of temporary entry of skilled professionals and seasonal workers relate to processes for obtaining visas, work permits and length of stay. There are also barriers created by a lack of mutual recognition of qualifications which needs to be addressed in the IA-CEPA. Basically, visa requirements between the two countries are imbalanced. While Australian tourists may use visa-free and businesspeople may use or visa-on-arrival entry when visiting Indonesia, Indonesians are still subject to a lengthy, burdensome process for obtaining a visa for travel to Australia.<sup>20</sup> However, Australian stakeholders have also pointed to difficulties in the process of acquiring multi-entry business visas or work permits (KITAS). In many cases, Australian business people

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<sup>20</sup> Interview with Association of Indonesian Congress and Convention (AKKINDO).

revert to a tourist visa when they should be travelling on a business or work visa and this impacts the reporting and classification of travel to Indonesia by Australians.<sup>21</sup>

The IA-CEPA creates an opportunity for the development of a new visa category with characteristics that can be drawn from existing Australian visa schemes such as the Pacific Seasonal Worker Scheme<sup>22</sup> (providing seasonal employment) and the Enterprise Migration Agreements<sup>23</sup> (providing project-based temporary employment). IA-CEPA should include a relaxed and novel visa scheme which allows Indonesians and Australian skilled workers to easily move across the border as envisaged in the ASEAN Economic Community. With a more relaxed visa scheme Indonesians will benefit from on-the-job experience (such as internships and secondments) to improve their English language and professional skills before returning to Indonesia to further contribute to economic development. Similarly Australians could benefit from in-market experience in Indonesia and Indonesian language skills.

Indonesian stakeholders believe that qualifications required to enter the Australian services market are unfair.<sup>24</sup> Representatives from the Indonesian private sector stressed that there is an unnecessarily high level of English competency required for Indonesian migrant workers (semi-skilled labour) to enter the Australian market under the 457 visa scheme. For instance, Indonesian nurses find it difficult to practise in Australia because of the stringent requirements which must be met. In order to obtain nursing registration, foreign nurses are required to obtain a relatively high IELTS test result of 7.0 out of 9, in addition to other requirements such as obtaining sponsorship or a resident visa, as well as undergoing a medical examination. Indonesian graduates from Australian universities have voiced concerns about the difficulties of obtaining post-graduation work experience or job opportunities; graduating from an Australian university does not guarantee the ability to undergo work experience in an Australian workplace. On the other hand, Australian medical and legal practitioners who seek to practise in Indonesia face similar restrictions.

However, changing conditions in the global labour market in coming years may drastically alter the situation in this area. Predictions of a massive skilled labour shortage across Australia by 2030 due to a service-dependent and ageing population could lead to significant opportunities and benefits for Indonesian skilled workers.<sup>25</sup> With a view to this eventuality, Indonesia and Australia should now take the necessary steps to facilitate alignment of skills qualifications, skilled labour standards, training, capacity development and visa requirements to ensure that the needs of the skilled labour market are met and future mutually desired and expected outcomes are achieved.

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<sup>21</sup> Submission from AFS Intercultural Program Australia.

<sup>22</sup> The Seasonal Worker Program commenced on 1 July 2012, building on the Pacific Seasonal Worker Pilot Scheme in contributing to the economic development of participating countries, while also offering Australian employers in the horticulture industry access to workers from eight Pacific island nations and East Timor when they cannot find enough local labour to satisfy seasonal demand. (DEEWR – Australia).

<sup>23</sup> EMAs are a custom-designed, project-wide migration arrangement suited to the resource sector. EMAs ensure that skill shortages do not create constraints on major projects and jeopardise Australian jobs. EMAs help major resource projects to access labour from outside of Australia to cover genuine skill vacancies that cannot be filled from within the Australian labour market. (Department of Immigration – Australia).

<sup>24</sup> Submission from Indonesia Service Dialogue (ISD).

<sup>25</sup> ANZ Bank, “News Release: Australian Service Dependent Economy and Ageing Population could cause Skilled Labour Shortage by 2030”, June 2016.

## ➤ **FOREIGN DIRECT INVESTMENT RESTRICTIONS**

In terms of foreign investment, stakeholders from both countries highlight the implementation of Indonesia's most-recent Negative Investment List (*Daftar Negatif Investasi/DNI*). On 18 May 2016, a new negative investment list was issued containing significant changes; most importantly it provides preferential treatment to ASEAN countries. The DNI now allows ASEAN investors to invest in certain previously closed business fields and have an increased shareholding of up to 70% in specified sectors. The liberalisation of foreign investment in more sectors is welcomed as a positive development by the IA-BPG. Preferential treatment, at least at the same level as that offered to ASEAN countries, should also be provided to Australian investments under the IA-CEPA.

Australian business has expressed concern that even with the changed provisions of the Negative Investment List, some sectors remain restricted and some that have been liberalised are subject to Ministry regulation that imposes new or ongoing restrictions. Consistency of regulation is needed to build investor confidence.

IA-CEPA needs to address liberalisation of investment regulations as a priority. IA-BPG notes that AANZFTA does not currently have most favoured nation or market access commitments relating to investment.

In Australia, the Foreign Investment Review Board reviews foreign investment applications over the national threshold on a case-by-case basis which maximises the flow of investment and at the same time protects Australia's national interests. In Indonesia, the responsibility of managing foreign investment lies with the BKPM,<sup>26</sup> but is mostly regulated sector-by-sector by the relevant minister.

Both, Indonesia and Australia are in need of foreign investment. Growth in the two countries depends on high levels of investment, with the majority of investment from foreign sources. BKPM investment figures show that over the past decade, more than 65% of all investment in Indonesia has been from FDI, with that pattern expected to continue in the face of unprecedented demand for total investment across all sectors. Australia also relies heavily on FDI but with a smaller proportion (13%) of total investment, largely because of well-developed domestic capital markets. Barriers to investments therefore are not beneficial to both countries and should be considered disadvantageous to Indonesian as well as Australian national interests.

IA-BPG believes that two-way investment data is inadequate and encourages both governments to work together to improve bilateral investment data.

Despite their geographic proximity and their longstanding relations, bilateral investment levels in Australia and Indonesia are relatively small. In 2015, Australian FDI in Indonesia reached AU\$5,321 million while Indonesian FDI was only AU\$13 million.<sup>27</sup> Consultations with Australian business have revealed that these relatively low levels of FDI are in large part due to a number of impediments to investment in Indonesia, including ongoing investor uncertainty about the regulatory system, particularly in mining and also in other sectors like financial services. For services, the Negative Investment List and other regulations have restricted investment in

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<sup>26</sup> Indonesian Investment Coordination Board.

<sup>27</sup> Australian Government: Department of Foreign Affairs and Trade, "Indonesia," accessed on 20 July 2016, <https://dfat.gov.au/trade/resources/Documents/indo.pdf>.

several sectors that are strengths of Australian business. However, the introduction of the recently-amended Indonesian Negative Investment List of 2016 should improve prospects for foreign investment in a number of sectors.

Limits on foreign investment represent a major factor in reducing investment flows between the two countries. In agriculture and agribusiness, Indonesia applies a maximum 49% foreign ownership to farms where the main crops are corn, soy, peanuts, green beans, rice, cassava and sweet potato. In addition, foreign investment in plant culturing, nurseries, genetic agriculture and GMO products may be subject to limitations and must obtain a recommendation from the Indonesian Minister of Agriculture. This policy reflects how the Indonesian government is of the view that foreign investment in agriculture should support agricultural production, job creation, and contribute to the prosperity of rural communities and the broader economy.

Australian government agriculture policy is similar but also a bit different – to boost Australia’s productivity, jobs and exports and to encourage investment to ensure Australia remains a globally competitive agriculture producer. The reduction in the threshold to just AU\$15 million for Australian Foreign Investment Review Board (FIRB) review of purchase of Australian agricultural land by foreigners is seen as an impediment to Indonesian investment or co-investment in agriculture in Australia. IA-BPG notes that there are higher thresholds for purchases by companies from countries such as the US. In line with the agreement that both Indonesia and Australia aim to provide to each other at least the outcomes in existing free trade agreements, then IA-BPG recommends that Australia should allow a similar threshold for Indonesian agricultural investment. FIRB thresholds for other classes of investment should similarly be benchmarked against those in other agreements.

FDI restrictions also hamper development in the mining and energy sectors. Investment uncertainty exists due to foreign ownership divestment regulations under the current Indonesian mining regime which has led to decreasing interest from foreign investors in Indonesia. Through Government Regulation No. 24/2012, foreign mining companies holding permits or special permits, known as IUP or IUPK, are required to divest their shares to Indonesian stakeholders at a range of between 20% and 51% of total shares.

In the services sector, commercial presence of foreign services providers in Indonesia is not permitted without engaging local partners. This applies to all business services including lawyers, accountants, architects and consultants. Further, legal barriers can be found in the Negative Investment List which limits FDI in a number of key sectors such as transportation, health and education, as well as foreign labour restrictions which impede growth in services sectors.

Many companies lack access to capital, and especially during the global economic slowdown it is difficult to rely solely on domestic investment sources. Business opportunities can be more easily seized if there is available capital to support a company’s operational capacities. Both countries should support business to target and activate investments that create the most value for the economy – i.e. those that are able to generate employment and stimulate productivity.

## KEY ISSUES TO BE ADDRESSED TO ACCELERATE TRADE, INVESTMENT AND ECONOMIC COOPERATION

While there are many sector-specific and cross-sectoral barriers restricting trade and investment between both countries, the IA-BPG has also identified a number of more subtle but important issues that directly or indirectly impede trade, investment and economic cooperation. These issues may hinder the many opportunities presented by a stronger economic relationship between Indonesia and Australia. The IA-BPG understands that many of these issues go beyond the capacity of the IA-CEPA alone, but it is of the opinion that there are prospects for the IA-CEPA to lay the foundations for economic cooperation to overcome these issues.

### ➤ **MARKET FAILURE DUE TO LACK OF COMMUNICATION AND EXCHANGE OF INFORMATION**

Business practitioners from both countries have expressed a need for greater communication and information exchange regarding the available business opportunities in each country. Reliable information is an important element of business decision making, and uninformed parties are unlikely to be willing to invest in a new market.

Readily available information on consumer preferences, import-export conditions and requirements, as well as government policies and regulations would enable businesses to come up with the right strategies to meet consumer demands. This lack of information is a major hindrance to the increase of trade and investment cooperation. While a significant business relationship already exists between the two countries, business stakeholders feel that there is little in the way of organised and systematic business forums facilitated by government with the involvement of business associations. Such measures would further stimulate the interest of Indonesian businesses to enter the Australian market and vice versa.

As in 2012, Indonesian stakeholders continue to view Australia as a relatively small market with inscrutably complicated and stringent entry standards compared with other markets such as the EU or US. Moreover, Australia is seen as having closer relationships with Commonwealth countries such as Singapore and Malaysia.<sup>28</sup> Indonesian stakeholders also expressed a belief that the Australian market is more suited to premium products as consumers have high purchasing power. These perceptions create a strong reluctance among Indonesian businesses to engage in doing business in the Australian market.

On the other hand, Indonesia's complicated set of trade regulations is seen as one of the main obstacles for Australian businesses to engage in business in Indonesia. Considering the significant prospects which exist in both markets, businesses in both countries are in need of reliable and credible information on governmental regulations and market conditions, in order to attract further investment.

This lack of communication and information exchange also affects investment flows between both countries. Australian investors have expressed the need to be informed of the opportunities for investment and of the regulatory environment which exists through sector/group discussion sessions, seminars and tailored publications. While platforms for bilateral business cooperation

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<sup>28</sup> Indonesia-Australia Business Partnership Group, "Position Paper: on Considerations Towards the Indonesia-Australia Comprehensive Economic Partnership Agreement," 2012.

already exist – the IA-BPG is one example – stakeholders have expressed a view that there is a lack of organised and systematic business forums facilitated by government, with the involvement of business associations, such as consultation forums or training for entrepreneurs.

Indonesian business people also regularly point to a need for enhanced capacity building among Indonesian public officials.<sup>29</sup> Performance of government officials in a particular sector may be a key factor in facilitating, or impeding, trade – therefore, government representatives are encouraged to develop close links with the private sector through regular consultations, facilitated through such communication forums, to develop the technical and practical knowledge required to facilitate trade activities and settle trade disputes.

A submission to IA-BPG proposed the establishment of a Jakarta-based centre of excellence to address various impediments to trade. While the initial focus will be bilateral trade between Australia and Indonesia, the opportunity exists to expand this concept and for the facility to become the regional centre of excellence for SEA and/or ASEAN. The centre should:

- Provide a regional facility for dialogue between the public and private sectors to identify and analyse impediments to bilateral trade, including those which impose additional costs on exporters and consumers;
- Provide Indonesian Customs (and subsequently other SEA administrations) with technical assistance and training in effective cross-border management practices and procedures;
- Address other identified cross-border priorities of IA-CEPA.

Appropriate technical assistance and capacity building would initially need to be provided to the Centre, including the provision of management development initiatives, technical training and mentoring.

## ➤ **FINANCING AND ACCESS TO CAPITAL**

As discussed above, both Indonesia and Australia rely heavily on foreign investment. Growth levels in both countries depend on high levels of investment, with the majority of investment coming from foreign sources. In Australia the Foreign Investment Review Board advises the Treasurer regarding foreign investment applications on a case-by-case basis with consideration to maximising the flow of investment that is not contrary to Australia's national interests. In Indonesia, the responsibility for managing foreign investment lies with the Indonesia Investment Coordination Board (BKPM).

Indonesia's economy, similar to Australia's, is significantly comprised of SMEs. SMEs are the biggest contributors to GDP growth. They account for more than 90% of Indonesian firms across all sectors and provide jobs for more than 90% of the workforce.<sup>30</sup> A major issue for SMEs in Indonesia is the lack of necessary investment and funding to scale up their businesses. Investments are also necessary to provide funding for the development of innovations in SMEs. A lack of financial resources and difficulty accessing finance are key factors that have hampered innovation in SMEs.

Improving access to capital will improve overall supplies of goods and services and help to meet demand; not only in Indonesia and Australia but also in other countries. Based on stakeholder

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<sup>29</sup> Issue repeatedly raised during consultations with Indonesian stakeholders from all sectors.

<sup>30</sup> Ministry of Cooperatives and SMEs and the Indonesian Bureau of Statistics.

input, there is concern about Indonesia's domestic finance regulations as they relate to capital access. Foreign banks in Indonesia have been extremely concerned about an Indonesian Ministry of Telecommunications mandate from 2012 that all public services companies (including the banking sector) must process their transactions and data in onshore data centres.<sup>31</sup> While the mandate will not come into effect until October 2019, and it is possible that the banking sector will be excluded from its operation, the issue is still one of considerable concern to industry.

Further, the Australian banking sector has expressed concern about the possibility of Indonesia's Financial Services Authority (OJK) adopting a policy to limit foreign ownership in the financial sector to around 40%. The policy would have a negative impact on investment in Indonesia at a time when foreign investment is needed.

Meanwhile, representatives from Indonesia's banking sector regularly refer to the significant difficulties faced in opening branches in Australia. In many respects, the problem stems from ineffective negotiations between the respective national banking regulators. The Indonesian Central Bank (BI) and the Indonesian Financial Services Authority (OJK) do not usually pursue reciprocal arrangements for opening branches of Indonesian banks abroad. Additionally, Indonesian banking industry stakeholders have stated that they would require guarantees of streamlined access and a conducive regulatory regime to be able to proceed with opening operations in the Australian market.<sup>32</sup> Facilitating access to the Australian market for Indonesian banks may trigger significant further engagement with Australia by Indonesian businesses.

## ➤ **INFRASTRUCTURE AND LOGISTICS**

Briefly mentioned previously, infrastructure development has cross-sectoral implications. Poor conditions of roads increase costs for transporting goods and contribute to food insecurity through product spoilage during transport. Power shortages reduce production capacities, and lack of access to clean water often becomes a source of disease. Improved infrastructure encourages business innovation and improves a country's global competitiveness. Conversely, high freight costs severely reduce a country's competitiveness in the global market.

To illustrate the point, Australian grain industry stakeholders point out that Australia's competitive freight advantage for wheat exports to Indonesia is being eroded by low oil prices and an over-supply of vessels. This has exposed inefficiencies in Australia's rail infrastructure which mean that it is now US\$5 per ton cheaper to transport grain from the Ukraine to Indonesia, than it is to transport grain 350 km by rail within Australia.<sup>33</sup> This creates a significant advantage for wheat exports from Black Sea countries to penetrate into the Indonesian market; which is Australia's largest wheat export market. An IA-CEPA could potentially assist alleviate this situation with more liberal shipping and servicing from Indonesia. Australian state governments have also acknowledged the need to improve rail infrastructure as the industry grapples with the urgency of improving its supply chain.

In terms of facilitating transport links between Australia and Indonesia, stakeholders in Australia's Northern Territory have pointed to a need for the Australian government to relax cabotage restrictions for new international flights servicing Northern and regional Australia. This

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<sup>31</sup> Australian submission from AIBC.

<sup>32</sup> Forum Group Discussion consultations with Indonesian banking industry representatives conducted by IA-BPG.

<sup>33</sup> Submission from Australian Chamber of Commerce and Industry.

would complement the Australian government's commitment to the development of Northern Australia and other regional development policies. Future negotiations of Australia's and Indonesia's Air Access Agreements could sensibly form part of the IA-CEPA, so as to create new point-to-point air services between the two countries.<sup>34</sup> Indonesia is liberalising several sectors including logistics under AEC and similar provisions should be considered under IA-CEPA.

Logistics is a vital element for economic performance. In Indonesia, logistics, transportation infrastructure, and transportation services are high-priority and especially challenging issues. Indonesia's geography and the distribution of industry and resources pose a major challenge for efficient and low-cost logistics. Approximately 60% of the population of about 240 million people live on Java while the remaining 40% are distributed among 6,000 inhabited islands; many of which are very sparsely populated. Manufacturing is also centred in Java, while natural resources production is widely spread over the archipelago.

Current shipping services require most Australian exports to eastern Indonesia to be transhipped via Java or Singapore, creating significant and obvious inefficiencies. Trans-shipment arrangements and rules should be trade facilitative to ensure supply chains can operate efficiently. Customs Pre-Inspection Facilities, such as one which was established in Darwin in 2005 and later suspended, may provide an important means for facilitating efficient international trade between the two countries. The Darwin-based Indonesian customs facility was able to clear customs requirements for exports to all ports in Indonesia. Reciprocal arrangements for customs pre-inspection facilities for all ports in both countries would have the potential to greatly facilitate increased bilateral trade.

Shipping cabotage is strictly applied in both countries, with Indonesia also mandating local construction of vessels. IA-CEPA negotiations could tackle this difficult issue with a view to offering each nation access to the other's domestic shipping in the context of building much stronger shipping links between the two economies.

Mandating of locally constructed ships by Indonesia severely limits its ability to improve shipping efficiency with state-of-the-art fast ferries, where Australian companies are leading suppliers via yards in Australia, the US and the Philippines. Given that Indonesia is a major supplier of vessels and modules for Australian oil and gas projects, it is reasonable for Australia to have access to the fast ferry market in Indonesia.

Investment in port infrastructure and logistics will follow on from the confidence generated by sound trade rules, and solid and growing trade volumes. It should be noted that Indonesia's current administration has prioritised infrastructure development. Throughout Indonesia, the ambition is to construct new dams and roads, railways, airports, etc. to facilitate the movement of goods and persons. As discussed above, the existence of good infrastructure will create positive economic knock-on effects; and creates significant opportunities for Australian investment in Indonesian infrastructure projects. IA-CEPA should consider removing barriers to infrastructure cooperation between businesses in Indonesia and Australia.

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<sup>34</sup> Submission from Chamber of Commerce of the Northern Territory.

## ➤ **FOSTERING SMALL AND MEDIUM ENTERPRISES**

SMEs are often threatened by concessional cross-border trade agreements as they see new competitors enter the market. This view was repeatedly expressed by Indonesian stakeholders during consultations, indicating a lack of belief on the part of Indonesian SMEs in the benefits of trade liberalisation. Similar concerns also arise among Australian SMEs fearing unfair competition from developing countries with more lax labour and tax regulations and standards enabling them to produce at lower costs. Consequently, the IA-CEPA should address the importance of SMEs through deeper involvement and engagement. SMEs should be well informed on the potential benefits from trade liberalisation and participating in global supply chains.

SMEs need support both to participate in opportunities generated by the IA-CEPA (and other agreements like AEC and AANZFTA), and for adjustment to deal with enhanced levels of competition. As the IA-CEPA recognises, the different levels of development of Indonesia and Australia may require differentiated responses, including capacity-building and adjustment arrangements.

Businesses, especially SMEs, have reported difficulties obtaining information on market opportunities required to build sound business strategies and planning. Indonesian regulatory frameworks do not sufficiently differentiate between SMEs and larger enterprises. “Sunk costs” to open a business in Indonesia are too high across the board for SMEs and red tape and lengthy establishment procedures result in some businesses commencing operations in competitor countries such as Malaysia. Many SMEs from Australia explain that the lack of transparency is one of the factors hindering them from increased trade.<sup>35</sup> In terms of export and import regulations, SMEs often find non-transparent elements which are not only time consuming, but also impose unfeasibly high costs.

Australian SMEs object that import licensing procedures in Indonesia are complicated and often inefficient, such as those arising from a simple change of address of an SME. While Indonesian stakeholders point out that Australia’s quarantine system creates higher costs and risks for Indonesian exporters, especially SMEs, which discourages trade with Australia.

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<sup>35</sup> Australian submission from AIBC.



## Chapter 3

# OTHER SUBJECTS FOR DISCUSSION IN THE IA-CEPA

The following subjects have been raised by a number of stakeholders during the consultation process. The IA-BPG believes that further discussions on these subjects may be required and developed in more detail by an expert committee as the IA-CEPA negotiations take place.

### GOVERNMENT PROCUREMENT

Government procurement processes should be transparent and non-discriminative. Governments should consider progressively granting fair and equitable access to government procurement.

Government procurement should promote transparency, value for money, open and effective competition, fair dealing, accountability and due process, and be non-discriminative in its decision making. Opportunities for increased cooperation and issues which can be addressed in discussions on the nature and scope of any provisions could include:

- Consultation mechanisms
- Suppliers' rights
- Principles of non-discrimination and their application
- Coverage of any agreement
- Minimum procedure requirements in respect of procurement processes.

Given that government procurement did not feature under the AANZFTA, the IA-CEPA may prove an appropriate context in which to develop bilateral disciplines in this area.

### RULES OF ORIGIN

In order to exclude non-parties from the agreement it is necessary to establish a system of determining the origin of goods in order to apply the correct tariff concessions. The 2006 Revised Kyoto Convention on Simplification and Harmonisation of Customs Procedures and implementation of the WTO Trade Facilitation Agreement will help reduce the level of complexity and regulation for those involved with international goods trade. Consistency with these two global agreements will

ensure low cost and simple compliance. They also create a challenge for IA-CEPA to go beyond, what is already available under existing and potential agreements. The IA-BPG supports the system used within AANZFTA including the use of certificates of origin as a verification system – inclusive of the First Protocol amendments.

It is in the best interests of business to pursue coherence and consistency with ASEAN Rules Of Origin as much as possible, but also seek to simplify administration with the objective to facilitate ease of use and economies of scale for business, in particular SMEs.

As Indonesia and Australia are already partners in AANZFTA, and as one agreement does not supersede the other, there is good reason for government and business to remain consistent with the AANZFTA approach. This is preferable to establishing another system under the IA-CEPA which would potentially create confusion and variation for business and the customs service.

However, IA-BPG is supportive of the application of a risk-based approach to customs' acceptance of certificates of origin. That is, provided both nations have confidence in the system, customs offices need only review a statistically relevant number of the certificates to ensure scheme integrity according to a risk profile of the goods in question. Other administrative simplification is also desirable for business.

Such an approach would be beneficial to business as it would decrease the time taken to complete the border crossing and so reduce costs.

## DISPUTE SETTLEMENT MECHANISM

To further enhance cooperation in trade and investment, it is imperative to establish fair, transparent, timely and effective procedures to facilitate settlement of commercial disputes. Both Indonesia and Australia see the importance of setting up dispute resolution mechanisms that are efficient and enforceable.

At present, there is a major legal deterrent to foreign investment in Indonesia, namely inefficiency in the court system. The uncertainty of legal protection in Indonesia is experienced not only by foreign investors in the country, but also by Indonesian businesses. There is a clear need for a simple and direct mechanism to resolve disputes.

There is an agreed dispute settlement mechanism within AANZFTA and the IA-CEPA should not vary from this. Business is also able to take advantage of mechanisms such as those offered by ICC, UNCITRAL, ICSID, ITC, etc which all offer model clauses and contracts and then dispute processes using both mediation and arbitration.

However there may be advantages in expanding the settlement of disputes by mediation, which may provide a more cost and time efficient alternative to litigation, and this should be considered for inclusion under the provisions of the IA-CEPA, or alongside it.

As well as arbitration mechanisms, a mechanism for settlement of disputes by mediation, which may provide a more cost and time efficient alternative to litigation should be considered for inclusion under the provisions of the IA-CEPA. Mediation may offer several advantages in the context of IA-CEPA, for example:

- Mediations can be arranged, prepared and conducted to a conclusion in days or weeks, not months or years as in the case of adversarial procedures. As a non-legal process, mediation is

capable of crossing borders and does not have the legal and jurisdictional constraints inherent in adversarial proceedings.

- The procedure is adaptable to fundamental tenets of Indonesian culture such as “*musyawarah*” – the tradition of amicable discussion and consensus among Indonesian people.
- Mediation can be used as an adjunct to any dispute resolution process at any stage of any dispute. There can be multiple mediations within the one major dispute or mediation of part only of any dispute.
- Even where mediation doesn’t achieve a final result it can achieve a significant narrowing or shortening of the dispute.
- Because the parties control the process and reach their own agreement mediation is generally perceived to be fair.

To emphasize the sensitivity of ISDS, both parties should agree that Dispute Settlement is the last resort when direct negotiation or mediation cannot reach a mutually acceptable output. ISDS should be carefully crafted and does not single out any particular goods or sectors.

There are opportunities for joint capacity building for legal professionals and government officials in dispute resolution.

## PROTECTION OF INTELLECTUAL PROPERTY RIGHTS

Protection and enforcement of intellectual property rights (IPR) are essential for safeguarding innovation and creativity and sustaining economic development in the information age. Despite being a signatory to numerous IPR protection agreements, concerns remain regarding the protection of IPR in Indonesia. There are still rampant infringements of IPR in the field, including piracy, pharmaceutical patent infringement, apparel trademark counterfeiting and an inconsistent enforcement regime.

This situation significantly discourages investment flows from foreign firms and limits access for Indonesian businesses to research and technology which is lacking. The IA-CEPA could strengthen protection in this area by establishing a sound framework for capacity building, including raising awareness on the importance of IPR protection for economic development.

The capacity of SMEs to manage IPR is also a key area of concern. SMEs are reportedly not prepared to maximise the economic benefits of IPR, such as protecting, selling and licensing rights. The IA-CEPA should include frameworks for capacity building on managing IPR as a way to boost innovation among SMEs.

Australia and Indonesia are signatories to the WTO TRIPs agreement. As piracy and counterfeiting are still major problems in Indonesia, there is a need for capacity development to enforce IPR protection for investors and manufacturers in order to gain greater investor confidence. IPR protection is needed across all forms of intellectual property which include copyright and related rights, trademarks, geographical indications, industrial designs, patents, integrated circuit layout-designs and undisclosed information.<sup>36</sup>

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<sup>36</sup> [http://www.wto.org/english/tratop\\_e/trips\\_e/tripfq\\_e.htm](http://www.wto.org/english/tratop_e/trips_e/tripfq_e.htm).

## COMPETITION POLICY

The ongoing implementation of competition policy is a vital component of reforms to the Indonesian economy that are necessary to attract investment and underpin economic growth.

Government policy and legislation to ensure competitive practices and independent rivalry in the market can provide significant benefits to consumers and encourage investment and economic growth. Benefits may include better prices and variety of products for consumers, protection for businesses from corrupt, unfair or anti-competitive practices, better quality products through increased research, development and innovation, increased product safety and truthfulness in product claims.

There are opportunities for capacity building within agencies involved in market design and competition regulation, and for access to high level Australian services capabilities in these fields. Capacity building and knowledge exchange can take place between the competition authorities of both countries, that is the ACCC<sup>37</sup> and the KPPU<sup>38</sup>, to assist in prevention of anti-competitive practices and the detection and prosecution of conduct which breaches competition laws.

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<sup>37</sup> ACCC – Australian Competition and Consumer Commission.

<sup>38</sup> KPPU – *Komisi Pengawas Persaingan Usaha*.

## Chapter 4

# STRATEGIC MODELS FOR PARTNERSHIP

### KEY OPPORTUNITIES FOR THE IA-CEPA

The IA-BPG has identified some key opportunities for partnerships that can be developed between Indonesia and Australia. As mentioned above, the two countries have resources and capacities that are complementary. The IA-CEPA should go beyond conventional trade agreements by seeking ways to maximise this complementarity and enable both countries to succeed together as partners. Thus, economic partnership opportunities should encompass, in summary:

1. **Developing cross-border, integrated industries and value chains** in both goods and services that utilise the comparative advantages of each country to supply both domestic and third-country markets in the AEC, EU, UK, US and China, that neither country could achieve on its own.
2. **Building two-way investments**, enhancing Australian investments in Indonesia and encouraging Indonesian long-term investments in Australia. This should be achieved by developing competitive markets, lowering barriers, reducing risks and promoting investment opportunities, including joint ventures.
3. **Enabling greater sharing of knowledge and technology** through harmonising standards and regulations; recognising qualifications; recognising intellectual property rights; establishing dispute resolution mechanisms; building education, training and professional development cooperation; facilitating joint ventures and business licensing; and encouraging movement of skilled people between the two countries.
4. **Facilitating economic cooperation through an enhanced program of development assistance** that is focused on building economic capacity, developing skills, sharing market information, enabling market access, facilitating development of value chains, building local businesses and enhancing cooperation between government development assistance activities and the private sector.
5. **Acknowledging the direct link between investment in the services sector and capacity building**, through enhanced formal education and training, on-the-job learning and professional development, technology transfer and knowledge 'spillovers' that flow from the presence of international services firms.
6. Businesses in both countries have expressed the immense opportunities that exist for an **enhanced business collaboration and deeper partnerships between Indonesia and Australia in key sectors**. Hurdles remain, however, which the IA-CEPA should address so that gains from trade liberalisation will be the greatest and the partnership potentials fully fulfilled. The IA-BPG believe that opportunities can and should be prioritised in sectors where quick and visible outcomes are the most attainable. In general terms, the following principles can be applied to make the most of existing opportunities as quickly as possible:

7. **Preferential treatment.** To work well to the benefit of Indonesia and Australia, the IA-CEPA must be overtly preferential. Australia and Indonesia should provide each other with preferential status at a starting point of status offered to others, but each having a clear preference for trade and investment with the other. Where possible, Indonesia and Australia should declare and activate trade and investment preferences that operate above other preferential arrangements.
8. **Taking advantage of Indonesia's Special Economic Zones (SEZ) whenever possible.** SEZs as currently identified and as may be identified in the future, could provide the venues for investment and collaboration unrestricted by regulation applied elsewhere in Indonesia. Proving the model in a SEZ may then provide the socialisation and impetus to roll it out elsewhere. The IA-BPG takes a very positive view of such proposals, but notes that many current SEZs are located well away from centres of population and therefore markets. IA-CEPA SEZs could be developed and implemented as a way to create faster delivery of liberalisation in priority sectors or regions. IA-BPG identified six specific sectors where significant potential exists for cross-border economic engagement and where benefits may be realised within a relatively short time-frame. Each of the six sectors is discussed in detail below.

## OPPORTUNITIES FOR EXPANDING TOURISM AND ENHANCING HOSPITALITY

The tourism and hospitality sectors in Indonesia and Australia continue to experience steady growth. In 2015, international arrivals to Australia increased 8% from the previous year.<sup>39</sup> Meanwhile, foreign tourist arrivals in Indonesia have increased significantly in the last decade, nearly doubling in number from 5.51 million arrivals in 2007 to 9.73 million in 2015,<sup>40</sup> and expected to reach the Indonesian government targets of 20 million foreign visitors per year by 2020.

The ASEAN's rising middle class presents an opportunity for both Indonesian and Australian tourism exports. The similarity of activities and experiences available in Indonesia and Australia offer a strong potential for tourism and hospitality businesses – especially small and medium-sized enterprises – to partner and expand their markets.

The investment potential for tourism and hospitality in Indonesia – especially for infrastructure developments, hotels, and Public Private Partnerships – is high. This investment is expected to move towards new destinations in Indonesia, whether established as special economic/tourism zones or not, such as Lombok, Tanjung Lesung, Bunaken, Labuan Bajo, Komodo, Derawan, Wakatobi or Toba. It should be noted that 10 SEZs for have been proposed for tourism, and three of those have already been accepted. These SEZs provide the opportunity for more unrestricted investments from Australia to Indonesia.

### RECOMMENDATIONS

- A freer movement of natural persons would boost the capabilities of businesses from both countries to expand in the tourism and hospitality sector. Indonesia has already applied a 30-day visa-free entry mechanism for 169 countries including Australia, while Australia has begun to provide greater flexibility for Indonesian citizens with the option to apply for a three-year multi-entry visitor visa. More can be achieved by Australia however, and the IA-BPG believes that tourism from Indonesia to Australia as well as the movement of skilled workers between both countries must be facilitated as much as possible to support the tourism sector.
- Skills and training, notably through the Skills Exchange program between Indonesia and Australia, should be further developed. The improvement of human resources and skilled hospitality personnel is a high priority for the Indonesian tourism sector. With the introduction of the AEC, high-quality tourism professionals are needed so that Indonesia can maintain its competitive edge. Tourism is a sector where Australia has tremendous knowledge and can thus contribute towards capacity building in Indonesia.

<sup>39</sup> [http://www.tourism.australia.com/documents/Statistics/TAINT10315\\_International\\_Market\\_Update\\_March\\_2016.pdf](http://www.tourism.australia.com/documents/Statistics/TAINT10315_International_Market_Update_March_2016.pdf)

<sup>40</sup> <http://www.indonesia-investments.com/business/industries-sectors/tourism/item6051>.

## OPPORTUNITIES FOR SECURING DOMESTIC FOOD AVAILABILITY AND PARTICIPATION IN GLOBAL FOOD SUPPLY

The rise in Indonesia's middle class, and increasing concentration of the population in urban areas (projected to reach 71% by 2050) contribute to some of the food availability challenges faced by the country. The value of food consumption in Indonesia is projected to quadruple between 2009 and 2050 but local food production is only expected to double. This leaves a significant gap that is filled by foreign imports, especially of high-value produce.<sup>41</sup>

The IA-CEPA negotiations should take into consideration that the assumption that food security in Indonesia can be achieved through food self-sufficiency is flawed. Food availability can be realised much more quickly and reliably through cooperation. Indonesia's food availability problem is significantly due to a low productivity. Australia, on the other hand, is capable to produce enough high quality food to feed 60 million people<sup>42</sup> thanks to its world-class agricultural expertise and productivity levels. By working together, Australia and Indonesia can help each other meet their agriculture and food objectives. Hence, there is much potential for investing in agribusiness innovation and research in both nations to increase productivity and secure food availability.

Australia and Indonesia should work together to create agricultural systems designed to meet food security. In the longer term, however, there are greater opportunities for Indonesia and Australia to collaborate in accessing third markets. In the interim, one of the market and capacity-building strategies is for Indonesia to develop high value agriculture supply chains to Australia.

The Indonesia Australia Partnership on Food Security in the Red Meat and Cattle Sector is an example of how stronger business partnerships can be created and that IA-BPG hopes will lead to building competitive advantages in delivery to third markets.<sup>43</sup> Due to the relatively high cost of beef in Indonesia, only about 20% of households are occasional consumers. The latent demand from the other 80% can only be met by locally produced beef. This is an opportunity for both countries to pay even greater attention to capacity-building and joint ventures in-market. Other sectors could benefit from similar initiatives.

Sugar, for instance, presents such opportunities. Indonesian businesses have expressed that more investments in on-farm and off-farm technologies to increase productivity, in sugar refinery and in technology and knowledge transfer, can bolster quality standards and enable Indonesia to access Australian markets, and potentially global markets.<sup>44</sup> Australia is able to cooperate with Indonesia in building capacity in sugar production, while Indonesia should ensure that Australian sugar competes on a level playing field with ASEAN producers. A reduction in the tariff that applies to Australian imports of raw sugar to a level equivalent to that applied to Thailand would ensure Indonesian refiners would continue to be able to source raw sugar imports from Australia and they and food manufacturers maintain access to a competitive high quality alternative source of supply.<sup>45</sup>

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<sup>41</sup> Horizon report by Perth USAsia Centre, May 2016.

<sup>42</sup> PMSEIC (2010). Australia and Food Security in a Changing World, The Prime Minister's Science, Engineering and Innovation Council, Canberra, Australia.

<sup>43</sup> Succeeding Together: Maximising the potential for joint opportunities between Australia and Indonesia.

<sup>44</sup> Interviews with Asosiasi Gula Indonesia (the Indonesian Sugar Association) and Asosiasi Gula Rafinasi Indonesia (the Refined Sugar Association of Indonesia).

<sup>45</sup> Submission from the Australian Sugar Industry Alliance.

Similar stories can be extended for other items such as tropical fruits and coffee from Indonesia to Australia or grain from Australia to Indonesia. In fact, GrainGrowers propose to form a Centre of Australian grain within an Indonesian university that would teach Australian baking and noodle making know-how, conduct courses in wheat milling, and courses in grain storing and testing. The Centre could undertake strategic projects by academics and post-grad students in cooperation with Australian Export Grains Innovation Centre.<sup>46</sup>

The IA-BPG commends these type of initiatives, that are in line with its 2012 “A Healthy Diet” pilot project proposal but notes that remaining tariffs, free trade exemptions, trade restrictions, technical barriers and quarantine procedures still presents a challenge to achieving the opportunities in forming global value chains in agriculture.

## RECOMMENDATIONS

- Facilitate preferential treatment between both countries for trade in food products. For instance the horticulture trade provisions of the Thailand-Australia FTA can provide a precedent, including in facilitating Thai exports of fruit to Australia. The agreement between New Zealand and Indonesia in June 2016 to cooperate and facilitate access for Indonesian agricultural products to New Zealand, particularly for tropical fruits, can serve as another example.
- To tackle issues of differing standards, both countries should also adopt similar *Codex Alimentarius* standards as much as possible.
- To expand the red meat and cattle partnership, and to apply a similar approach to other sectors of mutual interest such as grains, seafood, and horticultural products.

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<sup>46</sup> Submission by GrainGrowers.

## OPPORTUNITIES FOR HUMAN CAPITAL DEVELOPMENT THROUGH ADVANCED EDUCATION AND TRAINING

A significant barrier for movement of natural persons from Indonesia to Australia is the high level of standards and certification demanded by Australian businesses. Investing in human capital in Indonesia through joint investments in higher education and training facilities and personnel from Australia is a mutually beneficial opportunity that promotes both Australian certification and standards training, and domestic investment within Indonesia that can be utilised in both countries, and globally. Partnerships between higher education establishments, for example the introduction of “double degrees” for certain professions, can promote cross border movement and encourage growth in specific sectors. Areas with high potential for return with this approach include medical research, where outcomes may be commercialised, the nursing profession, which is chronically understaffed in Australia, agribusiness, and tourism.

Joint programs on nursing, accounting, tourism, legal, engineering, and maritime needs to be intensified. For instance, capacity of Indonesian nurses should be built to be able to meet Internationally Qualified Nurse Certification that are globally recognized. For the legal profession in Indonesia, training can become a starting point before fully opening the sector to Australian lawyers.

The Vocational Education and Training (VET) sector is underdeveloped in Indonesia, particularly relative to the large latent demand for workers with VET skills and consequent massive training task. Australia’s TAFE Directors Australia (TDA) in December 2011 began a project focusing on the Indonesian VET sector and its engagement with business and industry. This project was supported by the Governments of Indonesia and Australia and business. One of the proposals coming from these activities was for a new public-private networked model for Indonesian VET. In September 2013, TDA and the Indonesia Australia Business Council (IABC) co-hosted the inaugural Indonesia Australia Industry Skills Training Roundtable in Jakarta. However, these activities then stalled for several reasons, including cuts to and reprioritisation of the Australian government aid budget. There remains a clear need and an opportunity for an Indonesia-Australia partnership to help build a public-private networked approach to VET institutional capacity and consistent skills formation. This needs to be based on an internationally-recognised qualifications framework and consistent curricula.

There is an opportunity to invest in higher education in Indonesia since many universities are privately-owned. On the other hand, Australia also welcomes Indonesian institutions to invest in the education sector. It should be noted, however, that there are major restrictions on investments in VET and Universities in Indonesia. Furthermore the movement of people still faces challenges as it is difficult to bring in academics and trainers from Australia to Indonesia, which impacts on the availability of high quality academic teaching and training.

## RECOMMENDATIONS

The IA-CEPA and allied projects should include measures to encourage universities to work more closely together in teaching, learning and research, including joint degree programs and joint research activities and centres. As well, the IA-CEPA should include:

- Provisions for opening the university sector for foreign investments.
- Provisions for opening the training sector to allow for resourcing of much-increased school to university transition programs.
- Provisions for cooperation and capacity-building in the VET sector to enable it to better train skilled workers to international standards.
- Provisions for movement of skilled people to undertake research and conduct teaching.

## OPPORTUNITIES FOR IMPROVING HEALTH AND QUALITY OF LIFE

Indonesia's healthcare industry continues to experience good levels of growth, in all areas including hospitals, medical insurance and medical devices. In 2016, 60% of hospitals in Indonesia were government owned and operated, with the remaining 40% run by the private sector.

The Indonesian government's willingness to work with foreign investors in the healthcare sector is a significant step towards reducing the health spending by Indonesian citizens abroad – for example, in Singapore and Malaysia. New regulations have opened up some business sectors within the healthcare industry to 100% foreign investment, including pharmaceutical raw materials, business and management consulting services, and healthcare support services which includes medical equipment rental, laboratory clinics and medical check-up clinics. As Indonesia is still heavily reliant on imports of pharmaceutical raw materials and medical equipment, this provides a key opportunity for foreign investors.

Investments in high-quality hospitals are highly sought after in Indonesia, and Australian healthcare providers can help Indonesia develop world-class healthcare services, including hospitals, clinics and aged and disability care. Australian companies led by Ramsay Healthcare are major investors in the Indonesian healthcare sector and have started to provide world-class services to Indonesian consumers. The IA-BPG welcomes the regulatory adjustments which allow 100% foreign ownership in some sectors of healthcare, although there are still restrictions in place for foreign doctors to practice in Indonesia.

Within the healthcare industry, Indonesia's affordable human resources is a strength that can be utilised to great benefit by Australia. Due to Australia's ageing population, demand for skilled healthcare professionals, especially in the nursing profession, is rising. Investment in personnel training and facilitating movement of skilled professionals in this sector is a potential strategy to combat this future need, as Indonesian labour can fill in the gap in Australia's demand.

### RECOMMENDATIONS

- To focus on exchange programs in healthcare as a way to rapidly increase capacity and expertise of doctors from both countries.
- To relax restrictions on movement of people, so as to help build capacity and increase the overall quality of healthcare services in Indonesia. For instance, Australian doctors and nurse trainers providing training in Indonesia are severely limited by Indonesian regulations such as to handle patients even in the context of training. These restrictions need to be eased to enable effective capacity-building.
- Open up opportunities for investment in hospitals and healthcare facilities.

## OPPORTUNITIES FOR ACCELERATING DIGITAL ECONOMY, E-COMMERCE AND CREATIVE INDUSTRY

IA-CEPA should address the opportunities created by the digital economy, e-commerce and creative industries, and include mechanisms to facilitate cross-border growth of these sectors as well as application of e-commerce to all trade. IA-BPG notes that the AANZFTA chapter on e-commerce is limited in scope and IA-CEPA needs to take a comprehensive approach.

The global digital revolution and shifting industry profiles in Australia and Indonesia increase the numbers of and need for innovative, technology based companies.

Indonesia is one of the top places in the world for developing apps, and has one of the fastest growing app markets in the world. The size of the Indonesian entertainment and media market in 2013 was US\$10.2 billion, with the fastest growing segment shown to be internet advertising. Newspaper publishing in 2013 accounted for 34.3% of the market spending, with revenues of US\$3.5 billion.<sup>47</sup> It has been predicted that Indonesia will outpace overall growth in entertainment and media spending both across the Asia Pacific and globally through 2018.

Electronic commerce provides a significant opportunity to provide a platform for trade for small and medium sized enterprises in Indonesia and Australia. E-commerce will be increasingly important for business to be able to access global markets. E-commerce is also an important sector in its own right for Indonesia and Australia to develop and harmonise. It is therefore important that e-electronic commerce is provided with a significant boost in IA-CEPA. Measures could include injecting trade rules that foster confidence in the on-line environment and limit the ability to put up roadblocks to such trade in the future.

In line with RCEP discussions on e-commerce, the IA-CEPA will need to adopt rules that enable information flows and prohibit data localisation, allow the cross-border provision of services, encourage the growth of online businesses, make it easy for SMEs and users to get online, and enable the usage of simple online payment systems.

Business cooperation should be enhanced to gain advantages in the digital economy sector. Mitrais, an Indonesian ICT company with a presence in Australia and South East Asia is a success story showcasing the potential of business cooperation and expansion in this sector. An Indonesia-Australia digital economy summit should be established as a way to bring investors together, not only from both countries but also from other countries.

Nevertheless, the Indonesian Internet Service Providers Association (APJII) has stated that they still need more access to foreign investments for their members, which are mostly SMEs.<sup>48</sup> Foreign investments in internet service providers are limited to 67%. Furthermore, although the recent DNI list allows 100% foreign ownership in e-commerce with capital investments above IDR100 billion, it still places restrictions on foreign ownership in e-commerce systems for investments under IDR100 billion (approximately AUD10 million) which hamper investment by SMEs. The IA-CEPA should encourage two-way investments in the digital economy sector including e-commerce and creative industry to boost investment and growth of SMEs. On the other hand, data sovereignty is known as a security-related issue in Indonesia. In this respect, the Indonesian government requires data centres

<sup>47</sup> <https://www.pwc.com/gx/en/global-entertainment-media-outlook/hot-topics/assets/pwc-indonesia-summary.pdf>.

<sup>48</sup> Interview with Asosiasi Penyelenggara Jasa Internet Indonesia (the Indonesian Internet Service Providers Association).

to be located in Indonesia, which has caused concerns from the banking sector as well as the ICT sector in general.

Vast opportunities exist in the creative industry. According to the Indonesian Creative Economy Agency, the creative industry contributes IDR 642 trillion or 7.05% of Indonesia's GDP. The key contributors are culinary business, fashion, and handicraft with 32.4%, 27.9%, and 14.9% contribution respectively. Considering that Australia has one of the most sophisticated arts and creative sectors in the world, Indonesia and Australia can cooperate on design and manufacturing to improve the export capabilities of Indonesian products while creating stronger business and people-to-people linkages between Australia and Indonesia.

For instance, more than four million Indonesians and 220,000 Australians work in the fashion sector, adding AU\$12 billion to Australia's economy each year. Indonesia's exports of fashion products have grown exponentially in the last five years. A total of 25 Indonesian fashion entrepreneurs have received scholarships to attend the two-week International Business Readiness program in Queensland, while established designers in both countries have been supported to showcase their work at premier fashion events in Jakarta and Melbourne. One of these emerging Indonesian designers, Toton, will compete for the Australian-founded International Woolmark Prize in Paris later this year.

## RECOMMENDATIONS

IA-BPG recommends that IA-CEPA e-commerce, digital and creative industry measures should include:

- Trade rules that foster confidence in the on-line environment and limit the ability to put up roadblocks to such trade in the future. In particular the IA-CEPA will need to adopt rules that enable information flows and prohibit data localisation, allow the cross-border provision of services, encourage the growth of online businesses, make it easy for SMEs and users to get online, and enable the usage of simple online payment systems.
- Building a harmonised, borderless system for conduct and regulation of e-commerce
- Consider training and capacity-building requirements for both governments and business to utilise e-commerce.
- As a principle, the IA-CEPA should support the free-flow of information while respecting personal information security concerns as much as possible. Governments should not seek to create treaty terms where contract law is sufficient.
- To create an environment that supports industries in the digital economy sector, especially SMEs, by allowing freer flow of investment and people and removing any remaining foreign ownership restrictions in digital sector.

## OPPORTUNITIES IN INFRASTRUCTURE AND ENERGY

Infrastructure in Indonesia is generally lacking in quality and quantity. Indonesian business feels that the availability of reliable infrastructure primarily affects supply chains and logistics, creating increasingly high production costs, which leads to higher and less competitive product prices. Indonesia's current administration is pushing for infrastructure development with ambitions to construct new dams and roads, railways, airports, etc. to facilitate the movement of goods and people. Additionally, the government plans to build 35GW of electricity infrastructure to support the country's growing energy needs. The Indonesian Government has set a target of 25% renewable and 25% gas-fired generation.

Governments and the private sector are already exploring the opportunities for cross border gas and electricity grid connections and international electricity markets in Southeast Asia based on experiences in Europe and elsewhere. It could be possible for IA-CEPA to encourage investigation of a grid connected electricity market with energy supply from Australia to Indonesia and beyond.<sup>49</sup>

Naturally, good infrastructure will give positive spill-over impact for the Indonesian economy. Conversely, Australia is one of the world's largest energy suppliers and has access to abundant renewable energy resources in solar and wind. Australia has developed technologies and expertise in operating renewable and hybrid power systems that may be eminently suited to adaptation for Indonesia's islands. Australia also has significant infrastructure requirements and an emphasis on developing Northern Australia. Both countries are also striving to reduce their use of fossil fuels and greenhouse gas emissions in line with the Paris Agreements on Climate Change. These common and mutually supportive interests could be harnessed through IA-CEPA.

In regards with IA-CEPA, Indonesia's plan to invest massively in infrastructure should be an ideal opportunity for Australia to deepen its cooperation with Indonesia. While Indonesia needs better infrastructure, Australia can invest and provide expertise to achieve a common benefit. Opportunities include cooperation in infrastructure such as the building of toll roads, development of ports, design and supply of remote power systems, and cooperation within the banking sectors in Indonesia and Australia in terms of financing and asset management.

Australian financial institutions, infrastructure consulting firms and government infrastructure agencies have world-class expertise in public-private partnerships to deliver infrastructure. But the potential for cooperation is inhibited by lack of knowledge of the opportunities and how to operate in Indonesia, and by lack of trust in the operating environment, as well as barriers to operation of foreign companies and to movement of people.

Other inhibitors to greater Australia-Indonesia cooperation in infrastructure identified by the AIBC through its IA Infrastructure Dialogue initiative include:

- Uncertain processes at all stages of project design, contracting, delivery and operation
- Severe restrictions on provision of services to infrastructure delivery, either through the Negative Investment List or regulation by Ministries, including restrictions on the operation of financial services and professional services firms with the required capacity
- Restrictions on engagement of expatriate professionals necessary to deliver expertise and capacity for complex infrastructure projects.

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<sup>49</sup> Submission from Chamber of Commerce of the Northern Territory.

## RECOMMENDATIONS

To be able to fully embrace opportunities in the infrastructure and energy sector, the IA-BPG proposes to:

- Encourage both Governments to create together an Indonesia-Australia PPP Centre, which would help fulfil Indonesia's need for high quality design, structuring and documentation of projects on offer. Such a centre working closely with BKPM would streamline investment and workflow in this crucial sector. Examples of similar centres recently created exist in the Philippines with Australian assistance and regional examples exist such as the Makassar PPP centre.<sup>1</sup>
- Find mechanisms to ensure Australian involvement in PPP projects without having to go through international competitive tender requirements. Recommendations G-to-G platforms such as an MoU on a specific infrastructure project should be established.
- Governments in both nations should be open to accepting unsolicited bids for regional development and infrastructure projects from the private sector willing to invest in projects they have identified unilaterally.
- Although investment in the energy sector is quite open, all classes of infrastructure need to be more open to foreign investments.



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