MAYER • BROWN

Mayer Brown Consulting
Trade Alert
5 September 2018

Indonesian Government Plans Various Measures to Curb Imports

The rising interest rates in the United States, higher oil prices and the full-blown US-China trade war have affected Indonesia's economic and investment growth.

In order to improve its trade balance, the current account balance, and strengthen the rupiah, the Indonesian government plans to impose several measures to stem the flow of imports into the country.

Additional Tax on Imported Goods

The Indonesian government is proposing a new Finance Ministry regulation to impose an additional 7.5 percent tax on certain imported goods. The additional 7.5 percent tax will likely be levied as income tax, and calculated based on the CIF value of the imported good plus duty.

On 14 August 2018, Finance Minister Sri Mulyani Indrawati announced that the government is in the process of identifying 500 goods that may be subject to the new tax. Such goods should be available (and are manufactured) locally and are not categorized as "strategic products". She said that the new tax will also apply to goods purchased via e-commerce.

The ministries of finance, industry and trade, and the customs department are holding internal discussions to determine the list of products. The list will likely include goods such as paper and wood products, rubber and plastic, etc., which are already manufactured in Indonesia.

The implementation date for the additional tax has not yet been announced.

Discouraging Capital Goods Imports

The government will also discourage imports of capital goods, most of which are imported by PT. Pertamina, a state-owned oil and natural gas corporation, and Perusahaan Listrik Negara (PLN), a state-owned electricity producer.

The most likely method of doing this would be by removing any direct and indirect tax exemptions (including removal of import duty exemptions) and requiring the importer to apply for import permits for all shipments. In other words, capital goods importers will not only have to pay the applicable import duties and taxes, but will also be required to go through the long and arduous process of obtaining a permit/licence to import. It is not clear whether

this policy will apply only to imports by the two state-owned enterprises named above or whether it will affect all importers of capital goods.

The government hopes that this policy will encourage the use of local goods. However, it is uncertain whether there is any local production of the capital goods, and if there is, whether the locally manufactured capital goods are of the same or better quality.

Indonesia's Chamber of Commerce and Industry (Kadin Indonesia) as well as the Indonesian Employers Association (Apindo) are urging the government to think very carefully on the implementation of these measures and the effects.

While the government is not obliged to offer direct and indirect tax exemptions in relation to capital goods, imposing a non-automatic import permit requirement may be considered a non-tariff barrier if imports are unduly impacted by the permit application requirements or process. The proposed capital goods measures are reminisce of past Indonesian measures which were subject to challenge at the World Trade Organisation (WTO). But would Indonesia really be concerned? A case brought to the WTO dispute settlement body may take years to settle. Given that Indonesia's proposed capital measures are supposed to be short-term measures, the Indonesian government may be counting on the long lead-time for the dispute to make its way through the WTO system, to "buy" some time to protect its domestic industry.

For companies, the more critical concerns would be whether the locally manufactured capital good is of the same quality and whether the local manufacturer is able to meet delivery schedules. There will also be concerns about existing contracts with overseas suppliers/manufacturers. Are there exit clauses in the contracts which can address the regulatory changes? What are the costs involved in breaking contracts and in finding new domestic suppliers? Do domestic suppliers have the capacity to meet the new demands? As it currently stands, there is no indication of the criteria on which the government is evaluating goods produced locally, simply by identifying similar goods or assessing the good's quality and local manufacturing capacity.

Restricting Ports of Import

The Indonesian government is also considering limiting the ports of entry for certain imported goods. Currently there are five Indonesian ports of entry: Tanjung Priok (Jakarta), Belawan (Medan), Tanjung Emas (Semarang), Tanjung Perak (Surabaya), and Soekarno-Hatta (Makassar). Imports also enter through the international airports.

The Ministry of Industry is proposing closing several harbours to imports of certain goods. Its intention is to strengthen the supervision of the flow of imported goods, and support the domestic manufacturing industry.

While the Indonesian government has not revealed how it will determine the commodities to be imported at a particular port, the most likely mechanism will be via the Harmonised System (HS) classification. Thus, companies should review the tariff classifications of goods to make sure that they are correctly classified as this would affect their port of entry. Furthermore, while it may be advantageous for importers to have HS classification consistency applied by customs at one port, it could also mean that the port customs would have access to a greater volume of imports of one product to draw comparisons.

The restriction on the ports of entry could also create considerable logistics problems for importers. The underdeveloped infrastructure within Indonesia, when coupled with a restriction on the ports of entry for certain products, may stretch delivery schedules and hamper just-in-time (JIT) delivery. In particular, the roads leading to/from some of the ports of entry are often very congested and cargo can take days or weeks to arrive at their final destination.

Furthermore, an importer may have chosen a particular port for convenience and accessibility but, due to the port of entry restriction, may now be required to import through another port which may not be as convenient or efficient and may add to the costs. In addition, if an importer imports a range of commodities falling under different HS classifications, it may have to use different ports for different products. This would turn into a logistics nightmare for the importer.

Environmental Excise Tax on Plastic Bags

The government of Indonesia announced in its 2018 budget that it is in the process of preparing new regulations which will establish the principles for the application of an excise tax on plastic bags. While the rate or rates of excise are currently unknown, we understand that different rates will be applied based on the extent to which companies apply environmentally friendly principles in their products. In the current draft of the proposed new regulations, the excise on plastic bags will likely be levied directly on the plastic bag producers. This tax will undoubtedly be passed on to retailers and customers.

The Minister of Industry Airlangga Hartarto said that he proposes to introduce the excise tax gradually, which will provide time for Indonesian plastic bags producers to add eco-friendly bags to their production lines. We understand that the Indonesian government is ready to offer local plastic bag manufacturers fiscal incentives for the import of industrial capital goods for the production of environment-friendly plastic bags.

The government aims to collect IDR 500 billion in excise tax from the plastic bags; many opponents state that the additional revenue generated will not be significant. They also say that it will put a major burden on the manufacturing industry.

Fajar Budiyono, secretary-general of the Indonesian Olefin, Aromatic and Plastic Industry Association (Inaplas), has come out against the excise tax. He said that it will not be a solution to environmental pollution. He also said that the additional income for the state will not be significant, while it puts a major burden on the manufacturing industry.

This is not the first time that the plastics industry is targeted for an excise tax. In 2016, the Indonesian government announced a plan to impose an excise tax of at least IDR 200 (approximately USD 0.01369) on plastic bags. This would have been charged directly by supermarkets and shops each time a customer requested for a plastic bag. The reasoning then was that this would lead to a reduction in the use of plastic products, thereby protecting the environment while at the same time contributing to tax revenues. That scheme is now only implemented by a few shops.

While the environmental focus of the Indonesian government is very laudable, it would be unrealistic to expect the industry to be able to rapidly switch to bio-plastics production.

It is estimated that currently, local production of eco-plastic bags can only meet one percent of Indonesia's total plastic bags demand. This means that the conversion to local manufacture of eco-friendly plastic bags will require a considerable amount of time. If local manufacturers are unable to convert their operations to bio-plastics, they would be hit by the excise tax. In such a scenario, they may then begin to import bio-plastics, which would defeat the intent of the policy to encourage local production.

For more information about the topics raised in this Trade Alert, please contact the Author or your Regional Contact below:

AUTHOR

Anthony Kerr
Senior Director
Mayer Brown Consulting
+65 6327 0638
anthony.kerr@mayerbrown.com

REGIONAL CONTACTS

Sydney H. Mintzer
Partner, Washington DC
+1 202 263 3866
smintzer@mayerbrown.com

Paulette Vander Schueren
Partner, Brussels
+32 2 551 5950
pvanderschueren@mayerbrown.com