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To Participate or Not to Participate: China's One Belt One Road Initiative

When promoting the TPP agreement, former President Barack Obama once said that 'if we don't write [the trade rules], China will write the rules in that region'. However it is apparent from the 'one belt one road' (OBOR) that China's economic and geopolitical agenda focuses more on investing in the massive infrastructure projects rather than writing the rules. The OBOR initiative was initiated by President Xi Jinping in 2013, three years after the US decided to join the TPP talk in 2010. Today, the initiative seems to gain its momentum after President Trump withdrew the US from TPP trade deal.

The OBOR initiative is also known as China's infrastructure-led development. It is not a free trade agreement agenda, but more of a China's grand vision for integrating China and its regional trading partners by building up their infrastructure such as ports, roads and railways and other network links. Put differently, the initiative is intended to be a revival of the ancient Silk Road trading route.

The 'one belt' represents a 'silk road economic belt' or land routes from China through Central Asia and the Middle East before reaching Northern Europe. The 'one road' refers to China's '21st century maritime silk road' or sea routes that pass Southeast Asia, South Asia and Africa before turning up toward the north to the Suez Canal and terminating in the Northern Adriatic Sea.

There are at least three questions that come to mind about the initiative. They are as follows: (a) where does the money comes from? (b) how is it going to be deployed? (c) should Indonesia join the initiative or not?

In his keynote speech to the Belt and Road Forum for International Cooperation in Beijing in May 2017, President Xi affirmed that China will pledge at least US\$113 billion in extra funding for the initiative. Moreover, most funding

One belt, one road

China is pushing to revive its ancient overland and maritime silk routes to Europe. The route connects many land and sea ports over three continents.



will likely come from the Export and Import Bank of China, China Development Bank and China's policy and commercial banks. Two multilateral banks, namely the Beijing-based Asia Infrastructure Investment Bank (AIIB) and the Shanghai-based New Development Bank (NDB/formerly known as the BRICS Development Bank) also appear to be the key financier for the initiative. For example as reported by several media, AIIB helps to bolster China's OBOR initiative by financing various China's OBOR Economic Corridor projects. The Pakistan motorway project as a part of 'China-Pakistan' Economic Corridor is an example of this sponsorship.

In May 2017 (prior to the Belt and Road Summit) the Cai Xin Global, a Beijing-based media group providing financial and business news, reported that about 50 Chinese state-owned enterprises (SOEs) have invested or involved in nearly 1700 projects since 2013 including high-speed highways projects in Africa and energy projects in more than 20 countries along the Belt and Road routes. The high degree of China's SOEs involvement leads to concerns raised by some commentators. Spencer Sheehan in his short article entitled 'The Problem with China's One Belt, One Road Strategy' highlights that 'projects are often tied to political pacts through which China's state-owned enterprises get exclusive bidding rights, as opposed to competitive tenders...' When Kenyan government decided to build a new standard gauge railway (SGR) line to improve their outdated railway system, the project was funded 90% by the Export Import Bank of China and the Kenyan government covered the remaining 10%. However, a number of commentators criticise that Chinese companies delivered the SGR line at a cost that close to three times the international standard and four times the original estimate. According to Anzette Were, a development economist, there are no major rivers or lakes or big hills to justify such high costs of the SGR.

Other experts are also questioning whether the infrastructure development projects will be profitable or economically sound. Considering that many belt-and-road countries particularly in Central Asia, Africa and Southeast Asia are prone to corruption, poor public governance, and political and economic instability. It was reported by the Reuters that in January 2015 the new Sri Lanka's president suspended the \$1.4 billion Sino-Sri Lankan infrastructure project called the Colombo Port City project which was agreed by their (authoritarian) former president. Moreover, in a report entitled 'China's One Belt and One Road Initiative Brings Risks', Fitch Ratings casts a doubt that 'China's banks can identify profitable projects and manage risks better than international commercial banks and multilateral lenders.' According to the report, the banks do not have a track record of allocating resources efficiently at home. Consequently, commentators argue that countries particularly those with weak institutional capacity can be trapped in a massive amount of debts incurred to finance dubious projects that are not benefit to their overall economy.

Indonesian President Joko Widodo was among 29 head of states attending the Belt and Road Forum for International Cooperation in China last May. Prior to his departure to Beijing, President Widodo stated that he would study the initiative offered by China during his 2-day visit in the country. In general Indonesian government sees that the initiative is in line with President Widodo's sea toll route programme. The sea toll programme is aimed to building up economic connectivity and narrowing economic gap among provinces/islands in Indonesia. Thus, the OBOR initiative is seen as a thriving and mutually beneficial economic opportunity to boost more investment to further Indonesia's infrastructure development programme.

However as elaborated on previously, various commentators have expressed their concerns particularly in relation to the poor delivery of infrastructure projects in countries targeted by China's OBOR initiative. In the case of Indonesia, the Jakarta-Bandung high-speed railway project is a most striking example. The project has not had any significant development since its ground breaking ceremony in January 2016, facing issues ranging from environmental, rising land prices to swelling costs issues that will threaten the project's feasibility.

Finally, the OBOR initiative indeed will encounter a lot of problems, but simply predicting the failure of it would be a misguided attempt. China has invested much on the initiative thus it is reasonable to believe that they have a strong commitment to push forward the initiative. The initiative would potentially have a significant impact and contribution to the economy in the region, and it is essential for Indonesia to assess and evaluate the benefits and risks of participating in the initiative. Regardless of whether or not Indonesia will join the initiative, a mutually beneficial Indonesia-China economic relationship should always be maintained.



New Rules for Ride-Hailing and Ride-Sharing: Leveling or Tilting the Playing Field?

In the past, you probably have to stand on the side of a street to hail a taxi. Today, you can order one just through several taps on your smartphone and it will come right at your doorstep. Ride-hailing application was first introduced approximately 10 years ago as a ride-sharing application which allow people to share their car with another person heading the same direction. Now, ride-hailing and ride-sharing services are offered in almost all big cities.

Despite of the amazing growth, last decade has been hostile for companies offering ride-hailing service. Everywhere, whenever a ride-hailing company tries to penetrate a market, it is always welcomed with protests and controversies. Proponents say ride-hailing apps provide consumers with more efficient transportation, attract investment, create employment, reduce number of private cars and ultimately help protecting the environment. Opponents, mostly conventional competitors, argue that ride-hailing apps operate with predatory price thus cornering established companies and steal jobs, do not protect consumers' rights, do not provide legal certainty to consumers and do not contribute to government's tax revenue.

In Jakarta and Greater Jakarta, a number of protests against ride-hailing taxi and companies turned anarchic and left several drivers injured. Conventional taxi companies also filed protests to the government, demanding the government to create regulation for a fair competition. In April 2016, the government came up with a new regulation (Permenhub No. 32/2016) intended to ensure fair competition between conventional car taxi and application-based car taxi. Later, the government revised the regulation and set the regulation to be fully in force by July 2017.

The new regulation comes with 11 key points. This regulation, among other things, include provisions on fleet quota, tax, fare limit, taxi stand, safety, maintenance and ownership status of the car. Many parts of this regulation can be understood as a way to protect consumers and ensuring fair competition. For example, requirement to pay tax for both conventional and application-based transportation service is completely understandable. It is unfair for conventional taxi companies if their younger competitors are not subject for taxation. With regards to safety, it is reasonable that every car used to carry passengers should pass the 'vehicle roadworthy' test (KIR) before hitting the road. It is true that safety comes with a price, but this is a necessary cost to protect consumers.

"Many parts of this regulation can be understood as a way to protect consumers and ensuring fair competition."

However, some parts of the regulation are seemingly tilting the playing field rather than creating a fair competition. The fleet quota, requirement to have taxi stand and requirement to shift the ownership of the car to a legal entity could end adversely affect the operation of ride-hailing and ride-sharing apps.

The creators of the apps had no intention to create a taxi company. Ride-hailing and ride-sharing apps use a totally different business model with conventional taxi. In many countries, these companies don't even own a single car. They are more like a technology company providing services through their apps instead of providing cars to rent.



The apps were invented to allow car owners to share the space in their car for people going in the same direction. It is true that some car owners rely on these apps to make a living and in fact operating as a taxi. However, to equate all cars using ride-hailing or ride-sharing apps with conventional taxi may not be right.

Another key provision in the regulation is the fare limit. The new regulation sets out the price floor as well as the price ceiling for both conventional and application-based transportation service. The government argued that tariff setting will avoid unhealthy competition between public transport providers and level the playing field for business

owners and provide certainty to passengers. However, Syarkawi Rauf – Chairman of The Business Competition Supervisory Commission (KPPU) disagrees with the government. He stated that by setting the price floor, fares will get higher and burden the people. Moreover, it is a disadvantage to business owners and will weaken the ability to innovate.

Mr. Rauf has a good point. Cheaper price was actually one of the benefits that attract consumers. By setting the price floor, users of ride-sharing or ride-hailing services become subject to certain higher fares, and remove one incentive to use this service. Indeed, the application-based transportation services calculate their price based on market's demand, and sometimes in peak hours the surge can go as high as 3 times normal fare. When this happens, consumers can easily shift to conventional taxi whose fares are flat at any time. It is best to provide alternatives to consumers and let them choose from the available alternatives.

Consumers do need their rights to be protected, especially related to safety. It is the task of government to ensure that every vehicle that hit the road are 'roadworthy'. However, the government should not interfere with the price mechanism. The price of goods or services should be left to the market to decide. Furthermore, the government may want to reconsider whether they see the application-based transportation service is similar with conventional taxi company or not. Regulations should be made to encourage, not obstruct innovation. The future will rely on digital technology. After all, change is coming, is Indonesia ready to embrace it?

Indonesia's Local Content Requirements for 4G LTE Mobile Devices

While there is no universally agreed definition of local content requirements (LCRs), they have been long associated with (a) policy instruments employed by government; (b) focusing on the economic benefits of the local economy; (c) in the form of non-tariff measures (including, but not limited to, measures expressly requiring or incentivizing use of local goods, services or labour).

As an instrument, LCRs are politically appealing and have been widely used. They are easier to implement compared to tariff or subsidy programmes; and unlike subsidies or incentives, they do not tax the national treasury (see Pierre Sauv  'Life beyond Local Content: Exploring Alternative Measures of Industry Support in the Context of WTO Accession' (2016) 1 Journal of International Trade).

The proponents of local content policies often support their standpoint from a development perspective. In their view, LCRs promote development goals by increasing local production and employment and encouraging transfer of technology. The policy also provides support to micro, small, and medium sized enterprises to aid their development and to assist them in integrating in global/regional value chains. In contrast, the opponents argue LCRs force companies to use local inputs and restrict access to global markets. Thus, the policies produce economy inefficiency and discourage foreign investor from investing in a country. LCRs also limit the available supply of inputs; consequently, they increase the costs of production that ultimately would transfer high prices to consumers. They often applied in non-transparent manner, associated with illicit practices and favoritism.



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A vast number of countries have made use of LCRs in shaping their local industries – for example the US' Buy American Hire American provisions, India's local sourcing requirements in retail sector, the local content rules in the Canadian province of Ontario's Green Energy Act, China's measures requiring local content on ICT equipment used by the banking sector, and various countries' (such as Brazil, Nigeria and Norway) local content rules in extractive sector.

In July 2015, Indonesian government, namely the Ministry of Industry, Ministry of Trade and Ministry of Communications and Information, announced that as of 1 January 2017 all 4G-capable smartphones sold in Indonesia are required to have 30 percent local content (both in hardware and software). This requirement was stipulated in the Regulation of Communication and Information Ministry No. 27/2015 on the Technical Requirements for Long Term Evolution Technology Standard Based Telecommunication Tool and Equipment. Prior to 2015, local content requirements for electronic devices were already regulated by the Regulation of Ministry of Industry No. 69/2014. As regards implementation, the Ministry of Industry issued Regulation No. 65/2016 regarding Conditions and Procedures for Calculating the Value of the Domestic Components in Cell Phones, Handheld Computers, and Tablets. This regulation provides for calculating methods whether or not the companies have met the local content threshold. In sum, the local content threshold for subscriber station (any device that connects to a mobile network such as mobile phone, laptop and tablet) was set at 20% in 2015 and increasing to 30% in 2017 and to 40% in 2019.

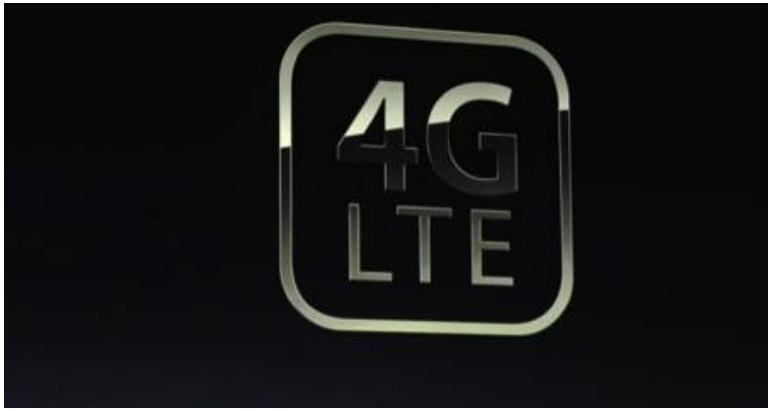
In the Committee on Trade-Related Investment Measures (TRIMs) meetings, during the period of 2015-2017, a number of WTO Members (the US, Japan, Canada, Australia, Korea, Taiwan and the EU) have constantly expressed their concern regarding Indonesia's local content requirements in 4G-enabled devices. Addressing their concerns, Indonesia stated that the 'policy is not an investment measure as it only regulates the technical standards and minimum local content requirements'. Indonesia also highlighted that the policy was applied in transparent and non-discriminatory manner. Indonesia's responses did not resolve the relevant Members' concern. The US, for example, disagreed that the local content requirements were not investment measures as they did not see the possibility to meet the local content requirements without investing in Indonesia.

“Article 2.1 of TRIMs clearly prohibits certain LCRs in the form of performance requirements relating to investment measures.”

Today, the use of LCRs is constrained by international trade and investment rules either under the multilateral trading system or under bilateral/plurilateral free trade agreements. This article focuses on the multilateral disciplines under the WTO rulebook.

Various WTO agreements, notably the General Agreement on Tariff and Trade (GATT), the Agreement on Trade-Related Investment Measures (TRIMs), the Agreement on Subsidies and Countervailing Measures (ASCM), the Agreement on Government Procurement (GPA) and the General Agreement on Trade in Services (GATS) appear to discipline the application of LCRs. National treatment provision specified in Article III, for example, is the key principle that outlines the criteria for the compatibility of LCRs with the principle of non-discrimination. Article III:8(a), however, carves out government procurement from the disciplines of Article III (national treatment obligation).

Moreover, Article 2.1 of TRIMs clearly prohibits certain LCRs in the form of performance requirements relating to investment measures. An illustrative list annexed to TRIMs provides measures that are potentially inconsistent with the Agreement. The panel in *India – Autos* stated that the illustrative list 'provides additional guidance as to the



identification of certain measures considered to be inconsistent with Article III:4 and XI:1 of the GATT 1994.' Similarly, Appellate Body in *Canada – Renewable Energy* upheld the panel's finding that the local content provision violated Article III:4 GATT and therefore was *ipso facto* a violation of Article 2.1 TRIMs.

Interestingly, a few cases relating to the LCRs have been brought to WTO dispute settlement. According to Cimino and Hufbauer, it is partly because WTO Members may reluctant to highlight the measures that many of them may have

introduced or practiced or maintained similarly at home (see Cathleen Cimino and Gary C Hufbauer 'A Proposed Code to Discipline Local Content Requirements', Policy Brief Number PB14-6).

Indonesia's local content measures on 4G-enable devices would potentially be found inconsistent with WTO law. There are however flexibilities and alternative measures available to Indonesia. TRIMs Agreement, for example, applies to investment measures affecting trade in good and not to measures arising in trade in services. To fall under the discipline of GATS, performance requirements including LCRs should be included in a country's schedule of commitments. Moreover, the GATT Panel in the *Canada – FIRA* dispute concluded that export performance requirements were not covered by the GATT.

The SCM Agreement does not apply on subsidies granted to service industries. Also, as long as the subsidies are available broadly (not a sector or industry-specific manner), they are excluded from the discipline of SCM Agreement. Finally, Indonesia does not ratify or adopt WTO's plurilateral GPA, thus it can subject state purchases to local content rules that are not constrained by WTO law.

A number of commentators have proposed alternative policies to LCRs. Hufbauer promoted the use of corporate social responsibility (CSR) policies that encourage transactions with local suppliers and provide comprehensive training programmes to locals. Sauvé suggested horizontal policies measures such as: (a) improvement of 'doing business' conditions; (b) building up 'connectivity' infrastructure; (c) pro-competitive reforms; (d) institutional reforms; (e) human development; (f) boosting productivity and efficiency; (g) better access to finance.

In sum, Indonesian government should make careful assessments whether the current LCRs policy measures bring more good than harm to Indonesian people in general and explore other alternatives that can promote a business-friendly environment and can help Indonesia to achieve its policy objectives without breaching Indonesia's global trade commitments.



UPH-CITI Participated in a Focus Group Discussion about Local Content Requirement on 4G LTE hosted by the Ministry of Industry
Depok, 21 June 2017

In the week before Eid Mubarak, the Ministry of Industry hosted a FGD to discuss local content requirement on 4G LTE. The panelists were: **Mr. Harjanto** – DG of International Industrial Cooperation, **Mr. Ahmad Firdaus** – Head of Trade Advocacy Bureau, **Michelle Limenta** – UPH-CITI, **Ms. Dini H.** – Directorate General of High Technology Industry. The session was chaired by **Mr. Riris Marhadi** – Secretary to DG of International Industrial Cooperation.

Technical Meeting on Preparation of Economic Cooperation and Capacity Building I-EU CEPA Working Group.
Tangerang, 19 May 2017

As a follow up to second round negotiations of Indonesia – European Union Comprehensive Economic Partnership (I-EU CEPA), the Ministry of Foreign Affairs hosted a technical meeting to strengthen the draft of ECCB chapter in the agreement. Michelle Limenta of UPH-CITI participated in the meeting and presented her view on cross-cutting issues in ECCB Chapter.



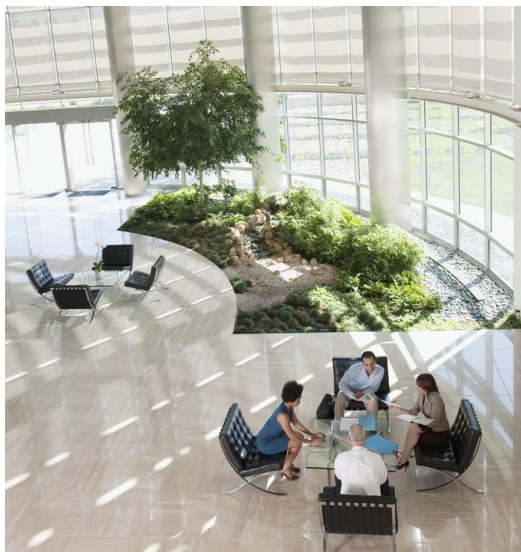
ECCB Chapter: Cross-Cutting Issues in International Trade Rules
Serpong, 19 May 2017

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Seminar “Trade and the Rule of Law in the Trump Era” and Book Launch “WTO Retaliation: Effectiveness and Purposes”
Jakarta, 26 April 2017

The seminar featured **Associate Prof. Michael Ewing-Chow** - National University of Singapore, **Paolo Vergano** – Fratini Vergano European Lawyers and **Michelle Limenta, Ph.D.** – UPH-CITI. The seminar was chaired by Jessica V. Marpaung from UPH Faculty of Law. The seminar was followed by a book launch to introduce a book authored by Michelle Limenta of UPH-CITI.



Universitas Pelita Harapan - UPH

Founded in 1994 with the vision of educating a new generation of leaders for Indonesia and the wider ASEAN region, Universitas Pelita Harapan is the number one private university in Indonesia according to the QS World University Ranking 2013. UPH was the first University in Indonesia to introduce programs entirely taught in English, the first to offer a liberal arts curriculum, and the first to introduce a multi-disciplinary approach to its programs. While consistently underlining the vision of "knowledge, faith and character", UPH, in cooperation with overseas partner universities, has developed a very rich curriculum in many areas of study, ensuring that its graduates are respected globally and appreciated by modern business and industry.

The Center for Trade and Investment - CITI

Established in September 2014, CITI's objective is to raise awareness in Indonesia of the importance of an outward-looking and liberal trade and investment policy, so as to ensure the country's continued commercial competitiveness and support its economic development goals. CITI runs a number of research, education and outreach initiatives with the generous support of the Swiss State Secretariat for Economic Affairs (SECO) and the World Trade Institute (WTI), Switzerland.

Our goal: To be the preeminent center for thought leadership and expertise on trade and investment policy and law in Indonesia

This quarterly newsletter seeks to provide updates, insights and analysis on current developments in trade and investment law and policy in Indonesia. Constructive feedback and comments are always welcome.

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- Oscar Fernando – Research Associate of UPH CITI (Article 2)

Disclaimer: The articles are representative of the author's view, not necessarily the general view of the Center

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