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INDONESIA – LOCAL CONTENT REQUIREMENTS FOR 4G LTE EQUIPMENT AND MOBILE DEVICES

QUESTIONS FROM THE UNITED STATES

The following communication, dated 25 March 2015, is being circulated at the request of the Delegation of the United States.

In early January 2015, Indonesia's Ministry of Communication and Information Technology (KOMINFO) issued two draft regulations related to mandatory local content requirements for the 4G LTE spectrum, affecting both the networks and the devices that use the networks. The two KOMINFO drafts were: *Technical Requirements for Equipment and Facilities for Purpose of Long-Term Evolution Time Division Duplexing (Lte Tdd) and Long-Term Evolution Frequency Division Duplexing (Lte Fdd) Broadband Services* and *Procedure for Calculation of Local Content in Telecommunication Devices*. These regulations appear to build on Ministry of Industry (MOI) Regulation 69/2014 on the *Conditions and Method of Calculating the Value of the Land Component Level Role in Electronic and Telematics Industry*, adopted in September 2014.

These measures seem to be part of Indonesia's broader plans to move up the value-chain of manufactured products by requiring companies investing in Indonesia to develop domestic manufacturing. As we understand the draft regulations, products using the 4G LTE spectrum – including LTE smart phones – that are sold on the Indonesian market would have to meet certain specifications for local content. LTE time division duplexing (TDD) devices would have to meet a threshold of 30% local content upon issuance of the regulation, with the threshold increasing to 50% 5 years thereafter. For LTE frequency division duplexing (FDD) devices, the initial local content threshold would be 20%, increasing to 30% within two years. The draft regulations also seem to indicate that companies must meet the local content requirement from 20% intangible value (IPR, R&D) and 80% tangible local content. Although this provision is not entirely clear, it appears that in order to fulfil the local content requirement an investor must use local goods in a manufacturing process.

In addition, according to our understanding, not only do the draft regulations appear to impose local content requirements benefitting investors who use Indonesian inputs, they also appear to make it significantly easier for Indonesian-owned companies to meet those local content thresholds than foreign-owned companies. According to the draft regulations, local content values will be weighted both by <u>who</u> produces the product (domestic versus foreign ownership) and <u>where</u> the product is produced (domestic versus manufacturing). For instance, an Indonesian company manufacturing in Indonesia gets 100% credit on the manufacturing value of Indonesian equipment and components that go into a 4G-enabled device; however, a similarly-situated foreign-owned firm manufacturing in Indonesia would get credit for only 75% of the value.

Further, a manufacturer using <u>non-Indonesian</u> inputs can nevertheless get credit for local content, <u>but if it is 100% owned by Indonesians</u>. Likewise, a joint venture between foreign and Indonesian partners can receive "local" manufacturing value credit even if using non-Indonesian inputs, on a sliding-scale based on the percentage Indonesian ownership in the JV. Thus, an Indonesian company using non-Indonesian inputs gets "local content" credit for 75% of the manufacturing value; a 50/50 JV with one Indonesian partner, using non-Indonesian inputs, gets "local content" credit for 50% of the manufacturing value; a foreign firm using foreign inputs gets no credit.

Finally, we also understand that, beyond the local content requirement, the regulations may provide an additional tax incentive. This incentive seems to provide an additional financial benefit to companies that use domestic content, rather than foreign content, over and above the minimum local content requirement imposed by the regulations.

MOI 69/2014 also outlines the process for companies to obtain a "certificate of production", which includes an assessment of the "production aspects" of a company, as well as the calculation of the value of local content. The assessment must be carried out by the MOI Directorate for Electronic and Telecommunication Industry or an independent surveyor appointed by the Minister of Industry.

While the MOI regulation has been adopted, the KOMINFO regulations are still in draft form. As we understand it, although the decision to require local content in 4G-enabled devices has been made, the way in which local content value is calculated and how quickly the requirements will be implemented are still up for discussion.

The United States is very concerned about these regulations, and seeks to understand their requirements and their current status.

Questions for Indonesia

1. Is our understanding above of the two regulations correct? Are there aspects of the regulations we have misunderstood and/or omitted?

2. How is credit towards local content calculated for a foreign company when it manufactures a 4G enabled device in Indonesia using Indonesian equipment or inputs? How is credit towards local content calculated for a foreign company when it manufactures a 4G enabled device in Indonesia using foreign equipment or inputs?

3. What would be the consequences for a foreign company if it were to sell 4G enabled equipment in Indonesia that does not meet the local content threshold?

4. Would Indonesia please describe the tax incentive that a foreign investor may receive if it exceeds the minimum local content thresholds? Under what conditions can manufacturers benefit from that incentive? Is the incentive the same for Indonesian-owed manufacturers as it is for foreign-owned manufacturers?

5. When does Indonesia anticipate that KOMINFO will finalize the regulations?