



**USAID**  
FROM THE AMERICAN PEOPLE



**SENADA**  
INDONESIA COMPETITIVENESS PROGRAM

# SUMMARY REPORT ON INDONESIAN PRIVATE SECTOR ASSOCIATIONS AND REGULATORY REFORM

**DECEMBER 2007 – GARY GOODPASTER**

THIS PUBLICATION WAS PRODUCED FOR REVIEW BY THE UNITED STATES AGENCY  
FOR INTERNATIONAL DEVELOPMENT. IT WAS PREPARED BY **DAI**

# SUMMARY REPORT ON INDONESIAN PRIVATE SECTOR ASSOCIATIONS AND REGULATORY REFORM

## **DISCLAIMER**

THE AUTHOR'S VIEWS EXPRESSED IN THIS PUBLICATION DO NOT NECESSARILY REFLECT THE VIEWS OF THE UNITED STATES AGENCY FOR INTERNATIONAL DEVELOPMENT OR THE UNITED STATES GOVERNMENT.

# TABLE OF CONTENTS

---

- 1. OVERVIEW OF SENADA ..... 1**
- 1.1. SENADA’s RegMap Program ..... 1
- 2. REGULATION AND THE BUSINESS ENABLING ENVIRONMENT ..... 3**
- 2.1. Regulation in Indonesia ..... 3
- 3. A BRIEF PRIMER ON DEREGULATION AND REGULATORY REVIEW..... 5**
- 3.1. Related Regulatory Problems: Vagueness; Broad Discretion; bribery ..... 6
- 3.2. Regulatory impact analysis compared with policy analysis ..... 7
- 3.3. Regulatory review in Indonesia ..... 7
- 3.3.1. Regulatory Review And The Indonesian Private Sector ..... 8
- 3.4. The context of regulatory reform ..... 8
- 3.4.1. Donor Analysis ..... 9
- 3.4.2. Domestic Research Institutions And Ngos ..... 9
- 3.4.3. Private Association Analysis ..... 10
- 4. POLICY ADVOCACY AND ANALYSIS ..... 11**
- 4.1. Advocacy ..... 11
- 4.2. Analysis ..... 11
- 5. INDONESIAN PRIVATE SECTOR ASSOCIATIONS ..... 12**
- 5.1. Types of associations ..... 12
- 5.2. Private associations as participants in regulatory reform ..... 12
- 5.2.1. Private Sector Policy Positioning And Decision-Making ..... 13
- 5.2.2. Additional Analysis ..... 14
- 5.2.3. Additional Value For Private Sector Policy Analysis ..... 14
- 5.3. Alliances ..... 14
- 5.3.1. Private Sector Alliances In Indonesia ..... 15
- 6. POTENTIAL PROBLEMS ..... 16**
- 6.1. Dealing with the Problems ..... 16
- 7. CONCLUSIONS AND RECOMMENDATIONS ..... 18**

# 1. OVERVIEW OF SENADA

---

SENADA is a USAID funded private sector development project focused on working to improve the competitiveness of five important Indonesian value chains: footwear, textiles and garments, furniture, handicrafts, and auto parts. As some part of the inferior competitiveness of these Indonesian value chains, as compared with competitors like China and Vietnam, stems from increased costs and inefficiency due to government regulation, SENADA has a concern to assist its value chains in deregulation and in obtaining more business friendly regulation. SENADA is also interested in the long-term sustainability of reforms and believes the private sector can play a significant role in reform.

As SENADA focuses on private sector development, it does not aim its regulatory reform and private sector assistance efforts directly or primarily at the government, but rather at the private sector and private sector associations. For Indonesian value chain competitiveness purposes, consequently, SENADA's regulatory reform issues are: what role can the private sector play in reducing the regulatory burden that Indonesian businesses face; and how can SENADA help them play that role effectively. The purpose of this report is to explore these issues and to provide recommendations regarding the actions that SENADA might take with the private sector to facilitate, or catalyze, an improved regulatory environment for the businesses in its value chains.

## 1.1. SENADA'S REGMAP PROGRAM

One of SENADA's major planned activities, called RegMap, is to create an inventory of all regulations, from the national to the local level, that affect businesses in SENADA's value chains. When the inventory, which is likely to be quite large, is complete, SENADA plans to screen the regulations, using "filters", to determine which regulations have the greatest adverse impact on the SENADA value chains. It then proposes to conduct a regulatory impact analysis of approximately fifty of the most significant regulations, ten for each value chain.

As there is so little regulatory review in Indonesia, but much concern about the regulatory burden, the RegMap activity is important and useful. If the RegMap results show, as expected, that Indonesian regulatory regimes damage sectoral competitiveness vis-à-vis international competitors, then SENADA will have made an independent, objective case for each sector that supports sectoral complaints against government policies and regulations. SENADA can hold workshops and publicize results, and share its analyses with governments, businesses, business associations, and other interested parties.

Private sector representatives, who have strong interests in sectoral competitiveness and regulatory reform, are best positioned to use the results to successfully pressure the government for change and reform. Whether they can and will do so depends on how well the sectors have organized as interest and lobbying groups and how effective they are at advocacy. If they are capable, they may use SENADA's results to good effect.

Nonetheless, the RegMap and its analytic results are, however large the effort, one-time donor-supported activities. If such activities are to have enduring value, it is essential that Indonesian private sector interests not simply make use of SENADA regulatory impact analyses to assist them in their policy reform efforts. They should also embrace policy analysis and advocacy as their own tools to use to help create a better business regulatory environment, and they should institutionalize use of these tools in their own development of policy positions and in their interactions with Indonesian governments. To achieve these goals, SENADA can seek to transfer policy research, analytic and

advocacy skills – of the kind involved in carrying through the RegMap study – to the Indonesian private sector. For sustainability and institutionalization purposes, Indonesian private sector associations are the appropriate targets for such assistance.

In considering how to approach and assist private sector associations for regulatory reform purposes, however, it is important to address and answer a series of questions. What is the business problem with government regulation? What methods are available that governments can use to regulate appropriately and in business friendly ways? What are Indonesian governments doing with respect to regulation and regulatory reform? What are the current sources of regulatory reform in Indonesia? What role can, and should, private associations play in regulatory reform in Indonesia? What are the capacities and willingness of private associations to play that role? What problems may arise when associations improve their policy analysis and advocacy skills? Finally, in what ways can SENADA work most effectively with Indonesian private associations to achieve value chain competitiveness gains through regulatory reform?

## 2. REGULATION AND THE BUSINESS ENABLING ENVIRONMENT

---

Government regulation is often a source of reduced business competitiveness. This may be regulation that increases business costs and reduces business efficiency, that creates perverse incentives or authorizes anticompetitive behavior, or regulation that distorts the operations of markets. It can also be regulation that is vague and capable of multifarious official interpretations, depending on the whim or personal interest of the official.

As countries around the world have tried to open, reform, and liberalize their economies, they have often focused on government regulation, sometimes an inheritance from an authoritarian or socialist past, as the source of economic and competitiveness ills. To improve their economic performance and competitiveness, these countries have deregulated and have instituted systems to conduct cost-benefit and similar analytic reviews of proposed regulations.

Economic globalization also makes deregulation important for countries participating in multilateral trade agreements, such as the WTO agreement, and in similar trade enhancing bilateral agreements. These agreements subject a participating country's industries and businesses to intense international competition, both in domestic and international markets. Deregulation, and better regulation when regulation is appropriate, in eliminating a major governmental cause of business inefficiencies and cost non-competitiveness, can help domestic businesses become internationally competitive.

### 2.1. REGULATION IN INDONESIA

Like the countries, that have undertaken regulatory reform, Indonesia has a large, and largely negative, regulatory legacy. Indonesia has a huge inventory of regulations, both national and local, accumulated from the long past and still accreting in the present. There are many regulatory authorities, and different authorities regulate the same matter in different, and sometimes duplicative, multiplicative, and conflicting ways. Many of these regulations are vague, unclear in objectives, or confer unbridled discretion on officials, and provide a basis for opportunistic, discriminatory, or abusive enforcement (as a way to extract rents, to intimidate, or hamper private sector activities). Many appear designed solely to raise funds. Even when not described as taxes, but as fees (*retribusi*), often – perhaps in most cases – there is no service provided.<sup>1</sup> As stated by The Asia Foundation, with respect to licensing regulations, “[l]ocal governments in Indonesia often use licenses to generate revenue without providing protection, control, or associated administration services, and often without fully analyzing the impact of a license on business behavior.”<sup>2</sup>

Although the total costs extracted from businesses by these regulations may be small, cumulatively they are costs that affect competitiveness if businesses in other countries do not experience similar impositions. More importantly, it is the business administrative time (and aggravation) required to deal with all these regulations and regulatory enforcers that detracts from business activity. Without

---

<sup>1</sup> Even where there is a putative “service” or public interest regulation, for example the case of weigh stations where trucks are weighed to insure there is no overloading; there is no weighing of trucks. Instead, the pretext of weighing becomes an occasion to stop trucks and charge a fee. This practice has the perverse effect of increasing truck overloading and highway damage since haulers overload in order to make up for the fees charged. *Trucking and Illegal Payments in Aceh* (World Bank, 2007); Ray, D., and Goodpaster, Gary, *Indonesian Decentralization*, in Damien Kingsbury & Harry Aveling, *Autonomy and Disintegration in Indonesia* (Routledge Curzon, London, 2003).

<sup>2</sup> *Making Sense of Business Licensing in Indonesia* 11 (The Asia Foundation, 2007).

regard to the money costs, this may make Indonesian businesses less competitive than their counterparts in competing countries.

Aside from regulations which governments design to raise fees, however, there are also regulations that do impose more than nuisance costs on businesses, e.g., labor regulations, local hire regulations, employment quotas, and various anticompetitive regulations designed to favor particular local interests. For example, the governors of Sulawesi provinces banned the export of rattan to Java in the interests of developing a rattan furniture industry there. Such a ban violates a principle of free trade within the country; has a serious, negative impact on Java rattan furniture producers; and damages the international competitiveness of Java's rattan dependent industries. Similarly, the national government policy of an export quota on rattan, limiting the amount of exported rattan to far less than annual production, has had a serious negative impact on parties at the beginning of the rattan supply chain, the rattan growers and harvesters, who have little incentive to produce if they cannot sell.

Indonesian governmental decentralization has unveiled the size and scope of the regulatory problem. In granting greater autonomy to local governments, and transferring former central government functions to them, Indonesia has enhanced the authority of local governments to enact regulations. Since decentralization began, the regulatory activity of DPRD's and local administrations has become a focus of business concern. Because the central government does not fully fund local governments, many of the new local regulations impose taxes and fees of various kinds. These taxes range from tariffs on imports and exports from the locality, cargo hauling and loading and unloading levies, forced "contributions" from various kinds of production companies, to road and transport charges. In addition, local governments have added regulatory and quarantine inspection requirements. Some of these many levies and requirements interfere with free domestic trade, and many appear to lack any purpose other than raising money.

In addition to local regulations imposed to raise funds, there are also a number of new regulations that aim at establishing local monopolies, call for local labor quotas, provide competitive advantages for local businesses, including government owned companies or competitive disadvantages on competitors, and so on.

Indonesian governments since the demise of the Suharto regime have undertaken some deregulation and have moved positively away from state domination of the economy in the direction of a more fully market-based economy. In addition, the rush to local regulation that attended decentralization has abated somewhat. The central government has also asserted some control over local regulatory activity by reviewing, and overturning, local enactments. Nonetheless, there remains a regulatory hangover, and a bureaucratic regulatory mindset, that together imposes unnecessary costs on business, create barriers to trade, and interfere with the operation of markets.

### 3. A BRIEF PRIMER ON DEREGULATION AND REGULATORY REVIEW

---

Countries undertaking deregulation and seeking to improve their regulatory environments do so through some form of regulatory review. The principal aim of regulatory review is to optimize policy for as many stakeholders as possible. Such review undertakes a policy analysis of government regulations and the policies they embody to provide relevant government decision-makers with the information necessary to evaluate the need for, and usefulness of, particular regulations. Where regulations do not serve legitimate purposes, or do not serve them well, are unnecessarily burdensome, distort markets, or contribute to a high cost economy, they are revoked or amended.

The information a regulatory review analysis provides should include a real understanding of the problem the regulation addresses, the legal and policy basis for government action, the expected economic costs and benefits of the regulation, alternatives ways of solving the problem, and any other factors that will affect the effectiveness of the regulation and minimize its negative impacts. Of particular concern are the costs that a regulation imposes on stakeholders, for some regulations cost more to implement than they produce in benefits. Regulations that have anticompetitive purposes or effects, for example, regulations restricting markets, conferring monopolies and monopsonies, protecting local businesses or potential employees from competition, also warrant serious scrutiny.

The regulatory review process consists of a careful analysis of the economic and other effects of proposed regulations and calls for consultation with parties proposed regulations may affect. The analysis and consultation lead to a *Regulatory Impact Assessment* (RIA). This is a document that analyses what a regulation does to the economy and to competition and that discusses the best ways a government can achieve its regulatory aims.<sup>3</sup> The RIA thus is a report that officials can use to assist them in deciding *whether* to regulate at all, and *how* best to regulate if it is necessary to do so.

When a government adopts regulations, it does so because it seeks to solve some problem. There are usually many ways to solve problems, and the regulation chosen may or may not be the best way to solve a particular problem. Sometimes one discovers that the regulation isn't really doing the job intended and that the problem persists or even becomes worse. Governments then often try to correct the regulation, either by amending it or by enacting further regulations that address the newly arisen problems caused by the original regulation.

In addition, regulations often have unintended consequences. Governmental actions in one area may produce problems in other areas. For example, when the government subsidizes kerosene sales to the entire public, some people will buy kerosene and smuggle it internationally to countries where the price of kerosene is much higher because it is not subsidized. In this case, while the original government policy may have been to help the poor who rely on kerosene for light and fuel, the particular regulation does not exactly hit its target, which is the poor, and other people take advantage of a subsidy not meant for them.

Government ministries also often adopt regulations without regard to the regulations adopted by other ministries, with the result that there is an inconsistency between the regulations of different ministries. This would be the case, for example, where one government ministry, say Forestry, creates

---

<sup>3</sup> Many countries, including the U.S., Canada, Australia, Ukraine, and the U.K. carry out this process, and even in countries that have not implemented it, recognize it to be the international best practice with respect to regulatory reform.

a national park where development is not allowed, while another ministry, say Mining, granted mining permits for national park areas. In this case, different government ministries are acting in contradictory ways, confuse parties attempting to obey government regulations, and interfere with one another's work and goals.

Finally, regulations often impose costs on various parties that the government doesn't really take into account at the time of regulation. For example, in Indonesia, in order to operate as a small business, entrepreneurs must obtain many different government permits and licenses. There are five main business licenses, sectoral and product and activity specific licenses as well, and there is a redundancy between a numbers of different licenses.<sup>4</sup> Each permit and license imposes a number of costs: the paperwork and time costs involved in filling out the applications; the time lost in going to government offices to file papers; the fees imposed for each license or permit. There are also bribe costs as obtaining licenses requires interactions with government officials and gaining approvals.<sup>5</sup> All such costs, in money, time, and lost opportunities increase the cost of doing business. In order to survive, businesses must charge more for their products and services to recoup these costs. This makes goods and services more expensive than they would otherwise be and contributes to a higher cost economy.

Regulatory impact assessments, which consider these and other matters, are rather simple in form, but, depending on the complexity and circumstances of particular regulations, can involve substantial analysis. Overall the aim is to analyze what a regulation actually does, in terms of achieving the government's goals, the benefits the regulation is likely to realize, the costs it imposes on business, the consumer, and the government, and its effects on competitiveness and competition.

### **3.1. RELATED REGULATORY PROBLEMS: VAGUENESS; DISCRETION; BRIBERY**

Regulations may require government agencies to take certain actions when citizens provide certain information and pay certain fees, e.g., to grant a license. However, where there is little oversight of government employees, they may act as though they had discretion whether or not to grant a request. In addition, where laws and regulations are vague, multiplicative, or inconsistent, government agents must of necessity interpret them. This need to interpret confers on them a power of discretion. That discretion allows them to grant, or to refuse to grant, what a citizen may request. In such circumstances, the power to refuse creates an opportunity to grant a request for a price. The government agent's control over something a citizen needs gives the agent the power to demand a payment to him, over and above any proper fees required.

Similarly, officials can use agency power to issue regulations to extract rents. A domestic business that produces a product for which there is import competition could ask the relevant Ministry to issue a regulation restricting imports of the competing product. Because the Ministry has so much discretion over such matters and because there is neither openness nor accountability in the issuance of ministerial regulations, this creates an opportunity for the relevant officials, if they are so inclined, to seek a payment in exchange of the requested regulation.

For such reasons, a further aim of regulatory review is to increase the clarity of regulations, to greatly reduce unfettered official discretion, and to reduce the number of interactions with public officials that regulations may call for. All of these actions increase the consistency of regulation, reduce regulatory conflict, preclude or narrow interpretive creativity and abuse, and reduce occasions for bribes as well as reducing it takes to get government approvals.

---

<sup>4</sup> Making Sense, *supra*, n. 2. at 9.

<sup>5</sup> Kuncoro, Ari, Bribery in Indonesia: Some Evidence from Micro-Level Data, *Bulletin of Indonesian Economic Studies*, vol. 40, no. 3 (2004).

### **3.2. REGULATORY IMPACT ANALYSIS COMPARED WITH POLICY ANALYSIS**

Regulatory impact analysis is primarily a governmental discipline. It is certainly a kind of policy analysis, but one that seeks to consider policy choices from the point of view of all affected stakeholders. It is properly a governmental role to aggregate, consider, reconcile, and balance interests, and, ideally, to make policy choices that are in the best interests of society as a whole. When stakeholders other than the government undertake policy analysis, they usually undertake it only from their own point of view, and one can reasonably expect that their policy analysis and prescriptions would be tailored to their own interests and not necessarily take into account the interests of other stakeholders. We thus should distinguish between governmental regulatory impact analysis as a kind of policy analysis and stakeholder policy analysis that must be presumed to be much more self-interested.

In a well-ordered government policy competition and decision-making process, concerned stakeholders would promote their particular policy positions with supporting information, while the government would review all policy claims independently and on the basis of its own analysis. Stakeholder analyses would help inform the government, as stakeholders have knowledge that the government does not have, but would not control governmental policy dispositions. In this sense, stakeholder policy analysis serves the governmental consultative interest in the process of making good policy.

### **3.3. REGULATORY REVIEW IN INDONESIA**

Regulatory impact analysis was introduced to the Indonesian national government, via the then Ministry of Industry and Trade by the 2002 ADB Deregulation and Competition Project. The Project produced a training manual and trained a cadre of Ministry officials in the methodology. The manual was translated into Bahasa Indonesia, and the manual, along with revised Indonesian iterations of it, remains in circulation for government use. Through this effort, the idea of regulatory review and regulatory impact analysis secured a small foothold in at least one ministry. Today, the research arm of the current Ministry of Trade, Litbang, uses this form of cost/benefit thinking in its policy analytic work. To date, it has conducted two substantial regulatory impact analyses, one on rattan and the other on cocoa. More importantly, it has adopted a cost-benefit mindset in its consideration of regulations.

Because of the transfer of government authority to localities through decentralization, and increased local regulation, The Asia Foundation, among others, took on the cause of regulatory review in Indonesia and has conducted 25 trainings in regulatory impact analysis for local governments. TAF also encouraged local governments to adopt the methodology as a part of their ordinary operations, and, where they were receptive, to assist them in institutionalizing the practice. To date, Pare Pare and Sragen are only localities that have fully embraced regulatory review, while institutionalization efforts have so far been less successful in other localities, although RIA efforts are ongoing. To further assist localities, TAF helped conduct regulatory impact analyses of two local business licensing regulations for each kabupaten participating in its trainings, and these analyses are available for use by the localities. GTZ has also conducted a number of regulatory impact analyses. TAF now plans to work with fewer localities and focus its efforts on institutionalization of the process.

While these are positive national and local developments in regulatory reform, Indonesian governments, for the most part, do little in the way of using regulatory review methodology to improve regulatory regimes. It is also fair assessment to say that, by and large, Indonesian ministries and other governmental agencies, national and local, have neither the interest, the human resources, nor the technical ability to carry out large-scale and systematic regulatory review. Regulatory review and evaluation are not parts of the ordinary working of Indonesian bureaucracies, and these bureaucracies, for the most part, do not take cost-benefit considerations into account in decisions to regulate, nor do they give much consideration to the best form of regulation. Introducing regulatory review and evaluation to the many Indonesian administrative agencies and educating Indonesian civil

servants to the skill levels required to do such analyses and evaluations well is a major reform that calls for long, sustained efforts.

### **3.3.1. REGULATORY REVIEW AND THE INDONESIAN PRIVATE SECTOR**

While Indonesian governments have been slow to embrace and use regulatory impact analysis, the Indonesian private sector has been more active, at least in noticing and complaining about regulatory problems. The Indonesian Chamber of Commerce (Kadin) and its research arm on decentralization, KPPOD, have collected and examined local government regulations adversely affecting businesses and have published annual surveys regarding the business friendliness of localities in Indonesia. Most of the regulations compiled imposed taxes, fees, or increased business licensing requirements. These surveys have been useful for the information provided, for the pressure they put on local governments to improve their regulatory regimes, and for the competition for rankings they have created among local governments.

Notwithstanding this positive private sector deregulatory activity, deregulation work has just begun. Systematic regulatory review would benefit Indonesian business competitiveness.<sup>6</sup> As Indonesian governments don't do this, however, and as Indonesian associations have thus far played a limited role in a systematic and ongoing review of regulations, what's to be done?

### **3.4. THE CONTEXT OF REGULATORY REFORM**

As a matter of setting the context, it is well worth noting here that, less than ten years after the collapse of the Suharto regime Indonesia, as a state, continues in a process of major transformation. When Suharto lost power, significant structural arrangements of the Indonesian government changed, but others remained intact. For example, the DPR, or Parliament, became an independent, major political actor, there were genuine, democratic elections, the military's role in politics and government was greatly reduced, and there was a major decentralization of governmental authority. Nonetheless, many of the day to day operations of government in its bureaucracies and administrative agencies continued much as they had in the past. In these agencies of government, ideas of what governments do and how they go about their business did not change quickly – in large part because the civil service personnel that managed them did not change.

In these circumstances, where there are no powerful and effective root-and branch reformists driving change throughout the government, the regulatory agencies of day to day government have been slow to change. At best, one can say that they are in the process of learning new governmental roles, along Western model lines. In these roles, there is considerable focus on economic growth and development through the market, rather than through state direction and state choice of winners and losers. The state takes on a more neutral position as guarantor and enforcer of fair and efficient markets, and seeks to find paths to the common good or public interest among the forces competing over governmental regulatory policies.

In this situation, even if Indonesian governments and regulatory agencies, of their own initiative, do not yet conduct regulatory impact analyses, they are not necessarily set against reform. While some are certainly recalcitrant and resist learning and adopting the new roles, others are simply uncertain or confused or do not know how to occupy the new roles. Even where there is recognition and desire,

---

<sup>6</sup> Ideally, Indonesian governments, at both national and local levels, should undertake a “regulatory guillotine”. This is a commitment to inventory and review all regulations, within a set, relatively short, period of time, and to abolish those that are duplicative, ineffective, too costly or burdensome, or that interfere with competition, and to revise all those retained to insure they meet their objectives in ways that provide the most benefit at the least cost. Given present Indonesian politics and the heavy legacy of Indonesia's bureaucratic past, this is most unlikely to happen for quite some time, except perhaps in some exceptional locality.

there may not be capacity and resources to analyze regulatory regimes for the common good. This suggests that there are reforms that some Indonesian governments cannot or are not likely to initiate, yet nonetheless might adopt were some other party or parties to do the underlying analytic work for them, as well as lobbying effectively for change.

Thus, when presented with good data about the adverse consequences of particular regulations, and enough pressure, some Indonesian governments or agencies of government may respond positively. This may also become increasingly likely over time for two reasons: increased governmental responsiveness arising from democratic politics; and competition between localities for business and economic development.

Where governments are unable or unwilling to *initiate* change and reform, the reform impetus, as well as the cases to be made for particular reforms, must come from another source. Given the marginal state of official regulatory reform in Indonesia, what institutions are there that can play this initiating role? The institutions that have the interest and capacity to undertake some form of critical review of regulatory policies and regulations as well as advocate reforms are donors and some NGOs, and they currently do some of this. Indonesian private sector business associations also have a substantial interest in regulatory policy and reform.

#### **3.4.1. Donor Analysis**

Donor-conducted policy analysis might, to some degree, make up for the absence of governmentally conducted regulatory impact analyses and can certainly be a source for reform ideas. While the analysis would be done, however, there would be no Indonesian ownership. Even where reforms are promoted through conditionality, there is often a grudging embrace and less than full compliance. Without conditionality attached to loans, donor promoted reforms has difficulties in getting responsive hearings, and even less success in getting action. Donor-driven reform, without enduring enticements or incentives, is also not sustainable – although it is possible there is some associated learning that does carry over. Nor, where governments lack capacity and resources, and do not see their interests served, is there any likelihood that reform and reform processes will be taken over and institutionalized.

This is not to say that donor-conducted analyses and policy advocacy are not useful. They certainly are: they address some of Indonesia's analytic and policy-making resource gaps, and provide valuable information and ideas. Donors usually make them widely available and, where loans may be involved, design development loan packages around them. Nonetheless, such efforts are not likely to have the impact of Indonesian originated and owned policy analysis. Finally, it is necessary to note that, like all policy advocates, donors have agendas, often associated with making loans, but also deriving from development ideologies that as yet do not resonate in Indonesia. They are not neutral, nor are they perceived to be neutral in their policy prescriptions. Most pointedly, they are not Indonesian.

#### **3.4.2. DOMESTIC RESEARCH INSTITUTIONS AND NGOS**

Indonesia has a number of well-respected research and advocacy institutions, such as CSIS and SMERU, some University research institutions, and there are many NGOS, both domestic and foreign, operating in Indonesia. These institutions sometimes provide detailed policy analysis and more often take policy and advocacy positions. The research institutions, if not independently funded, sometimes do researches on contract, often on donor, government, or even private party hire. While these institutions can be an important source of policy analysis and advocacy, it is not at all clear, with some exceptions, how effective they are, what their access to government is, nor how they go about their advocacy work. Nonetheless, they are a source of policy ideas and critique and are players in the competition for policy.

### **3.4.3. PRIVATE ASSOCIATION ANALYSIS**

The distinction between governmental regulatory impact analysis and stakeholder policy analysis and advocacy comes more sharply into play as one considers the role of the private sector in governmental policy-making. Simply put, we should not expect business associations to take responsibility for the overall public interest, as governments should do. Business associations should represent the interests of their members, and these may not always coincide with the public interest. Business associations, however, have a stake in regulations that affect their members, so they have an important role as significant stakeholders in regulatory review. They can play this role through policy advocacy and analysis.

Where the government fails to improve the regulatory regime, there is a greater need for the private sector to step in and to use competent policy and regulatory analysis and advocacy to prompt positive changes. It is in the interests of Indonesian business associations to undertake ongoing policy analysis and advocacy. As parties affected adversely by regulation, they are stakeholders in government policies and regulations. They are also best positioned to assess and uncover the costs and other competitive disadvantages the government's policies impose. As explained below, they also appear to be interested in these activities.

## 4. POLICY ADVOCACY AND ANALYSIS

---

### 4.1. ADVOCACY

What does “policy advocacy” mean? Obviously, advocacy of any particular policy can range from the slightest gesture of support to an orchestrated media campaign of promotion of a particular set of ideas, with all sorts of supporting analyses, documentation, endorsements and the like. For the purposes of this report, policy advocacy means persuasions, to change or adopt particular policies, directed at decision-makers who control policy making and to parties that can influence these decision-makers. Policy advocacy involves arguments in favor of a policy as well as arguments against the policy to be replaced, if there is one. It also involves countering arguments of those who would oppose the proposed policy.

Because policy advocacy is directed at decision-makers *and* those who influence them, the persuasions or arguments involved in the advocacy can be shaped to appeal to the interests of the target audience. A policy advocacy campaign would thus call for an analysis of whom it is essential, and useful, to persuade, how to reach them, and what arguments to use to persuade them. For any particular audience, this calls for an analysis of what the audience values, what its interests are, and how to shape policy proposals and arguments in ways that appeal to those values and interests. If this is not possible, then it is helpful to shape them in ways that do not threaten the values and interests of the target audience. There is even more that can be said. For present purposes, however, what is essential to understand is that policy advocacy, at least where governments are involved, calls for analysis, planning, and strategy, as well as skills in framing persuasive argument. Policy advocacy also presumes policy analysis.

### 4.2. ANALYSIS

Policy analysis can take many forms, and there can be different sorts of analyses that policy choices should generate. At heart, all forms of policy analysis seek to determine the likely impacts of a policy and policy alternatives on those affected by it, the stakeholders. This entails a stakeholder analysis (who will be affected); a means analysis (how will they be affected); a goals analysis (what will be achieved); an impacts analysis (in what ways and how much will stakeholders be affected) allied with some sort of cost-benefit or similar analysis, including an analysis of how costs and benefits are distributed among stakeholders who wins and loses). Ideally, a policy analysis would include similar analyses of policy options and the tradeoffs between them.<sup>7</sup>

These kinds of analyses, which may require some empirical research, provide justifications for policy choices and reasons for choosing one policy over another. From a policy advocacy point of view, these analyses provide the arguments and counterarguments that a policy advocate needs to make a persuasive case for his or her preferred policy. Were Indonesian private business associations to undertake these kinds of policy analysis and advocacy activities, they could significantly help to transform the business regulatory environment in Indonesia. Whether they can undertake these activities, and how SENADA might assist them in their efforts to do so is discussed below.

---

<sup>7</sup> Listing so many seemingly different kinds of analysis might cause a reader to think of analysis as a kind of contagious disease – leading to a fatal condition of analysis paralysis – or to conclude that analysis is a really complicated matter not suitable for Indonesian private associations. Frankly, despite the varying targets of analysis, these analytic efforts are not necessarily difficult: it is more a matter of systematic thinking about consequences of potential choices. Of course, a sophisticated cost-benefit analysis can be complicated and demanding. At this stage of development in Indonesia, however, instituting a cost-benefit mindset is more important than instituting a complicated and time-consuming methodology.

## 5. PRIVATE SECTOR ASSOCIATIONS

---

Businesses need to analyze governmental policies and regulations to determine exactly how they negatively impact business operations and competitiveness, and to effectively advocate policy and regulatory changes. The most promising private sector vehicles for undertaking such analyses and advocacy are private sector business associations. For SENADA, these are the associations that represent the interests of the parties involved in the five value chains. These are not solely value chain associations, e.g., API, the textiles association, or ASMINDO, the furniture association, but also associations with cross-cutting interests, e.g., the Importers and Exporters Association, and perhaps, to include the lower end of the value chain, SME associations or basic goods and supplier associations. In addition, given the large regulatory authority of local governments, and the heavy impact of local regulations on SMEs and on lower portions of national value chains, SENADA also has an interest on working on regulatory reform with regional and lower level associations.

### 5.1. TYPES OF ASSOCIATIONS

There are many types of associations in Indonesia: sectoral associations, such as API (textiles association), APRISINDO (footwear association), and ASMINDO (furniture association), and a whole host of product associations too numerous to mention; function associations such as APINDO (employers' association), IIEA (importers and exporters association), ALI (logistics association), KADIN (chamber of commerce association), and others; and some of these associations have national and provincial or local chapters.

While SENADA has a particular interest in working with Indonesian private sector associations that represent their value chains, it is important to note that parties engaged in these value chains may participate in more than one association, e.g., in API and in APINDO, and that there are non-value chain associations whose work has impacts on the value chains, e.g., the Importers and Exporters Association. For these reasons, SENADA's work with associations should not be limited to value chain associations, but rather should focus on working with those associations, whatever they may be, that can make a significant contribution to value chain competitiveness.

### 5.2. PRIVATE ASSOCIATIONS AS PARTICIPANTS IN REGULATORY REFORM

If regulatory impact analysis were a standard government practice in Indonesia, national and local governments would consult with private sector actors when any proposed regulation affected them. For the most part, Indonesian governments, however, do not effectively consult with non-governmental stakeholders in government policies and regulations.<sup>8</sup> As affected parties, private sector actors, and their representatives, such as associations, are usually strong supporters of deregulation. They are stakeholders in public policy and are parties best positioned to know the impacts of government policies and regulations on business and business competitiveness. If the Indonesian regulators do not effectively consult with businesses, as stakeholders, over regulatory matters, the associations could take the initiative and consult with the regulators.

Initial discussions with some Indonesian business associations connected to SENADA's value chains (such as API, ASMINDO, APRISINDO, and IAE) reveal that they are interested in developing their capacities to analyze policy and regulations and to advocate with the Indonesian national and local governments for policy and regulatory reform on issues affecting them. Some, like API, would also

---

<sup>8</sup> There appear to be some legal requirements regarding public consultation, particularly at the local level. Experience suggests, however, that it is the letter, rather than the spirit, of such laws that is followed. Consultation is seen as a formality, rather than as a means of securing better regulations.

like to strengthen their ability to analyze trade issues and to participate more effectively in governmental policymaking regarding international trade.

While private sector associations, in different ways and to different degrees, want policy development and advocacy assistance, they evidence varied stages of development and effectiveness. None, with the exception of APINDO, appear to have staff dedicated solely to policy analysis and advocacy, and none appear to do disciplined, systematic policy analysis or advocacy (KADIN's KPPOD efforts aside). Where an association takes policy positions, it generally develops them through Board level discussions. As for policy advocacy, board members of some associations have good contacts in government and can arrange meetings with government officials to discuss policy. Thus, the policy reform effectiveness of some associations appears to depend primarily on personal relationships between board members and government officials to effect policy changes, rather than on quality analysis or well-organized advocacy programs. Most of the associations relevant to SENADA's value chains, however, do not operate on even this ad hoc, personalized level of effectiveness.

Overall, it appears that the associations involved in SENADA's value chains are scattered along a policy development continuum from national associations able to take a position at least on some matters and to lobby the government regarding them, to those having no kind of policy engagement at all. For example, although it would like to, because of lack of resources and knowledge, the Bandung APRISINDO chapter doesn't even take policy positions, much less advocate for policy or regulatory changes. Instead, this chapter, which is composed of SMEs, appears to be primarily a networking entity focused on skills and human resources development. Overall, initial investigation suggests that Indonesian private sector associations, except perhaps one or two operating on the national level, are not playing as significant role in governmental policy development or in regulatory reform as they could.

### **5.2.1. Private Sector Policy Positioning and Decision-Making**

In general, advocates for a policy or regulatory change should be able to demonstrate to government officials that existing or proposed policies or regulations damage sectoral or value chain competitiveness. The analysis required is not a simple matter of canvassing an association's board of directors regarding possible injury, but rather a cost-benefit analysis of the differential impacts of a policy or regulation on different subunits of the value chain as well as on the comparative competitiveness of the entire chain.

This is easiest to illustrate with the example of a ban on rattan exports. Depending on the size and kind, Indonesian rattan is either grown like a crop in gardens or harvested in forests. Small traders buy the rattan from growers and harvesters. Larger traders buy from the smaller to increase lot sizes, and sometimes do some cleaning, curing, and basic finishing work. A larger buyer will take these products, may do more finishing, grading, and sorting, and then sell them to local manufacturers who use rattan or to exporters. A ban on rattan exports injures the exporters, injures growers and harvesters who don't have an incentive to produce for a larger market, and benefits the local manufacturers who likely have a large and cheap supply of rattan. A ban, of course, also encourages smuggling.

In a case like this, a differential impacts analysis of the rattan export ban would show how the ban affected each segment of the production chain. It might show that while an export ban is in the short-term interest of local manufacturers who use rattan, it is neither in their long-term interest nor in the overall interest of the health and competitiveness of the value chain. This is so because of the disincentive to growers and harvesters and because of smuggling (in which case local manufacturers might lose any competitive advantage that a captive market in rattan gave them). Alternatively, the analysis might turn out otherwise. In any case, the analysis would show what the actual tradeoffs were

and would permit an intelligent decision regarding which policy choices were the best, taking into consideration all the costs and benefits.

### **5.2.2. Additional Analysis**

Even differential value chain impact analysis is not enough, however, to fill the policy void, nor to provide the complete basis for effective policy advocacy. Indonesian circumstances dictate that an additional kind of policy analysis would be useful. This reflects the fact that a number of different government ministries or offices may have differing interests in the same policy that reform proponents are seeking to change. This means that policy or regulatory reform proponents should also analyze the differential government interests in a policy or regulation.

Changing government policy is often not a simple matter of lobbying a single ministry or government office with good data and arguments. At the national level, effecting changes in government policy often requires negotiations with several ministries, e.g., MOT, MOI, MK, MA; and sometimes a grand negotiation with several ministries or offices at the same time. Similar multi-party governmental interests exist at the local level. Proponents of a regulatory or policy change therefore need to analyze the impacts of proposed changes on the interests that the involved government offices represent. To effect change, they should conduct a differential interest's analysis and should tailor their policy or regulatory proposals in ways that satisfy, or neutralize, as many resisting governmental interests as possible.

### **5.2.3. Additional Value for Private Sector Policy Analysis**

Indonesia is a party to many bilateral and multilateral trade agreements, and will be negotiating many further such agreements. Well in advance of any trade treaty negotiations, the Indonesian government needs to work out its positions on a host of issues, issues that affect Indonesia's industries and producers. As a part of its preparations for negotiation, the Indonesian government should confer with business sector representatives, and find out what these representatives believe to be in their interests and want. These are not simple matters, and of the many possible positions that Indonesia's trade negotiators might take, there are many permutations and combinations of tradeoffs. For any trade policy package, Indonesia's negotiators need to know what is in the best interests of Indonesia's industries and producers, what they can accept and can't accept, who will win and lose, how, and how much. This means, however, that Indonesia's industries and producers must confront the possible impacts of different trade regimes and rules and make decisions about what they believe are in their best interests. They cannot do this effectively without analyses of possible trade regimes, rules and the costs, benefits, and differential impacts of these structures on their sectors. Independently of any value that good policy analysis may have concerning Indonesian internal regulatory reform, it is essential that Indonesian private business associations develop professional level policy analysis abilities.

## **5.3. ALLIANCES**

Private sector policy analysis and advocacy are important sources of pressure for regulatory reform, both overall regulatory reform and reform of particular policies and regulations. Private sector associations can increase this pressure by forming alliances or coalitions among associations, and between associations and civil society groups.

Parties generally do not form alliances or coalitions out of good will form, but rather because they need others to help them to secure gains they cannot secure alone. They must perceive a potential ally as having related, if not identical, interests and that joining with the ally enhances their strength. It must be in the interest of every member of an alliance or coalition that the group succeeds in achieving its aims, even though every party to the alliance need not share equally in the gains.

There is a further aspect of alliance or coalition formation that is important to note. Parties who form alliances often must reshape, or compromise, on some of their goals. This is because other parties in the alliance may have goals that are at least somewhat dissimilar, if not actually conflicting. An alliance must find an encompassing goal that all parties to it share, or it must focus on achieving aims that satisfy the different, yet compatible goals of other alliance members. In alliance formation, if the parties need each other to achieve their major goal, they must be willing to make tradeoffs to secure one another's loyalty to the effort. Each party will, of course, attempt to maximize its gains, but in dealing with other alliance members will discover what those gains can be under conditions of alliance. In its own way, this process is similar to governmental participatory policy making, where a government agency consults stakeholders to determine which policy choice best meets the interests of as many stakeholders as possible while also serving the government's aims.

What this means for regulatory policy reform is that the policy choices of a private sector alliance – and the more encompassing the alliance the better - will reflect the interests of more parties than the policy choice of a single private sector actor, even an association. It amounts to private sector stakeholder consultation and agreement.

### **5.3.1. Private Sector Alliances in Indonesia**

At present, we do not know how much alliance activity there is regarding regulatory reform in Indonesia. Certain “apex” associations, such as Kadin (Indonesian Chamber of Commerce) or APINDO (Employers' Association) represent many different kinds of businesses and may take on policy issue aggregation and clearinghouse functions. There do appear to be informal alliances created on an ad hoc basis and based primarily on existing relationships between persons in different associations. There does not appear to be any systematic attempt to mobilize alliances for analysis or advocacy purposes.

Given the narrow sectoral interests of many associations, and their level of development, it is unlikely that they much concern themselves with forming alliances or coalitions with other associations or organizations. In order to become interested in forming an alliance on a policy issue, an association would have to understand not only how the policy they wished to change affected their own membership, but also how it might affect the membership or interests of other organizations. They would also have to consider how their preferred policy potentially affected these other entities. Since it appears that few private sector associations now do any significant policy analysis, it is even more unlikely that they concern themselves at all with the needs, interests, and concerns of others.

If there is little alliance activity among Indonesian private sector associations, this is a lost opportunity to effect regulatory change and to improve governmental policies in business friendly ways. Considering the role that alliances or coalitions might play in reform, however, suggests that an important way to strengthen the private sector role in policy-making and advocacy is to assist them in understanding the value of coalitions and enabling them to analyze the interests of possible allies. This activity, which primarily would involve training, would aim at increasing the ability of private sector associations to ally. It is an activity that can also be connected directly to policy advocacy training and policy advocacy itself because part of a campaign to change governmental policy would include the formation of alliances for change.

In addition, were SENADA to work with a number of different associations on policy issues, SENADA itself would be in a position to see where the interests of different associations aligned and it could demonstrate this to its clients. This is not to suggest that SENADA play the role of alliance broker, but simply rather that it show associations how to build their strength and effectiveness through alliances.

## 6. POTENTIAL PROBLEMS

---

Associations are self-interested actors; they act for the benefit of members, not necessarily in the public interest (e.g., protectionist policy). In the case of a developed country with many competing and able interest groups, this might not be a significant issue, for one could expect an intense competition over policy choices, with the government as final decider, and, hopefully, protector of the overall public interest. Presently, however, Indonesia does not have many of these effective countervailing forces. There is, therefore, some risk – although it is difficult to estimate how great – that enhancing the policy capacity of private sector associations will increase their ability to capture public policy formation in their own interests and at the expense of the public. This, of course, is not a problem unique to Indonesia. All countries experience it in one way or another, and the only effective check appears to be governmental transparency, accountability, openness to different voices, and countervailing civil society forces.

Another problem is that some national associations appear primarily to represent the interests of the producers at the end of the value chain, and the policy positions that associations take appear to reflect the interests of those controlling the association. Those interests, depending on the issue and the nature of the association, may or may not reflect the interests of all segments of the value chain or all the members of the association. One could hope that a proper policy analysis would educate association decision makers regarding the impacts of different policy choices on the value chain and convince them to consider them in making policy position choices. Still there is a risk that enhancing the policy capabilities of private sector associations, in some cases, simply benefits those who control the association. This is ultimately a question of internal association politics and the nature of the membership. In this regard, working with multiple associations that have different memberships and interests in parts of the value chain so that they could all weigh in on policy would mitigate this problem of narrow and unrepresentative policy advocacy.

These concerns do not arise for all private sector associations. For example, regional associations, even if affiliated with national associations, are more likely to represent SMEs than big players at the end of the value chain. For regional associations, local regulations are of greater concern than national policies, and it is most likely that the focus of regional association policy analysis would be to better the business enabling environment for all. In addition, some associations, like the Importers and Exporters Association, have cross-cutting sectoral interests that focus on benefiting all importers and exporters, regardless of size, and association capture, at least in ways adverse to most members, seems most unlikely. Similarly, APINDO, the employers' association has an encompassing interest that spans all sectors and employers.

### 6.1. DEALING WITH THE PROBLEMS

With private sector association policy analysis and advocacy in such a rudimentary state in Indonesia, the problems posed are speculations about some of the possible adverse consequences of enhancing the associations' policy and advocacy abilities. Providing such assistance to a number of associations having different sorts of interests in the value chains, and to both national and regional associations, mitigates the risks involved. This is simply because the greater the kind and number of interests represented, the more likely there will be healthy competition over policy. Further, as private associations form alliances to achieve policy goals, they must take the interests of allies into account and find policy positions acceptable to all alliance members.

Government regulatory bodies, because they may represent interests different than those of private associations, also provide a check. Given the record of many Indonesian government offices, one might consider this idea far-fetched, but some government offices represent sectoral and other

interests, and, sometimes, in their own way, consider the overall public interest. There are other countervailing forces in the competition for policy as well: Indonesian research institutions, NGOs and civil society groups (increasingly organized and vocal), the media, and donors. Global competition and international trade agreements, sanctions, and remedies also create policy pressure – both on the Indonesian private sector and on Indonesian governments – towards competitiveness improvements and liberalized trade, and away from protectionist trade policies likely to favor the few.

Further, whether or not a given association might use enhanced policy analysis and advocacy abilities primarily for the benefit of its controlling members, or seek self-interested, e.g., protectionist, policy changes, depends greatly on the structure of the association. For example, some of the influential company members of API, the textiles association, operate throughout the value chain – importing material to make fabric, manufacturing and dyeing it, making fabric designs, and then exporting the textiles or using some of the fabric to make garments for export. In a case like this, such a company experiences all the differential value chain impacts of regulatory changes affecting textiles. As it represents the entire value chain, it isn't likely to support policies that injure, to company disadvantage, any part of the value chain.

Finally, some of the larger, and more effective, associations, such as APINDO, with the exception of labor law matters, have policy concerns that focus more on local governments than on the national government. The same appears to be true for regional or regional chapter, associations, which appear often to be composed of small and medium enterprise members, for whom the major regulatory complaint is the activity of local government. In such a case, there is no issue of national policy capture, and the focus of policy activity is most likely to be on reducing the local regulatory burden.

In the case of API, another effective association, the greatest self-identified need is assistance in understanding international trade law and trade remedies. All the national associations whose members engage in international trade probably have this same need. They may have other needs as well, but an accurate assessment depends on further investigation.

This is not to say there is no public choice or policy capture problem that arises from enhancing private association policy abilities. It is rather to point out that every private sector association is different from others in structure, representation, operations, and interest aggregation of its members. What is needed is a thoughtful assessment of particular private sector associations, their needs, abilities, and potential positive impact on advancing regulatory reform in Indonesia. Based on such assessments, SENADA can decide what kinds of assistance it can provide to such associations that will most likely contribute to regulatory reform, a business enabling environment, and increased Indonesian business competitiveness.

## 7. CONCLUSIONS AND RECOMMENDATIONS

---

Indonesian private sector associations can play an important role in advancing regulatory reform in Indonesia. They represent the demand for a more business friendly regulatory environment. If they analyzed the adverse impacts of regulation, rather than simply complaining, and effectively advocated for regulatory reform, they can be a force for considerable improvement.

For the most part, Indonesian private sector associations do not conduct cost-benefit or similar analyses of regulations, nor, with some exceptions, do they conduct advocacy campaigns. They are less effective forces for regulatory reform than they could be. Indonesian private sector associations evidence varying levels of development, sophistication, and resources. While different associations have different needs, all would benefit from training – tailored to the organization – on policy issues, policy analysis, and advocacy.

Some national private sector associations have identified major reform issues, in particular, labor law and labor regulations, and energy policy and provision. These are cross-cutting issues that affect most Indonesian businesses. A concerted effort to assist these associations in analyzing the adverse impacts of the current labor law regime and energy infrastructure issues, to devise satisfactory reforms and remedies, find allies, and organize an advocacy campaign could lead to major beneficial reforms.

National private sector associations that represent importing and exporting businesses that compete in the international market have training needs that focus on understanding international trade law and on preparing such associations to represent their members' interests in international trade negotiations. It is not clear how well Indonesian private sector associations understand, or concern themselves with, value chain competitiveness issues. Some training in this area might be useful for some associations.

SENADA should undertake discussions with interested private sector associations that involve, or affect, businesses in its five value chains. After assessing associational needs, interests, abilities, and resources, SENADA can decide what policy, advocacy or other assistance it can provide them that will enable the associations to become effective agents for regulatory reform, reform that creates a business friendly regulatory environment and contributes to Indonesian business competitiveness.

**SENADA – Indonesia Competitiveness Program**

BRI II Tower, 8<sup>th</sup> Fl, Suite 805

Jl. Jendral Sudirman No. 44 – 46

Jakarta 10210

[www.senada.or.id](http://www.senada.or.id)