5.4 Future Port Hierarchy

5.4.1 Port Classification

For the sake of identifying importance of ports in terms of function and investment priority, port facilities shall be classified. In this study, mainly international container cargo handling, conventional cargo handling and passenger transportation/ferry are considered as the function for classifying facilities of public ports. In classifying port facilities, role of port facilities which is judged from the scale of the influence in the hinterland of ports is considered as a main standard criteria. (See Table 5.4.1.1)

Based on the above consideration, we propose to categorize ports into six classes namely "Class AA", "Class A", "Class B", "Class C", "Class D" and "Class E". These classified ports play an important role as an international level center, a national level center, a regional level center, a provincial level center, a local level center and a daily life supporting place respectively. (See Table 5.4.1.2)

Degree of the public sector's financial commitment such as port development investment is different among those port categories. In the Class AA Port, degree of the public sector's financial commitment will be the lowest. On the other hand, in the Class E Port, it will be the highest. However, public sector has to be responsible for port planning and port space management/control in the higher class ports as well as the lower class ports.

Table 5.4.1.1 Classification of the Port Facilities by Function

Role of the Port Facilities	Function of Port Facilities				
	International Container Cargo Handling	Conventional (general) Cargo Handling	Passenger Transportation / Ferry	Industrial Development Support	Tourism Support
International Center	Hub International Container Terminal				
National Level Center	Major Container Terminal	Hub Conventional Cargo Terminal	Hub Passenger Terminal		
Regional Level Center	Feeder Container Terminal	Major Conventional Cargo Terminal	Major Passenger Terminal		
Provincial Level Center		Provincial Conventional Cargo Terminal	Provincial Passenger Terminal		
Local Level Center		Local Conventional Cargo Terminal	Local Passenger Terminal		
Daily Life Support		Small Conventional Cargo Terminal	Small Passenger Terminal		
				Special Port	Special Port

Table 5.4.1.2 Classification of Ports by Evaluating Roles of Port Facilities

Role Sharing between Public and Private Sector in Fund Rising	Rank of Ports	Status of Port	Criteria for Determining each port class
Private / Public	Class AA	International Center	- Ports having International Hub Container Terminal are classified as "Class AA" port. - Usually "Class AA" port has international hub container terminals as well as conventional cargo terminals and passenger terminals.
	Class A	National Level Center	- Ports having national level center terminal(s) of any function are classified as "Class A" port. - Usually "Class A" port has multi functional port facilities.
	Class B	Regional Level Center	- Ports having regional level center terminal(s) of any function are classified as "Class B" port. - Basically each province should have at least one port which level is higher "Class B" port.
	Class C	Provincial Level Center	- Ports having provincial level center terminal(s) of any function are classified as "Class C" port.
	Class D	Local Level Center	- Ports having local level center terminal(s) are classified as "Class D" port.
	Class E	Daily Life Support	- Ports, which play a role on supporting people's livelihood, are classified as "Class E" port.

Note : Role sharing between Public and Private Sector in Fund Rising depends on the type of port facilities. For breakwaters and basic infrastructure facilities, degree of the public sector's financial commitment will be high. For the crane and other relatively beneficial facilities, degree of it will be low.

5.4.2 Policy for Selecting Strategically Important Ports (Class A or AA ports)

(1) General

The Study Team focused on selecting the class AA or A ports (International or National Level Center) from Class B ports (Regional Level Center) mainly from the viewpoint of national level development policy. In this study strategically important ports are equivalent to the Class A or AA ports.

For selecting strategically important port, we shall take into account not only activity of port but also contribution of port to socio-economic activity in the hinterland. In addition character of transportation in the area such as a sea transportation dependence rate of total cargo transportation shall be also taken into account.

It is recommendable to invite opinions from port users, related national and local organizations about the procedure how to select the strategically important ports. By doing so, accountability and transparency of port development can be secured.

(2) Policy for selecting strategically important port

Roles of ports shall be the most important factor to be considered for selecting strategically important port.

Based on the fabric of the port development strategy (Chapter 4), expected roles of ports can be summarized as follows. Criteria for selecting strategically important ports are shown in Table 5.4.2.1.

Role I Supporting Socio-economic Development
1. Establishment of the effective cargo distribution system
2. Contribution for maintaining, sophisticating and introducing the industrial activities

Role II Rectifying Regional Disparity
1. Contribution for extending the future land development axis
2. Contribution for promoting the regional development in the less advanced regions

Role III Surviving in the Age of Global Exchange and Great Competition
1. Contribution for strengthening the international competitiveness
2. Contribution for promoting the international economic cooperation with neighboring countries

From the viewpoint of Role I , ports whose hinterland has large scale socio-economic

activity, such as ports in Java and Sumatra are basically prioritized more than others.

On the other hand, from the viewpoint of Role II , less advanced areas shall be prioritized.

From the viewpoint of RoleIII, areas which are close to international sea lanes and have large amount of international cargo traffic demand shall be prioritized.

Based on the above examination and consideration of the regional balance, the strategically important ports (Class A, AA Ports) are examined. Preliminary idea is shown in Table 5.4.2.2.

Table 5.4.2.2 Provinces which have Strategically Important Port

Island or Island Group	Province which should have the Strategically Important Port	Number
Sumatra	Sumatra Utara, Riau, Sumatra Selatan and Lampung	4
Java	Java Barat, Java Tengah and Java Timur	3
Bali, NTT, NTB, TT	NTT	1
Kalimantan	Kalimantan Barat, Kalimantan Selatan and Kalimantan Timur	3
Sulawesi	Sulawesi Utara and Sulawesi Selatan	2
Makulu, Irian Jaya	Irian Jaya	1
Total		14

Prepared by OCDI

Table 5.4.2.1 Expected Roles of Ports and Representing Criteria for Selecting the Strategically Important Ports

Role of Ports			Criteria for Selecting which contribute to achieve	Strategically Important Ports the Expected Role
Main Item	Sub Item	Detailed Item	Items	Representing Data
I Supporting socio-economic development	1. Establishment of the effective cargo distribution system	1) Establishment of international and domestic cargo transportation system	a) Socio-economic condition of the hinterland	- Population - Growth rate of population - GRDP - Growth Rate of GRDP
		2) Modernization of the international cargo transportation system	b) Transportation condition of the hinterland	- Dependence rate of sea transportation - Length of national and provincial road
		3) Modernization of the domestic cargo transportation system		
		4) Contribution to promoting the modal shift to the mass transportation system	c) Cargo condition	- Cargo volume - Growth rate of cargo volume
	2. Contribution to maintaining and sophisticating the industrial activities	1) Supporting the promotion of assembly industry (Establishment of effective system for transporting the materials and products)	a) Economic (Industrial) condition of the hinterland	- GRDP of manufacturing - Growth Rate of GRDP of manufacturing
		2) Supporting the industry which utilize national resources (Establishment of effective system for transporting the materials and products and providing the space for industry)	b) Transportation condition of the hinterland	- Distance from the port to Industrial zone by access road

(Table 5.4.2.1 Continued)

Role of Ports			Criteria for Selecting which contribute to achieve	Strategically Important Ports the Expected Role
Main Item	Sub Item	Detailed Item	Items	Representing Data
II Contribution to realizing the well balanced land development structure	1. Contribution to extending the future land development axis	1) Contribution to extending the future land development axis in the short and middle term	a) Fitness to the direction of the National Policy	- Existence of the prioritized KAPET - Development prospect in the future land development structure
		2) Contribution to extending the future land development axis in the long term	b) Fitness to the future prospect of national land development	- Dependence rate of sea transportation - Length of major road
	2. Contribution to promoting the regional development in the less advanced regions	1) Supporting the peoples' livelihood in less developed district	a) Socio-economic condition of the hinterland	- GRDP/Population
		2) Contribution to establishing the effective transportation system for the materials and products in the regional areas	b) Transportation condition of the hinterland	- Dependence rate of sea transportation

(Table 5.4.2.1 Continued)

Role of Ports			Criteria for Selecting which contribute to achieve	Strategically Important Ports the Expected Role
Main Item	Sub Item	Detailed Item	Items	Representing Data
III Contribution to coping with the international competitiveness and cooperation	1. Contribution to strengthening the international competitiveness	1) Contribution to establishing the effective international cargo transportation system	a) Condition of International Cargo	- International cargo volume as of 2018 - Growth rate of international cargo
		2) Contribution to establishing the effective domestic cargo transportation system	b) Strategic Geographical Location	- Location with relation to international sea lane
	2. Contribution to promoting the international economic cooperation with neighboring countries	1) Contribution to promoting BIMP-EAGA and other international economic cooperation	a) Strategic Geographical Location	- Designation in the International Economic Regional Cooperation
		2) Contribution to promoting APEC, NAFTA and other international economic cooperation	b) Sea transportation condition	- Number of Cruising Vessels

Chapter 6 STRATEGY FOR PORT FINANCE AND PRIVATE SECTOR PARTICIPATION

6.1 Strategy for Port Finance

The strategy for port finance is presented in Figure 6.1.1.1.

6.1.1 Roles of Government, IPC and Private Sector

(1) Clarification of Roles of Government, IPC and Private Sector in Indonesia

There are 656 commercial ports in Indonesia. While 112 profitable ports are managed and operated by corporatized IPCs, the remaining 544 small and unprofitable ports are directly managed by the government. Since 1994, private sector participation has been encouraged in port development and operation. In spite of the slow pace, PSP has made positive progress step by step in the last five years. Although the pace has been further slowed by today's monetary crisis, private sector participation will definitely be most important key in promote port development and enhancing the port efficiency.

On the other hand, the increase of PSP can't change the important roles of the government (public sector) form national, neutral and financial view point. The most important is to clarify or reconfirm what kinds of roles the government, IPCs and private sector should play in the process in order to develop the long term policy for port development. The present main roles of each are summarized as follows ;

1) Roles of the Government

The government usually plays a role of "regulator", "policy maker", "planner", "safety watcher", "developer" and "shareholder of IPC".

2) Roles of IPC

IPC usually plays a role of not only "planner" but also "manager" and "day-to-day operator" in commercial ports.

3) Roles of Private Sector

The private sector must plays positive roles to alleviate the government's burden and bring high efficiency to port development and operation by participating all kinds of port activities with some exceptions.

The main roles of the government, IPC and private sector is summarized in Table 6.1.1.1

Figure 6.1.1.1 Strategy for Port Finance

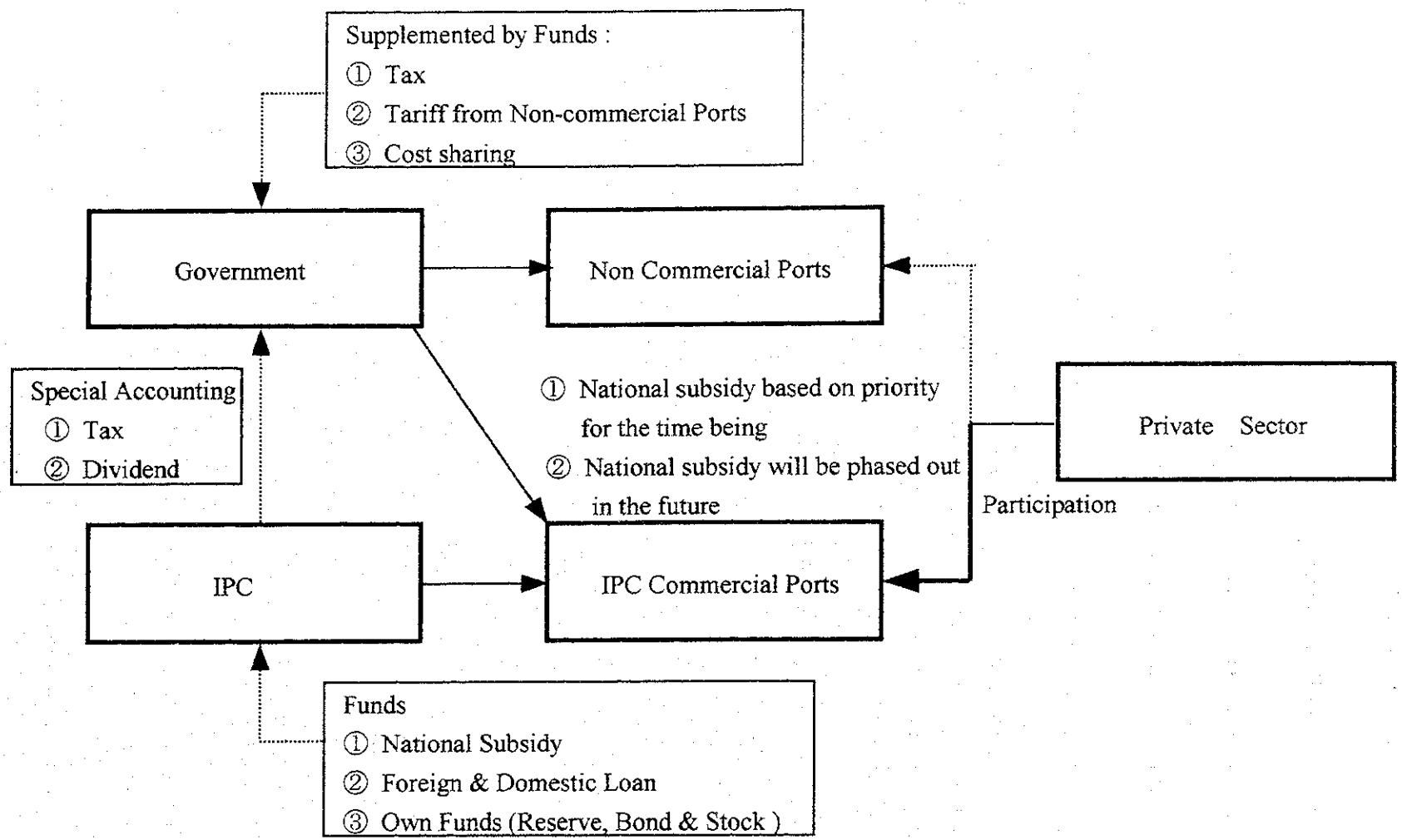


Table 6.1.1.1 Summary of Main Roles of the Government, IPC and Private Sector

Main Roles of the Government
① To establish basic principles, related laws & regulations and formulate "Port Master Plan" in cooperation with IPC
② To develop and maintain "channel", "breakwaters" and facilities of "maritime safety" which protect livelihoods of the people from national view point
③ To manage port-related space
④ To develop, manage & operate unprofitable "non-commercial ports" in order to secure the "national minimum"
⑤ To allocate national subsidies to main facilities of IPC ports

Main Roles of IPC
① To formulate "Port Master Plan" in cooperation with the government
② To develop, manage and operate "profitable" ports
③ To provide day-to-day port services to users
④ To invite the private sector to participate in development, management & operation of IPC ports

Main Roles of Private Sector
① To participate in development of port facilities in cooperation with IPCs
② To participate in operation of commercial ports in cooperation with IPCs
③ To relieve government form high investment burden and to introduce higher standards of efficiency & technology though fair competition
Exception ; (a) Port basin for ship safety
(b) Possession of land & waters in port areas

Prepared by OCDI

(2) Recommendation

1) Necessity of Establishment of Clear-cut Policy

It is very advisable for the Indonesian government to establish a clear-cut policy for the roles of the government (public sector), IPC and the private sector. To this end, the Japanese system may serve as a valuable reference.

2) Creation of Competitive Ports

① In Japan, while the fundamental policies are determined by the government, the actual management and operation are left to the port management body (mostly, local government) and the private sector.
② However, the Japanese national government has been responsible for development of infrastructure facilities through the examination of the "Port Master Plan" and allocation of national subsidies in major ports.
③ Japanese national government has been playing a crucial role in cooperation with local

government in the port development, especially "basic infrastructure facilities". The financial sources usually come from "general revenues" such as tax. That is, the "general beneficiary" (people) shoulders the burden.

④ This concept also can be applied to Indonesia. In Indonesia, it is advisable that the government should be responsible for development of non-profitable facilities such as channel dredging, breakwaters and related roads even in commercial ports operation. These infrastructure facilities should be developed by using general tax from the point view of national interest.

⑤ These fundamental facilities will be important as a common property of the people. This concept also will be useful for encouragement of private sector participation in IPC ports.

3) Promotion of Private Sector Participation

① The promotion of private sector participation is also an important task of the government. The government should dismantle the monopolistic structure and create a good environment in which the private sector will be able to participate in port development and operation as freely as possible.

② The government should ensure efficient and effective port development and operation by introduction of "competitive theory".

6.1.2 Establishment of General Policy for National Budget

6.1.2.1 Allocation Policy of National Budget for Port Development

Recommendation

Taking account of the above mentioned matters, allocation policy for national budget in Indonesia should be elaborated as follows ;

(1) National Budget

1) Non-commercial ports

The national budget must be used for non-profitable infrastructure development and port development of "non-commercial" ports.

2) IPC ports

① In principle, the national budget shouldn't be used for port development of IPC ports.

② As a rule, the national government must be responsible for the development of non-profitable infrastructure such as "main channel dredging" and "breakwater" for the following reasons ;

(a) Those facilities are regarded as the facilities to protect the national land and maintain security of people from natural forces.
(b) Those facilities are basic requirement of port development similar to national roads in land development.
(c) The social benefit for Indonesian people can be expected to be maintained for a long time.
(d) A large amount of investment is required for construction of channels and breakwaters In addition, those facilities are non-profitable basic facilities, and thus it is difficult for IPC to develop them by themselves from the financial viewpoint.
(e) It takes a lot of time before such infrastructure can be used.
(f) The government needs to make every effort to create desirable circumstances to induce the private sector into playing a more active role in port activities.

③ However, the national budget should be used for port development of even IPC ports from practical viewpoint. In this case, specific standards should be introduced as follows ;
(a) The government should prepare the "project list" of port development subject to the national budget disbursement for IPC ports.
(b) The "priority" of the projects shall be determined based on a national policy.
(c) The national budget shall be allocated according to the "national priority" in order to optimize the national budget allocation.

④ But, if some financially sound IPCs are privatized in the future, the government shouldn't subsidize them. At most, the government has only to provide "low-interest" foreign or domestic loans. The government should take gradual steps to phase out the national subsidies in the future.

(2) IPC Budget

1) IPC must use its own budget for the development of IPC ports.
2) In this case, IPCs should consider carefully diversification of their financial sources including surplus, borrowing from banks, foreign loan, issue of bond and sales of stock.
3) In principle, IPCs should not depend upon national subsidies. IPCs must be able to finance their own activities by improving their financial situations.
4) It should be remembered that IPC was established to promote efficient and effective management and operation. This concept is in line with the original purpose.

(3) Difference of Cost Sharing System between Japan and Indonesia

1) "Public Sector" Type

As explained before, in Japan, the cost-sharing scheme between national and local government is clearly defined for each port structure & facility. In this case, both organizations are public sector, and therefore it is very rational that both public sectors share the cost for infrastructure developments according to a fixed ratio from the "public" point of view. Both public sectors can invest general tax revenue in profitable and non-profitable basic port facilities. It can be called "Public Sector" Type.

2) "Private Sector Participation-supporting" Type

① Nature of IPCs

Different from the Japanese type, the counterparts of the government are profit-making "state-owned corporations"(IPCs), which plan to be privatized in the future. IPCs are required to keep retained earnings for port investment of commercial ports. Besides, IPCs are very interested in inducing the private sector into port development as well as port operation. Therefore, the nature of both countries is different.

Hereafter, IPCs are strongly required to enhance their financial abilities. IPCs will not only have to secure funds for the port development but also to induce the private sector into port development projects. Their poor performances, which will lead to low value in the market, will make it difficult for IPC to secure funds from the market.

② Lessons form European Ports

In "competitive ports" (Hamburg, Rotterdam & Antwerp) on the European main land, the allocation of roles between the public and private sector is clearly defined. While the public sector is responsible for unprofitable facilities (channel, breakwater & road), the local government plays a role of "land-lord" port management body and the private terminal operator provides efficient port operation.

This theory can be applicable to Indonesian ports. In order to create a competitive port system, the roles of each sector shall be carefully considered as follows ; In principle, the government should be responsible for development of "unprofitable" infrastructure facilities in order to create a good environment for the private sector. While the government is responsible for "unprofitable" basic facilities (channel, breakwater & related roads), IPCs and the private sector cooperatively invest in port development and operation of the "viable ports". This type can be called "PSP-supporting" Type.

6.1.2.2 Establishment of Special Account For Funding of Port Development

Recommendation

Taking account of the current tax and dividend system in Indonesia and the merits of special account system, the following recommendation can be made ;

1) The government should use the "tax" and "dividend" revenues paid by IPC as the basic funds for the port development. In this case, it is wise to establish "Special Account System" or similar system for port development.

2) "Special Account System" allows specific revenues to be used only for specific purposes. The system is very useful to clarify the relationship between the revenue and expenditure.
   The reasons of adopting " Special Account System" are as follows ;
   ① It is rational to collect tax and dividend revenue from "profitable commercial" ports and allocate them to development of "non-commercial" ports. This is because IPCs use the facilities developed by the national government for nothing, and thus IPCs should give back to the people part of what they have earned.
   ② It is important for the government to reallocate the wealth for the sake of balanced development of the national ports.
   ③ It is necessary for the government to secure "national minimum" for the people living in remote areas, and therefore the government needs stable and firm funds.
   ④ "Special account system" is very useful not only to clarify the relationship between the revenue and expenditure but also to encourage the efficient and effective use of the limited budget.

3) The shortages of the budget should be supplemented by general revenue such as general taxes and tariff of non-commercial ports for the time being.

The following Table 6.1.2.1 & Figure 6.1.2.1 show imagined examples of special account system for port development in Indonesia.

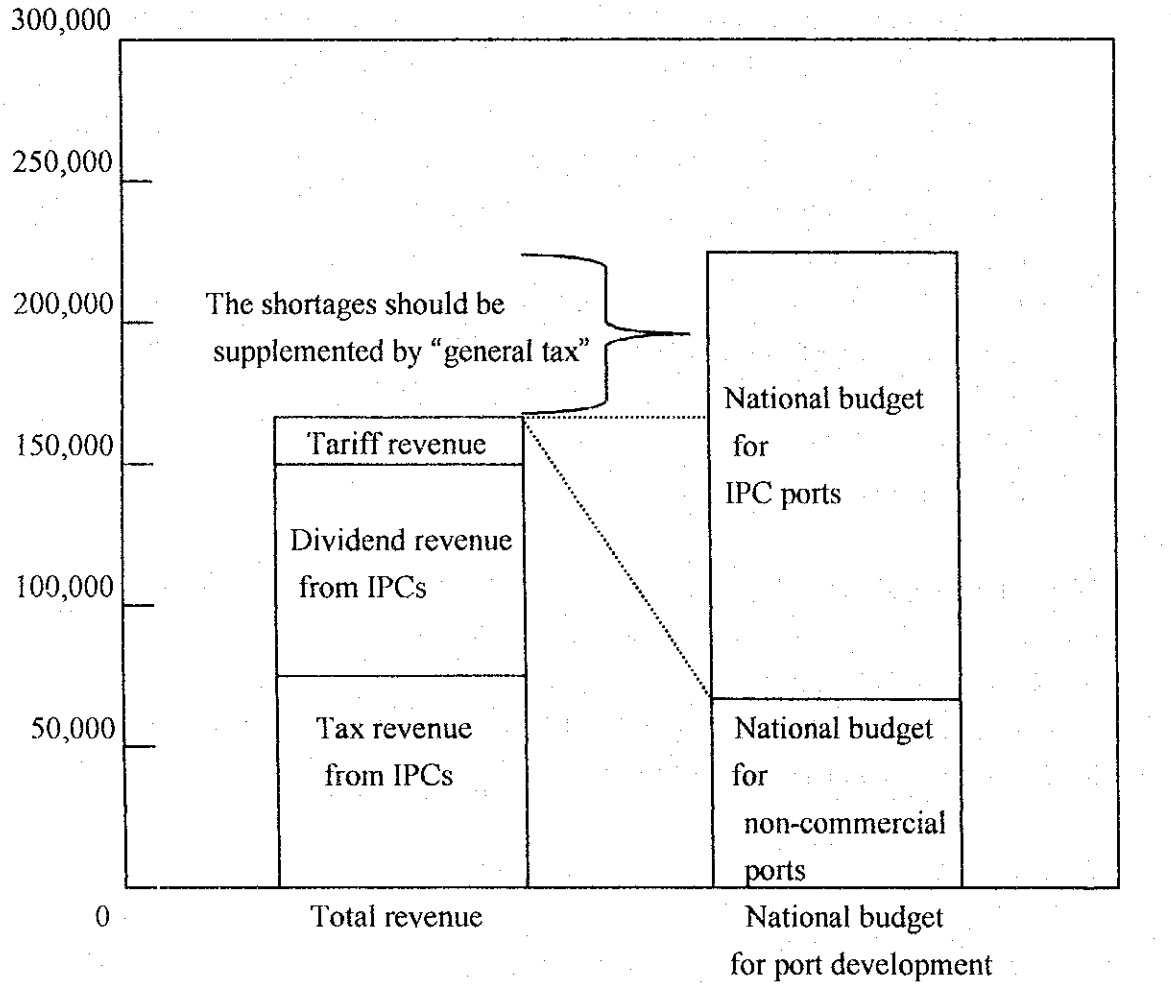
Table 6.1.2.1 Imaginary Special Account System in Indonesia

(Unit: million Rp.)

Description	1995	1996
① Tax revenue from IPCs	85,105	76,766
② Dividend revenue from IPCs	65,052	79,867
③ Tariff revenue from non-commercial ports	9,791	11,497
④ Total revenue (①~③)	159,948	168,130
⑤ National budget for port development	257,485	226,816
⑥ National budget for development of non-commercial ports	96,590	67,457
⑦ National budget for development of IPC ports	160,895	159,359
⑧ ④／⑤	0.621	0.741
⑨ ④／⑥	1.655	2.492

Figure 6.1.2.1 Imaginary Special Account System in 1996

(Unit : million Rp.)



6.1.2.3 Cost Sharing System with Beneficiary

(1) Enrichment of National Financial Sources for Port Development

Taking account of the importance of the sea transportation mode in Indonesia, the government should pump more funds into the port development. Furthermore, in some cases, it is irrational for the government to use only tax and tariff revenues for the development of the ports.

For example, the following concrete measures shall be considered ;

① To collect port charges without fail
② To set tariff in accordance with construction costs
③ To increase tariff rate as necessary (e.g. inflation)
④ To establish "cost sharing system"

For example ;

(a) Sharing cost by the source
(b) Obligation of beneficiary (willingness-to-pay)
(c) Sharing cost for port environment improvement work
(d) Charges for proprietary or mining sand and earth

(2) General Explanation of "Cost Sharing System" in Japan

Generally speaking, the port management body (usually, public sector) should use "general tax" and "port tariff" revenues as funds for port development. While tax is imposed on "general beneficiary" like residents, port tariff is laid on "natural beneficiary" like port users.

However, in specific cases, it is very unfair and irrational to use only "tax" or "tariff" revenues for the port development works. In such specific cases, the port management body should raise the costs of port work sharing from "special beneficiary" (cost sharing system).

For example, in Japanese "Port and Harbor Law" and other related laws, some cost sharing systems are introduced. Similar stipulations are often seen in other foreign laws and regulations.

For reference, the following Table 6.1.2.2 shows the outline and basic concept of the cost-sharing system for port development in Japan .

Table 6.1.2.2 Outline & Basic Concept of Cost Sharing Systems in Japan

Name of system	Legal base	Cost sharing party	Actual situation
① General tax	National and local tax law	General beneficiary : "Residents" must pay the tax.	In principle, general tax is used for infrastructure development.
② Port tariff	Port & harbor Law Article 44	Natural beneficiary : "Users" must pay port tariff.	In principle, port tariff is determined based on "Cost Accounting"
③ Sharing cost by the source	ditto Article 43-3	Special beneficiary : The party who caused the port work must share the cost.	It is determined on case-by-case basis
④ Obligation of beneficiary	ditto Article 43-4	Special beneficiary : The party who receives the most benefit from port work must share the cost	It is determined on case-by-case basis.
⑤ Sharing cost for port environment improvement work	ditto Article 44-2	Special beneficiary : "Factories " or businesses located in port area must share the cost.	Only six major Japanese ports including Tokyo & Osaka collect this charge.
⑥ Charges for proprietary or mining sand and earth	ditto Article 37⑦	Special beneficiary : The person who obtained authorization for the proprietary use must pay the charge.	The charges are determined based on local law.

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(3) Cost Sharing System in Indonesia (Tariff Levy System in Special Port & Wharf)

1) General

In Indonesia, cost sharing system with special beneficiary does not yet exist. Instead, the government and IPC collects tariff (anchorage, berth dues & wharfage) from special port & wharf according to the following Table 6.1.2.3. The reasons are summarized as follows ;

① The government and IPC are burdened with management and maintenance costs such as "security", "supervision", "channel maintenance" and so on.

② Thus, the users of special port & wharf should share the costs through port tariffs.

Table 6.1.2.3 Tariff Revenue in Special Port & Wharf

Description		Special wharf		③ Special port
		① IPC	② Government / non commercial port	
Whose revenue. ?		IPC	IPC	Government
① Anchorage	Own purpose *	100%	100%	100%
	General purpose	100%	100%	100%
② Berth Dues	Own purpose	Negotiation	-	-
	General purpose	Negotiation	50%	50%
③ Wharfage	Own purpose	Negotiation	-	-
	General purpose	Negotiation	50%	50%

* Note : own purpose : material, production & equipment

2) Evaluation of the Tariff System

With the exception of "anchorage", it seems to difficult to justify collecting port tariffs from users for the following reasons.

① In Japan, users of special port don't need to pay those port tariffs to the central or local governments because special ports are constructed at their own costs.

② In principle, "no service" means "no charges".

③ The relationship between the tariff revenue and expenditures related to special port & wharf is not clear.

④ The tariff levy system seems to lack rational reasons, transparent procedure and check system from certain public organizations. For example, in Japan, in case of "sharing cost for port environment improvement work", local governments are required to consult with and hear the opinions from the "Local Port and Harbor Council".

⑤ There is a danger that the tariff levy and excessive intervention of IPCs would discourage private sector participation within IPC's jurisdiction (see Chapter 7.1.4).

(4) Recommendation

1) The government should make every effort to justify collecting port charges from users of special port & wharf for general purpose.

2) Even if the tariff levy can be justified, in principle, the government and IPCs shall not collect port charges from users because "no service" usually means "no charges".

3) From the long term perspective, it is desirable for Indonesian government to establish more

transparent and clear standards of cost sharing system based on firm legal framework.

4) It is one idea to legitimate the following "cost-sharing with beneficiary" in place of tariff levy system in specific general port laws such as "Shipping Law No.21 of 1992" or "Government Regulation No.70 of 1996".

① Sharing cost by the source

② Obligation of beneficiary

③ Sharing cost for port environmental improvement work

6.1.3 Establishment of General Policy for IPC's Financial Sources

6.1.3.1 Present Situation of IPC Financing

The following Table 6.1.3.1 shows the present IPC's financial status. Based on understanding of the current situation, the status in the future should be envisioned. In this case, the starting time of following matters should be considered.

1) Privatization

Profitable IPC II and III are interested in privatization in FY 1998. The government also intends for other IPCs to follow suit in the future.

2) Issue of Bond

Issuing bonds is as an effective way to collect funds for port development on its own judgment. IPC II already started to issue bonds from 1994. Other IPCs are considering the issue of bonds for project funding. The details will be explained in the following section.

3) CT Terminal Operation by the Private Sector

"Lease of container terminals" is commonly seen in Japanese and major Asian ports. In the future, the leasing should also be taken into consideration as an effective way of management and operation.

In Indonesia, CT terminals are not yet leased or contracted out. However, at CT III in Port of Tg. Priok, "joint operation" between IPC II and the private sector has already started. Furthermore, anotherr "joint operation" between IPC III and a private partner will start in 1998 at CT III in Tg. Perak. The details of terminal operation by the private sector are referred to in Chapter 6.3.3.

Table 6.1.3.1 Present IPC's Financial Status

Description		IPC I	IPC II	IPC III	IPC IV
Establishment Year		1992	1992	1992	1992
Personnel Number (officers) in 1996		1,571	5,086	3,444	1,428
Net fixed Assets in 1996 (billion Rp.)		1,119	3,316	1,333	498
Financial Situation in 1996 (billion Rp.)	① Revenue	117	519	245	67
	② Cost	71	308	145	51
	③ Profit before tax	46	211	100	16
	③ / ①	39%	41%	41%	31%
Working ratio (%)	In 1994	54%	48%	47%	68%
	In 1995	52%	48%	41%	62%
	In 1996	51%	53%	44%	56%
Operating ratio (%)	In 1994	73%	59%	66%	83%
	In 1995	69%	57%	55%	74%
	In 1996	68%	63%	58%	71%
Return on F/A (%)	In 1994	2%	5%	5%	2%
	In 1995	3%	7%	9%	4%
	In 1996	3%	6%	9%	4%
Starting year of issuing bond		-	1994	-	-
Starting year of "joint operation" Or "lease" at container terminals		-	1997 (Tg. Priok)	1998 (planned) (Tg.Perak)	-

Note : (1) Working ratio = "working expenses" divided by "operating revenues"
Operating ratio = "operating expenses" divided by "operating revenues"
Return on F/A = "operating income" to "net fixed assets"

(2) The standards of the World Bank are as follows ;

① Working Ratio ≦ 50～60%

② Operating Ratio ≦ 70～75%

③ Return on Fixed Assets ≧ 7%

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6.1.3.2 Necessity of Diversification of IPC Funds for Port Development

Hereafter, the following financial sources can be envisioned. Due to the risk of foreign exchange, ③ and ④ must be avoided for the time being.

① Loan from foreign public sector (OECF loan, development bank loan)

② Domestic Rupia-based loan

③ Domestic Foreign currency-based loan

④ Off-shore loan

⑤ Issue of bond (domestic or foreign market)
⑥ Sales of stock (domestic or foreign market)

The following Table 6.1.3.2 shows the comparison of "foreign loan", "issue of bond" and "sales of stock". It is important for IPCs to understand the merits and demerits of them and carefully consider how to utilize them.

For reference, in the next section, "issue of bond" and "sales of stock" in other countries will be introduced.

Table 6.1.3.2 Comparison of Foreign Loans, Issue of Bond & Sales of Stock

Item	Foreign Loan	Issue of Bond	Sales of Stock
1. Creditor	International Financial Organization	Public/Investors	Public/Investors
2. Average Interest Rate (per year)	* 1 ADB 10.50% OECF 2.7%	* 2 MTN 8.06%	-
3. Merits	① Stable ② Gather a large amount of money from reliable funds	① Stable and safe for investors ② In principle, Lower interest rate ③ Gather a lot of money from the public on its own judgment	① Gather a lot of money from the public on its own risk.
4. Demerits	① Bureaucratic and time-consuming procedures are required ② Determination depends upon other organizations	① Depends upon the financial performance and market conditions ② Foreign currency based-loan brings a risk of foreign exchange.	① Risky, unstable for investors ② Depends upon the market situation and financial conditions.

Prepared by OCDI

* Note

1) Long-term notes of IPC III (ADB688 & ADB 797), & IPC IV (ADB 797 & ADB951)

2) "MTN" issued by IPC II

6.1.3.3 Issue of Bond

For Japanese, American & other port management bodies, issue of public bond is the most popular and effective way to collect the vast amounts needed for port development. In Japan, port management bodies (local government) usually issue bonds in the market in order to gather funds for large-scale projects because it can be repaid over a long term period by future generation which will actually gain benefit.

For example, in 8 Major Japanese Ports, approximately 18~24% of total revenues came from bond-issuing from 1989 to 1994. In U.S. major ports, about 25% of the total funds came from bond-issuing in 1994 (general obligation bond & revenue bond), and the ratio of bond revenues is expected to increase to 54 %from 1995 to 1999.

The most effective points of this system are to obtain "a large amount of money" with "lower interest rate" from the public & investors and to repay by installments "over a long period of time".

As the Asian market including Indonesia becomes mature, issuing bonds will be a more effective mechanism to gather a lot of money for port development. Owing to risks of foreign exchange, it will be important for the government to foster "bond market" based on "domestic currency".

6.1.3.4 Sales of Stock (Privatization)

"Port privatization" throughout the world doesn't have a long history. There are only a few examples in the "United Kingdom", "New Zealand" and "Malaysia". Today, corporatized PSA in Singapore also plans to be privatized in a few years. Nevertheless, in Indonesia, the profitable IPCs (IPC II and III) are interested in privatization ("Initial Public Offering"), which means the sale of shares on the stock exchange.

Sales of stock is an attractive way to gather funds from the public. In this way, IPCs could obtain sufficient funds for the port development. It is also possible to give benefits to the Indonesian people through the increase of its value.

However, public offering may bring some difficulties at the same time. For example, as a lot of general investors get involved, it may get more and more difficult for the government to control overall administration of the corporation. The government must approach privatization carefully considering some important factors such as issues deriving from it, the market situation in Indonesia and financial abilities of IPC.

6.1.3.5 Recommendation

Taking the above-mentioned matters into consideration, the following recommendations are made.

(1) Financial Policy of IPCs

1) From the long term perspective, each IPC shouldn't depend upon the national subsidy, and IPCs are strongly required to strengthen their self-funding ability.
2) Financially sound company like IPC II and III should try to further enhance its financial position and self-funding ability. In this case, they should carefully consider diversification of their financial sources (loan from commercial banks, issue of bonds & sales of stocks).
3) From the practical viewpoint, the government should maintain the financial support to IPC I and IV for the time being. Therefore, IPC I and IV should postpone drastic privatization for the time being. However, IPC I and IV also should make efforts to enhance their financial abilities. In this case, it is one idea to reduce the number of deficit-stricken ports and revert those ports to the government.
4) IPCs shall consider the change of port operation system from "operating port type" to "tool port type" or "land port type" system in order to secure more efficient and effective port system. It is desirable that "tool port" or "land port" system is introduced in major Indonesian ports by 2018.

(2) Issue of Bonds

1) General
① It is very important for the government to foster the "bond market" in Indonesia, which can generate the funds required for the development of infrastructure facilities.
② As the bond market in Indonesia becomes mature, the maturity of bonds issued should become longer and longer. Thus the government eventually will be able to take advantage of the merits of the bond system.
③ Financially sound IPCs should promote the bond system as the most effective way to raise funds from the public in a short period.

2) Setting Limit for Total Debt Service
① The government and IPC should always pay careful attention to the total amount of bonds they issued, because issue of bonds means debt service of principal and

interest. A clear cut standard or limit for the total debt service in one fiscal year should be set up.

② For example, the City of Los Angeles in the U.S. has two limits for the total debt service as follows ;

(a) The City Charter limits "general obligation indebtedness" to 3.75 % of assessed valuation. The result of FY 1995 was as follows ;

Table 6.1.3.3 Percentage of General Obligation Indebtedness in total Los Angeles City assessed Valuation

FY	General Obligation	Assessed Valuation	Percentage
1995	about $ 665 million	about $ 191,675 million	0.34 %

(b) The City also sets the limit that its debt service costs paid by "General Fund Revenue" remain below 10 % of total "General Fund Revenue". Results in the last three years are as follows ;

Table 6.1.3.4 Debt Services as a Percentage of General Fund Revenue

FY	Debt Service Payment	* General Fund Revenue	Percentage
1994-95	$ 145,856,000	$ 2,491,872,000	5.85 %
1995-96	$ 183,731,000	$ 2,462,454,000	7.46 %
1996-97	$ 207,846,870	$ 2,543,922,860	8.17 %

* General Fund Revenue :
the revenue whose purposes of use are not restricted and which is comprised mainly of tax & fees.

3) Incentive for Bond-Issuing

There are two incentive measures ("Government-guaranteed bonds" & "Bonds with Tax Credit") to stimulate purchase of bond-buyers. In Indonesia, the government should carefully consider introducing those incentive measures. The conditions of those bonds shall be discussed among the relevant government agencies.

① Government-guaranteed bonds

In Japan, bonds issued by 41 government corporations (e.g. Japanese Road Corporation, Kansai International Airport Company) are now guaranteed by the government. The objectives of the bonds are to increase social capital (roads, railways, houses, etc.), support the public development and strengthen the basis of the industries

& people's life.

② Bonds with tax credit

In the U.S., the "Tax Credit System" offered by the government is often employed by public organizations. For example, the exemption or reduction from tax on the "interest income" may be a good policy. The system enables IPCs to raise a lot of funds more easily, because the investors don't need to pay the tax and therefore IPC's bonds are more attractive for investors. This system will possibly encourage the private sector to participate in the development of infrastructure including port development.

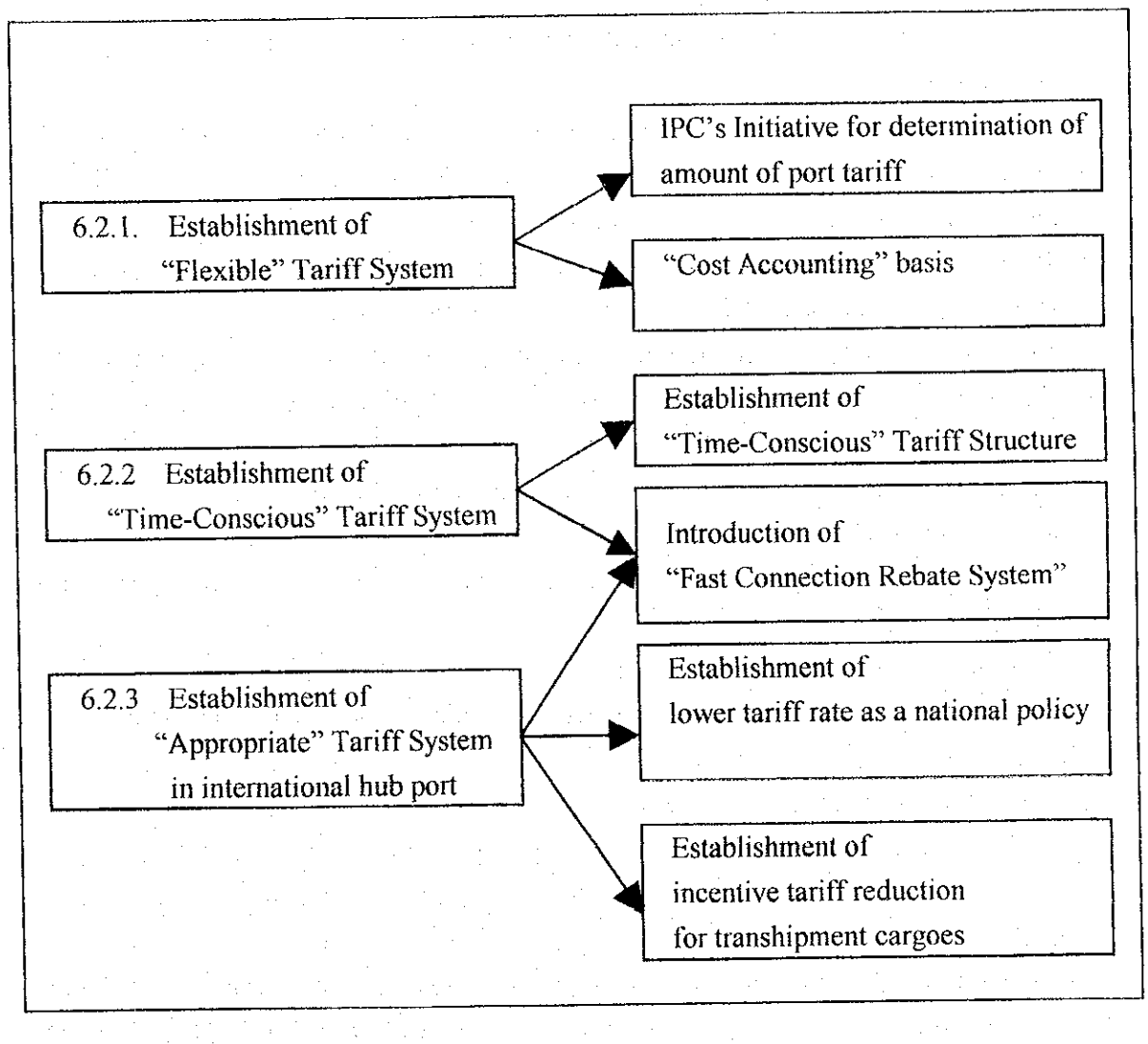
(3) Sales of Stock

1) The government must carefully approach privatization considering important factors such as issues deriving from it, the market situation in Indonesia and financial abilities of IPCs.
2) The government should carefully consider how to harmonize both requirements from the market (maximization of profits) and public (establishment of port master plan, management of related land & water areas).
3) Even if some IPCs are privatized, the government should retain more than 50 % of stocks for the time being in order to secure stable control over the administration.
4) It is one idea for IPCs to adopt "Employee Stock Option System", which encourages employees to raise the financial performance, and it also increases their loyalty to IPCs. For example, in "Auckland Port Company" in New Zealand, 87 % of employees own the company's stocks. In "KCT (Kelang Container Terminal Bhd)" in Malaysia, 5 % of the total stocks were owned by KCT employees.

6.2 Strategy for Port Tariff System

The strategy for port tariff system is presented in Figure 6.2.1.1. Details will be explained item by item.

Figure 6.2.1.1 Strategy for Port Tariff System



6.2.1 Establishment of "Flexible" Tariff System

Recommendation

Based on the above reasons, the following basic idea for the port tariff system in Indonesia should be considered.

(1) Flexible Tariff Determination

1) Port tariff levels in "non-commercial ports" should be determined by the government.
2) In principle, the amount of "anchorage" should be established by the government from the national point of view considering the necessity of applying uniform rates to some extent.
3) The amount of the "other port tariffs" in "commercial ports" should be determined by each IPC. Before the determination or review, IPC should consult with the cooperative investors (e.g. private sectors).
4) It is advisable for IPC to consult with and hear opinions from "port users"(e.g. users associations).
5) Thus, the tariff rates among ports can be different from each other taking the investment costs into account. This also enables IPC to raise or reduce the tariff rates more flexibly in accordance with the economic situation.
6) In case of rise of tariff, IPC must clarify the reasons (e.g. inflation) and strive to improve quality of the port services for users at the same time.
7) However, under the current monopolistic situation of IPC, government involvement should be required to some extent form the national point of view (e.g. to protect the livelihoods of the people or to prevent unreasonable rise of tariffs).
8) For example, it is one choice for the government to set a "tariff ceiling" (an upper limit) as follows to prevent unreasonable rise of tariffs.
   ① If the amount of port tariffs is within the ceiling, IPC has only to report to the government
   ② If the amount of port tariffs is more than the ceiling, IPC must obtain approval.
9) However, the government should respect the initiative of IPC as much as possible. Therefore, this approval should not be exclusive.
10) The government shall not regulate the fields in which the "competitive theory" works out well. Today, private sector participation is gradually increasing in port services (e.g. terminal operation at conventional terminal, joint operation at container terminal of Tg.Priok).
11) In the future, the "competition" brought by the increase of private sector participation in port services will require the government to further deregulate the tariff determination. In this case, IPCs and other private sector would only have to report to the government.

(2) "Cost Accounting" Basis in Major Ports

1) Under the present system in which the port tariff is regulated by the government laws, IPC finds it difficult to change the rates flexibly according to the economic situation.

As a result, IPC may not be able to recover all costs that they invested. Besides, the tariff regulated "uniformly" by the government greatly discourages the private sector from participating in major port projects.

2) In principle, the port tariffs should be determined so that moderate income, the depreciation cost, and management & operational costs etc. can be recovered from operation revenues for a certain period. At the same time, the tariff rates should be established taking into account the "increase of inflation rates".

3) Therefore, the government and IPC should make every effort to establish tariff rates based upon "Cost Accounting", especially in major ports.

6.2.2 Establishment of "Time-Conscious" Tariff System

(1) Importance of Establishment of "Time-Conscious" Port

It is very important for the government to establish a "time-conscious port system" in order to become a "user-oriented" port. This means that time is very important for cargo owners and shipping companies and, therefore ports in Indonesia always must be conscious of time to encourage efficient and effective use of port facilities.

This system enables a port management body to reduce the berthing time of ships and promotes quick turn-round of the cargoes for users. This will be useful not only for international hub ports but also major ports in Indonesia. The following two strategies shall be considered.

1) Establishment of time-conscious tariff structure

2) Introduction of "Fast Connection Rebate System" (FCR system)

The following Table 6.2.2.1 shows major differences in the tariff structures of Indonesia and Singapore. It can be seen that Singapore's tariff puts much more emphasis on time. For example, the "anchorage due" in Indonesia is uniform as long as the staying period is within 10days (KM28 of 1997 : per call).

Table 6.2.2.1 Major Differences of Tariff Structure between Indonesia and Singapore

Description	* Indonesia	Singapore
① Port dues (Anchorage)	Per GRT/10days	Per 100GRT/24hours
② Pilotage fees	Per Ship/GRT/movement	Per GRT/every 1st hour or every 1/2 hour
③ Berth dues	Per GRT/etmal (24hours)	Per hour for the first 150m
④ Stevedoring charges for un-containerised cargo	Per box/load	Per box/load/hour
⑤ Stevedoring charges for an OH FCL or OH transhipment container	Per box/load	Per box/lord/hour

* Note : old tariff structure based on "KM 65 of 1994" & "KM 67 of 1994"

(2) Recommendation

1) Establishment of Time Conscious Tariff Structure

This port structure will encourage shipping companies to leave the port as early as possible and cargo owners to receive the cargoes as soon as possible. This system also enables the port management body to reduce the berthing time of ships and promote quick turn-round of the cargoes. Finally, this leads to the reduction of management and operational costs for shipping companies and cargo owners, and therefore services with more reasonable prices can be provided for the people.

Making reference to the examples of port structure, DGSC should amend the port structure of Indonesia to promote quick berthing & unberthing and swift turnaround of cargoes. Therefore, the tariff structure in Indonesia should be changed as in the following Table.

Description	Old tariff structure	New tariff structure
① Anchorage	Per GRT / 10days	Per 100GRT / 24hours
② Pilot fees	Per Ship/GRT/movement	Per GRT & every 1st hour or half an hour
③ Bert dues	Per GRT/etmal (24hours)	Per length of vessels / hour
④ Stevedoring charges for un-containerised cargo	Per box / load	Per box / load / hour
⑤ Stevedoring charges for an OH FCL or OH transshipment container	Per box / load	Per box / load / hour

It should be noted the above concept is compatible with the port tariff structure of the "ESCAP" (Economic and Social Commission for Asia and the Pacific) model.

2) Introduction of FCR System

The tariff structure should be established to encourage effective and efficient operation of the facilities. Therefore, the port administrator is required to prevent overstaying of ships and cargoes and promote turn-around of berths and yards for users. In this sense, it is desirable for Indonesia to introduce a system such as the "Fast Connection Rebate System" in Singapore.

This system uses cost incentive to promote quick turnaround of transhipment containers, thereby freeing container yard space. This system is very effective not only for enhancing efficient operation of cargo handling but also for giving discount-incentive to transhiment cargoes. FCR is granted when transhipment containers fulfill the following conditions (Table 6.2.2.2).

Table 6.2.2.2 Contents of FCR System

No	Condition	Rebate
①	When transhipment containers connect to 2nd carrier within 24hours of completion of discharge from 1st carrier	A rebate of 35% from tariff rates (stevedoring charge)
②	When transhipment containers connect to 2nd carrier within 48hours of completion of discharge from 1st carrier	A rebate of 25% from tariff rates (stevedoring charge)
③	When transhipment containers connect to 2nd carrier within 72hours of completion of discharge from 1st carrier	A rebate of 15% from tariff rates (stevedoring charge)

Prepared by OCDI

6.2.3 Establishment of "Appropriate" Tariff System in International Hub Port

6.2.3.1 Conditions to become an International Hub Port

It is important for the government to compete with neighboring competitive ports such as Singapore and to resume calls of direct shipping line vessels in international competitive hub ports.

In order to do this, the following conditions must be met.

① To establish "time-conscious" tariff system
② To establish lower tariff rate as a national policy
③ To give proper incentive tariff reduction for transship cargoes
④ To establish feeder network service to regional ports

⑤ To improve cargo handling productivity
⑥ To establish just on-time service system for users
⑦ To give strong supporting services including supplies and repair to users

The condition ① is already mentioned in Chapter 6.2.2. The conditions ②and ③ , which have much to do with the port tariff, shall be mentioned in the following 6.2.3.2 & 6.2.3.3.

6.2.3.2 Establishment of Lower Tariff Rate as a National Policy

The following Table 6.2.3.1 shows that the tariff level of Tg. Priok is about 24% lower than that of Singapore under the same condition. In the normal condition, the differences shall be taken as rational.

In spite of its lower tariff, it is very difficult for Indonesia to compete with competitive Singapore, which has already built up firm and stable networks in the world. The government agencies should discuss carefully how to break up the network system. The establishment of "a drastically lower" tariff rate in "potential" international hub port as "a prioritized national policy" is one idea.

Table 6.2.3.1 Comparison of Tariff Levels of Indonesia and Singapore

Description	Indonesia (Tg.Priok)	Singapore
① Port dues	US $1,980	US $2,142
② Pilot fees	US $268	US $347
③ Towage	US $715	US $940
④ Berth dues	US $2,610	US $1,960
⑤ Container handling fees at container terminal	US $62,000	US $84,000
Total	US $67,573 (cheaper by24.4 %)	US $89,389

Prepared by OCDI

6.2.3.3 Recommendation

(1) Establishment of Lower Tariff System

In spite of its lower tariff, it will be difficult for the Indonesian government to compete with competitive countries like Singapore, which have already built up firm and stable port networks in the world. Therefore, in order to break up parts of the network system and

resume calls of direct shipping line vessels, the establishment of a drastically lower tariff rate in potential international hub port as "a prioritized national policy" may be necessary.

(2) Establishment of Incentive Tariff Reduction for Transhipment Cargoes

1) Taking account of the above-mentioned systems in Singapore, it is desirable for Indonesia to establish more a lenient and more elaborate system for transhipment cargoes in its potential international hub ports.
2) For example, it is one good idea to establish "longer free storage" for transhipment containers and "discounted storage charges" for transhipment containers.

Although Indonesian ports have no incentive system for transhipment cargoes, Singapore has very detailed incentive system as shown in the following Table 6.2.3.2 & 6.2.3.3 Singapore has two discount systems for transhipment containers as follows ; Careful attention should be paid to various kinds of incentive tariff reduction systems for transhipment cargoes. This is because transhipment cargoes don't physically give terminal operators a lot of trouble compared with import and export cargoes.

1) Longer free storage for transhipment containers
2) Discounted storage charges for transhipment containers

Table 6.2.3.2 Free Storage for Containers in Singapore

Description	Type	Free storage period
FCL import & export Containers	FCL empty	48hours
	FCL loaded	72hours
Transhipment containers	Empty & loaded	168hours

Table 6.2.3.3 Storage Charges for Containers in Singapore

(Unit : per day / per box)

	Empty	Loaded	Transhipment	Discount rate
20'	US$3.36	-	US$2.52	25%
	-	US$6.72	US$3.36	50%
40'	US$6.72	-	US$5.04	25%
	-	US $13.44	US$6.72	50%

6.3 Strategy for Private Sector Participation

The strategy for private sector participation is presented in the following Figure 6.3.1.1.

6.3.1 General Philosophy for Promoting Private Sector Participation

6.3.1.1 Purposes for PSP

(1) General Explanation

There are some purposes for promotion of PSP. It is very important for the government to clarify the purposes in order to promote private sector involvement not only in port services but also in port development. Those purposes are summarized as follows ;

1) To relieve government from high investment burden
2) To increase capacity of port facilities
3) To introduce higher standards of efficiency through fair competition
4) To provide high quality of service with cheaper price to users
5) To transfer technology and know-how
6) To facilitate fast-track implementation

In Indonesia, purposes 1) and 2) tend to be emphasized owing to the lack of government fund. However, the priority should be given to more positive purposes, especially 3) and 4).

(2) Optimization of PSP

The market in Indonesia must be in a state of sound competition in order to optimize these merits brought by PSP. Without a mature market and enough demand for working fields, it will be difficult to succeed in PSP. Therefore, the government needs to consider the following ;

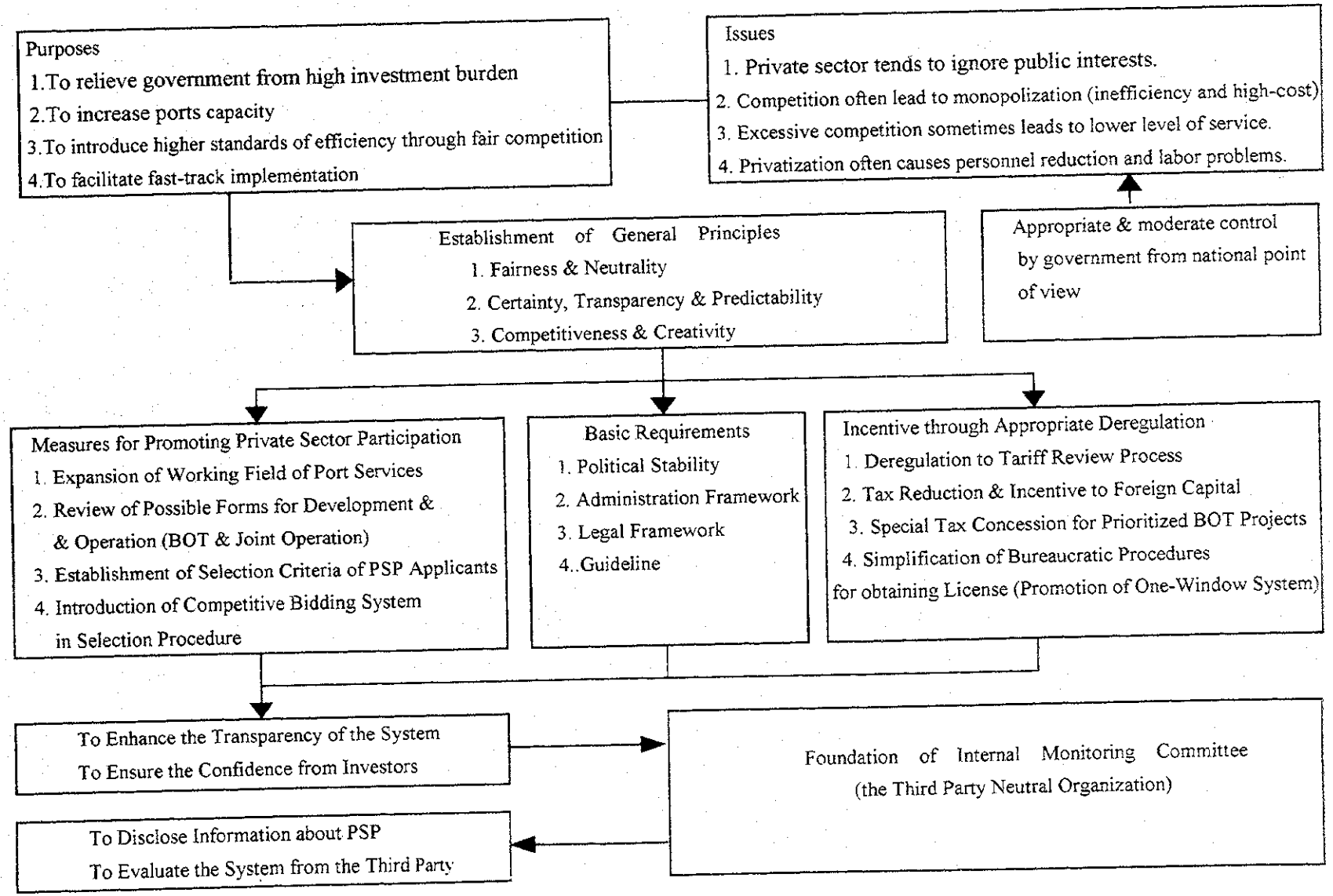
1) To create a competitive environment in which the private sector will be able to compete with each other
2) To distinguish between working fields suitable and unsuitable for PSP.

6.3.1.2 Issues of PSP

On the other hand, some potential problems can be pointed out as follows ;

1) Unlimited PSP tends to ignore the public interests including environmental consideration and living conditions of the people.

Figure 6.3.1.1 Strategy for Private Sector Participation



2) Competition sometimes result in monopolization by strong private sector, which leads to inefficient operation and high-costs of service.
3) As a result, there is always a danger that some private companies go bankrupt.
4) Excessive competition often leads to lower service level and discriminatory treatment .
5) PSP often forces the government and IPC to streamline and restructure their organizations with reduction of a large number of the employees. This sometimes leads to labor issues.

6.3.1.3 Necessity of Moderate and Appropriate Control by Government

With respect to PSP, we tend to put emphasis only on the merits. But at the same time, more careful attention should be paid to the negative aspects. In this sense, moderate and appropriate control through "Port Master Plan" and laws & regulations by the government in private sector is strongly required.

On the other hand, when "competitive theory" works well, too much involvement by the government often discourages the private sector from participating in projects. Therefore, it is necessary for the government to balance both requirements.

6.3.1.4 Establishment of General Principles for PSP

It is indispensable for the government to establish a general principle, which applies to all procedures of PSP, in order to invite more private sector participation in projects. In particular, the following three concepts should be stressed.

(1) "Fairness" and "Neutrality"
(2) "Certainty", "Transparency" and "Predictability"
(3) "Competitiveness" and "Creativity

From the long term perspective, a fair and neutral public sector will eventually earn the confidence of the private sector and promote PSP in infrastructure development in Indonesia.

Transparency, especially in the selection process is essential to obtain the confidence from the investors and to make the private sector participate in the projects. The government also must provide a desirable environment where private sector can freely enter the infrastructure projects with legal certainty and predictability that their rights will be protected.

On the other hand, it is important for the government to promote healthy competition in the private sector and to make the private sector exert its creativity.

The government should take gradual steps to improve the quality of PSP system through realizing those general principles when the staff plans, implements and monitors the PSP projects.

6.3.1.5 Basic Requirements for Promoting Private Sector Participation

Generally speaking, whether or not private sector will invest or not will hinge upon the attitude of the government to PSP. In the case of foreign investors, this trend is more predominant. Initially, it is important to establish the most basic requirements for PSP.

In general, the following four basic requirements are necessary ;

(1) Political Stability
(2) Administrative Framework
(3) Legal Framework
(4) Guide Line for PSP

The government is required to establish the firm and stable administrative framework to be responsible for PSP projects. In port development, DGSC and IPCs are regarded as the "Executing Agencies" to directly promote, implement and supervise PSP projects Therefore, DGSC should establish a section or team in charge of PSP in DGSC. Furthermore, it is necessary for DGSC and IPCs to communicate and coordinate closely together as the executing agencies.

On the other hand, adequate and clear legal framework enables the government to give confidence to the private sector and as a result, to attract more investors. In this way, the establishment of a clear and unified legal framework should be required.

Furthermore, the government must formulate more detailed and clear "Guideline for PSP" based on the legal frameworks to give a clear and concrete guidance to IPCs and investors. At the same time, the government should flexibly improve and upgrade the guideline as necessary in order to catch up with the change of circumstances.

6.3.1.6 Roles of Public and Private Sectors regarding PSP

(1) Roles of Government

As mentioned before, the government must play a most important role as a "policy maker", "regulator" and "promoter" for PSP.

On the other hand, it is important for the government to promote PSP projects for investors by issuing & distributing a promotion booklet written in both Indonesian and English versions. DGSC should actively conduct port promotion in cooperation with MOC,

BAPPENAS, IPCs and related organizations.

On the other hand, it is important for the government to protect public interests from the national point of view. In this case, the government should retain final authority to control IPC and the private sector in a moderate and appropriate manner by using the following measures (e.g. supervise through relevant laws and regulations, "Port Master Plan" &approval of MOU and contract between IPC and private sector).

At the same time, excessive and unnecessary intervention by the government does more harm than good for PSP projects.

(2) Roles of IPC

The main roles of IPC are to implement and execute policies and principles of the government as "an executing body", to coordinate and arrange all relevant procedures between public sector and private sector and to implement the project with private sector.

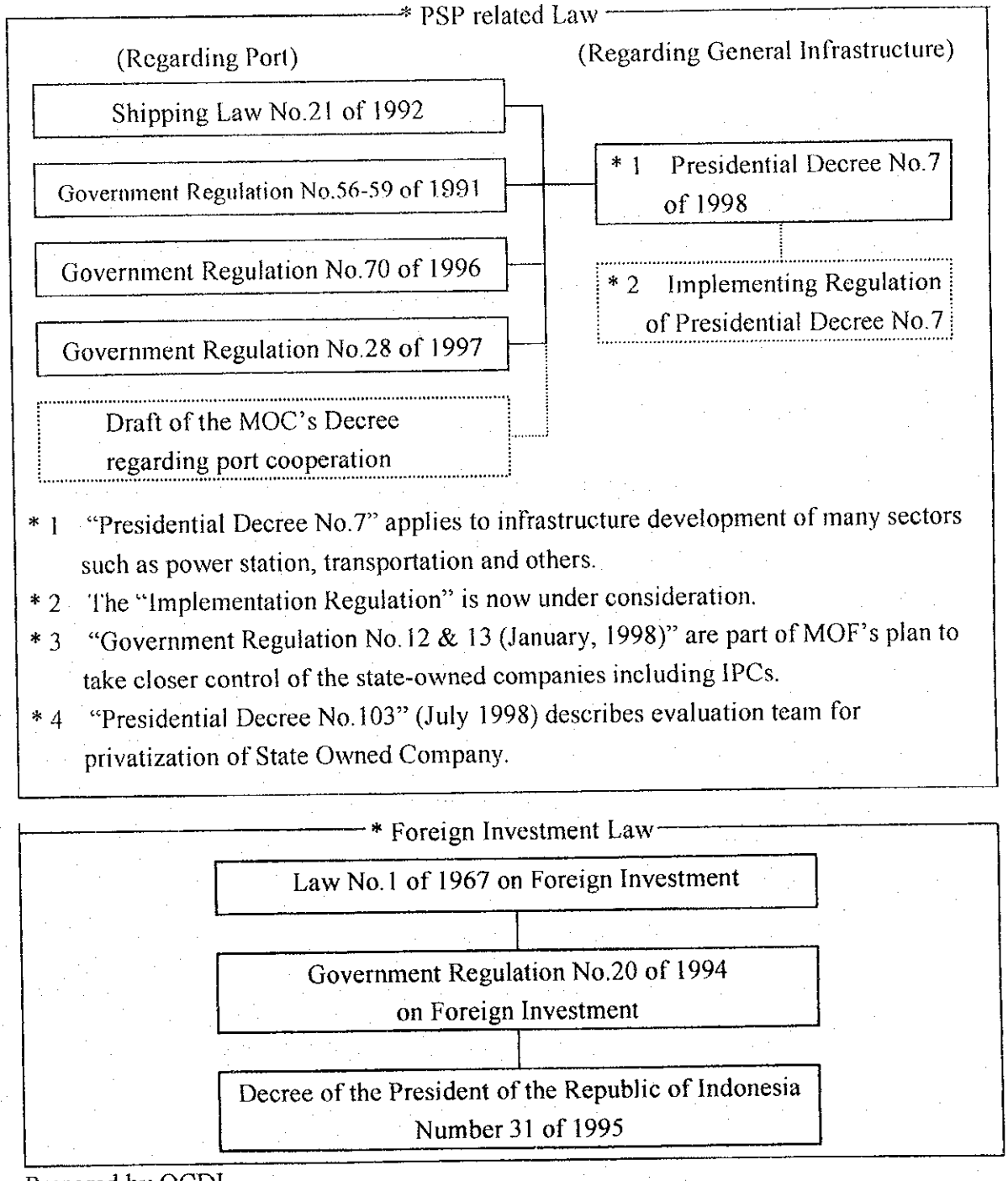
(3) Roles of Private Sector

On the other hand, the main roles of private sector are to undertake project management and finance and to undertake all activities necessary to manage the project from invitation to pre-qualify through bidding, contract, construction and commissioning to the end of the operating period

6.3.2. Review and Reevaluation of the Present Legal Framework

The following Figure 6.3.2.1 represents the current legal framework in Indonesia with respect to PSP and foreign investment.

Figure 6.3.2.1 Current Legal Framework Regarding PSP and Foreign Investment



Prepared by OCDI

6.3.2.1 Recommendation for Existing Legal Framework Regarding PSP

Based on the importance of the legal framework and evaluation of the present situation in Indonesia, the following recommendation can be made.

(1) Presidential Decree No.7

1) "Presidential Decree No.7" is very effective to promote PSP and gain the confidence of investors, however, the most important point is how to endorse the ideals of the Decree.
2) The government should establish more detailed "implementing regulations" to execute the articles of the Decree as soon as possible so as not to confuse or misdirect IPCs and the private sector.
3) The roles of BAPPENAS as a coordinator and evaluator should be further clarified.
4) The monitoring from inside of the government is not sufficient.
5) The details of "Evaluation Team" should be further mentioned.

(2) Total Legal Framework

1) Furthermore, the enforcement of "Draft of the MOC's Decree" will be useful to enhance the transparency for port PSP projects although there are some areas to be improved. However, the actual application will be more crucial.
2) In this sense, the related agencies should enrich their experience through the actual application. It is more important for the government to improve the whole system through the actual application and experiences.
3) In addition, the existing laws and regulations in Indonesia don't mention PSP matters in detail. Inadequate legal framework can't provide clear-cut guidance to government, IPC, private sector and foreign investors. Based on "Presidential Decree No.7", the government should make efforts to arrange the whole legal system and maintain consistency of the whole legal framework.
4) Some subordinate regulations supplement and implement articles of existing laws and regulations. However, the "implementing regulations" on Shipping Law in 1992 or PSP matters also don't exist. The absence of implementing regulations is enough to discourage potential private sector and foreign investors.

(3) Compulsory Requirement of Cooperation with IPC

1) As mentioned in Progress Report II , this compulsory requirement (Shipping Law No.21 & Government Regulation No.70) is one of the main reasons preventing the private sector from taking part in the port development and operation. From the long term perspective, the government should consider reevaluating the articles.
2) This necessity is more stronger for the new port or new terminal projects because it is necessary for the government to create more conductive atmosphere so as to attract the private sector, especially for the project with "marginal financial feasibility".
3) In this case, the private sector has only to pay some concession to the government directly the same with the "mining sector".
4) The government should strive to create an environment in which the private sector can participate in the port services as freely as possible and compete with each other in order to provide more efficient services with lower prices.
5) IPC must regard the private sector not as a "mere tenant" but as an "equal business partner".

6.3.2.2 Recommendation for Existing Legal Framework Regarding Foreign Investment

Based on the evaluation of the present situation in Indonesia, the following recommendation can be made.

(1) Relationship between "Law No.1" (1967) and "Government Regulation NO.20" (1994)

The relationship between both regulations is ambiguous. For example, while the former prohibits foreign investors from taking part in various infrastructure developments including harbor projects (Article 4), the latter allows them (Article 5). It is strange that a mere regulation is superior to law. The government shall make effort to solve the discrepancy.

(2) National Company Requirement

Some economists believe that national company requirement is an unnecessary restrictions. This kind of constraint may discourage participation of private parties. Taking account of the importance of foreign investment and deregulation-oriented trend in the world, " A Straight Investment Company " for port activities should be considered.

(3) Joint Venture Requirement

It is irrational that foreign investors are always required to participate in joint ventures with Indonesian parties. There is a danger that the existing requirement makes Indonesian parties mere "rent chasers". As a result, it will lead to an increased cost of the services for the people in Indonesia.

(4) Minimum Requirement of Local Investor

Compared with the regulations in other Asian countries, minimum requirement of local investor in Indonesia is very lenient. It is desirable for the government to maintain this level. This is because domestic companies can get not only profits from the operation but also know-how and technology through the joint venture operation. However, taking into consideration the importance of foreign investors, participation of "100 % foreign-owned company" for "prioritized" port development projects also should be carefully considered (see Chapter 6.3.6).

6.3.3 Expansion of Working Field of Port Services

6.3.3.1 Port Operation Type

(1) Comparison of Operating port, Tool port & Land-Lord Port Type

Generally speaking, port operation type is classified into three types ("operating port", "tool port" & "land-lord" port type). The three types are compared in Table 6.3.3.1. In container terminal operation in Indonesia, "operating port type" has been employed so far. However, operating port type has the following issues ;

1) Operating port type originally has monopolistic structure, and thus users have no choice.
2) Direct management & operation by port management body tends to result in inefficient operation & bad productivity.
3) Tool port and land-lord port type, which induces the shipping companies into the terminal development and operation will be useful to revive the direct calls and increase the ship calls to Indonesian ports.
4) As the Table shows, major ports in the world already adopt "tool port" or "land-lord port" type.

In Indonesia, it is desirable to shift the port system gradually from "operating port type" to "tool port type" or "land-lord type".

(2) Roles of Central Government, Port Management Body and Private Sector in Terminal Development & Operation

It is important for DGSC to know what kinds of roles each sector in major ports in the world is playing in terminal development & operation.

Especially, examples of major ports on the European mainland (Hamburg, Rotterdam & Antwerp) may be instructive for Indonesia. In those "competitive" ports, the roles of each sector are quite clear (Land-lord port type). The "public sector" (central government) is responsible for unprofitable basic facilities (channel, breakwater & related roads), "port management body" (local government) is responsible for development of infrastructure facilities (wharf & yard) while the "private sector" provides superstructure and operation.

(3) Utilization of Terminals by Shipping Companies

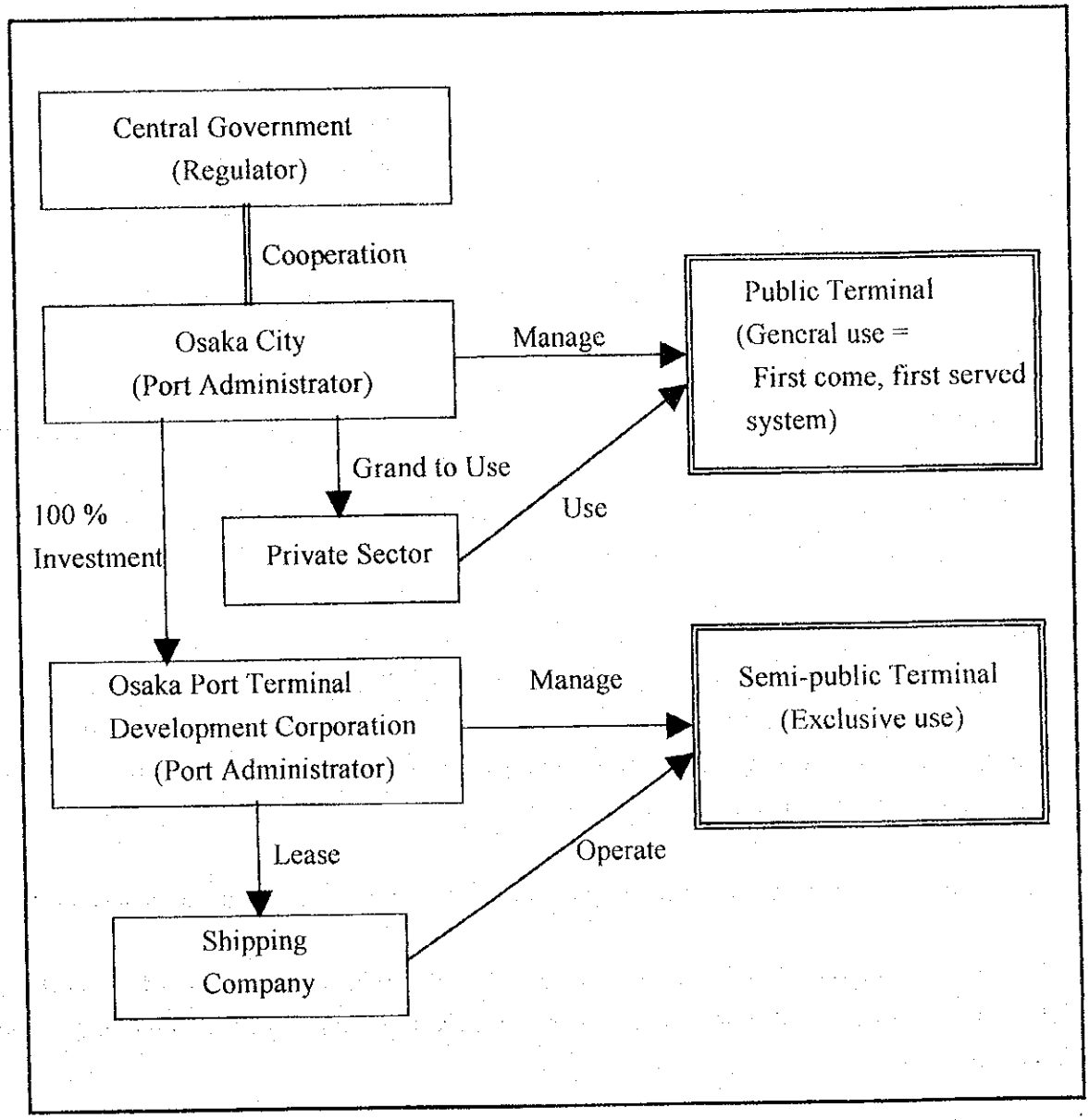
There are three types of terminal utilization (public use, prioritized use & exclusive use). Generally, each type has some merits and demerits, but "exclusive use" is popular among countries at "Trans-Pacific Lines" (Japanese and U.S. major ports). In Japanese major ports, "public use" is used in "public terminals" and "exclusive use" is employed in "semi-public terminals". It is advisable for Indonesian government to use "public use" together with "prioritized use" or "exclusive use".

Table 6.3.3.1 Comparison of "Operating Port", "Tool Port" & "Land-lord Port" Type

Type of Administration		Operating Port Type	Tool Port Type (Land-lord with equipment)	Land-lord Type (Land-lord without equipment)
1. Developer & Operator	Basic facilities	Port Management Body	Port Management Body	Port Management Body
	Supporting facilities	Port Management Body	Port Management Body	Private Sector
	Port Operation	Port Management Body	Private Sector	Private Sector
2. Features of Type		Direct Management & Operation by Port management body	Only operation is open to private	"Lease Type" & "Exclusive Use"
3. Examples of Types		· Indonesia /IPC (Container Terminal) · Singapore (PSA) · Bangkok Port in Thailand (PTA)	· Japanese Public Ports (Kobe & Yokohama) & Port Terminal Development Corporation · Gaoxiong (Chinese Taipei) · Pusan (South Korea) · U.S. Ports (Seattle) · Laem Chabang in Thailand	· European Major Ports (Rotterdam, Hamburg) · U.S. Major Ports (Los Angeles, Long Beach, New York/New Jersey) · Kelang Port in Malaysia
4. Merits		① Direct management & operation	① Efficient & effective Operation by using technology of private sector	① Small investment ② Efficiency and cheaper price through competition
5. Demerits		① Monopoly & no competition ② No other choice for users ③ Inefficient operation & bad productivity	① Difficult control of Productivity	① Exclusive use & discriminatory treatment

6.3.3.2 Comparison between Port of Tg. Priok and Port of Osaka

Figure 6.3.3.1 Relationship between Central & Local Government, Public Corporation and Private Sector in Japan



Prepared by OCDI

(1) Outline of Japanese Port Administration System

1) Characteristics of the System

The central government supervises each port, which is under the direct management of local government, through the establishment of a national port plan, disbursement of

subsidies, and construction. The main responsibilities of port administration in Japan are the development and maintenance of port facilities, including not only projects undertaken at the local level, but also the maintenance and management of facilities put into operation by the central government. In major Japanese ports, generally, almost all port services have been provided by the private sector. In this sense, it can be said port management bodies in Japan are "landlord-type" organizations.

2) Character of "Public Terminal" and "Semi-Public Terminal"

In "Osaka Port", Osaka City manages 6 "Public Terminals" for "general use" (First Come, First Served System). In this case, the City allows the private stevedoring companies to operate the public terminals. The private stevedoring companies make a direct contract with shipping companies for providing stevedoring services. The City must not obstruct or interfere with such private affairs.

In container and conventional terminals operated by "Osaka Port Terminal Development Corporation", the corporation "leases" all conventional terminals as well as container terminals to private companies such as shipping and stevedoring firms ("Exclusive Use"). In semi-public wharves operated by the corporation, almost all port services have been provided by the private sector. Therefore, the style also can be said to be "landlord-type".

3) Outline of Port Operation

As explained, the port authorities in Japan are "landlord" bodies and are not deeply involved in day-to-day operations. Article 13 of the "Ports and Harbors Law" restricts port authorities from intervening with private companies, consistent with the spirit that port services should be provided by the private sector.

(2) Comparison of Port Management & Operation between Indonesian and Japanese Port

Comparison between Port of Tg. Priok and Port of Osaka in Japan regarding working fields among government, port administrator and private sector can be summarized in the Table 6.3.3.2.

1) Regulatory Administrations

Basically, both in Japan and Indonesia, the overall administrations such as navigation safety, immigration and custom must be controlled by the "central government" from the view of national interests.

2) Port Planning

In Japan, in principle, the Port Master Plan is established by local government (port

management body) through the approval of "Central Port Committee" and "Regional Port Committee". In Indonesia, port planning should be established by cooperation between IPC (port management body) and the government.

3) Port Management and Operation

In "public terminals" or "semi-public terminals" in the Port of Osaka, utility, pilot and tug services are provided by private sector. However, only in cases when the private sector can't provide necessary services, the port administrators can offer these services. Therefore, these services also have been provided by the city staff.

On the other hand, in Indonesian ports, most of those services are directly provided by IPC. But, IPC II attempts to introduce capital and technology of the private sector by some way or another.

4) Terminal Operation

As explained before, in Osaka port, the terminal operation at both "public" and "semi-public" terminals have been provided by the private sector.

In Tg. Priok port, PSP in terminal operation has been advanced to some extent. Some terminal services such as stevedoring operation are already provided by IPC or private sector. In 1993, the port began experimenting with agreements in which private stevedoring companies are responsible for all operations within specified areas of the break-bulk sections of the port. In 1998, "joint operation" between IPC and the private sector at CT III has just started. However, different from neighboring major ports in Asian countries, all terminal operations are not yet left to the private sector.

Table 6.3.3.2 Comparison between Port of Tg. Priok and Port of Osaka Regarding the Working Fields

Function		Port of Tg. Priok Indonesia	Port of Osaka Japan
Regulatory administration	Navigation safety	Central Government	Central Government
	Immigration	Central Government	Central Government
	Custom	Central Government	Central Government
	Quarantine	Central Government	Central Government
	Security	Central Government	Central Government
Establishment of Port Master Plan		Central Government / IPC	Local Government / Central Government
Port management / operation	Management body	IPC	Local Government
	Utility supply	IPC	* Public wharf Local Government * Semi-public wharf Private Sector (Management Contract)
	Pilot service	IPC	Private Sector (Management Contract)
	Tug service	IPC / Private Sector	Local Government/ Private Sector (Management Contract)
Terminal operation	Cargo handling at container terminal	IPC	Private sector
	Cargo handling at conventional terminal	IPC / Private sector	Private Sector
	Stevedoring	IPC / Private sector	Private Sector
	Warehouse / shed	IPC / Private sector	Private Sector
	CFS	IPC	Private Sector
	Trucking	*IPC (from wharf to warehouse) *Private sector (from warehouse to factory)	Private Sector

Source : IPC II , City of Osaka

6.3.3.3 Terminal Operations in Major Asian Ports

(1) Laem Chabang Port in Thailand

1) General Explanation

The port is designated as a full-scale seaport for international trade to render services to large container ships and bulk carriers which can't be accommodated at Bangkok port. It consists of 8 terminals, 5 (B1～B5) of which are container terminals. The present situation of terminal operation is shown in the following Table 6.3.3.3

PAT constructed the basic facilities (quay, breakwater, channel basin, land reclamation & so on) at CT B1～B4. Only CT B5 has been developed under the "BOT-based" contract. Since the government has the policy to encourage PSP so as to achieve high efficiency and to be internationally competitive, these container terminals have been privatized.

The operation of all 4 container terminals (B1～B4) is left to the private sector through "lease" or "contract out". All contractors of PAT include international companies. Different from CT B1-4, the construction and operation of CT B5 was left to a tender based on "BOT style" in 1996. LCIT has started part of its operation since December 1997, and it expects full-scale operation in 1998.

2) Particularities of the Terminal Operation in Laem Chabang

① In Bangkok port, in principle, PAT does not leave all operation to private companies through lease or contract out, and directly manages and operates the terminals. Private sector only participates in some operations such as cargo handling service. However, even Bangkok port has now strong pressure for more efficient management and operation.

② However, in Laem Chabang port, the operation of all container terminals is now left to international private sector. In this case, PAT plays only the role of "land-lord". In the port, the concept of the operation is to secure the effective and efficient operation through the competition of "plural terminal operators". Laem Chabang has a very good reputation as an efficient and user-oriented port.

. Table 6.3.3.3 Terminal Operation in Laem Chabang in Thailand

Description	B2	B3	B4
Length	300m	300m	300m
Depth	-15m	-15m	-15m
Contract style	Lease	Contract out	Contract out
Management body	PAT	PAT	PAT
Contractor (Operator)	Evergreen Container Terminal Co., Ltd.	Eastern Sealaem Chabang Co., Ltd (=ESCO) * Consortium of Thai company (51%) & Japanese capital (49%)	Thai International Port Service Co., Ltd (=TIPS) (e.g.) TIPS Co. ltd. & Japanese Shipping Lines
Contract year	1992	1992	1992
Terms of contract	12 years	12 years	12 years
Facilities provided by PAT	Terminal, Gantry crane, Yard, others Transtainer, Trailer	Terminal, Gantry crane, Yard, others	Terminal, Gantry crane, Yard, others
Equipment provided by counterpart	-	Transtainer, Trailer	Transtainer, Trailer
Lease charge	Fixed rent	Share of total terminal income PAT : contractor = 33% : 67%	

Description	B1	B5
Length	300m	450m
Depth	-15m	-15m
Contract style	Lease	Lease BOT base
Management body	PAT	PAT
Contractor (Operator)	Laem Chabang Container Terminal Co., Ltd. (LCB)	Laem Chabang International Terminal Co., Ltd (LCIT) * P&O 49% Thai companies 51%
Contract year	1995	1996
Terms of contract	12 years	30 years
Facilities provided by PAT	Terminal, Gantry crane, Yard, others Transtainer, Trailer	-
Equipment provided by counterpart	-	Construction costs : About US$60 million
Lease charge	Fixed rent	Lease charge for 30 years : About US$40 million

Prepared by OCDI

(2) Manila Port in the Philippines

Major container terminals at MICT (Manila International Container Terminal) have been operated by ICTSI (International Container Terminal Services Inc.) since 1988 based on 25-year lease agreement. On the other hand, The operation of the container terminal at South Harbor has been left to the private sector (ATI = Asian Terminal Inc.).

(3) Keran Port in Malaysia

Terminal operations of almost all terminals (container terminals & non-container terminals) at the North, South & West ports are left to the private sector through "long-term" lease contract (21-year or 30-year lease). As a result of privatization, the jobs of KPA (Keran Port Authority) are limited to "formulating port master plan", "supervising the standard for construction of facilities" and "managing small portions of the properties". To put it shortly, almost all services are provided by the private sector, and KPA (port management body) plays a role of only "land-load".

6.3.3.4 Recommendation

(1) General Concept

It is important for the government and IPC to invite the private sector in port activities by degrees. Generally, private sector involvement in those fields will bring not only efficient & effective works with lower costs for the government but also a higher level of services for users.

At the same time, the government shouldn't neglect the issues brought by PSP. For example, the disorder and uncontrolled private participation often causes excessive competition and therefore lower level of service. The government must make good use of the merits, gradually introducing the know-how & technology of the private sector.

(2) Recommendation

1) The government should promote PSP in port services except for "regulatory administration" and establishment of "Port Master Plan".

2) "Utility supply", "pilot service" and "tug service" should be widely opened to the private sector in order to provide sufficient service with lower fee. These services are relatively

profitable for the private sector, and the services directly provided by IPC tend to be unreasonably costly, inefficient and ineffective. Therefore, it is very important for the government to encourage private sector involvement.

3) PSP in port services such as "terminal operation" should be promoted. The most effective way to make port activities more "market-oriented" is to introduce the private sector to port operation to a considerable extent.

While the government and IPC should take responsibility for the whole management & operation, it is advisable for the public sector to entrust the terminal operation to commercial private sector based on "market principles". As explained before, in major ports in the world including Japanese & neighboring Asian ports, the port management bodies play the role only of "land-lord".

4) Especially, the operation services of existing "container terminals" should be provide by the private companies through lease or management contract. In the near future, the operations of existing "full container terminals" for international vessels should be left to the private sector as shown in the following Table 6.3.3.4. However, the operation of other terminals should be directly provided by IPC for the time being.

Table 6.3.3.4 Existing Full Container Terminals in Indonesia

Port Name	Terminal Name	Length	Recommendable Contract
Belawan	Gobion Berth	500m	Lease or management contract
Tg. Priok	CT I	900m	Lease or management contract
	CT II	510m	Lease or management contract
	CT III	450m	* 2 Joint operation
Tg. Perak	CT II	500m	Lease or management contract
	CT III	500m	* 2 Joint operation
Tg. Emas	Container	345m	Lease or management contract
Panjang	Berth E	300m	Lease or management contract
Ujung Pandang	New Hatta	490m	Lease or management contract

* Note 1 : These terminals and container handling facilities are constructed by IPC.
2 : These terminals are being operated or will be operated by "joint operation".

5) The government should strive to introduce "tool port type" or "land-lord port type" for terminals of "new ports" such as Bojonegera and Batam.

6) The "shipping company" (tenant) and "stevedoring company" (terminal operator) shall play a key role in container terminal operations. In "land lord type" ports, the shipping companies shall be given an opportunity to provide "superstructure" by themselves.

7) In "tool port" or "land-lord" ports, the effective and efficient operation will be promoted through the competition of "plural terminal operators" including IPCs.

8) It is a good idea for the government to encourage the merger of small-capital maritime related companies including shipping, stevedoring and warehouse companies so that those companies will be able to provide higher quality of services with lower prices for users.

6.3.4 Review of Possible Forms for Port Development and Operation

6.3.4.1 Scope of Works of PSP

(1) Present Situation of PSP Port Development Projects by Type

So far, progress has not been very rapid in introducing PSP into the port development. The few projects underway are mainly "joint venture type" agreements with IPC (Joint Operation) providing the infrastructure and the private sector providing equipment. Although DGSC wants to employ more "BOT-type", there are not so many BOT projects at present.

Furthermore, in general, the private sector is interested only in profitable port projects such as development and operation of container & bulk terminals. The government and IPC should patiently and carefully consider how to induce the private sector in port projects by some way or another.

The scope of works which should be done by private sector is now summarized in a booklet titled "INVESTMENT OPPORTUNITIES IN INDONESIAN PUBLIC PORTS" issued by DGSC on August 25, 1994. There are no well-established rules for deciding which projects should be implemented by PSP. It is important for the government and IPC to establish a clear mechanism for identifying and selecting PSP projects.

(2) Recommendation

1) Operation of (Existing or New) Container, Conventional & Bulk Terminal
As explained in Chapter 6.3.3, the introduction of "lease" or "management contract" should be considered for the operation of container, conventional & bulk terminals.

2) Ship's Service, Water Supply and Electric Supply
The introduction of PSP through "management contract" in the field of port services such as "pilotage", "towage", "utility" and other port services makes it possible for the

government to provide the services to users at lower costs.

3) Handling Equipment and Waste Collection

In those fields, the employment of "contract out" agreements should be considered. Compared with the services directly provided by IPC, the services provided by the private sector will be cheaper for users.

4) Reclamation

In case of reclamation project, "BT" (Built and transfer) type also should be introduced.

The new scope of works by the private sector is envisioned in the following Table 6.3.4.1.

Table 6.3.4.1 New Scope of Works by Private Sector in Indonesian Ports

No	Business Segment	Description	Possible Forms
1	Container Terminal ① Wharf ② Yard ③ CFS ④ Equipment	Development & Operation	JO / BOT
		Operation	Lease / Contract Out
2	Conventional Terminal ① Wharf ② Yard ③ Equipment	Development & Operation	JO / BOT
		Operation	Lease / Contract Out
3	Bulk Terminal ① Wharf ② Storage ③ Equipment	Development & Operation	JO / BOT
		Operation	Lease / Contract Out
4	Passenger Terminal ① Wharf ② Terminal ③ Supporting Facilities	Development & Operation	JO / BOT
5	Ship's Service	Pilotage & Towage Operation	Contract Out
6	Water Supply	Development & Operation	JO / BOT
		Operation	Contract Out
7	Electricity Supply	Development & Operation	JO / BOT
		Operation	Contract Out
8	Handling Equipment	Procurement & Maintenance of Equipment	JO / Contract Out
9	Waste Collection	Development and Operation	JO
		Operation	Contract Out
10	Reclamation	Development and Operation of Reclamation	land lease, Profit Sharing or BT (Built & Transfer)
11	Port Services	Procurement and Operation of Information System	JO
12	Port Training	Training Program	JO

6.3.4.2 Review of Possible Forms for Development Projects

(1) Risks of BOT Projects

In BOT projects, only private sector must take a risk from funding for development to recovery of the investment. The risks regarding BOT projects from the view point of the private sector are summarized in the following Table 6.3.4.2.

Table 6.3.4.2 Risks of BOT Projects

Imaginable Risks	Contents of Risks
1. Funding	① Private sector must take all risks from funding to recovery of the investment. ② Investors tend to be involved themselves in non-profitable infrastructure developments (e.g. channel dredging & land acquisition) ③ Construction costs tend to increase.
2. Financial risks	Long-term period of payment often brings financial risks. (e.g. foreign exchange risk & inflation)
3. Tariff	① Tariff system exclusively & uniformly regulated by the government discourage PSP. ② The private sector has no discretion to amend the tariff in line with inflation rates.
4. Cargo volume	There is always a danger that "cargo volume" will be less than that projected.

Prepared by OCDI

(2) Establishment of Risk-Allocation Policy

BOT projects sometimes cause risks only to investors. In this case, all kinds of risks should be allocated, avoided or minimized as much as possible by the government so that private sector will participate in them more easily.

In order to eliminate or minimize the market risks, it is necessary to balance the risks between public and private sector. Especially, various kinds of government support are thought to be essential for large-scale projects based on BOT. The appropriate measures should be considered carefully by the related government agencies (DGSC, MOC, BAPPENAS, MOF & so on) & IPC to avoid risks incurred to BOT participants.

(3) Recommendation

Taking the above matters into consideration, the following recommendations can be made.

1) The government and IPC should promote BOT and JO schemes for large-scale port development projects such as development of container, conventional & bulk terminals.
2) The scheme should be judged on "a case by case basis".
3) In BOT based projects, appropriate "risk allocation policy" & "incentive measures" shall be considered carefully as "a national priority" among related government agencies.
4) In this case, the decree and type of the government support should be determined pragmatically and realistically on a case-by-case basis.
5) The preference of risk allocation policy shall be considered among the related organizations as seen in the Table 6.3.4.3

Table 6.3.4.3 Preference of Risk Allocation Policy for BOT Projects

Item	Preference	Risk Allocation Policy
1. Funding & Financial Risks	◎	Government's borrowing on behalf of developer (eg. a long-term "soft loan" on "bond")
	◎	Allowing of issue of government "guaranteed bonds"
	○	Allowing of issue of bonds with "tax credit"
2. Tariff	◎	Deregulation to tariff determination
	◎	Allowing "different" tariff rates & tariff based on "Cost Accounting"
	○	Allowing tariff rate in line with "Inflation" (Accurate charge adjustment mechanism)
3. Cargo Volume	△	Introduction of "A Guaranteed Rate of Return System"
4. Incentive for Private Sector	◎	Offer of "special tax concession" for "prioritized" BOT projects ① Reduced "corporate tax" ② A reduced rate of "withholding tax" on dividends ③ Accelerated depreciation & amortization ④ Extension of "loss carry period" for up to 10 years
5. Others	◎	Government's full responsibility for related infrastructure development
	△	Offer of "offsetting measures" (other profitable concessions)
	×	Government's guarantee for monetary compensation

Note : ◎ Most preferable ○ Preferable △ Consideration × Difficult to adopt

6.3.5 Establishment of Transparent Selection Procedure for PSP

6.3.5.1 Establishment of Selection Criteria of PSP Applicants

Recommendation

Taking account of the review, DGSC is required to clarify the selection criteria. It is desirable that the government should establish firm and concrete selection criteria in the "Guideline" based on the "Presidential Decree No.7". For arbitrary use of the selection criteria is sure to create distrust among the investors. In this case, the following criteria should also be considered.

1) The private sector should have enough funds, know-how, equipment and human resources to perform the port projects properly. These abilities should be evaluated from financial and technical aspects.
2) Private sector is not always required to have general experience in the sector and past performance on similar projects. However, such experience should be highly evaluated.
3) At the same time, other programs such as improvement program, management & operation system, maintenance program also should be evaluated.
4) Furthermore, the quality of service which will be provided should be evaluated.
5) The private sector must meet the legal requirements.

6.3.5.2 Introduction of Competitive Bidding System in Selection Procedure

(1) Issues of the Present Selection Procedure

As explained in the Progress Report, there are presently two kinds of procedures in PSP projects in Indonesian ports as follows ;

① Initiative comes from IPC
② Initiative comes from private sector (unsolicited proposal)

However, based on PSP projects in the past, the following observations can be made.

1) Almost all projects are unsolicited even though DGSC has a list of port projects for PSP.
2) These projects tend to be promoted behind the scenes and without notice of other investors.
3) In this case, the investment often leads to monopolization of capital, contrary to the true purpose of PSP. The monopolization causes inefficiency and increases operation

cost.

4) As a result, private sector can't provide high quality services at low prices to users.

5) On the other hand, it takes a lot of time to obtain approval from the related government agencies including MOF. "Delay of approval" often distracts the attention of the private sector.

(2) Reasons to Introduce "Competitive" Bidding System

Therefore, it is very important for the government to introduce a more competitive and open selection process. The reasons can be summarized as follows ;

1) Allowing the participation of many investors makes it possible for the government or IPC to select the most efficient, cost-effective bidders.

2) The bidding process can encourage competition among bidders. As a result, the users can be provided with more efficient services at lower prices.

3) Transparent and fair bidding system encourages foreign investors to take part in port development projects.

4) Competitive bidding system is taken as a matter of course in the projects of major ports in neighboring countries. For example, in bidding of "Kelan container terminal" in 1987, the Malaysian government showed its enthusiasm for the participation of foreign investors although the government recently has not encouraged PSP by foreign investors.

5) In "Thailand", international competitive bidding is now required for all large projects. Furthermore, in "the Philippines", attracting foreign investments is a priority program of the government, and therefore, in principle, competitive bidding must be adopted.

(3) Recommendation

1) Introduction of "Competitive" Bidding System

The most important thing in the selection process of private sector is to choose the lowest and most effective bidder through healthy and fair competition. In this sense, "Presidential Decree No.7 of 1998" will provide good guidance to the government and private sector.

Therefore, the following matters can be recommended ;

① The government should promote a competitive selection process.

② In this case, the government should pay more careful attention to secure fairness and neutrality of the selecting and enhance transparency of the whole process.

③ This principle is also applied to "unsolicited" proposals.

④ The examples of toll-road projects in Indonesia and in the Philippines provides a good reference for DGSC.

⑤ In order to attract potential private sector, the government and IPC need to make every effort to solicit interest and obtain competitive PSP tenders.

2) A Fast-Track Procedure for Small-Scale PSP Projects

The government should consider a fast-track procedure for small-scale projects in order to avoid time-consuming and bureaucratic procedures. Presidential decree has already introduced the procedure, but the system should be further improved.

3) Importance of Disclosure of PSP-Related Information

MOC and DGSC should make every effort to open the PSP-related information to the public as much as possible in order to upgrade the quality of PSP system and protect the interests of the public. Such efforts are sure to bear fruit in the future.

4) Necessity of Appropriate Involvement by DGSC

In bidding process, IPC has two aspects, i.e. "commercial corporation" and "neutral & public agency". It is difficult for IPC to be compatible with both aspects. DGSC is strongly required to instruct and supervise IPC and private sector from public view through the approval of MOU and contract in order to promote fair and healthy competition.

6.3.5.3 Foundation of "Internal Monitoring Committee" (The Third Party Neutral Organization)

Recommendation

Taking the mentioned matters into consideration, the following can be recommended ;

1) The monitoring from inside of the government (BAPPENAS) is not sufficient.
2) MOC (or DGSC) should establish the appropriate monitoring committee in MOC (or DGSC) whose members are possibly limited to persons of learning and experience, business people and other specialists in order to maintain neutrality and fairness.
3) The main purposes of the Committee " are to enhance transparency of the whole system and ensure confidence from investors by introducing ideas and opinions from experts and to evaluate and assess the whole PSP system through eyes of the third party
4) The monitoring committee should be given appropriate authority to monitor and improve the whole PSP system.
5) The major roles of the Committee are to assess, monitor and review the overall procedures including scope of working fields, selection criteria, selection procedure and implementation, to hear the opinions and views from users, and domestic & foreign investors and to give advice and recommendation to the Minister of Communication and

related agencies including DGSC, BAPPENAS & state-owned companies

6) Every year or every certain period, the monitoring committee should submit the recommendations to the related organizations and prepare the PSP related information for the public.
7) The government and the related State-owned Corporations should have the duty to respect the recommendations submitted by the committee.
8) In the future, it is more advisable for the government to have a "fully independent" – monitoring system.
9) In the future, separation of "regulatory" and "monitoring" organizations will become more important in Indonesia. While the former (executing agency) shall be responsible for day-to-day PSP affairs, the latter (monitoring organizations) should be for "ex post facto" check.

6.3.6 Incentives Through Deregulation

(1) Importance of Deregulation and Foreign Investment

Generally speaking, it is important to give appropriate incentive to domestic and foreign investors through promoting deregulation in order to attract more investment. The more regulations the government dismantles, the more investment the government can obtain.

On the other hand, owing to lack of domestic capital and current monetary problem in Indonesia, foreign investment for large-scale projects will be inevitable. Foreign experience of PSP management, operational & financial skills will be crucial to the quality and quick implementation of port development projects.

Thus, the government should arrange the "well-organized & trustworthy institutional frameworks", prepare "well-developed basic infrastructure" and provide "certain incentive package" to attract more foreign capital. In order to do so, "an appropriate tax incentive system" for foreign investment and prioritized BOT projects shall be carefully elaborated. Simplification of "licensing procedure" for foreign investors also should be promoted.

Furthermore, it is necessary for the government to be able to flexibly cope with any changes in the situation. Making reference to examples in other countries, the government should establish appropriate deregulatory and incentive measures.

(2) Recommendation

Based on the understanding of the importance of deregulation and foreign investment, the following deregulatory and incentive measures shall be carefully considered.

1) Deregulation to Tariff Review Process (see Chapter 6.2.1).
2) Expansion of Working Field of Port Services (see Chapter 6.3.3).
3) Participation of "100% Foreign-Owned Company" in "Prioritized" Port Development Projects (see Chapter 6.3.2.3).
4) Promotion of Participation of Foreign Capital in Port-Related Business such as "Freight Forwarding"
5) Tax Incentive System for "Foreign Investors" & " Prioritized BOT Projects"
   ① Tax Incentive System for "Prioritized Projects" by "Foreign Investors"
   ② Tax Incentive System for " Prioritized BOT Projects"
6) Simplification of Licensing Procedures for Foreign Investors
   ① Promotion of "One Window Shop System"
   ② Simplification of License Procedure
   ③ Reduction of Number and Volume of Related Documents