

LEGAL ASPECTS AND POLICIES FOR INDONESIAN SMEs AFTER THE OMNIBUS LAW-CHALLENGES IN THE REGIONAL FREE TRADE

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ABSTRACT

As an active developing country, the Republic of Indonesia plays a mammoth role in regional economic cooperation, inter alia, bilateral Free Trade Agreement, Free Trade under the ASEAN Economic Community (AEC), and even in the Regional Comprehensive Economic Partnership (RCEP). After enacting the omnibus law in 2007, the country has highlighted the protection and enhancement of the Small and Medium Enterprises (SMEs) environment. Nonetheless, the weak performance of SMEs and myriad FTAs in the country relatively generate confusing challenges. Hence, the purpose of the study is to analyse the Challenges of legal policies for SMEs to evoke a clear understanding for incoming improvement. Regarding the expected result of this study, the research was based empirically on analysis of primary and secondary data with considering surveys reported by some authors. Based on the finds, this paper examines holistically the treatment of SMEs under domestic regulations related to SMEs` regulations under regional FTAs, and further to Challenges of SMEs in Indonesia in the regional Free Trade despite the enactment of the Omnibus law and other legal aspects. Expressly the research found the challenges are arisen due to volatility of domestic system and regional (international) issues.

Keywords: Legal Aspects, Indonesia, Challenges, SMEs, Investment policies, and FTA

A. Introduction

In most developing countries, SMEs contribute the economic growth prosperously. In Indonesia, the arrangement of SMEs is specified in certain regulations¹, to encourage

economic implication by creating of employment, alleviating poverty, and enhancing its agile competitiveness against corporate and regional enterprises². The SMEs have been

1 Based on the 1945 Constitution of the Republic of Indonesia, (article 33) it is necessary to make sustainable national economic development. Underlined by Decree of the People's Consultative Assembly of the Republic of Indonesia Number XVI/MPR1998 concerning the economic policy in the context of economic democracy, investment policies should at all times underlay the people's economy that commits itself to the enhancement of micro, small and medium enterprises, and cooperatives.

2 Stated by the Ministry of Trade of Indonesia[2020] that majority of economy is almost occupied by SMEs

underlined distinctly after the enactment of Omnibus law and other legal aspects. The Law on SMEs of 2008 defines it as an enterprise domiciled and conducts business in Indonesia and meets the criteria as follows: having a net asset of more than five hundred Million Rupiah up to ten billion Rupiah, and having maximum annual sales proceeds of more than two billion and five hundred million Rupiah up to a maximum amount of fifty billion Rupiah. On the other hand, the Government of Indonesia has been enlarged its FTAs in order to promote in the regional market its SMEs` capacities³. However, despite legal aspects for enhancing SMEs in Indonesia, it still faces challenges because the domestic policy is not much agile, and as well the expansion of Regional FTAs may hamper relatively the SMEs` environments because of unbalanced competition, the regional SMEs or goods may flood

the market especially the developed countries⁴.

The research places its significance in highlighting the challenges faced by SMEs in Indonesia through domestic legal issues and external issues generated by regional FTAs. Meanwhile, the study set to consider the possible improvement of SMEs to face regional FTA. Consequently, it becomes problematic to grasp the domestic legal policies, and Regional economic policies are not realistic and conducive to SMEs despite their provisions to protect and enhance SMEs in Indonesia. Henceforth, how do legal policies, inter alia, omnibus law, the law on SMEs, and regulation on special treatment of SMEs and other aspects, function to expand the interest of SMEs in Indonesia? Do the rules for protecting SMEs under the Regional FTAs lay down convergent with omnibus law? Moreover, what are the reasons that

about 90% of total business and 97% of employment, "Ditandatangani di Tengah masa Pandemic Covid-19, RCEP Tumbuhkan Harapan Baru di Kawasan," [signed in the middle of the COVID-19 pandemic, RCEP brings a new hope], Press Release, 15 November, <https://www.kemendag.go.id/id/newsroom/press-release/ditangani-di-tengah-masa-pandemi-covid-19-rcep-tumbuhkan-harapan-buru-dikawasan-1>

3 Indonesia is a party to the region-wide Association of Southeast Asian Nations (ASEAN) Free Trade Area. ASEAN, and by extension, it also has preferential trade agreements with Australia, China, Hong Kong India, Japan, Korea, and New Zealand and concluded text-based negotiations of the Regional Comprehensive Economic Partnership in November 2019. Indonesia has signed bilateral free trade agreements (FTAs) with Australia, Chile, Mozambique, as well as with Iceland, Liechtenstein, Norway, and Switzerland under the European Free Trade Association, but as of the end of 2019, none of these FTAs are yet in force except with Chile. Indonesia recently concluded negotiations with Korea on a Comprehensive Economic Partnership Agreement. Indonesia is negotiating other FTAs with the European Union (EU), India, Tunisia, and Turkey as well as reviewing its trade agreements with Japan and Pakistan. Available at trade- <https://www.trade.gov/knowledge-product/indonesia-agreement>

4 The SMEs may not able to compete or participate in regional markets dominated by large enterprises. This is the main reason why India withdrew its assumption for signing the entry into in force of RCEP agreement in December 2020, but does not mean regional FTA agreement is thoroughly impact negatively the SMEs, the policy of Developing country has to rigorously set forth the protection of SMEs interest and its economic implication into state economic growth by partnership with MNE, or restriction of some sectors targeted only to SMEs.

factually challenge the SMEs and what remedial steps the government might have to take?

The first part of this study highlighted the legal policies for SMEs in Indonesia under the domestic rules and with regional FTA rules stipulating the treatment of SMEs to which the country has to commit. The following part focused mainly on the Challenges of SMEs in Indonesia in facing Regional FTAs rules impact. The rules addressing the treatment of SMEs in FTA looks a bit unrealistic in terms of protecting the interest of SMEs because they cannot be a subject of intense competition with corporate enterprises internationally, and low rate of trade liberalization is systematically booming products from developed countries in large scale to developing country into Indonesia's Market. At the very least, the research talks about the possible amelioration of SMEs legal policies to render conducive Regional Free Trade implications to Indonesia.

B. Research Method

In general, the method used in this research focused basically on doctrinal methodology by analysing, commenting, and interpreting qualitatively laws relating to investment law in Indonesia, such as omnibus law and other rules related to SMEs and the regional Free Trade Agreements. In order to understand the Challenges of SMEs in the Regional Free Trade deeply, the present study

lays down on the collection of all relevant primary and secondary data and analysing pragmatically for the objective of attaining the main point of the research. In detail, the analysis took into consideration all previous empirical researches, surveys guided by previous author and all statements posted by the Minister of Commerce in Indonesia on its official website, the statements on the official website of the regional FTAs, among other things, AEC website, RCEP website and others. Furtherly, the study also examined all interviews directed by some searchers online.

Adversely this research proffers its weakness by lack of direct interviews to SMEs in Indonesia in facing the expansion of regional Free Trade, the practical implementation of legal aspects for SMEs, and other possible challenges that may appear in the future which will be generated by mega FTA such as the future impact of RCEP FTA. In doing so, the author genuinely intended to complete the research more pragmatically, yet the circumstances paralyzed it.

C. Discussion

After enacting Omnibus law with other rules and regulations set out the SMEs and ASEAN Economic Community policy, which means the year 2007 to 2021, several academic researchers have been conducted to point out challenges of Indonesian SMEs' legal policies in encountering Regional Free Trade.

However, those cited hereinafter are relevant for this study. The role of small and medium-sized enterprises (SMEs) related to private sector engagement is often neglected by policymakers. But SMEs are mostly the main driver of local socioeconomic welfare in Indonesia (Neise Thomas, Diez, Javier Reveilla, 2018). Iwan Koerniawan (Iwan Koerniawan, 2020) states in his study on understanding SME in Indonesia the policy issues had brought multi-dimensional emergency of SMEs in Indonesia;⁵ Irfan Ridwan Maksum (Irfan Ridwan Maksum, 2020) found that expansion of the global economy increases negative factors for SMEs.⁶ Moreover, Raden (Aswin Rahadi, 2016) advanced in his study that the challenges of SMEs are because of lower performance to enable in the regional market; Arias Kurniawan (2019) found the challenges through weak courage of SMEs to enhance the quality of its enterprise to reach regional standards company. In order to enhance and extend the economic contribution of SMEs in Indonesia, it is needed to improve social security and business performance (Nina TORM, 2020), but Sembiring (Meliadi Sembiring, 2008) stated that

the weakness of Indonesian SMEs in technology, human resource quality, productivity competence of information communication, and performance of the company and business climate obstacle its competitiveness in the regional market.⁷ Actually, SMEs do not contribute to the export activity due to SMEs' lack of global competitiveness to compete in the regional market. Furtherly examined that the main challenge is, SMEs in Indonesia has no proper legal protection in facing AEC trade liberalization and has advantages under the Omnibus law and other legal aspects by restricting regional business in accessing to some sectors, most of the sectors are open to SMEs only rather other types of enterprises (Peach, Melissa 2013). Due to systematic changes they were expected to get the opportunity to enter the market better than larger companies, but the concept of competitiveness is not well enforced (Anton, Setyawan Agus Muzakan, Isa Muhammad, Wajdi Farid, 2015).⁸ The implication of regional FTA impacts the growth of SMEs due to higher competition and the market mostly flooded by the regional goods (Thomas Neise, 2018).⁹ There are many

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- 5 Koerniawan, I Samiha, Y T Fatimah, C E A Terminanto, A A Irviani, R, "Understanding micro small medium enterprise in Indonesia." *European Journal of Molecular & Clinical Medicine*, ISSN 2515-8260, Volume 07, Issue 02, 2020
 - 6 Maksum, Irfan Ridwan Yayuk, Amy Rahayu, Sri Kusumawardhani, Dhian, "A Social Enterprise Approach to Empowering Micro, Small and Medium Enterprises (SMEs) in Indonesia." *Journal of open innovation: Technology, Market, and Complexity*, published in 20 July 2020
 - 7 Anton, Setyawan Agus Muzakan, Isa Muhammad, Wajdi Farid <https://www.cjournal.cz/files/190.pdf>
 - 8 Anton, Setyawan Agus Muzakan, Isa Muhammad, Wajdi Farid, "An Assessment of SME Competitiveness in Indonesia." *vol.7,2*, 2015, p.60-74
 - 9 Thomas Neise, "Firms' adaptation strategies to floods and their potential on regional economic-Insights

constraints endowing to SMEs, such as lack of capital, lack of sponsor from the government, cumbersome business regulation, restrictions, and poor governance, weaken the accession to inter-regional market (Talus Tambunan, 2009). Lastly, Burger (2015) in his study axed on reforming policies for Small Medium-Sized Enterprises in Indonesia examines the importance of reform for SMEs policies in Indonesia in broadening strategies to promote economic growth. And additionally, he added a recommendation for policymakers assisting capacity of productivity, facilitating the expansion of their business, and eliminating notably overlaps between government's offices responsible for supporting SMEs may not be feasible.¹⁰ The study of Rothenberg, Alexander D Gaduh, Arya Burger, Nicholas E (2016) shows up the incapability of SMEs accessing to an international market is due to their informality, they cannot reach the international standards required to be regional traders and investors, and consequently it remarkably suggested the formalization of SMEs.¹¹

1. Treatment of SMEs in Indonesia

Threaten of SMEs is governed by two dependents regulations which are domestic and regionals. Indonesia has its myriad national legal framework for treating and protecting its domestic investment activities, at the same it has also its inter-regional commitments relating to standards of treatment and protection of trade and investment operations from its regional partners. Thereafter, the treatment and protection of SMEs at the national level and regional will be discussed.

1.1. Domestic legal policies for SMEs in Indonesia

Despite the fact that Indonesia has signed myriad Regional Free Trade Agreements with vast trade liberalization mechanisms, the treatment of SMEs is remaining restricted areas in order to provide for special treatment of SMEs, with the objective of maintaining persistence of sustainable viability of SMEs for economic growth, among other things, creation of long-term employment and economic growth to peoples of Indonesia. As a result, some sectors remain reserved

from Jakarta and Semarang, Indonesia" Published in 2018 retrieved at <https://www.semanticscholar.org/paper/Reforming-Policies-for-Small-and-Medium-Sized-in-Burger-Chazali/998b70baba5d75ea1dafb7a93e32b32959109ad1>

- 10 Burger, Nicholas Chazali, Charina Gaduh, Arya Rothenber, Alexander D Tjandraningsih, Indrasari Weilant, Sarah, "Reforming policies for small and medium-sized enterprises in Indonesia." RAND Corporation in collaboration with Tim Nasional Percepatan Penanggulangan Kemiskinan (TNP2K), retrieved at 2015, P.136 s/Reforming SMEs_0529_lowres_2015-1.pdf
- 11 Rothenberg, Alexander D Gaduh, Arya Burger, Nicholas E, "Rethinking Indonesia's Informal Sector" World Development Vol. 80, pp. 96-113, 2016 0305-750X/ 2015 The Authors. Published by Elsevier Ltd. This is an open access article under the CC BY license (<http://creativecommons.org/licenses/by/4.0/>).

for small-scale enterprises, and their coverage has been widened (covering 19 activities in the chicken, fishery, forestry, mining, industrial, trading, transportation, telecommunications, and health industries). Large-scale domestic or foreign investors are allowed only in partnership with a small local business or cooperative (tubers-related agricultural businesses, particular fish cultivation, forestry).¹²

Firstly, looking at the legal evolution of investment regulations in Indonesia, before the omnibus law there were several laws introduced and replaced subsequently, such as Law Number 1 of 1967 concerning Foreign Investments marked with limited provisions of foreign investment regulations,¹³ it was amended by Law Number 11 of 1970 concerning Amendments and Supplement to Law Number 1 of 1967 concerning Foreign Investments,¹⁴ and Law Number 6 of 1968 concerning Domestic Investments, as amended by Law Number 12 of 1970 concerning Amendments and Supplement to Law Number 6 of 1968 concerning Domestic Investments need a replacement for no longer being consistent with the need of accelerated national economic enhancement and law development, most notably, in the field of investment. Those previous laws

are mostly marked by a lack of legal protection of SMEs and contained a limited understanding of SMEs' economic contribution to State development.

Due to a lack of awareness of the previous regulations on SMEs, therefore, the government of Indonesia enacted Omnibus Law for the reason of improving the provisions of previous regulations in strengthening the legal protection of the SMEs. In the light of its provisions article 13: "The Government must establish business sectors that are reserved for micro, small and medium enterprises, and cooperatives, as well as business sectors that are open to large businesses on condition that they cooperate with micro, small and medium enterprises, and cooperatives." Meanwhile, the SMEs are granted to be treated by the Government profitably as the country's economy relies on its contribution.¹⁵ By this provision, the Government has to settle agile policy to promote the participation of SMEs in a business environment in the country by the measures of protecting them of domination of market may be generated by the corporate enterprises. The Government shall guide and enhance micro, small and medium enterprises, and cooperatives through partnership programs, increase competitiveness, inducement of innovation and market

12 Presidential Decree No. 99/98 on small-scale enterprises as amended by Presidential Decree No. 127/2001 (published on 14 December 2001).

13 [http://www.flevin.com/id/lgsso/translations/Laws/Law/Foreign%20Investment%20\(BI\).pdf](http://www.flevin.com/id/lgsso/translations/Laws/Law/Foreign%20Investment%20(BI).pdf)

14 <http://www.flevin.com/id/lgsso/translations/Laws/pdf>

15 See article 13 section 1 of Law of the Republic of Indonesia Number 25 of 2007 concerning Investments, signed by the President on April 26, 2007

expansion, and wide dissemination of information¹⁶. Expressly article 4 previews: “The Government shall adopt major investment policies: to encourage the creation of a conducive national business climate for investments in order to strengthen the competitiveness of the national economy; and to expedite the increase of investments”,¹⁷ This provision is elucidated in same article © says: “Government shall give opportunities to the enhancement of and give protection to micro, small and medium enterprises, and cooperatives”. It implicates that the Government has a legal obligation to push up SMEs partnership programs, an increase of competitiveness, market expansion, and wide dissemination of information Enlarge cooperation of Large Enterprises with SMEs by limiting their advantages in order to promote SMEs and promote small enterprises to enlarge in the business environment and international business. Accordingly the mandate of Decree of the People’s Consultative Assembly of the Republic of Indonesia Number XVI/MPR-RI/1998 regarding Economic Policy in the Context of Economic Democracy; Micro, Small, and Medium Enterprises need to be empowered as an integral part of the

people’s economy that has a strategic status, role, and potential to materialize the national economic structure that has increasingly become more balanced, developed, and equitable.

Secondly, by the omnibus law, the Government has implemented a business sectors policy in which treatment of SMEs is extended mainly to prevent risks induced by corporate enterprises in the market or business sectors. Accordingly, considering enhancing investment activities both from domestic and foreign countries and accelerating development, it is essential to protect the SMEs by establishing business field Open with conditions means particular business field subject to investment activities¹⁸. The objective of the regulation is highlighted to improve the economic competitiveness in facing the ASEAN Economic Community era and incentives of the global economy. Besides, the regulation of investment sectors targets SMEs’ advantages and sets aside business reserved for AEC¹⁹, either conducted by a domestic investor or foreign investors within the territory of the Republic of Indonesia²⁰. The details of the policy governing the determination of SMEs scrupulously is evoked by the Law of the Republic of Indonesia Number

16 See Ibid. section 2

17 See Ibid. article 4

18 Stated by Presidential regulation of the Republic of Indonesia Number 44 of 2016 concerning list of business fields that are closed to investment and business fields open with conditions to Investment, meanwhile, stipulated by Article 2(2)(a) of said regulation, a business which consists of reserving for SMEs

19 Ibid article 2(2)(B)(5), the business field Open with condition consists of limited capital ownership in the context of the Association Southeast Asian Nations cooperation

20 See, *ibid* first Chapter article 1.4

20 the year 2008 regarding micro, small, and medium enterprises in the objectives of empowering SMEs²¹. Article 1(9) of this law previews: Business Climate shall be condition striven for by the Government and Regional Governments in order to empower Micro, Small, and Medium Enterprises in a synergized manner through the stipulation of various laws and regulations as well as policies in various aspects of the life of economy so that Micro, Small, and Medium Enterprises obtain favoring, certainty, opportunity, protection, and support for running a business as broad as possible". In elucidating, SMEs need special treatment and protection in order to conduct a comprehensive, sustainable, and conducive climate of business. As a result, the law on SMEs in Indonesia welcomes the regional SMEs or Investors to conduct their investment under the sectors determined by the law, for example, AEC but has to comply with specific rules, which means that there are business sectors that are not allowed to be subject on FTA with Corporate enterprises. Concerning the business sector protection, this regulation is due to the implementation of Article 12 paragraph (4) and Article 13 paragraph (1) of Law Number 25 of 2007 concerning Investment, the President has issued Presidential Regulation

Number 39 of 2014 concerning Lists of Business fields that Are Closed to Investment and Business fields that Are open with conditions to Investment. The Omnibus Law mostly updates and prioritizes the SMEs in facing regional market. Consequently, Law Number 44 of 2016 set out that the amendment of the provisions on lists of business fields that are closed to investment and business fields that are open with conditions to investment is the pathway to accelerate development while remaining improving protection on Micro, Small, and Medium-scale Enterprises and Cooperatives and various national strategic sectors, and to improve the economic competitiveness in facing the ASEAN Economic Community (AEC) era and the dynamics of the global economy from home to overseas. In view of article 2 of this law stipulates the types of business fields open, closed, and open with conditions.²²

Knowingly all Free Trade Agreement signed by developing countries has almost to set aside the treatment of SMEs since their economic growth relies on a good environment of it, inter alia, all FTA agreed by Indonesia highlights the SMEs as an integral part of the agreement in order to prevent possible domination of the market by MNE, or by the flood of goods²³.

21 See Law number 20 of 2008 concerning Small, Micro, and Medium-scale Enterprises. Retrieved at <http://eng.kppu.go.id/wp-content/uploads/LAW-OF-THE-REPUBLIC-OF-INDONESIA-20-OF-2008.pdf>

22 Business fields that are Open with conditions as intended in paragraph (1) letter c shall consist of: Business fields that are Open with conditions, which are reserved for or in partnership with a Small, Micro, and Medium Enterprise, and Cooperatives.

23 Set forth in the agreement protection of SMEs in Indonesia by rules on Anti-dumping, countervailing, and

1.2. Treatment of SMEs in the view of Regional FTAs

The Republic of Indonesia has signed and implemented many Regional FTAs with various countries around the world; inter alia, FTA agreement under AEC and China, New Zealand, Japan, Korea, Australia, which sought to facilitate and reduce the import tariffs to 90% trade in goods²⁴. Through the comprehensive approach, the trend of FTAs in Indonesia is inclined to the ASEAN Free-Trade Area (AFTA). As known, Indonesia has agreed many FTAs around the world; consequently, this study may focus on some alleged FTAs that face or will engender challenges gloomily on its domestic SMEs.

Under the agenda of AEC to revamp the SMEs around country members is an integral part of the cooperation, it is based on the fact that SMEs contribute to the economy of 50% up to 80% and increase employment, and encourage capability of competitiveness²⁵. The AEC implicates a free market for trade liberalization, allowing free movement of goods, services, and foreign investment and free

flow of capital²⁶. Expressly, article 1(5) of the ASEAN charter introduces that “ To create a single market and production base which is stable, prosperous, highly competitive and economically integrated with effective facilitation for trade and investment in which there is a free flow of goods, services, and investment; facilitated the movement of business persons, professionals, talents and labor; and freer flow of capital To create a single market and production base which is stable, prosperous, highly competitive and economically integrated with effective facilitation for trade and investment in which there is a free flow of goods, services, and investment; facilitated the movement of business persons, professionals, talents and labor; and freer flow of capital”.²⁷ This provision seeks to promote investment business among member countries through trade facilitation, free flow of goods in a single market.

In further AEC rule ensure comprehensive policies data on the contribution of the SME. It also allows market access and internationalization and prioritizes

safeguards.

- 24 The framework was signed on 4th November 2002 which came into full effect on 1st January 2010. Retrieved http://www.gbgindonesia.com/en/main/business_guide/2016/indonesia_in_free_trade_agreements_11504.php#:~:text=Indonesia%20is%20a%20member%20of,signed%20on%204th%20November%202002.&text=Indonesia%20is%20also%20involved%20in,came%20into%20effect%20in%202008.
- 25 Zainuddin Djafar, “ASEAN Competitiveness, Is Indonesia Ready yet?” Vol.9 No. 4, July 2012, Depok: Faculty of Law Universitas Indonesia Page 599.
- 26 Koesrianti, “law reform of Small and Medium Enterprises (SMEs) and equitable cooperative for competitiveness improvement in AEC area”, Social science and faculty of Law Universitas Negeri Surabaya (UNESA), 14 September 2016.
- 27 The ASEAN was established on 8 August 1967. The member states are Brunei Darussalam, Cambodia, Indonesia, Lao PDR, Malaysia, Myanmar, Philippines, Singapore, Thailand, and Vietnam.

the social aspect of SME development²⁸. Accordingly to the AEC set its 2025 blueprint that it has five interrelated and mutually reinforcing characteristics which are: A Highly Integrated and Cohesive Economy; A Competitive, Innovative, and Dynamic ASEAN; Enhanced Connectivity and Sectorial Cooperation; A Resilient, Inclusive, People-Oriented, and People-Centered ASEAN; and A Global ASEAN. All of this is summarized into a common vision called as ASEAN Community Vision 2025.²⁹ However, aside from the already enforced FTAs, Indonesia has progressively agreed to some FTAs, including Indonesia-Chile FTA, Regional Comprehensive Economic Agreement (RCEP), and Indonesia-Europe Free Trade Association FTA (IEFTA, FTA), etc.

On the other hand, under the RCEP agreement, the SMEs are deemed to enhance economic growth and employment for signatories' countries, inter alia, developing and least developed countries. The agreement set forth opportunities for enterprises to acquire a large benefit from Free Trade³⁰. In light of chapter 14, article 14.1 recognises as well the importance of the SMEs "The Parties recognise that small and medium enterprises, including micro-enterprises, contribute significantly to economic

growth, employment, and innovation, and therefore seek to promote information sharing and cooperation in increasing the ability of small and medium enterprises to utilise and benefit from the opportunities created by this Agreement". Expressly, it emphasizes that the agreement seeks to strengthen economic cooperation for the SMEs in various areas, such as e-commerce, access to market, innovation, intellectual property rights, and involvement in Global Value Chains. The RCEP is perceived to modernize various national laws to address secure transactions, simplified registration, and bankruptcy. In chapter 14, article 14.3 determines commitments of parties to be aware of efficient cooperation which shall be taken, for example, the paragraph of the said chapter (b): improving small and medium enterprises' access to markets and participation in global value chains, including by promoting and facilitating partnerships among businesses. But this improvement is obviously very challenging in Indonesia therefore the benefits from such regional agreement are rarely seen its direct impact. Moreover, although the possible interest of RCEP agreement Indonesian SMEs, yet many lessons are seen from significant FTA that non-tariff barrier elimination in developing countries like Indonesia will impact the

28 See OECD/ERIA(12), SME Policy Index 2018: Boosting Competitiveness and Inclusive Growth, OECD Publishing, Paris/economic Research Institute for ASEAN and East Asia, Jakarta. <https://doi.org/10.1787/9789264305328-en>

29 See the publication of ASEAN (The Association of Southeast Asian Nations) in 2015 for its blueprint in 2025, the economic growth of the country is designed through the improvement of SMEs contributions.

30 Available at <https://perthusasia.edu.au/getattachment/Our-Work/Supporting-Indonesia%E2%80%99s-SMEs-to-benefit-from-RCEP/PU-189-V17-SMEs-RCEP-WEB.pdf.aspx?lang=en-AU>

SMEs gloomily in market competition³¹. Especially its fragile SMEs regulations will be affected if there is no stringent measure.

In short, Indonesian legal aspects for SMEs enacted with and after the omnibus seem to detain protectionism, as the treatment of foreign investors especially large companies do not have free access to all sectors, but under the provisions of the regional agreement, neither the ASEAN charter nor RCEP defines restrictions of the large companies in some activities conserved for the SMEs. The principle of national treatment may be hindered.³² Even if the omnibus law itself defines in its article 4 (2) a: “the government has to accord equitable treatment to domestic investors and foreign investors with due regard to the national interest.”

1. Challenges of Indonesia`s SMEs in facing Regional Free Trade

Although the policies set aside by the regional Free Trade Agreement like AEC and RCEP³³ preview attractive policies for protecting and encouraging SMEs, but have to put in mind that the signatories’

countries should establish clear domestic policies backing up SMEs in order to support the aims of the agreement so that the countries can benefit the opportunities granted. In Indonesia, legal investment policy restricts some sectors for trade liberalization in order to maintain the survival of its SMEs³⁴.

1.1. Weakness of domestic policy for SMEs in entrapping benefit from Regional Free Trade

Admittedly, Jakarta has been working hard to prepare for the regional FTA, especially AEC; however, the current situation appears very critical. The country has been failed to ensure balancing SMEs with regional Free Trade because of inappropriate policies and weak performance of Indonesian Small and Medium Enterprises in encountering trade liberalization environment. The reliance of the country on protectionism policy which limits some sectors in favor of domestic SMEs, abuses the expansion of the local market in the international sphere.³⁵ Accordingly a survey demonstrated the fragility of said type enterprises are knowingly, they

31 Gantz, David A. “The TPP and RCEP: Mega –Trade Agreements for the pacific Rim” *Arizona Journal of International and Comparative Law*, vol.33issue 1 (2016), pp.55-70

32 Each Party shall accord to investors of another Party, and to covered investments, treatment no less favorable than that it accords, in like circumstances, to its own investors and their investments with respect to the establishment, acquisition, expansion, management, conduct, operation, and sale or other disposition of investments in its territory

33 See “Summary of the Regional Comprehensive Economic Partnership Agreement”, <https://asean.org/storage/2020/11/Summary-of-the-RCEP-Agreement.pdf>

34 Peach, Melissa. “Eye of the Tiger: Examining Tension in Indonesia’s Trade Regime.” *Currents: International Trade Law Journal*, vol. 22, no. 1, winter 2013, p. 38-54. HeinOnline

35 Tulus Tambunan, “The impacts of Trade liberalization on Indonesian Small and Medium-Sized Enterprises”, *INT`L INSTITUTE FOR SUSTAINABLE DEV.*(2011),[www.iisd.org/tkn/pdf/impact-trade lib Indonesia.pdf](http://www.iisd.org/tkn/pdf/impact-trade%20lib%20Indonesia.pdf).

do not have mainly enough capital, the Nation does not take relevant measures to sponsor and finance their business operations. The regulation and restrictions are cumbersome problems hampering business activities in Indonesia reflect the poor governance in the country, likewise, the policy-generated barriers to domestic competition and trade which include the barriers to inter-regional and inter-island trade.³⁶ There is no reliable legal framework providing an opportunity for small domestic investors with foreign investors, whereas looks protectionism. SMEs in Indonesia encounter various export barriers at the pre-exporting and exporting stages. At the pre-exporting stage, SMEs are less likely to engage in export activities if they perceive difficulties in tariff and non-tariff barriers, informational and human resource barriers, distribution, logistics, and promotional barriers, business environment barriers, procedural barriers, and foreign customer and competitor barriers. SMEs are prevented from sustaining and developing their exports at the exporting stage mainly by informational and human resources barriers, distribution, logistics, promotional, financial, foreign government, procedural, and price

barriers.³⁷ For example, the relevance of AEC in Indonesia in internationalizing and widening the market is unfortunate, but the policy remains poor to benefit the SMEs. In addition, the interview on the challenges of SMEs in Indonesia guided by Rahadi confirmed the weakness of domestic policy in handling the prosperous development of SMEs hamper SMEs to develop to a higher level; the quality of productivity almost ever remains traditional.³⁸ Furthermore informality of SMEs sector in the country weaken their competitiveness skills over the regional market, the regularity is required while encountering competition with foreign companies or goods.³⁹

1.2. Weakness of Domestic SMEs to face Regional Free Trade competition

Many kinds of research asserted that challenges of SMEs in Indonesia to face regional SMEs competition in terms of product quality and productivity are because of the inadequacy of technology and infrastructures utilised by, for example, the use of Industry 4.0 in the country proffered many advantages of the SMEs in quality of product, yet evaluated that most of the SMEs in the country have

36 Tulus Tambunan, "Development and some constraints of SME in Indonesia", Center for Industry, SME & Business Competition Studies University of Trisakti, p.1-9, 2009

37 Raden Aswin Rahadi, "Opportunities and challenges for micro-small and medium business in Indonesia facing ASEAN Economic Community" JMK, VOL.18, NO.1, MARET 2016.145-53

38 See Ibid

39 Rothenberg, Alexander D Gaduh, Arya Burger, Nicholas E, "Rethinking Indonesia's Informal Sector" World Development Vol. 80, pp. 96-113, 2016 0305-750X/ 2015 The Authors. Published by Elsevier Ltd. This is an open-access article under the CC BY license (<http://creativecommons.org/licenses/by/4.0/>).

not yet proceeded to Industry 4.0 and 5.0.⁴⁰ Actually, SMEs in Indonesia has several advantages that are not granted for foreign investor's competitors, inter alia, abundant of natural resources to processed and marketed at international markets, and several competitive sectors include mining sector, fishery, handcrafts, and forestry, etc.⁴¹ Nonetheless an expert stated by lack of infrastructure, limited access to financing and business plan, its SMEs do not enable to compete successfully against their regional counterparts.⁴² And the main challenge is the imperfection of legal rules and legal reforms to improve the competitiveness and legal protection.⁴³ Jakarta has confirmed 90.5% of the AEC blueprint, yet limited transportation access, a lack of knowledge about ASEAN product standardization, and export-import procedures and insufficient technical understanding remain obstacles of

SMEs to take advantages of accessing to regional competition.⁴⁴ During the interview conducted by Rahadi, the first and second respondent affirmed that the SMEs in Indonesia have not capacities to compete with other ASEAN nations because of lacking knowledge and use of advanced technologies. The performance of SMEs in Indonesia is still lower compared to other regional enterprises caused by the imperfect legal framework, lack of accession to social security.⁴⁵ Consequently, they are unable to face challenges in the international market. In fact, in considering the above said the competitiveness of SMEs in the regional market does not rely on government policies only but also on the performance of SMEs concerned.

1.3. Obstacles on improving the partnership between SMEs and Large Enterprises

40 Aries Kurniawan, Beni Dwi Komara, Heri Cahyo Bagus Setiawan, "Preparation and challenges of Industry 5.0 for Small and Medium Enterprises In Indonesia" Volume 2, number, December 20-19. Retrieved at <http://journals.ums.ac.id/index.php/mijeb>

Furtherly Industry 4.0 consists of an integration of robots, interconnected devices, and fast data networks in a factory environment; the focus of such technology is automation and digitization, while Industry 5.0 is a new development of the 4.0, which consists of a combination of automation and personalized human involvement.

41 Ibid

42 Meliadi Sembiring, "SMEs Growth and Development in Indonesia", ADBI Joint Regional Workshop on SME development and regional economic integration, 22-26 September 2008, Tokyo, page 3-4, and see also "Indonesia SMEs: Increased Government support to overcome challenges" http://www.gbgingonesia.com/en/main/why_indonesia/2016/indonesia_smes_increased_government_support_to_overcome_challenges_11603.php

43 Dionisious Narjoko, "turning Dream into Reality?: Achieving the Goal of SME Development in AEC", International conference on ASEAN Vision 2015: Moving toward one Community, CIER, Tapei, May 2011, ERIA

44 See Randy W. Nandyatama "Indonesian SMEs and the ASEAN Economic Community". Retrieved at <https://thediplomat.com/2015/06/indonesian-smes-and-the-asean-economic-community/>

45 Torm, Nina. "To what Extent is Social Security Spending Associated with Enhanced Firm-Level Performance? A case study of SMEs in Indonesia." *International Labour Review*, vol.159, no.3, September 2020, p.339-336. HeinOnline.

The legal framework in Indonesia encourages a closer relationship between SMEs and Large foreign companies to enhance SMEs' capabilities and competencies in terms of productivity, technology, and managerial knowledge.⁴⁶ It is acknowledged that large enterprises⁴⁷ are not flexible to give range extensive of opportunities for SMEs in the sector of business operation,⁴⁸ therefore the engagement of the domestic private sector in the sphere of economic development contribution is still lower due to multinational firms dominates the sector, and the latter does not have a significant positive impact to local communities' economies.⁴⁹ To extend the domestic and regional rules for complete protection of SMEs are conceptualized not thoroughly realistic by the fact that large enterprises defend as well their interests. So, the legal framework for setting aside special treatment of SMEs remains controversial aspects when looking at regional free trade on the other side, because FTA is integrally based on liberalization of trade and market that is definitely dominate

the sectors where SMEs shall develop its capacity. A developing country like Indonesia whose economic development relies on SMEs faces challenges handling the multifaceted regional Free Trade therein. In order to meet the conducive participation of SMEs, the Government of Indonesia should set forth rigorous regulations making necessary financial assistance available and accessible, delivering capacity-building programs needed for SMEs' technological advancement. It should oblige the multinational corporations to optimize suppliers from local SMEs or affiliations of Foreign Direct Investment. In other words, the large company in Indonesia has no reliable support from the government to expand their partnership with SMEs, this reason why perceived that it looks very unrealistic to enhance the partnership between them without supporting legally their business by alleviating some restrictions in their activities.⁵⁰

46 Koesrianti, "law reform of Small and Medium Enterprises (SMEs) and equitable cooperative for competitiveness improvement in AEC area", Social science and faculty of Law Universitas Negeri Surabaya (UNESA), 14 September 2016.

47 Shall be productive economic business done by business entities with net assets or annual sales proceeds larger than that of Medium Enterprises, including state-owned or privately owned business, joint ventures, and foreign business that conduct economic activities in Indonesia.

48 Rothkegel, Senad; Erakovic; Ljiljana; Shepherd, Deborah, "Strategic alliances between SMEs and large firms: An exploration of the dynamic process" revue ISSN 1861-9916, Rainer Hamp Verlag, Mering, Vol.17, Iss.1, pp.50-70 available at <http://hdl.handle.net/10419/78877>

49 Neise, Thomas Diez, Javier Revilla, "ScienceDirect Firms' contribution to flood risk reduction – scenario-based Firms' contribution to flood risk reduction – scenario-based experiments from Jakarta and Semarang, Indonesia experiments from Jakarta and Semarang, Indonesia" vol. 212, 2017, p.567-575, available online at www.sciencedirect.com

50 Godwin, Andrew. Corporate Rescue in Asia-Trends and Challenges." Sydney Law Review, vol.34.no.1,2012, p. 163-188. HeinOnline

1.4. Implication of regional autonomy regulations

In Indonesia, the implication of Regional Free Trade rules waiving tariffs and the international goods which flood the market where the SMEs sell their products is tremendous problems of SMEs legal policy.⁵¹ In the concept of regional FTA (includes AEC and RECP), rules set out that liberalization and facilitation of trade mechanism implicate uncontrollable policy to protecting SMEs in Indonesia by the fact that the quality of the product is not identical, the foreign or large company products are definitely more chosen in the market; as a result, the domestic SMEs do not operate positively because their products are not valuable in the market and decline their performances. Unfortunately, the existence of pre-existing FTAs rules becomes a significant challenge for SMEs policies in Indonesia. Thus, the implication of RCEP rules which tends to reduce the customs duties at a lower rate among country members (LDC, developing and developed countries), is definitely going to disorder SMEs policies in Indonesia when the Government takes no rigorous measures to settle those afore-said main challenges. The commitment of Indonesia in this agreement likely generates further critical issues to SMEs policies because the products from Japan, South Korea, Australia, and China will increase more challenges in protecting SMEs.

D. Conclusion

After the omnibus law, the Government of Indonesia has made many efforts in revamping the SMEs environment in the regional investment by offering legal support through multi-dimensional law and regulations. One year after omnibus law, the law on number 20 the year 2008 concerning Small, Micro, and Medium-scale Enterprises for highlighting the importance and protection of SMEs in the economy of the State, and in 2016 the Presidential regulation of the Republic of Indonesia Number 44 of 2016 concerning List of Business Fields Closed to Investment and Business Fields Open with Conditions to Investment was in force in favor of SMEs. Despite those rules, SMEs' environment still bears challenges due to the inadequacy of domestic policies and the implication of autonomy of the regional rules.

The regional FTAs are deemed very critical. It is conceptualized as one tremendous cause of discrepancy of policy protecting the SMEs in Indonesia. Nonetheless, the existence of regional FTA may contribute to economic development in the country by implication of technology transfer, creation of job opportunities, and enhancing domestic SMEs quality through competition with regional countries' products. Hereby, to respond to the problematics stated above, first, in order to enhance the capacity of competitiveness, Indonesia

51 Raden Aswin Rahadi, "Opportunities and challenges for micro-small and medium business in Indonesia facing ASEAN Economic Community" JMK, VOL.18, NO.1, MARET 2016.145-53

should extend the internationalization of its SMEs as government policy, should coordinate and intensify participation of all key stakeholders. For instance, do implement some sort of globalization of entrepreneurship.⁵² Indonesian SMEs can benefit regional cooperation by involving directly or indirectly SMEs activities in the regional market, by all means giving highest priority to its SMEs, instead of multinational companies located in their countries especially those regional companies to be engaged in exports activities or in regional supply chains. The highest-ranking economies should promote trade by opening their markets and providing world-class infrastructure, administrative system, and regulatory system. Second, despite the adaptation of Indonesian investment law since 2007, the divergence of the domestic investment regulations and regional FTA exists. The implementation of regulations in 2008 relating to SMEs sectors is asymmetrical with AEC and other FTA agreements as it apparently looks protectionist. Consequently, instead of turning to protectionism in regional FTAs in the country, it is far better to enforce rigorous domestic policies for boosting local SMEs' competitiveness by special granting taxes, providing technical assistance, simplification of business procedures, customs system and disseminating understanding about

the standard of regional products. It is important to set aside priority for SMEs but not in form of protectionism or discriminatory measures. And last, the main challenges are the ineffectivity of domestic rules in governing the SMEs, the government does not implement conducive legal framework compatible, the SMEs do not have financial support, as a result, they cannot expand to inter-regional market. On the other side, the autonomy of inter-regional regulations capsize the environment of SMEs due to regional goods' floods to the domestic market, and large companies dominate the market, in fact, there is no effective enforcement of rules protecting domestic SMEs. In this regard, the government shall balance the interest of domestic SMEs and the inter-regional trade and investment leverage. The enforcement of effective regulations supporting the SMEs to enabling its activities will be capable to confront international market competitiveness.

52 Balbir B. Bhasin and Sivakumar Venkataramany. "Globalization of Entrepreneurship: Policy Considerations for SMEs development in Indonesia", *International Business and Economics Research Journal*, Vol 9 No.4, April 2010, page 95.

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Curriculum Vitae

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Short Profile

I am from Madagascar; I have been started learning Law since 2013 in Madagascar, TOLIARA province, at TOLIARA University, Faculty of “DEGS”, Department of Law. My undergraduate and Master of public law were done there in the late 2017. I was very interested in international law researches, which is reason why I applied to carry out my PHD of international law in China now on; it is supposed to finish altogether within couple of years.

In addition, my PHD research area concerns international law disputes. Hence, the paper awarded by the Indonesia government entitled on “Settlement of territorial Disputes in the perspective of international law and other Aspects” presents to me a great challenge, and broad occasions how I could internationally share my experiences and perspectives about international public law rules.

Participation as a PHD candidate

- Presentation and suggestion on the current territorial disputes between Madagascar and France, the Eparses islands in Mozambique Channel.
- Participation on NELSON Mandela Human rights moot in GENEVA, memorial in hypothetical case
- Research field; Approach on effectivity of disputes settlement in international public law

