

Changes in Non-Refined Mineral Export and Divestment Policies in Indonesian Mining

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Recent Indonesian regulations¹ implement a series of changes in respect of the regulation of the export of raw ores and concentrates but in doing so also implement very significant changes in respect of the conversion of contracts of work into Special Mining License (Izin Usaha Pertambangan Khusus – “IUPK”) and the requirement for divestment to local parties.

Mineral Export Policy – Background

Indonesia’s Mining Law² and implementing regulations promote processing and refinery of minerals domestically and prohibits the export of raw ore.

Under MEMR 1/2014, for a period from 11 January 2014 until 11 January 2017 (“Export Period”), export of concentrates was restricted to concentrates of a certain specification and in limited amounts approved by the Government. This approval was only given for mining companies who showed commitment to domestic refining of minerals, by either establishing a smelter themselves or through cooperation with others. The approvals were only given for a period of six months (extendable) with an export tax of up to 10% to be paid the “Export Conditions”).

Changes in Mineral Export Policy

Under MEMR 5/2017, as of 11 January 2017 the Export Period has been extended for a period of five years to 11 January 2022 for mining license holders subject to the Export Conditions.

The rights available during the Export Period to mining license holders that produce concentrates were also extended to those that produce unprocessed nickel ore with a nickel content of less than 1.7% or washed bauxite ore with an aluminum oxide content of 42% or above (“**Unprocessed Nickel and Bauxite**”) – such that they will be able to resume the export of Government approved quantities (subject to meeting the Export Conditions, having their smelter plans approved by the Government and, in the case of unprocessed nickel ore producers, meeting a domestic market obligation to collectively supply 30% of the low nickel ore content demand of domestic smelters).

¹ Regulation No. 1 of 2017 regarding the Fourth Amendment to Government Regulation No. 23 of 2010 on the Implementation of Mineral and Coal Mining Business Activity (“**GR 1/2017**”). This was followed by the issuance of two ministerial-level regulations to implement GR 1/2017 namely (i) MEMR Regulation No. 5 of 2017 on the Increase of Mineral Value Through Domestic Mineral Processing and Purification (“**MEMR 5/2017**”) that revokes MEMR Regulation No. 1 of 2014 on the same matter (“**MEMR 1/2014**”) and (ii) MEMR Regulation No. 6 of 2017 on the Procedure for the Granting of Recommendation for the Sale of Minerals to Foreign Countries as a Result of Domestic Processing and Purification (“**MEMR 6/2017**”).

² Law No. 4 of 2009 regarding Mineral and Coal Mining.

However, for miners that operate under a mining contract of work with the government (“**COW**

Conversion from Contract of Work into IUPK

In general, COW terms and conditions are more favourable than mining licenses under the Mining Law. Previously the Mining Law and its implementing regulations did not require miners to convert their COW into a license although the Mining Law did require COW holders to renegotiate their contracts to adjust to the provisions of the Mining Law.

In addition, article 19 of MEMR 5/2017 states that the conversion from contract of work into IUPK is to be effected by submitting an application for conversion and termination of the COW to the Minister of Energy and Mineral Resources and that there will be no tender requirement involved in this process. This conflicts with the Mining Law which requires an IUPK to be granted on a tender basis. This inconsistency may raise a question in relation to the authority of the Indonesian Government to issue an IUPK under MEMR 5/2017.

Export of Concentrates and Unprocessed Nickel and Bauxite

Before being qualified to export concentrates or Unprocessed Nickel and Bauxite, IUPK companies must obtain Export Approval from the Directorate General of Foreign Trade of the Ministry of Trade. In order to obtain Export Approval, IUPK companies must obtain a recommendation from the Directorate General of Mineral and Coal. The Export Approval is valid for one year and is extendable.

The concentrates which are exported in this five years period (after obtaining the required recommendation and approval) must also meet minimum processing requirements as set out in MEMR 5/2017.

Divestment

GR 1/2017 makes significant changes to the current divestment requirement. The changes cover the following matters:

- a. In the previous divestment scheme, the limit of foreign ownership in mining companies depended on (i) whether or not the relevant mining companies conducted their own processing and/or refinery activities, and (ii) whether the companies engaged in underground or open pit mining activity.
The new requirement states that foreign investors can only own 49% (forty nine percent) of the total shares in a mining company irrespective of the above two factors.
- b. Under the new divestment scheme, the shares for divestment purpose must be offered to (in this order), (i) the Central Government, (ii) Regional Government, (iii) State-Owned Enterprises or Regionally Owned Enterprises, and then (iv) private entities. This adds an extra layer, where previously, the offer could be done simultaneously to the Central Government and Regional Governments.
- c. Under the new divestment scheme, the time requirement for responding to an offer of shares is removed, with the consequence that the divestment process can be delayed for an indefinite time.

Under the new divestment scheme, the offer to the Government for divestment must be commenced at the latest 90 days after the expiry of five years of the issuance of the production mining license.

Conclusion

1. COW companies will no longer be able to export concentrates and will not be able to avail of the relaxation of restrictions on Unprocessed Nickel and Bauxite unless they convert to IUPK. For COW holders wishing to export production it presumably makes the ongoing COW re-negotiation process obsolete and leaves the recently amended COWs of exporters facing the reality that the conversion process that they thought their renegotiation had avoided must now take place. For those holding COWs the move to a licence is a negative development.
2. The requirements for higher foreign ownership in certain cases and longer divestment period under the previous regulation are now removed. This will impact on current divestment expectations and have a material effect on previously expected investment returns.
3. The removal of the time limit for response to an offer of divestment can be expected to cause delay in the divestment process and create uncertainties (as high profile previous divestment processes have informed investors) as to the validity of a license in the face of a failure of a license holder to comply with the divestment process due to the failure of an offeree to respond.
4. On a broader front it should not be forgotten this is just an extension for five years of the ban on export of unprocessed minerals. In the context of investment of exploration dollars or commitment to the development of large scale mines, the five year extension does not offer a solution for attracting NEW investment in the upstream mining sector. To make matters worse, Indonesia's commitment to a policy of in country beneficiation has now been brought into question. The sovereign risk cloud that had negatively impacted the investment of global mining companies in upstream exploration and mining project development in Indonesia has now extended to the downstream processing investment, putting further investment in that sector at risk as well.

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