

Contract of Work for IUPK OP: A Tough Decision

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The Indonesian government (“**Government**”) has issued a number of regulations to implement its mining policy, including GR 1/of 2017¹.

In moving towards a single Special Mining Permit Operation Production license (IUPK Operasi Produksi or “**IUPK OP**”) licensing regime, the Minister of Energy and Mineral Resources (“**MEMR**”) issued Regulation No. 15 of 2017 (“**Reg. 15/2017**”) on 10 February 2017 which provides for the replacement of a Contract of Work (“**COW**”) and Coal Contract of Work (“**CCOW**”) with an IUPK OP. Other regulations provide that a COW mining company must convert to an IUPK OP in order to export concentrates. However, there are some issues that arise under Reg. 15/2017 as discussed below.

Scope of Reg. 15/2017

Reg. 15/2017 deals with three matters:

- the conversion of mining operations from a COW to an IUPK OP;
- the procedure for obtaining an IUPK OP Extension for any COW or CCOW that will soon expire; and
- the management of mining areas that were designated under an expired COW or CCOW.

Conversion of Minerals COW into IUPK OP

Under MEMR Regulation No 5 of 2017, mineral mining companies operating under a COW must convert their COW to an IUPK OP to continue exporting concentrates and resume exports of Unprocessed Nickel and Bauxite for the next five years. Reg. 15/2017 further elaborates the COW conversion process for that purpose. Under Reg. 15/2017, the COW holder initiates the conversion process by filing a conversion and COW termination application along with the supporting documents to the MEMR through the Directorate General of Mineral and Coal (“**DGMC**”). The DGMC will have seven business days to evaluate the application and report on its review to the MEMR. Based on this report, the MEMR will approve or reject the application.

¹ See our earlier [Client Alert](#) “Changes in Non-Refined Mineral Export and Divestment Policies in Indonesian Mining” on Government 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**”), and other ministerial-level regulations.

The conversion process under Reg. 15/2017 does not involve an auction, unlike the process for obtaining a new mining permit (*Izin Usaha Pertambangan* – “IUP”) under the Mining Law². Presumably, this reflects the Government’s intention to remain bound by the terms of the existing converted COWs. However, it is arguable that this “auction-free” conversion process may not have a sufficient legal basis, being neither mandated nor recognised under the Mining Law.

Reg. 15/2017 provides that the terms of an IUPK OP must be in line with prevailing laws and regulations unless stipulated otherwise in the relevant COW and any previous agreements with the Government. All terms and conditions under the converted COWs and any other previous agreements between the Government and the COW holder will remain effective until the expiry of the relevant IUPK OP. However, given that many terms of an existing COW may differ from the current laws and regulations (such as those regarding taxation and mining area size), an issue may arise as to which COW terms will be enforceable. Currently, it is not clear whether the COW holder has any power to negotiate the terms and conditions of the conversion IUPK OP.

The conversion IUPK OP for minerals is granted for a period mirroring the relevant COW expiration date and can be extended twice: each extension for a further 10 year period.

Conversion of COW and CCOW into IUPK OP Extension

COWs and CCOWs that are not converted into IUPK OP will remain valid until the respective expiration date and are not eligible to be extended. To continue their mining activities in the same mining area, prior to the expiration of their respective mining contracts, the relevant COW or CCOW holder must convert their COWs or CCOWs into a license called IUPK OP Extension (*IUPK OP Perpanjangan*) by applying to DGMC. The application may be filed between six months and two years prior to the relevant expiry date. The MEMR should issue its decision at the latest two months before the expiry of the relevant COW or CCOW.

Rights and obligations under the IUPK OP Extension must be in line with the prevailing laws and regulations. The IUPK OP Extension is valid for ten years and is extendable for a further period of ten years.

Management of Mining Concession following COW or CCOW expiry

Mining areas under an expired COW or CCOW (or a COW that is not eligible to be converted into IUPK OP), will be declared to be either (i) an IUPK OP Area, (ii) an IUPK Exploration Area, or (iii) a State Reserve Area, based on MEMR’s decree. Mining areas in points (i) and (ii) can be offered to any IUPK OP or IUPK Exploration holder by priority or through an auction process pursuant to the Mining Law.

For the auction of IUPK Exploration and IUPK OP Areas of metal minerals previously excluded from an IUPK OP conversion, the former COW/CCOW holder who has been converted to IUPK OP has the right to match.

Conclusion

Even though the conversion of COW into IUPK OP is now regulated, the mechanism is not entirely clear. There are areas of uncertainty, such as: (i) what the effective terms and condition of the conversion IUPK OP will be (compared to the existing COW); and (ii) the possibility of a challenge being made to the validity of the conversion IUPK OP due to the insufficient legal basis. On the other hand, COW companies that heavily depend on the export of concentrates may not have much chance to negotiate or challenge the terms of a IUPK OK as they will have to convert in order to continue these activities.

The provisions governing the IUPK OP Extension gives a clearer mechanism for miners who wish to continue their mining business in Indonesia after their existing COW or CCOW expiration date.

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

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