

## MEMORANDUM

To : CASTLE ASIA

From : **ALI BUDIARDJO, NUGROHO, REKSODIPUTRO**  
Oene Marseille

Date : **14 January 2009**

Re : NEW MINING LAW

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### Minerals and Coal Mining Law UPDATE

The Indonesian Parliament passed the bill on Minerals and Coal Mining on 16 December 2008. The bill will come into operation as the Law on Minerals and Coal Mining (the New Law) in mid January 2009.

#### Key features of the New Law

- The former Contract of Work (CoW/CCoW) system for foreign investment in mining projects is replaced by a system of mining licenses.
- For “non strategic” mining areas, licenses may be issued by;
  - the regional government if the license area falls within a single regional government area;
  - the provincial government if the license area falls within more than one regional government area but within a single province; or
  - by the National Government if the license area covers more than one province.
- Equal treatment for foreign and domestic investment in mining licenses (except for limited priority for state owned companies in “strategic” mining).
- Mining can only be conducted in areas designated by National Government as being open for mining.
- New minerals and coal mining licenses are awarded through a transparent tender process (similar to existing licensing regime for oil & gas).
- The holder of an exploration license who has complied with the requirements of the license is guaranteed a production license.
- Requirement for all licence holders to comply with environmental and mine closure obligations.
- Existing CoW/CCoWs to remain valid for the balance of their existing term but to be transitioned to conform to the new licensing system within 1 year.
- License holders are required to process minerals within Indonesia (existing CoW companies will have 5 years to comply).
- Foreign investment companies holding mining licenses will be required to divest to Indonesians within 5 years of commencing production (but specifics of divestment will be subject to regulation).
- Priority to be given to “local” mining service contractors and mining services contracts between mining license holders and related parties are prohibited (subject to limited exceptions).

Jakarta, 12 January 2009

- The National Government will have substantial oversight control over regional and provincial governments who may be responsible for issuing and administering licenses.

The New Law provides the general regulatory framework but the implementation and administration of the New Law will be subject to more than 20 new regulations which the Director General of Mines has indicated should be issued in mid 2009.

Until the implementing regulations are issued, no new mining licenses will be granted.

### **Classification of Mining Business Licenses**

Under the New Law, there are 3 types of mining business licenses that can be granted:

1. Mining Business License (*Izin Usaha Pertambangan* or “IUP”)  
The IUP is the general license for conducting mining business activities.
2. Special Mining Business License (*Izin Usaha Pertambangan* or “IUPK”)  
The IUPK is the license for conducting mining activities in the “strategic” or special mining business area. The special mining business area is a part of the state reserved area in which mining business activities can be carried-out. The state reserve areas are to be designated by the National Government in consultation with the regional and provincial governments.
3. People’s Mining License (*Izin Pertambangan Rakyat* or “IPR”)  
The IPR is the license for conducting mining business in the people’s mining area with the limited area and investment. An IPR will not be applicable for foreign investment or general commercial type operations.

The New Law provides that an IUP or IUPK is granted in two separate phases of mining activities, that is, for exploration and production operation.

#### **IUP/IUPK for Exploration**

This license is for conducting general research, exploration and feasibility study activities. The IUP/IUPK for Exploration have the following limits;

<b>Metals</b>	Term, maximum of 8 years Area, maximum 100,000 ha
<b>Coal</b>	Term, maximum of 7 years Area, maximum of 50,000 ha.

#### **IUP/IUPK for Production Operation**

This license is granted for conducting construction, mining, operation, refining, transportation, and selling activities. The IUP/IUPK for Production Operation have the following limits;

<b>Metals</b>	Term, maximum of 20 years with 2 x 10 year extensions possible Area, maximum 25,000 ha
<b>Coal</b>	Term, maximum of 20 years with 2 x 10 year extensions possible Area, maximum of 15,000 ha.

### **Granting of IUP/IUPK for Exploration**

Jakarta, 12 January 2009

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An IUP for Exploration may be issued by;

- the regional government if the license area falls within a single regional government area;
- the provincial government if the license area falls within more than one regional government area but within a single province; or
- by the National Government if the license area covers more than one province.

An IUPK for Exploration is granted by the National Government.

IUP/IUPK for Exploration will be granted to a bidder following a tender process (except in cases of an IUP for “non metal” or an IUPK granted to a state owned enterprise).

The tender process is required to be transparent.

Although the procedure is still subject to implementing regulation, it is likely that the process will be similar to that applying to Production Sharing Contracts granted under the Oil & Gas Law 2001.

### **Granting of an IUP/IUPK for Production Operation**

The holder of an IUP/IUPK for exploration who has complied with the terms of their license and wishes to proceed to development of a project based on the outcome of exploration they conducted is guaranteed the grant of an IUP/IUPK for Production Operation.

An IUP for Production Operation may be issued by;

- the regional government if the license area falls within a single regional government area;
- the provincial government if the license area falls within more than one regional government area but within a single province; or
- by the National Government if the license area covers more than one province.

An IUPK for Production Operation is granted by the National Government.

### **Foreign Investment**

Foreign and domestic investors will both be eligible to hold IUP/IUPKs. The Indonesian Investment Law 2007 permits up to 100% foreign investment in mining companies (that is, mining may be conducted by companies described as “PMA Companies”).

The New Law requires foreign investors to divest ownership in companies holding IUP/IUPKs within 5 years of commencing production, although the specifics of the divestment are subject to regulation. It appears that companies holding KPs, upon transitioning to IUPs may be able to change their status to a PMA Company and have direct foreign investment (subject to restrictions on share transfers in IUP companies).

### **Processing and Refining**

The holder of IUP/IUPK Production Operation is obligated to conduct a processing and refining of the mining product within Indonesia. The holder of IUP/ IUPK may also process and refine the mining production from another IUP/ IUPK holder.

Further, the IUP/ IUPK holders may also cooperate with entities, which have already obtain IUP of Special Production Operation for processing and refining.

Jakarta, 12 January 2009

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It is not clear if a processing and refining business can be established by an entity which is not the holder of an IUP/IUPK to process and refine minerals in Indonesia.

It is also not clear if any “exemption” can be granted to export unprocessed minerals (for example, if there is no processing or refining available in Indonesia).

### **Mining Service Companies**

Mining services cover both consulting type services as well as operating and implementing services. Mining services includes transportation such as trucking, barging and shipping but appears to exclude marketing or sales services.

IUP/IUPK companies;

- Must give priority to “local” (that is, Indonesian owned) mining service companies over PMA mining service companies unless no local mining services company is available to provide the required services;
- Are prohibited from contracting with subsidiaries or affiliates (neither term is defined) to provide mining services unless the Minister permits on being satisfied there is no unrelated mining services company available.

### **Transition**

CoW/CCoW remain valid for the balance of their respective terms but are to be transitioned to comply with the New Law within one year.

All existing CoW/CCoW companies must submit development or operation plans for their respective areas to the National Government for approval within 1 year, failure to do so will result in the areas of the CoW/CCoW being reduced to comply with the limits for IUP/IUPKs (in many cases substantially smaller than the existing CoW/CCoW).

Existing CoW companies must comply with the domestic processing and refining obligations within 5 years.

There are no specific provisions in the New Law dealing with the transition of KPs. The Director General of Mining has indicated that regulations will deal with the transition of KPs.

## **What industry participants should be doing in 2009 and issues to be considered in 2009**

For many aspects of the New Law, implementing regulations must be issued in order for the New Law to be operational, however, the following are issues which industry participants should now be considering and planning implementation strategies.

### **CoW and CCoW Companies**

- preparing for transition to IUP/IUPK;
- submit all activity plans relating to exploration, production etc for the remaining term of the CoW/CCoW for government approval within 2009 to avoid the requirement to reduce contract

Jakarta, 12 January 2009

areas to comply with new limits on areas (production limits- metals 25,000 ha, coal 15,000 ha);

### **Exploitation KP Companies**

- reclamation plans to prepared to be in compliance with regulations;
- ability to provide surety for reclamation, particularly for KP company that has been operating for some time, (can KP company obtain bank guarantee or post funds?);
- if jetty or loading facilities operated by KP company are in a different regional government area from the mine, IUP may be administered by provincial Governor rather than Bupati resulting in change of reporting etc.

### **Existing Mine Operators (both CoW and KP)**

- review arrangements with mining services companies (need for contracting arrangements to comply with New Law);
- Mining services covers mining, transport (shipping, barging, trucking etc);
- contracts for mining services between a IUP/IUPK company and their subsidiaries or affiliates (not defined) are prohibited unless Minister grants a permit on being satisfied that no other mining services company is available or able so alternate ownership structures for the mining services company may be required.

### **Indirect foreign investors in KP Companies**

- take option over shares in KP Companies which may be exercised upon KP transitioning to IUP;
- note restrictions on transferring shares in IUP company still at exploration stage (restrictions are unclear);
- existing Cooperation Agreements with PMA mining service companies may need to be cancelled or the PMA mining services company converted to local company (possibly with foreign investor holding indirect interest).

### **Mining Services Companies**

- Existing contracts with mine operators may need to comply with New Law as existing CoW/CCoWs and KPs are transitioned to New Law;
- If services are provided by subsidiaries or affiliates of the mine operator, alternate ownership structures be put in place to overcome prohibition on contracts for mining services with between IUP/IUPK company and subsidiaries or affiliates;
- PMA Mining Services Companies;
  - Enter into arrangements with local mining service companies to provide technical services (in effect be able to operate as a “sub contractor”), particularly if PMA Mining



COUNSELLORS AT LAW

Jakarta, 12 January 2009

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Services Company has existing contract which may be subject to termination under new law;

- Local Mining Services Companies;
  - Enter into arrangements with PMA Mining Services Companies to provide technical services to enable Local Mining Services Company to have necessary technical ability to bid for contracts or takeover existing contracts currently held by PMA Mining Services Companies.

### **New Foreign Investors**

Establish PMA Mining Company to be able to apply/bid for new IUP/IUPK when available (noting it may take 3-4 months to establish).

### **Further information**

**For further information or assistance in relation to the New Law or any legal aspect of mining in Indonesia, please contact us**

### **Important Note**

This document only provides an overview of major issues arising from the New Law and nothing in this document constitutes legal advice.

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