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Executive Summary

The Minister of Energy and Mineral Resources ("MoEMR") has now issued the long awaited regulation regarding minerals and coal price benchmarking. This regulation will impact mining companies sales activities and royalty calculation. There are still some concerns/issues that have not been addressed, and developments in this area should be monitored.



Indonesian Minerals and Coal Benchmark Price

Ali Mardi / Alexander Lukito

The MoEMR recently issued Regulation No.17/2010 ("Reg.17") outlining the mechanism for determining the Indonesian Minerals and Coal Benchmark Price ("IMCBP"). Reg.17 is one of the implementing regulations to the Mineral and Coal Mining Law No.4/2009 and was signed on and is effective from 23 September 2010.

A key point to note is that, as expected, the regulation appears to have incorporated most of the issues brought-up in various discussions between stakeholders and the Directorate General of Minerals, Coal and Geothermal ("DGoMCG"). These include:

- a) the use of the average mineral/coal price from international market indices and the use of FoB mother vessel as the sale point to determine the IMCBP;
- b) the acceptance of certain costs as adjustments to the IMCBP (if the actual sale point is not FoB mother vessel);
- c) the use of a "floor" price approach, i.e. IMCBP vs. actual sales price, whichever is higher, for the Non-Tax State Revenue calculation.

It is worth noting that the Government has a strong desire for mining companies to comply with this IMCBP rule. This is reflected in Reg.17 as the Government will impose administrative penalties (from written warnings letters up to the cancellation of the mining licence) for those who fail to meet the requirements under Reg.17.

A high level summary of Reg.17 is outlined below.



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High Level Summary of MoEMR Regulation No.17/2010 on Indonesian Mineral & Coal Benchmark Price (“IMCBP”)

Descriptions		Minerals			Coal			
		Metal	Non-Metal	Rocks	Steam (thermal)	Coking (metallurgical)	Low Rank	Specific Type for Domestic Market
1)	Basis of IMCBP	Market price			Average coal price announced by international market indices		Average low rank coal price in accordance with market price	Negotiated
2)	Authority to issue	DGoMCG	Governor (in coordination with DGoMCG)	Municipal government (in coordination with Governor)	DGoMCG			Approval from DGoMCG
3)	Time of issue	Monthly basis			Monthly basis		Not clear (presumably monthly)	Not clear (presumably per contract)
4)	IMCBP sale point	FoB at mother vessel	Not clear	Not clear	FoB at mother vessel		Not clear	Negotiated
5)	Whether adjustment to IMCBP is allowed (for non-FoB vessel sale term)	Yes, for: - barging costs; - surveyor costs; - transshipment costs; - treatment costs/refinery costs and/or metal payable; - insurance costs.	Not clear	Not clear	Yes, for: - barging costs; - surveyor costs; - transshipment costs; - insurance costs.		Not clear	Not clear
6)	Basis for Non-Tax State Revenue calculation (e.g. royalty)	IMCBP or actual sales price, whichever is higher			IMCBP or actual sales price, whichever is higher			Approved price
7)	Price agreement	Needs to be notified to MoEMR via DGoMCG (both for spot and term contracts). For term contracts, the price should be renegotiated every 12 months.	Not clear	Not clear	Needs to be notified to MoEMR via DGoMCG (both for spot and term contracts). For spot contracts, actual sales price should refer to IMCBP at the relevant month, whilst for term contract, it should refer to average IMCBP on the last three months (when the agreement is made). For term contracts, the price should be renegotiated every 12 months.		Not clear	Approved by DGoMCG
8)	Sales reporting to relevant Government Authority (DGoMCG , governor and mavor)	Monthly basis (at 10 th of the following month, at the latest)	Monthly basis	Monthly basis	Monthly basis (at 10 th of the following month, at the latest)			

Non-affiliates Trading

Under Reg.17, IMCBP is aimed at not only capturing sales transactions between IUP/IUPK holders and their “affiliates” (which includes any party with direct share ownership in the IUP/IUPK holders and any party who may indirectly influence the IUP/IUPK holders’ decision) but also for sales transactions between the IUP/IUPK holders and third party customers. This practically means that, for all minerals/coal sales, the IMCBP shall apply as a floor price (i.e. irrespective of the customers and market).

Other Applications

Reg.17 also requires mining companies to:

- a) use Indonesian flagged ships/vessels to transport minerals/coal;
- b) prioritises the use of a national insurance company where CIF sale terms are adopted; and
- c) use surveyors appointed by the DGoMCG.

Transition Period

Reg.17 is applicable to Contract of Work (“CoW”) and Coal CoW (“CCoW”) holders. It provides however a transitional period for the IUP/IUPK holders and CoW/CCoW entities to amend their sales contract to conform with Reg.17. For a spot sales contract, Reg.17 provides a period for contract amendment until 22 March 2011 (i.e. six months from the Reg.17 effective date) whilst for a term sales contract (12 months or more), the contract amendment period is up to 22 September 2011 (i.e. twelve months from the Reg.17 effective date).

If however the IUP/IUPK and CoW/CCoW holders have previously renegotiated and amended a sales contract with customers in accordance with the Government’s request, the above sales contract amendment is not required.

Outstanding Issues/Questions

Reg.17 clarifies most of the questions that stakeholders have had on the implementation of IMCBP. However, in our view, there are still some concerns/questions that need to be addressed:

- a) if the IMCBP is somehow higher than the price that could be commercially agreed with a third party, the mining company will need to pay royalty/exploitation fee based on a higher sales price that can actually be achieved. This represents an additional financial burden to mining companies, unless the additional costs can be passed on to customers;
- b) the IMCBP will also be applicable to domestic sales, including those made to fulfill the coal Domestic Market Obligation/DMO. A question could be whether domestic customers will be able to afford this price;
- c) in the case where IMCBP is higher than the actual sale price, whether the IMCBP will also become the basis for the relevant mining companies’ Income Tax calculation (which should be under the Minister of Finance – Directorate General of Tax’s authority rather than the MoEMR’s). Our conjecture is that this may be the case but anticipate that a more definite confirmation should be provided through the issue of the relevant Government Regulation regarding Income Tax for the mining sector (which is currently still in draft and under discussion);
- d) the adjustment to the sale price with non-FoB vessel terms will need to be approved by the DGoMCG. Since the royalty/exploitation fees should now be paid on a monthly basis, a question is whether the approval will be able to be obtained by the mining companies on a timely basis.

Conclusion

Indonesian mining companies will need to consider this new regulation very closely and may be required to change their existing mineral/coal sales contract to comply with the regulation, which could be a protracted process.

Furthermore, more robust documentation will need to be maintained for the purpose of Non-Tax State Revenue (i.e. royalty) audits by the Government auditors.

Please contact your usual PwC Indonesia mining specialist for any queries.

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Delivering what we promise and adding value beyond what is expected.

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Teamwork
The best solutions come from working together with colleagues and clients.

Effective teamwork requires relationships, respects and sharing.

Leadership
Leading with clients, leading with people and thought leadership.

Leadership demands courage, vision and integrity.

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