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Winds of change for Indonesian mining sector

Sacha Winzenried

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Indonesia passed a new mining law in December 2008, the biggest change to mining regulation in the country in over 40 years. The new mining law represents a significant overhaul of regulations for the sector, including replacement of the well respected Contract of Work system for foreign investment, with a licence based system.

Initial reactions to the new law were not positive, with several multi-billion dollar greenfield projects seeking contracts of work being abandoned. The fact that the passing of the new law coincided with the onset of the global economic downturn did not help. However, recent increased activity from both foreign and domestic players (particularly in the coal sector) indicates that investors may be getting comfortable with the terms of the new law.

One reason may be the uncharacteristically swift action of the government in drafting implementing regulations for the new law. The new law requires a raft of government regulations to flesh out the details of the law, and prior experience has shown that these could take years to draft. However, within six months of passing the new law, drafts of the four key regulations had been circulated to stakeholders within the industry, and we understand that these drafts have now been submitted to parliament for review, and could be issued before the end of 2009. This would be a significant step towards allaying some of the lingering concerns of investors with the details of the new law.

Some of the significant matters covered by the key implementing regulations are:

- Mining permits – process for granting exploration and exploitation permits, including tender procedures
- Domestic obligations – requirement to meet domestic market needs prior to export (particularly relevant for coal producers) and local content rules
- Coal and minerals processing – requirement to conduct some form of downstream processing (crushing/washing likely to be sufficient for coal)

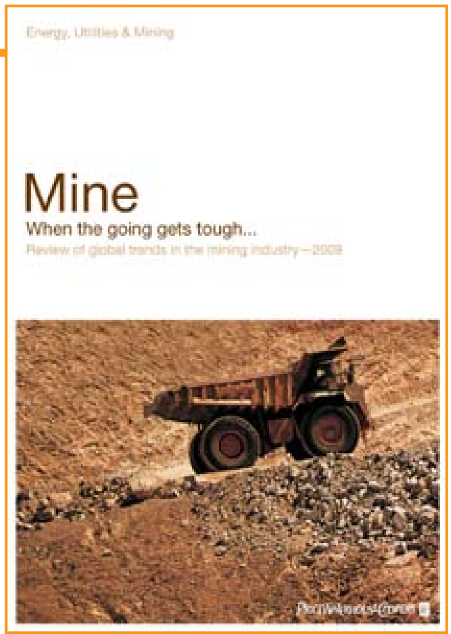
- Mineral pricing – government will set minimum prices for exported minerals and coal (ostensibly to limit transfer pricing issues)
- Foreign divestment requirements – likely to be 20% divestment requirement for foreign parties owning 100% of a project
- Mining areas – procedures for determination of areas open for mining and those designated as state reserve areas
- Reclamation and post-mining activities – covers the obligations of mining companies in respect of rehabilitation and mine closure.

A more detailed analysis of the key provisions of the draft Government Regulations implementing the new mining Law is covered in this NewsFlash.

PricewaterhouseCoopers Indonesia will continue to monitor the progress of the draft implementing regulations, and plans to issue a comprehensive analysis of the impact on investors once the regulations are issued. Further analysis of the new mining law, and other Indonesian mining issues, can be accessed at www.pwc.com/id or by contacting your usual PwC adviser. ■

Mine - When the going gets tough…

Sacha Winzenried



PricewaterhouseCoopers recently released its sixth annual survey of the global mining industry, as represented by the largest Top 40 mining companies by market capitalisation. Our report provides a comprehensive analysis of the financial performance and position of the global mining industry and also discusses current trends in the global mining industry.

Despite the strong financial results, 2008 was definitely a year of two parts with the good times quickly turning bad as the global economic crisis took hold in the last quarter and commodity prices went into freefall. The speed of the drop took many by surprise, and exposed a number of issues. Our survey highlights some of these issues, and also some innovative ways that mining company executives are dealing with the tough times.

Some of the key findings of the analysis by PricewaterhouseCoopers include:

- Despite a record year in terms of revenue and EBITDA, market capitalisation declined 62%, primarily due to the fall in commodity prices and the impact of the global economic crisis on shareholder confidence.
- Operating costs continued to rise at a greater speed than revenue, further eroding margins. In today's environment, the focus is on re-examining the feasibility of some projects, making difficult decisions where necessary whilst ensuring where possible, that their company still invests for the future.
- In the current climate there is no more valuable asset than cash, and for cash rich companies opportunities exist as asset values fall. The timing of action could be a lead indicator as to the industry's assessment of value and when asset prices have declined sufficiently to best utilise their cash resources.
- The boom encouraged the industry to invest heavily in capital projects and grow the top line. In these more cautious times, the ability to rein in costs quickly may be the difference between success and failure.

Much of the analysis is applicable to the issues being faced by Indonesian mining companies in these tough economic times, and consistent with the findings in PricewaterhouseCoopers Indonesia's latest report on the Indonesian mining industry, *mineIndonesia 2008* (available at www.pwc.com/id).

Copies of "*Mine - When the going gets tough…*" can be downloaded from www.pwc.com or contact your usual PwC Indonesia contact for a hard copy. ■

Draft Government Regulations Implementing the New Mineral and Coal Mining Law

Teuku Juliansyah / Ali Mardi

The Government has been drafting four Government Regulations ("GR") implementing the new Mineral and Coal Mining Law No.4/ 2009 with input from stakeholders. These draft GRs broadly cover:

1. Mining Areas;
2. Mineral and Coal Mining Business Operations;
3. Development and Supervision of Mining Business Operations and Management; and
4. Reclamation and Post-Mining activities.

The key features of these draft GRs are outlined below.

Key features	Draft provisions	PwC Indonesia note
Mining areas	Consists of Mining Business Areas, People's Mining Areas, and State Reserve Areas. The procedures to determine each area and the management of geographical information are included in the draft GR. The draft GR acknowledges the existence of mining licenses under the old mining law, i.e. (Coal) Contracts of Work ("(C)CoW") and Mining Authorisation (*Kuasa Pertambangan*/ "KP") and states that these licenses are valid until their expiry.	
Mining Business License (*Izin Usaha Pertambangan*/ IUP)	Mineral/ Coal IUPs can only be granted to the winner of an "IUP Area" tender.	
Special Mining Business License (IUP *Khusus*/ IUPK)	The IUPK is a mining license which covers a State Reserve Area. State-owned enterprises have priority in obtaining an IUPK (after the Government has determined specific State Reserve Areas open for mining). If no state-owned enterprise is interested in the area offered, the Government may make it publicly available.	Under the new mining law, mineral/ coal IUPK holders are required to pay an additional "royalty" to the Government equal to 10% of net profit. This may not be deductible for corporate income tax purposes.
Tender requirement	An IUP(K) Area should be granted through a tender process as outlined in the draft GR. The winner of the tender will be determined based on technical capabilities and bid price.	

Key features	Draft provisions	PwC Indonesia note
Ring-fencing, i.e. one company one IUP(K)	There will be IUP(K) ring-fencing, i.e. one company can only hold one IUP(K). This is not applicable for state-owned enterprises if special approval is obtained from the Minister of Energy and Mineral Resources (“MoEMR”).	We understand that a formal policy has not been decided due to various practical issues that will arise in implementing the rule, including tax concerns. For a mining company that holds more than one KP, there is the question of how to “transfer” costs that have been incurred for different KPs under one company to a newly-established company without incurring additional tax burden.
Area relinquishment	The draft GR includes IUP(K) concession relinquishment obligations and the maximum concession size that could be retained depending on the type of mining commodity.	
State revenue	IUP(K) holders are obliged to pay tax and non-tax state revenue based on the prevailing laws. In addition, there is an obligation to pay regional revenue based on regional regulations that have been approved by the Central Government.	This reinforces the government’s stance not to provide any other special financial and tax concessions to the mining industry other than those available under the prevailing laws/ regulations.
Land compensation	Prior to obtaining a Production Operation IUP(K), the Exploration IUP(K) holder should first settle part or all of any land status issues with the land rights holders.	Land compensation is one of the major issues faced by Indonesian mining companies due to unclear regulations on the procedures and amount of land compensation.
Periodic reporting	There are various reporting obligations for an IUP(K) holder, including submission of audited financial statements.	Currently, only companies that meet certain criteria are required to have audited financial statements. The Directorate General of Tax intends to use the periodic financial reporting as a basis for corporate income tax instalments. This will result in mining companies paying income tax instalments based on actual taxable income for the year, and so eliminating potentially significant income tax over or under payment at the end of the year.
Local content	The IUP holders must prioritise the use of local labour, goods, equipment, materials and imported goods that are already available in Indonesia. The Government will review the engagement of any expatriates. A purchase plan for capital expenditure, equipment, machinery, raw materials etc should be submitted to the Government.	It is not clear whether specific approval should be obtained for the engagement of expatriates and/ or use of imported goods, but some sort of review/ control from the Government is expected.
Domestic Market Obligation (“DMO”)	A DMO obligation is to be determined by the MoEMR on an annual basis. The DMO will be based on estimated domestic needs for minerals and coal, which must be submitted by the users to the MoEMR. The MoEMR can determine the price of mineral/ coal for the DMO.	Since coal is not a homogenous product, the Government will later determine the mechanism of how a mining company with a product not suitable for the domestic market can still meet its DMO. This may be in the form of a tradable DMO quota. In respect of pricing, we understand that the Government intends to apply the market price for DMO.

Key features	Draft provisions	PwC Indonesia note
Production and sale control	The MoEMR may issue regulations governing production and sale controls with goals to prioritise the supply to the domestic market, control over mineral/ coal pricing, conserving mineral/ coal reserves, or protecting the environment.	This is an area of concern for some investors because some (larger) mining projects require a minimum production/ sale level to be economics viable. It is not clear how this will be implemented by the Government, but we understand that this will be balanced with the Government's intention to maximise revenue from the mining industry.
In-country processing	IUP(K) holders are required to perform in-country processing either through their own facility or though cooperation with another local party. In respect of coal, the processing may be in the form of crushing, washing, blending and upgrading.	We understand that the Government will later determine the extent of processing required for each mineral/ coal product. For some minerals, processing up to concentrate level may be acceptable.
Benchmark price	IUP(K) holders are required to sell minerals/ coal at arm's length/ market prices. The MoEMR will introduce a mineral/ coal benchmark price, to be used as the minimum price of mineral/ coal sold by IUP(K) holders. The IUP(K) holders are prohibited from selling at a price lower than the benchmark price. The benchmark price will be based on an international price (FOB vessel for coal). For a long-term coal sale contract, the price should at least be the benchmark price in the month when the contract is concluded and it should be adjusted every twelve months. In addition, every mineral/ coal sale to an IUP(K)'s affiliate must be approved by the MoEMR.	There are many considerations to be taken into account when determining the benchmark price. These include how to differentiate price for heterogeneous products like coal, how to accommodate different terms of sale, etc.
Share divestment	Foreign investors that fully (100%) own an Indonesian mining company are obliged to divest 20% of the shares to a national party. The divestment should be completed at the latest by the end of the sixth year of production. The divested share price is to be determined by the Government prior to approving the commencement of the operating period. Government and state-owned enterprises are prioritised to acquire the divested shares.	The draft GR is not very clear on what should happen if the mining company is already owned by Indonesian nationals but the ownership is less than 20%. We understand that the Government intends to apply the divestment requirement in this case but that the shares to be divested are the difference between 20% and the existing national ownership percentage.
Community development and empowerment	This covers community relations, community empowerment and community services.	Community development and empowerment activities relate to corporate social and environmental responsibilities which is an obligation for a resources company under Article 74 of Corporate Law No. 40/2007. Under Income Tax Law No.36/2008, only the following costs are deductible: costs to construct public infrastructure, donations for education facilities, donations for sports development, donations for national disaster, and donations for research and development in Indonesia. The implementing Government Regulations of these provisions have not been issued to date.

Key features	Draft provisions	PwC Indonesia note
Reclamation and post-mining activities	IUP holders are obliged to provide guarantees for the reclamation and post-mining activities. A reclamation guarantee may be in the form of a time deposit, bank guarantee, insurance, or accounting reserve. Post-mining/ mine closure guarantees must be deposited in a national bank. The guarantee must be established on an annual basis and be fully funded at the latest by two years prior to mine closure.	Provisions for reclamation costs are tax deductible as long as established under the prevailing regulations. No deposit in a state-owned-bank is required now. In respect of the mine closure provision, the Income Tax Law is not clear on whether it is deductible. Therefore, it is likely that the costs are only deductible upon realisation, i.e. on a cash basis.
Transitional provisions	Existing (C)CoWs are still valid until expiry and can be extended without tender twice for ten years each through an IUP (except for those (C)CoWs that have been extended once, which can only be extended one more time for ten years). Existing KPs are still valid and must be converted into IUPs within one year of the effective date of the GR implementing the new mining law. Exploration/ Operation Production KP holders must submit an activities plan covering the whole KP area up to the KP expiry date within one year of the effective date of the GR implementing the new mining law. Existing KPs that have entered the production stage must perform in-country processing within five years from the effective date of the new mining Law. Existing (C)CoW and KP holders must establish a mine closure guarantee.	The draft GRs do not address the transition of (C)CoWs, which are governed under Article 169 of the new mining law. We understand that the government will negotiate with each (C)CoW holder on contract amendments.

These draft GRs are key implementing regulations of the new mining law. Many important issues are addressed in these draft GRs which hopefully will clarify questions from both existing and new investors on the new mining law. They will probably become the first mining regulations that involve extensive discussions between the Government and the stakeholders including the Indonesian Mining Association, the Indonesian Coal Mining Association and the Indonesian Chamber of Commerce and Industry. There are lots of hopes that these regulations will accommodate the key needs of both domestic and foreign investors which will drive the growth in the Indonesian mining industry and result in development of some of the most remote areas in Indonesia in a sustainable manner.

PricewaterhouseCoopers Indonesia strives to keep its clients abreast of the development in these draft GRs. Please contact your usual PwC adviser for any questions or concerns you may have. ■

Draft Discussion Paper for Possible new IFRS Extractive Activities Accounting Standard

William Deertz / Firman Sababalat

In August 2009 a working group comprised of staff of the national accounting standard-setters in Australia, Canada, Norway and South Africa (the "Working Group") issued a "Draft Discussion Paper on Extractive Activities" (the "Discussion Paper"). Although comments on the working draft are not currently being requested it has been made available to interested observers as the possible direction of financial accounting in accordance with International Financial Reporting Standards ("IFRS"). It is anticipated that the International Accounting Standards Board ("IASB") will invite comments on this project in the first quarter of 2010.

Background

In 2004 the IASB established the Working Group to research the accounting for extractive activities. The IASB has agreed that if it adds an extractive activities project to its agenda the Working Group's Discussion Paper will be the first stage in the due process. The Discussion Paper is the first step towards a possible IFRS for extractive activities that would address concerns and replace IFRS 6 Exploration for and Evaluation of Mineral Resources.

The main reasons for undertaking this project were to address the divergence of views on:

- the extent to which costs of finding, acquiring and developing minerals or oil & gas reserves and resources should be capitalized;
- the methods of depreciating (or amortizing) capitalized costs;
- the degree to which quantities and values of minerals or oil & gas reserves and resources, rather than costs, should affect recognition, measurement and disclosure; and
- the definition and measurement of minerals and oil & gas reserves and resources.

Possible New IFRS Extractive Activities Accounting Standard

The Discussion Paper considers the financial reporting issues for extractive activities and provides views on the definitions of reserves and resources for financial reporting disclosures, the basis for recognizing mineral and oil & gas assets, initial and subsequent measurement of mineral and oil & gas assets, and disclosures. The Discussion Paper makes five key recommendations which are highlighted in the table below along with PwC comments and observations:

Topic	Discussion Paper Highlights and PwC comments
Scope and Approach	**Scope** ▪ Extractive activities start with exploring for and finding minerals and oil & gas deposits, and are continued by developing and extracting those deposits. ▪ Minerals and oil & gas are non-renewable natural resources and subject to several significant uncertainties which revolve around the quantity of estimated deposits that can be extracted given the geological, technical and economic conditions. ▪ The Discussion Paper does not cover other similar non-renewable resources which differs from the existing standard covered in IFRS 6. **Approach** ▪ Because of the similarity of geological and other risks for mining and oil & gas activities the Discussion Paper proposes to use a single financial reporting model for all mining and oil & gas activities. Currently there is divergence in practice between mining and oil & gas activities because IFRS 6 allows companies to apply their existing accounting policies.
Definitions of reserves and resources	▪ The Working Group proposes to use the definitions established by the Committee for Mineral Reserves International Reporting Standards ("CRIRSCO") and the oil & gas reserve and resource definitions established by the Society of Petroleum Engineers ("PRMS") (in conjunction with other industry bodies) as the template since these are principle-based classification systems and rely on reserve estimators to use their professional judgment rather than provide prescriptive application guidance. Currently many companies use their own national codes and definitions which makes comparability of reserve and resource disclosures between companies difficult.
Asset recognition	▪ Asset definition and recognition criteria should be substantially based on the IFRS conceptual framework ("Framework") as compared to current common practice where cost is capitalized or expensed according to the different phases of extractive activities. ▪ In accordance with the existing Framework, an asset is recognized when: (a) it is probable that future economic benefit will flow to the entity; and (b) the asset has a cost or value that can be measured reliably. ▪ The Discussion Paper states that asset recognition is about legal rights to explore and to extract minerals and oil & gas deposits. The Working Group proposes that an asset should be recognized when the legal rights are acquired. Information obtained from subsequent exploration and evaluation activities and development work undertaken to access minerals or oil & gas deposits would both be treated as enhancements of legal rights assets. The Discussion Paper also outlines the unit of account selection. The unit of account determines the level of detail/aggregation at which assets and liabilities are recognized and presented in the financial statements. The Working Group's view is that geographical boundary of the unit of account would initially be defined according to the exploration rights held. As exploration, evaluation and development activities take place, the unit of account will progressively contract until it becomes no greater than a single area, or group of contiguous areas, for which the legal rights are held and which is managed separately and would be expected to generate largely independent cash flows. ▪ Current practice in this area is diverse with entities expensing the costs in a number of ways. Under the Discussion Paper's proposed approach there would be more capitalization of costs. Entities would need to assess their assets for impairment whenever evidence is available to suggest that full recovery of the carrying amount of an exploration asset is unlikely. This differs from the impairment rules under IAS 36.

Topic	Discussion Paper Highlights and PwC comments
Asset measurement	▪ The Discussion Paper highlights the deficiencies of both the historical cost measurement basis and the fair value measurement basis. Because of concerns over the subjectivity and degree of estimation involved with using a fair value measurement basis the Working Group recommended keeping the historical cost measurement basis, however, the historical cost basis would be supplemented with additional disclosure in respect of the volume and value of the reserves.
Disclosure	▪ Disclosure objectives for extractive activities are to enable users of financial reports to evaluate: o the value attributable to an entity's minerals or oil & gas assets; o the contribution of those assets to current period financial performance; and o the nature and extent of risks and uncertainties associated with those assets. ▪ The Discussion Paper proposes that the minimum disclosures to be provided inline with the above objectives are: o Reserve quantities which include proved reserves and proved and probable reserves ("2P reserves"), estimation method, main assumptions, sensitivity analysis to main assumptions and reconciliation of changes in reserve quantities with the level of detail by commodity, and further broken down by country or project (where material); o If an asset is measured at historical cost, the financial statements should disclose the range of estimated fair value or standardized measure of 2P reserves, preparation basis, main assumptions and reconciliation of changes in current value with the level of detail generally disclosed by major geographical region; o If an asset is measured at fair value, the financial statements would need to disclose a fair value estimate, the main assumptions and its sensitivity analysis, a reconciliation of changes in reserve values and others with level of detail by major geographical region; o Production revenues to be disclosed by commodity; and o To disclose exploration, development and production costs disaggregated as per reserve quantities and time series of disclosure over five years ▪ The Discussion Paper definitely contemplates significantly more detailed disclosures than is currently general practice.

Concluding Remarks

The draft Discussion Paper is available at www.iasb.org (see Projects / Extractive activities). Although Indonesia has not get adopted IFRS, the Indonesian Accounting Institute ("IAI") has committed to IFRS convergence by 2012. While a new IFRS accounting standard for the extractive activities may be 2 or more years away, having an understanding of the standard setters thought processes will be useful for anyone involved in financial reporting. We will follow the development of this possible new accounting standard and include updates in future newsletters.

Please contact your PwC contact for more information on the Discussion Paper or if you would like to discuss the potential ramifications to your business from this potential new financial reporting requirement. ■

Third amendment of VAT Law No.8 / 1983

Ali Mardi

On 16 September 2009 the Indonesian Parliament approved the third amendment of VAT Law No.8/ 1983. It is expected that the new law will be effective from 1 April 2010.

Key changes to the VAT Law that are relevant to the Energy, Utilities and Mining sectors include:

1. No VAT on transfer of assets in mergers/spin-offs: the transfer of VATable goods in relation to mergers and spin-offs are not subject to VAT, provided that the companies involved are VATable entrepreneurs (i.e. taxpayers subject to VAT).
2. No VAT on catering services.
3. VAT credit during pre-production stage: the new Law stipulates that Input VAT related to capital goods can be credited by a VATable entrepreneur even though there is no Output VAT/ production yet. Input VAT associated with non-capital goods is not creditable.
4. Timing of VAT refunds: an overpayment of VAT can only be claimed for a refund by a VATable entrepreneur at the end of the book year, except if the overpayment is due to, amongst other things, the following circumstances which mean that a claim may be made on a monthly basis:
   - The export of VATable goods (which is subject to 0% VAT)
   - Deliveries to VAT collectors (e.g. PSC and certain (Coal) Contract of Work companies)
   - The VATable entrepreneur is in pre-production stage.
5. Repayment of VAT refunds to the Government: a company must return to the Government any VAT refund if it fails to enter production within three years of the Input VAT credit date. The implementation of this rule will be governed further under a forthcoming Minister of Finance ("MoF") regulation.
6. The time to issue VAT invoices: in principle, a VAT invoice must be issued at the same time as the incurrence of the underlying taxable event (e.g. delivery of VATable goods or VATable services). Alternatively, a VAT invoice may cover all deliveries in the same month to a customer (note the VAT invoice must be issued at the latest by the end of the month of delivery). However, if a payment takes place before the underlying VATable event, a VAT invoice must be issued at the payment date. The implementation of this rule will be governed further under a forthcoming MoF regulation.
7. VAT payment and VAT return filing: VAT underpayments must be remitted to the State Treasury at the latest by the end of the month following the VAT period (monthly basis) and prior to the filing of the monthly VAT return. The VAT return must be filed by the end of the month following the VAT period at the latest.
8. Several liability: the purchaser of VATable goods or services is severally liable for the VAT payment if it cannot prove that the VAT has been paid to the vendor.

Points 3 and 5 above will have a significant impact on mining projects since the pre-production period of a mining company (covering the general survey up to the construction stage) may extend beyond three years (especially for larger mineral mining projects) and there could be significant Input VAT on non-capital goods during this period. This unfavourable position is compounded by the fact that, under Article 14 of General Tax Procedures Law No.28/2007, the Director General of Tax can issue a Tax Collection Notice (*Surat Tagihan Pajak*/ “STP”) on the VAT repayment plus a penalty of 2% per month calculated from the month of the VAT refund decision letter up to the date of the STP. This means that the penalty will reach 72% if the time gap is three years.

We also note that, under the new VAT Law, mining or drilling products taken directly from their source remain exempt from VAT. These include crude oil, natural gas (except for LPG), geothermal, coal (except for briquettes), gold bars and iron/ tin/ gold/ copper/ nickel/ silver/ bauxite ores. This means that companies producing and selling VAT-exempt products cannot credit/refund their Input VAT, unless governed separately under a contract with the Government (e.g. Production Sharing Contracts and (Coal) Contracts of Work).

Please refer to our TaxFlash (which can be accessed at www.pwc.com/id) for more complete comments on the key changes introduced by the new VAT Law.

We recommend that every company assess the impact of the new VAT Law on its operations. Please contact your usual PwC adviser with any questions or concerns you may have. ■

New Regional Tax Law

Ali Mardi

The Indonesian Parliament approved the new Regional Tax bill on 18 August 2009. The bill was passed into Law No. 28/2009 on 15 September 2009 and will be effective from 1 January 2010.

One of the key changes is that the new Law will adopt a "closed-list" system, meaning that the Regional Government can only impose taxes/ levies that are listed in the new Law. This is to respond to the current issues resulting from the existing Regional Tax Law No.34/2000, which adopts an "open-list" system. There are various regional taxes/ levies issued by the Regional Government based on wide interpretations of Law No.34/2000.

We note that the bill still allows the Provincial Government to impose tax on heavy equipment (although the rate is reduced to a minimum of 0.1% and a maximum of 0.2%). This is an industry issue that has not yet been resolved.

With regards to tax on non-metal minerals and rocks, the bill provides more certainty, clearly stating that there will be no regional tax on non-metal minerals and rocks mined in conjunction with other mining activities (e.g. overburden moved during coal/ mineral mining) as long as they are not commercially used. This is consistent with Article 130 of the new Mineral and Coal Mining Law No.4/2009.

A summary of the Regional Taxes (under the current Law and the bill) are presented below. Please note that, in order to impose the regional taxes/ levies, the Regional Government should issue an implementing regulation known as *Peraturan Daerah* (Perda). ■

	Type Regional Taxes	Under Current Law		Under Draft Bill		Imposition base
		Maximum Tariff	Current Tariff	Maximum Tariff	Proposed Tariff *)	
A. Provincial Taxes						
1	Taxes on motor vehicle and heavy equipment	1.5%	- 1.5% - non-public vehicles	10%	Non-public vehicles	
			- 1% public vehicles		- 1%-2% for the first vehicle owned	Calculated by reference to sales value and a weight factor (size, fuel, type, etc.) Government table will be published annualy to enable calculation.
			- 0.5% heavy equipment vehicle		- 2% - 10% for the second and more vehicle owned	
			- 1.5% above-water vessels		- 0.5% - 1% - public vehicles	
					- 0.1% - 0.2% heavy equipment vehicle	
2	Title transfer fees on motor vehicle, above-water vessels and heavy equipment	10%	0.03%-10% depending on type of vehicle and circumstances	20%	Motor vehicle	
					- 20% -on first title transfer	
					- 1% on second or more title transfer	
					Heavy equipment	
					- 0.75% - on first title transfer	
					- 0.075% on second or more title transfer	
3	Tax on motor vehicle fuel	5%	5%	10%	Public vehicles: at least 50% lower than tax on non-public vehicle fuel (depending each region)	Sales price of fuel (gasoline, diesel fuel and gas fuel)

Type Regional Taxes		Under Current Law		Under Draft Bill		Imposition base
		Maximum Tariff	Current Tariff	Maximum Tariff	Proposed Tariff *)	
4	Tax on the collection and utilisation of underground water and surface water	20%	20% underground water	10%	tariff on surface water only	Purchase value of water (determined by applying a number of factors).
			10% surface water			
5	Tax on cigarette		10%		10%	Government duty on cigarette
B. Regency and Municipal Taxes						
1	Tax on hotels	10%	Set by region	10%	set by region	Payment received by hotel
2	Tax on restaurant	10%	Set by region	10%	set by region	Payment received by restaurant
3	Tax on entertainment	35%		25%	- 75% for discotheque, karaoke, night club, sauna, massage, beauty contest	Payment received by organiser
					- 10% for traditional art	
4	Tax on advertisements	25%	Set by region	25%	set by region	Advertisement fee
5	Tax on street illumination	10%	Set by region	10%	- 3% utilisation by industry	Sales on electricity
					- 1.5% personal use	
6	Tax on non-metal mineral and rock (formerly C-Category mined substance collection)	20%	Set by region	25%	Set by region	
7	Tax on parking space	20%	Set by region	30%	Set by region	
8	Tax on groundwater	-	-	20%	Set by region	Purchase Value
9	Tax on bird nest	-	-	10%	Set by region	
10	Land and building tax	-	-	0.3%	Set by region	Only on certain types of land and buildings
11	Duty on the acquisition of land and building rights	-	-	5%	Set by region	Land and building sale value

*) A percentage of tax object value which can be either government-determined value, market value or transaction value

**) Will be moved from Central Government to Regional Governments

Potential New Upstream Oil & Gas Government Regulation

William Deertz / Tim Watson

PwC Indonesia has recently obtained a copy of a Draft Government Regulation ("DGR") circulating amongst industry players concerning “Cost Recovery and Provisions on Income Tax in the Upstream Oil and Gas Business”. We are uncertain how far this DGR is progressed but we understand from industry sources that implementation may be imminent. If the version of the DGR reviewed by PwC Indonesia were implemented it would have far reaching effects on the industry.

In the last Indonesia Oil & Gas industry survey released by PwC Indonesia in May 2008 “contract sanctity” and “uncertainty over cost recovery” ranked high on the list of challenges facing the industry in inhibiting optimal investment. If implemented this DGR would likely add to investor concerns in these areas. PwC Indonesia is in the process of doing a detailed analysis of this DGR but we have highlighted our initial observations below:

Lack of grandfathering provisions – as currently worded the DGR doesn't appear to offer any grandfathering provisions. In other words, all existing and future Production Sharing Contracts ("PSC") would be bound by the provisions of this DGR with no dispensation for existing contracts. The lack of grandfathering provisions would be a major concern for existing investors and may result in contract sanctity challenges.

Ring-fencing of cost recovery – the DGR would limit cost recovery to a field and/or a Plan of Development ("POD") level. The recent PSC bid rounds included this provision but earlier generation PSC's specified a single cost recovery pool. In addition the DGR contemplates limiting oil cost recovery to oil liftings and gas cost recovery to gas liftings. Any subdivision of the cost recovery pool could have a major impact on PSC economics.

Capping of cost recovery – the DGR indicates that the Minister may establish a maximum amount of Operating Cost Recovery (e.g. link cost recovery to production levels) in any given year to guarantee annual state revenues. Any capping of cost recovery is disregarding the PSC First Tranche Petroleum ("FTP") provisions. FTP was essentially implemented to guarantee a government share of production, particularly in the early years of operation.

Expenditures eligible for cost recovery – the DGR has carried on with the theme started with Ministerial Decree 22/2008 commonly referred to as the "17 Negative Cost Recovery" list. In addition the DGR is moving towards a more prescriptive approach to specifying expenditures that are eligible for cost recovery and possibly linking cost recovery to production levels. The terminology "effective and efficient" is used repeatedly throughout the DGR. While existing practice would implicitly require an Operator to undertake their operations in a professional and efficient manner if the DGR does not clearly specify the framework for measuring "effective and efficient" the risk is that this concept is used to arbitrarily disallow expenditures for cost recovery.

Taxation on non-lifting activities – the DGR explicitly expands the taxability of non-lifting activities. Historically PSC Contractors were only subject to taxation on liftings. Specifically the DGR is now targeting transfers of PSC interests (there is an exemption for transfers during the exploration phase if done for risk mitigation although the DGR doesn't define precisely what would qualify as risk mitigation circumstances), uplifts, other similar arrangements and a "catch all" other category.

While the above observations are not meant to be a comprehensive analysis of the DGR we hope that they provide readers with a "flavor" of a potential new government regulation that would have far reaching effects on the industry. Hopefully through additional input from industry stakeholders many of the contentious issues in the DGR can be addressed to allay existing and future investors concerns. We will report new developments in a future newsletter. ■

Government Regulation ("GR") No. 55 of 2009: The second amendment to GR No. 35 of 2004 on oil and natural gas upstream business activities: Domestic market obligations

Anthony Anderson

Since GR 35/2004 (which implements the Oil & Gas Law No.22 of 2001) was issued it has been amended twice. The first amendment in 2005 dealt with the insertion of four new Articles 103A, 103B, 103C and 103D providing for exceptional circumstances in the issuance of a Cooperation Contract.

The second recent amendment is pursuant to the decision of the Constitutional Court case No. 002/PUU- I/2003 concerning judicial review of Article 12 (3) and Article 22 (1) of Law No. 22 of 2001. Additionally, to meet domestic oil and/or natural gas needs, it has also been deemed necessary to revise GR 35/2004 as to the Domestic Market Obligation.

The GR now makes it clear that:

a) Contractors are required to supply an identified domestic need for oil and/or natural gas; and

b) The Contractors' obligation to participate in meeting the domestic needs shall be conducted by delivering 25% (twenty five percent) of the Contractors' share of oil and/or natural gas production yield.

The elucidation to the GR indicates that the provisions in regard to domestic market obligations shall apply to PSC's with an effective date after the effective date of Law No. 22 of 23 November 2001. This effectively clarifies the position for PSC's issued over the last six and a half years or so, as there has been some uncertainty over whether a DMO gas obligation exists.

Should the Minister indicate that a domestic need exists, contractors are required to start conducting negotiations with domestic consumers. The GR is silent however on how commercial the negotiations are required to be and the pricing/valuation of any DMO gas!

The GR is also silent on the impact of this development for PSC's which already have approved Plans of Development or have already otherwise committed their gas reserves. ■

Partial Liberalisation of Electricity Management in Indonesia

Yudhanto Aribowo / William Deertz

On 8 September 2009, the Parliament of the Republic of Indonesia passed a new Law Concerning Electricity Business (the "New Law"). The New Law replaced Law No. 15/1985 concerning the Electricity Business. Previously, Law No. 20/2002 concerning the Electricity Business was issued but subesequently cancelled by the Constitutional Court on 21 December 2004. The New Law was issued as a response to a electricity supply shortage in Indonesia, whilst electricity demand shows no signs of abating and is expected to grow further.

Rationale for the New Law

The Power demand in Indonesia is estimated to be growing at a rate of 10 percent per annum, one of the highest growth rates in Southeast Asia. The strong demand growth should accordingly be matched with additional power capacity. Indonesia has been facing supply shortages due to increasing demand from domestic users. The shortage in supply is due to delays in several power projects related with the "10,000 MW crash program". The program was critical to open the power industry to private-sector investors because PLN, being burdened by debts partly due to the depreciation of the Rupiah, simply does not have enough resources to expand its own transmission and distribution networks

Area of Liberalisation

The new Law has classified the electricity supply business into four categories:

- generation of electricity;
- transmission of electricity;
- distribution of electricity; and/or
- sale of electricity

Those businesses can be run by a state-owned enterprise, local government-owned enterprise, private-owned enterprise, cooperatives and a self-help community, although State-owned enterprise shall be given the first priority. The businesses can be carried out after obtaining a business license, which consists of electricity Supply Business License and an Operating License. The licences will be granted by the Central Government or local Government.

Government's and PLN's new role

In the New Law, the state's involvement is comprised of the Central Government and Local Government (city or province) which each have their own authority. In general, the Government's authority is primarily as follows:

- Stipulating laws, regulations, policies, guidelines, standards, and criteria in electricity;

- Decisions on electricity tariffs;
- Determination of electricity business areas;
- Issuance of the licenses; and
- Development and supervision of electricity business entities, including administrative sanctions

With the New Law, PLN is no longer the holder of the electricity business operation authority, rather it is a holder of a electricity supply business license. In other words, PLN's role will be a player in the electricity industry (similar to Pertamina in the oil and gas industry post 2002).

Electricity Tariffs
The selling price of electricity, rents for electrical networks and electricity tariffs for consumers is to be determined by the Central Government/local government, House of Representatives or provincial/regional parliament which shall approve electricity tariffs for consumers. We see two issues related with the tariff. First, it is unclear who will authorise the tariff/price, (i.e. whether it is the Central Government or local government). Second, even though the New Law states that the electricity price will be determined on the basis of healthy business principles, it is unclear whether electricity pricing remains at a level substantially below production costs. Although the mining law stated that the Government will determine a minimum price for domestic coal, our fear is that the coal price could be higher than the electricity price, even though both of the prices are determined by the Government.

Transitional Provisions
All licences that were granted based on Law No. 15/1985 will be honored until the expiration date. However it is also noted that such licences shall be adapted to the provisions of the New Law after a maximum of 2 years. It is unclear whether the existing agreements (e.g. Power Purchase Agreement or Energy Sales Contract) will be renegotiated to conform to the New Law.

The New Law and the Investment Climate
It is unlikely that investors would be interested in the electricity industry if the electricity price remains controlled by the Government at a level substantially below production costs.

Below are the potential upsides and downsides of investing in the Power sector in Indonesia.

Upsides	Downsides
Unsatisfied demand for electricity	High initial investment costs, leading to an unrealistic selling price. Selling price is still regulated by the Government, as such there is uncertainty over the economics of the project.
Abundant natural resources (coal, steam) to produce power Arguably greater certainty in coal supply as the new mining law regulates Domestic Market Obligation	Stranded cost of expensive developments.
Abundant and unutilised gas power sources	Lack of contract sanctity for existing agreements.

The above is meant only as a summary of the new Law. Many of the finer points concerning the new Law need to be stipulated in implementing regulations which are forthcoming (within 1 year, at the latest, since the effective date of the New Law). It will take some time to determine whether the New Law can achieve the objectives to overcome the shortage in electricity supply in Indonesia. Nonetheless, the power industry in Indonesia should provide plenty of opportunities for private investment in the near future. Please contact any of the PricewaterhouseCoopers representatives listed opposite if you wish to discuss how we can assist you in charting your course in the Indonesian electricity industry. ■

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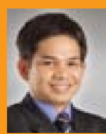

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NewsBytes

PwC Indonesia in the Mining Indonesia 2009 Exhibition and Conference 14 - 17 October 2009

PwC Indonesia will be hosting a booth at "Mining Indonesia 2009 - the 14th International Mining and Minerals Recovery Exhibition and Conference" at Jakarta International Expo Kamayoran. Come visit us at booth C-6018, Hall C1 area.

We will have senior members of our Energy, Utilities and Mining team available to discuss industry issues.

Hope to see you there !

Code of conduct
The way we do business*

Putting our values in action

Excellence

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

We achieve excellence through **innovation, learning and agility.**

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.**

This summary is not intended as professional advice. It is suggested to always consult with your usual PwC contact.

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