Mining in Indonesia

Investment and Taxation Guide

May 2017 - 9th Edition

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Photo source : PT Bukit Asam (Persero) Tbk

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Regulatory information current to 18 April 2017

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Glossary

Term	Definition
AMDAL	*Analisis Mengenai Dampak Lingkungan* (Environmental impact assessment)
BKPM	*Badan Koordinasi Penanaman Modal* (Indonesia's Investment Coordinating Board)
BUMN	*Badan Usaha Milik Negara* (National state-owned companies)
BUMD	*Badan Usaha Milik Daerah* (Regional state-owned companies)
CCA	Coal Co-operation Agreement
CIF	Cost Insurance and Freight
CIT	Corporate Income Tax
Corporations Law	Law No. 40/2007
CoW	contract of Work
CCoW	Coal contract of Work
contracts	CoW/CCoW/CCA
DER	Debt to Equity Ratio
DGFT	Director General of Foreign Trade
DGoMC	Director General of Minerals and Coal
DGT	Director General of Taxation
DMO	Domestic Market Obligation
Energy Law	Law No. 30/2007
Environmental Law	Law No. 32/2009
EPC	Engineering, Procurement and Construction
ET	*Eksportir Terdaftar* (Registered Exporters)
FOB	Free On Board
Forestry Law	Law No. 41/1999, as amended by Law No. 19/2004
Government	Government of Indonesia
GR 22/2010	Government Regulation [Reference Number]/[Issuance Year]

Term	Definition
ha	Hectare
IDX	Indonesia Stock Exchange
Investment Law	Law No. 25/2007
IPR	*Izin Pertambangan Rakyat* (People's Mining Licence)
ITL	Law No. 36/2008 (the prevailing Income Tax Law)
IUJP	*Izin Usaha Jasa Pertambangan* (Mining Services Business Licence)
IUP	*Izin Usaha Pertambangan* (Mining Business Licence)
IUPK	*Izin Usaha Pertambangan Khusus* (Special Mining Business Licence)
IUPK-OP	*Izin Usaha Pertambangan Khusus Operasi Produksi* (Operation Production Special Mining Business Licence)
IUP-OP	*Izin Usaha Pertambangan Operasi Produksi* (Operation Production Mining Business Licence)
KAPET	*Kawasan Pengembangan Ekonomi Terpadu* (Integrated Economic Development Zones)
KP	*Kuasa Pertambangan* (Mining Right)
L/C	Letter of Credit
Mining Law	Law on Mineral and Coal Mining No.4 of 2009
MoEMR	Minister of Energy and Mineral Resources
MoF	Minister of Finance
MoT	Minister of Trade
MW	Mega Watt
NPWP	*Nomor Pokok Wajib Pajak* (Tax Payer Identification Number)
PBB	*Pajak Bumi dan Bangunan* (Land & Building Tax)
PE	Private Equity
PER 47/2015	*Peraturan Direktur Jendral Pajak* (DGT Regulation) [Reference Number]/[Issuance Year]

Term	Definition
Permen 28/2009	MoEMR Regulation [Reference Number]/[Issuance Year]
PerMenDag 4/2015	*Peraturan Menteri Perdagangan* (MoT Regulation) [Reference Number]/[Issuance Year]
PMA	*Penanaman Modal Asing* (Foreign Investment Company)
PMDN	*Penanaman Modal Dalam Negeri* (Domestic Investment Company)
PMK	*Peraturan Menteri Keuangan* (MoF Regulation)
PT	*Perseroan Terbatas* (Limited Liability Company)
PTBA	*PT Bukit Asam (Persero) Tbk*
PwC	PwC refers to the network of member firms of PricewaterhouseCoopers International Limited, each of which is a separate and independent legal entity
SE 44/2014	*Surat Edaran Direktur Jendral Pajak* (DGT Circular Letter) [Reference Number]/[Issuance Year]
VAT	Value Added Tax
WIUP	*Wilayah Izin Usaha Pertambangan* (Mining Business Licence Area)
WIUPK	*Wilayah Izin Usaha Pertambangan Khusus* (Special Mining Business Licence Area)
WHT	Withholding Tax
WP	*Wilayah Pertambangan* (Mining Area)
WPN	*Wilayah Pencadangan Negara* (State Reserve Area)
WPR	*Wilayah Pertambangan Rakyat* (People's Mining Area)
WUP	*Wilayah Usaha Pertambangan* (Commercial Mining Business Area)


Photo source : PT Vale Indonesia Tbk

Foreword

Welcome to the ninth edition of the PwC Indonesia's "Mining in Indonesia: Investment and Taxation Guide".

It is now more than eight years since the 2009 Law on Mineral and Coal Mining No. 4 of 2009 (the "Mining Law") was promulgated. While various implementing regulations, including a number of amendments, have been issued by the Government in pursuing the goals of the Mining Law, there remain many challenges for investors, particularly in the current low commodity price environment.

These challenges apply for holders of both contracts of Work ("CoWs") and Coal contracts of Work ("CCoWs") issued under the pre-2009 mining regime, as well as holders of Mining Business Licences (*Izin Usaha Pertambangan*, or "IUPs") issued under the new regime.

These challenges include but are not limited to:

- The protracted CoW/CCoW renegotiation process;
- Difficulties in dealing with the downstream in-country processing requirements under the Mining Law;
- Foreign shareholder divestment requirements;
- Lack of coordination between the central, provincial and regional governments;
- Conflicts between mining operations and forestry regulations;
- Community relations and labour regulations; and
- Corruption, collusion and nepotism.

The Government has signed several renegotiated CoWs/CCoWs for some major mining operations, however many are still in the negotiation or memorandum of understanding stage. The completed renegotiations are generally for those contracts which were not *lex specialis* in nature, but rather were subject to prevailing laws and regulations. For those not yet finalised, there are some fundamental disagreements around the *lex specialis* status of the contracts. Some of the issues still being debated are changes to the applicable fiscal regime (including royalty rates); in-country processing requirements; reductions in the size of the contract areas; and foreign divestment requirements.

An urgent solution is key, as CoW/CCoW companies still produce the majority of Indonesian coal and minerals, and some significant projects have been put on hold as investors become concerned with uncertainty surrounding their contracts, and in particular the possibility for extension. Without certainty around the rights to extension of existing contracts, miners will not be able to commit to large expenditures on exploration, development or downstream processing.

Photo source :
PT Bukit Asam (Persero) Tbk

While many of these challenges remain unresolved, the Government issued PerMen 5/2017 regarding "Domestic Mineral Beneficiation through Processing and Refining" in January 2017, which has created some further concern. This regulation essentially requires a CoW holder to convert its contract into an *Izin Usaha Pertambangan Khusus Operasi Produksi* ("IUPK-OP") because it stipulates that CoW holders can only export processed products after conversion to an IUPK-OP. PerMen 15/2017 and PerMen 28/2017 issued by the Government in February 2017 and March 2017, respectively, clarify that the CoW and certain other existing agreements between the Government and CoW holders will remain valid where an IUPK-OK is granted as a continuance of a CoW/CCoW. However, uncertainties remain, as there is no detailed explanation provided in PerMen 15/2017 and PerMen 28/2017 regarding this matter, for example whether all or only part of the provisions under the CoW will be honoured. It remains to be seen how CoW holders will react to these changes.

Since the ban on exports of unprocessed (or insufficiently processed) mineral ores came into force on 12 January 2014, the Government issued various implementing regulations to allow mining companies to continue exporting certain types of concentrates provided that those mining companies paid export levies up to January 2017 (the end of the three-year transition period) and committed to building or supporting the development of processing/refining facilities in Indonesia.

In January 2017, Government Regulation (*Peraturan Pemerintah*, or "GR") 1/2017 (the fourth amendment to GR 23/2010) was issued allowing mining companies to continue exporting processed products for a period of five years from 11 January 2017, provided that they pay export duties under the applicable laws and regulations and fulfil the minimum domestic processing and refining requirements as set out in PerMen 5/2017. The regulations also relax the export ban on low-grade nickel ore and washed bauxite as these commodities can now be exported provided that certain requirements as set out in the regulation are met. While the relaxation of the export ban on low-grade nickel ore was well received by certain mining companies, many parties, including the Processing and Smelting Companies Association (*Asosiasi Perusahaan Industri Pengolahan & Pemurnian Indonesia*), have reacted strongly to the export ban relaxation as there is concern that this policy will hamper recent improvements in global nickel prices given Indonesia was one of the world's largest nickel ore exporters prior to the ban on exports of unprocessed mineral ores coming into force on 12 January 2014.

Questions continue to be raised regarding the economic feasibility of processing certain types of minerals, especially given current and forecast global and domestic demand and supply projections and commodity price considerations.

Another key concern is the inadequate supporting infrastructure (such as power, rail, roads and ports) to support downstream processing facilities in many areas of the country – meaning that for a miner to develop processing facilities it may also need to develop (or fund) much of the supporting infrastructure, which may not be economically feasible in some cases. At the same time, the ban on export of unprocessed ores means that cash flows may not be available to support investment in downstream processing. CoW holders have also questioned the applicability of the regulations to them, given the *lex specialis* status of CoWs.

Despite the good intention of developing a value-added downstream sector in Indonesia, the timing may not be right given current global supply and demand considerations for some minerals. The impact of these regulations to date has therefore been that: some (if not most) smaller-scale mineral miners have suspended operations, some large scale operations have reduced their mining activities and exports, with some leaving Indonesia altogether, while still investing elsewhere. This has not only impacted the miners themselves, but has had a significant impact on Indonesia's export revenues, tax and royalty returns, and domestic economic development.

The Government continues to work on stimulating the development of in-country processing facilities by providing much lower export levies for mining companies which are willing to commit to developing processing/refining facilities.

While this is welcome, other more tailored incentives to investors could be of benefit – for example providing tax holidays or other incentives for these highly capital intensive businesses, with sizable up-front investment required and a long payback period.

These investors' concerns have been compounded by the introduction of divestment rules that require the early divestment of foreign interests whenever there is a change in the shareholders of a company holding an IUP; the Government's stated plans to raise royalty rates; and a downturn in commodity prices in recent years. With respect to divestment rules, the Government attempted to provide some relief through GR 77/2014 which extended the divestment period and provided different divestment thresholds for mining companies which undertake underground and open pit mining, and those which have committed to development of onshore processing. This relief however is no longer available after the issuance of GR 1/2017 and PerMen 9/2017. Under these new regulations, the foreign divestment requirement has now reverted back to the regime prior to the issuance of GR 77/2014, i.e. foreign shareholders must upon five years of production divest their shares in stages, such that by the tenth year of production, foreign shareholders shall have a maximum 49% shareholding.

All of the above means that the Indonesian mining investment environment will continue to be challenging in the short-term. Many investors view Indonesia as having significant geological potential in terms of its coal and mineral resources, but the regulatory uncertainties and, to a certain extent, the royalty and fiscal regimes have become key deterrents to investment. This is particularly the case in this low commodity price environment when mining companies are looking to improve operating efficiency and productivity, and are limiting capital spending. There is therefore a real opportunity for improvement in the regulatory climate for mining in Indonesia as investors consider the allocation of their scarce investment funds in the lead up to the next round in the commodity cycle.

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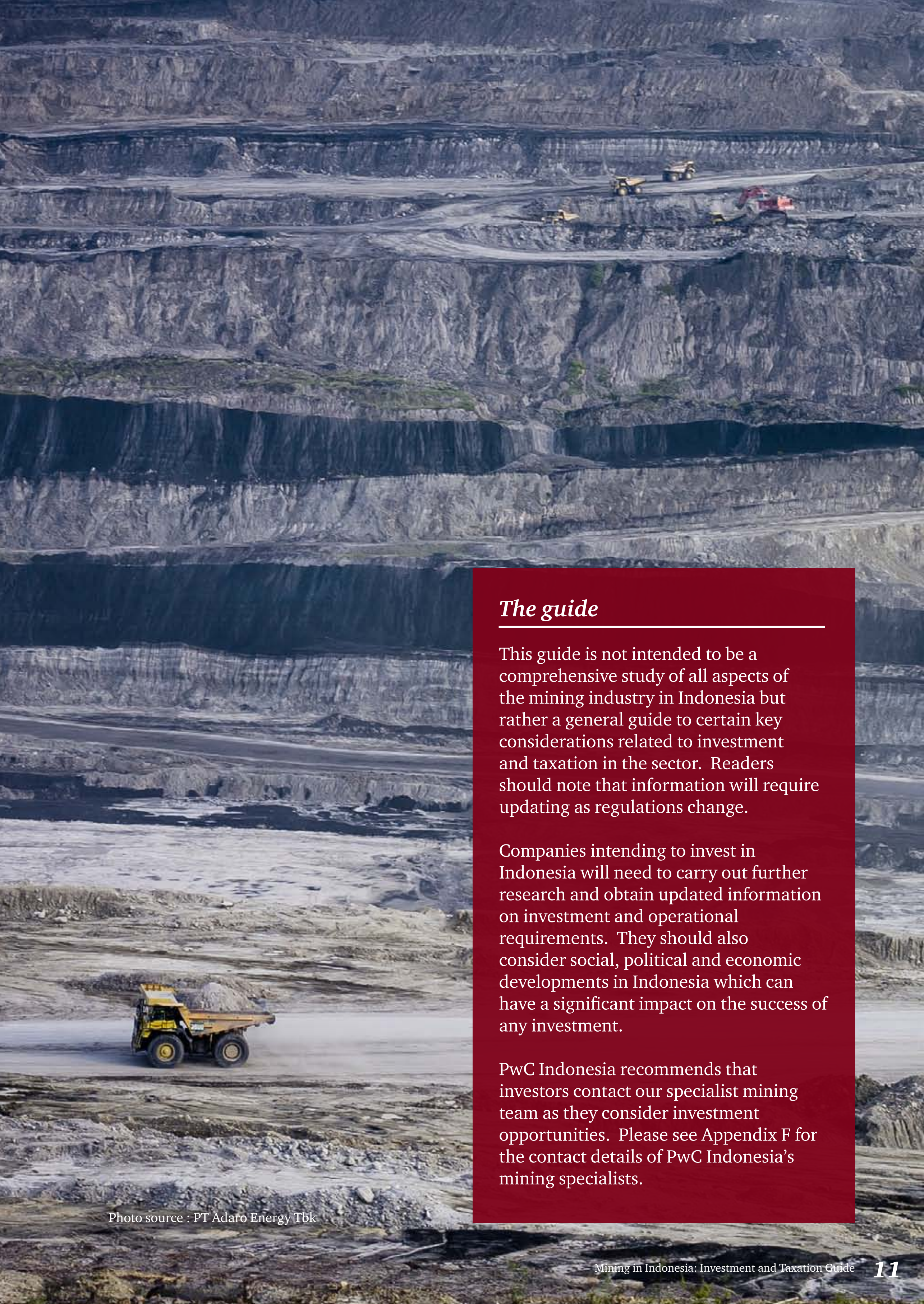


Photo source : PT Adaro Energy Tbk

The guide

This guide is not intended to be a comprehensive study of all aspects of the mining industry in Indonesia but rather a general guide to certain key considerations related to investment and taxation in the sector. Readers should note that information will require updating as regulations change.

Companies intending to invest in Indonesia will need to carry out further research and obtain updated information on investment and operational requirements. They should also consider social, political and economic developments in Indonesia which can have a significant impact on the success of any investment.

PwC Indonesia recommends that investors contact our specialist mining team as they consider investment opportunities. Please see Appendix F for the contact details of PwC Indonesia's mining specialists.

Photo source :
PT Aneka Tambang (Persero) Tbk

1.0 The Industry in Perspective

Regulatory concerns continue

Indonesia continues to be a significant player in the global mining industry with significant production of coal, copper, gold, tin and nickel. Indonesia also continues to be one of the world's largest exporters of thermal coal.

Global mining companies consistently rank Indonesia highly in terms of coal and mineral prospects, however assessments of the mining policy regime and investment climate have not been so positive. There has therefore been limited investment in mining in recent years, particularly in green-field projects.

It was hoped that the Mining Law and its supporting framework of implementing regulations would provide investors with the necessary regulatory certainty to spur new investment and strengthen Indonesia's position as a key player in the mining sector. However, after more than eight years, there is still a long way to go before Indonesia can fully realise its mining investment potential.

Indonesia's long standing CoW framework for foreign investment, and the licensing system for Indonesian investors, was replaced under the Mining Law with a new area-based licensing system applicable for all investors, incorporating tendering procedures for granting licences, with the involvement of local and provincial governments, as well as the Central Government.

Under the Mining Law, both central and regional governments play vital roles in the mining industry by setting up national mining policies, standards, guidelines and criteria, as well as deciding on mining authorisation procedures. Furthermore, the government is actively involved in development, control, evaluation and conflict resolution in the sector.

The Mining Law was heralded as the beginning of an era of greater certainty for investors in the mining industry in Indonesia. However, it has become evident in the eight years since its promulgation, that the Government has had a difficult task in balancing the interests of investors seeking to invest in Indonesia's highly prospective mining industry with the ultimate aim of ensuring that a fair proportion of the wealth generated from the exploitation of Indonesia's minerals is retained by Indonesians for the benefit of Indonesia.

Under the Mining Law, the Central Government determines the areas that can be mined and, except in certain exceptional circumstances, regional governments then have the authority to grant mining business licences within these pre-determined areas. Under this approach, it is expected that the Central Government will have more control over the determination of areas open for mining, and that this will reduce the instances of overlapping mining concessions with areas reserved for other purposes, such as forestry. However the complexity of adjudicating the competing claims of different land users has made this mapping exercise difficult and drawn out.

The implementing regulations which support the Mining Law also set up the framework for determining the annual Domestic Market Obligation ("DMO") for producers, as the Indonesian Government seeks to ensure a sufficient supply of natural resources to meet the expected growth in domestic demand as investment in infrastructure expands. So far this DMO has only been applied to coal production, for which domestic coal demand is likely to continue increasing given the Government's 35 GW power programme to improve Indonesia's electrification rate. Approximately 60% of the electricity capacity from this programme is expected to be generated from coal-fired power plants.

Mining licence holders are also required to demonstrate a greater level of responsibility for operation with the regulations requiring them to undertake some of their own mining activities rather than subcontracting them entirely to third parties. In circumstances where subcontracting is permitted, priority must be given to Indonesian-owned companies. In addition, since 12 January 2014, mineral licence holders have been required to carry out certain minimum levels of in-country mineral processing prior to export. During the period from 12 January 2014 to 11 January 2017, exports of concentrates were still permitted, subject to fulfilling certain requirements including a commitment to build or contribute to development of processing facilities and the payment of a progressively increasing rate of export duty. In January 2017, the Government issued GR 1/2017 and PerMen 5/2017 (as amended by PerMen 28/2017) which set out new minimum requirements for in-country processing and refining and export of mineral commodities. Under these new regulations, which have been seen as a relaxation of the ban on export of unprocessed ores, holders of *Izin Usaha Pertambangan Operasi Produksi* ("IUP-OP"), IUPK-OP and Processing and Refining IUPs may still export certain approved quantities of unprocessed or semi-processed product for a period of five years from 11 January 2017, upon payment of export duties and after satisfaction of the minimum domestic processing and refining requirements.

This theme of ensuring that more of the benefits of Indonesia's mining activity are retained and reinvested in Indonesia has been reinforced in the implementing regulations for the Mining Law that have been issued over the last eight years. Key implementing regulations which have been issued to date include:

- The requirement for the divestment of up to 51% of Operation Production IUP ("IUP-OP") interests held by foreign investors by the end of the 10th year of production;
- Restrictions on the export of unprocessed mineral ores (except for certain low-grade nickel ores and washed bauxite) and the requirement for further in-country processing. This includes recent regulations issued requiring CoW holders to convert their contracts into IUPK-OPs, i.e. CoW holders will not be granted approval to export before converting to IUPK-OPs;
- The requirement for each export to be verified by a surveyor appointed by the Government;
- Imposing minimum DMOs for coal;
- Imposing a benchmark pricing framework for coal and mineral exports to set a minimum price for transactions involving such commodities; and
- Specific pricing for coal used in mine mouth power plants.

While the GRs issued to date provide further details regarding the implementation of the Mining Law, there is still a lack of clarity in relation to some of the more recent regulations, such as the divestment, in-country processing and CoW/CCoW conversion requirements. At present, there still appears to be some reluctance on the part of investors to make significant investment decisions until these matters are resolved.

Most mineral and coal prices declined over recent years but showed improvement in 2016

Most mineral prices have declined over recent years given uncertainty around demand from China and other slowing emerging markets such as Brazil and Russia. This was particularly pronounced at the beginning of 2016 with fears of a "hard landing" for China. However, mineral prices continued to improve throughout 2016. The uptick in mineral prices in 2016 was driven by a number of factors. The price of gold for example is not driven by demand fundamentals but rather by reactions to general economic uncertainty, including most recently the concerns around Brexit, the US presidential election, and the US Federal Reserve's interest rate policies. Physical gold demand was very weak in 2016, and fell in the two largest consuming countries — India and China. Recent moves by the Fed to increase interest rates may put pressure on gold prices.

The prices of some base minerals (iron ore, nickel, tin, and copper) have been favourably impacted in 2016 by the better-than-expected performance in the property and infrastructure sectors in China. China's policy efforts to boost the commodity-intensive infrastructure and construction sectors has been a key driver of demand in 2016, which appears to be continuing into 2017. Going forward, China will continue to play a key role in the demand mix for these minerals as its share of of world metal consumption rose above 50 percent in 2015 and the country has accounted for a large part of global economic growth over the past 15 years. However, the transition to a consumption-led economy, along with industrial sector reform and environmental concerns, is expected to slow demand growth for raw materials. A key driver of uncertainty impacting the price of many minerals is the level of steel demand and production in China.

Supply constraints have also affected the prices of some minerals in 2016. For example, the tin price was affected by mine closures in China enforced by the Government due to environmental issues. Tin production in Indonesia, the world's largest exporter of tin, also declined as the Indonesian government sought to limit export quotas to deal with illegal mining and reserve depletion.

Nickel price movements in 2016 were affected by the loss of ore output in the Philippines due to the environmental audits of mines completed by governmental authorities in September 2016. Approximately 30 mines (most of which are nickel mines) were suspended as a result of the audits. As the Philippines is one of the world's largest nickel exporters, these suspensions have had a considerable impact on global nickel prices, particularly as supply was still hamstrung by Indonesia's restriction on export of unprocessed ore.

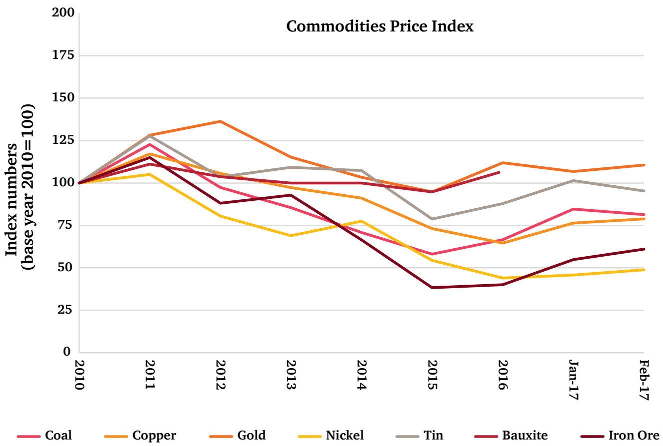
Thermal coal suffered a similar story. Since 2012, coal prices have declined roughly 15% per annum. This was largely due to softening demand from China, linked to China government policy, such as:

- Desire for a managed economic slowdown;
- Restriction on high ash/sulphur content for environmental reasons;
- Import tariffs to discourage coal use; and
- China's gradual move away from coal-fired power in favour of renewables.

However, starting from the second half of 2016, coal prices surged after a sharp decline in production and coal stocks, resulting from the Chinese Government's directive to coal mines to produce only on a 276-day basis, instead of the previous 330-days. Seaborne supplies of coal have also been limited due to the low price environment, supply constraints, and unfavorable demand prospects for coal.

The very high coal prices as seen in late 2016 are unlikely to be sustainable. In September 2016, the Government of China relaxed the 276-day policy by allowing some coal mines to temporarily produce on a 330-day basis to raise output in the fourth quarter of 2016. This policy together with increasing coal supply in response to prices began to show effect as coal prices (ex-Newcastle) rebalanced to a level of around US$80/tonne in the first half of 2017, having reached a level exceeding US$100/tonne at the end of 2016. China's coal policies will be key, given that the country consumes half of the world's coal output and coal still accounts for nearly two-thirds of the country's energy consumption.

Demand in Southeast Asia, particularly Indonesia, for the build out of the 35GW power programme, as well as demand from India, may support coal prices in the medium term. While India has now surpassed China as the main buyer of Indonesian coal, there are clearly risks in relation to Indian Government policy, and competition from other producing countries.



Source: World Bank, U.S. Geological Survey, PwC Analysis

Indonesian production of coal and most minerals increased in 2016, after a decline in 2015

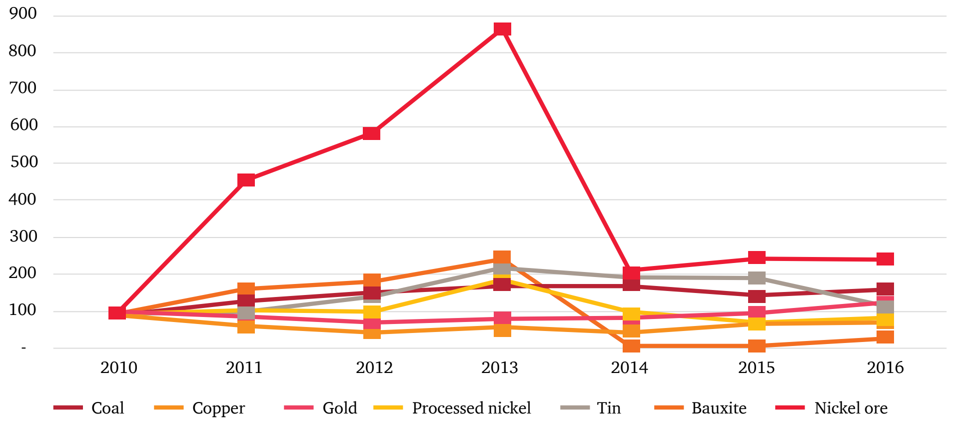
Despite the coal price decline during 2012 and 2013 Indonesia recorded increases in coal production during those years. Demand was strong from coal-fired power plants around the world, especially from plants in China and India during that period. In addition, a number of new power plants have come on-line since mid-2008 both in Indonesia and abroad. In 2014 thermal coal production decreased only slightly to 458 million tonnes, despite some attempts from the Government to limit production increases. In 2015 Indonesia saw a significant reduction in thermal coal production for the first time in many years, with the Government's official figures showing a decrease of 14% to 392 million tonnes. In 2016, the Government targeted an increase in thermal coal production to 419 million tonnes, expecting more demand from newly constructed coal-fired power plants. The actual result exceeded this target by 3.6% due to the significant increase in thermal coal prices in the second half of 2016. Consistent with expectations of increasing demand in Indonesia, coal supplied to the domestic market in 2016 increased by 14% to 91 million tonnes (up from 80 million tonnes in 2015). Given the Government's aggressive plans for coal-fired power as part of the 35 GW electrification programme, of which coal represents approximately 60%, domestic demand for coal will continue to increase.

There were no significant changes in the production levels of gold, copper and nickel during 2015, other than an increase in copper after delays in export permits for copper concentrate heavily impacted the 2014 volumes. In 2016, gold production increased by a considerable 20%, mainly in response to the higher gold prices while tin production decreased by a significant 63%, as a result of the Indonesian government's efforts to limit export quotas to deal with illegal mining and reserve depletion, and also due to the suspension of operations in several tin mines due to environmental related issues.

It is expected that the production of tin and copper will slow in 2017, considering the continuing efforts by the Indonesian Government to fight illegal tin mining and new regulations issued in

early 2017 requiring several large copper producers to convert their CoWs into IUPK-OPs prior to approval for export being granted. It is anticipated that copper production and exports will be heavily impacted by this new regulation in 2017. On the other hand, increases in the production of nickel ore, processed nickel and bauxite are expected in 2017 due to the relaxation in the ban on exports of nickel ore and washed bauxite by the Indonesian Government in the beginning of 2017 and anticipated new nickel smelters coming on line in 2017.

Historical Indonesian coal and minerals production trends are presented in the diagram below (indexed to the base year 2010 = 100 tonnes).



Source: Indonesia Coal Mining Association, U.S. Geological Survey, PwC Analysis

Although Indonesia is well placed geologically to capitalise on the continuing global demand for commodities, outstanding issues in relation to implementing regulations for the Mining Law need to be resolved to give investors the certainty needed to commit investment funds to Indonesia.

Photo source : PT Bukit Asam (Persero) Tbk

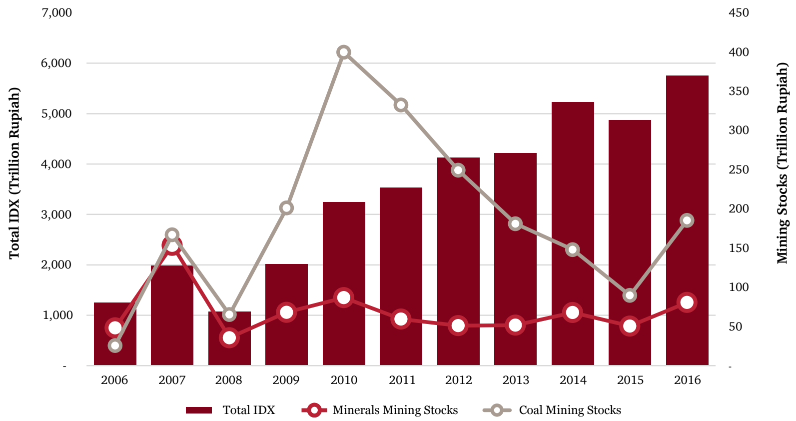
Market capitalisation of Indonesian mining stocks trending in line with commodity prices

Consistent with falling commodity prices and the negative trend in profitability over recent years, the performance of mining stocks on the Indonesia Stock Exchange ("IDX") was lacklustre in 2015. The total market capitalisation of mining stocks on the IDX fell significantly from Rp 216 trillion at 31 December 2014 to Rp 140 trillion at 31 December 2015, a decrease of 35%. This compares to a decrease of only 7% in market capitalisation for the Indonesian stock market as a whole over the same period. By the end of 2015, the market capitalisation of listed mining companies in Indonesia represented only slightly more than a quarter of its value in 2010, demonstrating the continued lack of confidence from investors in the mining sector driven by the historical performance of mining companies and the negative commodity price outlook.

In 2016, the prices of most mining commodities were much improved. Although there is a concern that such price improvement is not supported by improved demand fundamentals, it appears this contributed to restored investor confidence in mining stocks. The total market capitalisation of mining stocks on the IDX soared 90% from Rp 140 trillion at 31 December 2015 to Rp 266 trillion at 31 December 2015 – noting that over the same period, market capitalisation for the Indonesian stock market as a whole only increased by about 18%. Of this increase, the most significant contribution was from coal mining companies listed on the IDX. The market capitalisation of these coal stocks increased from Rp 90 trillion at 31 December 2015 to Rp 185 trillion at 31 December 2016, an increase of 105% while the market capitalisation of listed metal and minerals mining companies on the IDX only increased by about 59% from Rp 51 trillion at 31 December 2015 to Rp 81 trillion at 31 December 2016.

As can be seen in the following chart, the movements in market capitalisation of listed coal and mineral mining companies on the IDX generally follows the fluctuation in commodity prices.

Market Capitalisation of
Listed Coal and Mineral Mining Companies in Indonesia



Source: IDX
Note: The market capitalisation of listed mining companies in the above chart only includes coal, metal and mineral mining companies listed on the IDX

Indonesian mining exploration – time for a reset?

Photo source : PT Aneka Tambang (Persero) Tbk

Exploration is the lifeblood of the mining industry. Unfortunately, exploration spending, particularly in greenfield areas, has been virtually stagnant in Indonesia for a number of years. This situation has now been compounded by a sustained downturn in global commodity prices.

Similar to other countries, Indonesia is not immune to the commodities downturn. Since the fall in commodity prices in 2012, Indonesian mining companies have consistently reported a drop-off in their revenues and profitability. In response to falling commodity prices (and in many cases high leverage), Indonesian mining companies have shifted their attention from increasing production and development to cutting operational expenditure, and focusing on easier-to-mine mineral deposits, while curtailing capital expenditure. All of these have led to an essentially stagnant mining investment environment in Indonesia in recent years.

Based on data published by the Ministry of Energy and Mineral Resources, total investment in the Indonesian mining sector decreased by approximately 31% from US$7.4 billion in 2014 to US$5.2 billion in 2015. An independent survey of industry players conducted by PwC Indonesia showed similar results (noting that the survey only covers a sample of miners).

Survey results	2015 US$ million	2014 US$ million	Year-on-year movement
Greenfields exploration spending	29	36	↓ -20%
Other exploration and feasibility	58	75	↓ -22%
Total exploration	87	110	↓ -22%
Development	126	198	↓ -36%
Fixed assets	1,701	2,109	↓ -19%
Total investment	1,913	2,418	↓ -21%

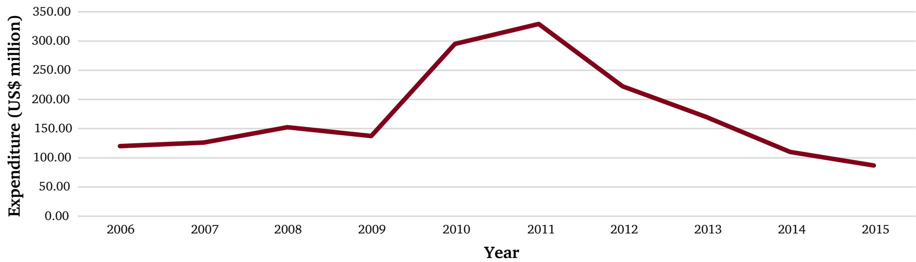
Source: PwC Analysis

Government data	2015 US$ million	2014 US$ million	Year-on-year movement
Total investments, as reported by the Government	5,152	7,430	↓ -31%

Source: The Ministry of Energy and Mineral Resources

Perhaps more significantly, when we consider only exploration spending, the sample of miners surveyed by PwC indicates that total exploration spending fell in 2015, for the fourth consecutive year, by 22% to US$ 87 million (the average for 2010-2014 was US$ 113 million). As can be seen in the following chart, this decline generally follows the decline in commodity prices.

Exploration Spending Trend of Indonesian Mining Companies



Source: PwC Analysis

Consistent with our surveys over the last several years, Indonesia is still yet to capture a fair proportion of the global exploration spend despite its acknowledged geological potential. As indicated in the chart below (which compares exploration spending in Indonesia based on PwC surveys and the global exploration budget based on SNL Metals & Mining's analysis), Indonesia has consistently received less than 2.5% of the global exploration budget during 2006-2015, and only around 1.0% in 2015 and 2016, which is extraordinarily low compared to its mineral potential.

Source: SNL Metals & Mining, PwC Analysis

International surveys of mining companies continue to rank Indonesia highly in terms of mineral prospectivity, but poorly in terms of its mineral policies and investment climate. Based on the latest survey issued by the Fraser Institute in February 2017, the global perception of the Indonesian mining sector is deteriorating. In terms of the policy perception index which gauges how friendly government policy is in the mining sector, Indonesia is ranked very poorly (99 out of 104 countries being analysed), a drop from rank 91 from 109 countries based on the previous survey.

2016 was a difficult year for the mining industry, both globally and in Indonesia, with continuing softness in commodity prices until late in the year causing reluctance to invest in exploration and development. In Indonesia this comes with continued uncertainty in the mining regulatory environment, which has dampened the appetite for investment – and has likely reduced the level of exploration, production, Government earnings, and export proceeds by more than the impact of low commodity prices alone. Many major international mining companies have left Indonesia, while still investing elsewhere, sometimes even in countries with far less geological potential.

This has in large part been due to challenges in implementing the new mining law since 2009 – particularly in relation to foreign investment in the mining sector; the desire for onshore beneficiation of mining products; and land management issues – including the competing interests of forestry and mining operations. While the stated aim of much of this new regulation – increasing the value-add of the sector to Indonesia, and supporting jobs and long-term growth in the economy – is good, the timing was unfortunate, and has meant that the sector significantly underperformed its potential.

This is particularly the case with the implementation of the in-country downstream processing requirements for minerals, and the ban on exports of unprocessed ores since 2014. At a time when many refined products are in over-supply globally, and Indonesia's economic growth does not yet fully support sufficient local demand, many projects are not economically feasible. In January 2017, the Indonesian Government has sought to address this by issuing a regulation which under certain circumstances relaxes the export ban for low-grade nickel ores and washed bauxite – this gives rise to its own issues, given that some investors have commenced investment in downstream processing facilities relying on the requirement for in-country beneficiation.

Uncertainty regarding contract extensions; foreign divestment rules; potential changes in royalty rates; and delays in tenders for coal-fired power plants have also impacted the coal sector in recent years.

The uncertainties described above result in increased investment risk which has meant that foreign investment in particular has waned, and as a result the industry is no longer dominated by large, long-term mining companies, but more by short term financial investors – which may not bring the long-term sustainable benefits the Government is looking for. This type of investment also does not focus on greenfield exploration, but more on known deposits, putting reserve replacement at risk.

The continued lack of exploration spending in Indonesia over the last decade is clearly a worrying sign as exploration spending is the lifeblood of the mining sector. The low level of greenfields exploration activity is a significant threat to the long-term success of the industry and may adversely affect the future growth of the Indonesian economy. An increase in exploration, discovery and development of new deposits is essential to sustain the industry over the longer term. Without substantial greenfield exploration in the coming years, we are unlikely to see significant new mine developments in Indonesia, other than for existing known deposits.

The mining industry is a high cost, capital intensive industry. Without certainty regarding laws and regulations affecting the mining business in Indonesia, there is unlikely to be significant new investment, even with an improvement in commodity prices. This is particularly the case in the minerals sector, given the comparatively higher investment costs relative to coal mining, and despite many under-explored areas of the country. This is only exacerbated by the current low price environment. This situation will continue to be a drag on growth in the industry in Indonesia in 2017 and beyond and should be an area of focus for the Government.

Given reported plans for a new mining law, this is perhaps the best time for the Government to provide the mining industry in Indonesia with the necessary stimulus to invest by providing a regulatory framework that:

- Removes hurdles to exploration investment such as uncertain and uneconomic foreign divestment rules;
- Simplifies permitting at the licensing stage (e.g. direct application for concessions rather than tenders);
- Provides incentives at the exploration stage when risk capital is required from the investor (e.g. waive Value Added Tax ("VAT") during exploration, tax credits when production commences, assistance with land acquisition/compensation, etc.); and
- Encourages exploration to support long-term downstream processing initiatives.

There are some clear steps that can be taken to work towards a better framework for investment in exploration in Indonesia. Some things to consider include:

- Preparing a detailed economic study of the benefits to the Indonesian national and regional economies derived from each of the exploration, mining production, and downstream processing phases of a mining life cyle. This should make clear the often overlooked benefits to the economy derived from exploration and development of mines;
- Designing best practice mining policy covering among others: streamlining exploration phase permits; tax, royalty and other incentives; improving the foreign ownership regime, etc.; and
- Development of a strategic national mining policy, with the buy-in of all stakeholders – both central and regional governments, as well as the mining industry. Perhaps most importantly, there needs to be clear coordination and consistent policy implementation by the various arms of Government – a perennial concern of investors.

Exploration is the lifeblood of the mining industry. Reserve replacement is urgently needed if Indonesia is to remain a major mining country.

Regulators need to find a balance between securing state revenue and attracting investment (and particularly greenfields exploration investment) and developing a sustainable mining industry. An investor-friendly mining regulatory regime is needed to boost the sector.

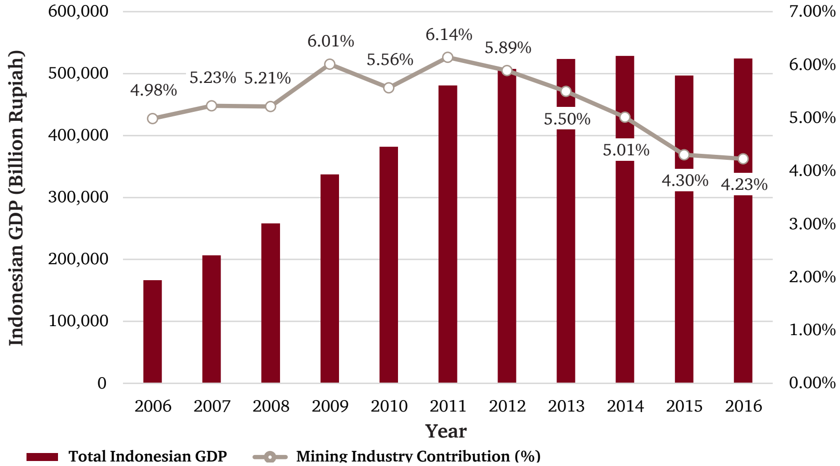
Mining is a cyclical business. Global mining companies will again come hunting for projects in high potential geographies – the question is whether Indonesia can establish an attractive and competitive mining investment framework before the next round of investments. Now may be the time for a reset.

Mining industry contribution to the Indonesian economy is on the wane

The mining sector has been one of the key sectors supporting Indonesia's economic growth for many decades. The sector makes a significant contribution to Indonesian Gross Domestic Product ("GDP"), exports, government revenue, employment and, perhaps most importantly, the development of many remote regions of Indonesia which otherwise may not have occurred to such an extent or at such a pace. Mining companies are in many cases the only significant employers in some of these remote areas.

While it remains a significant contributor to the Indonesian economy, it appears that the mining sector's contribution to the Indonesian economy is waning. Mining industry contribution to Indonesian GDP has continually declined from 6.14% in 2011 to 4.23% in 2016. The trend appears positively correlated with fluctuations in commodity prices – with a higher contribution in years of high mineral and coal prices. In 2016, the mining industry contributed approximately 4.2% to Indonesian Gross Domestic Product. However, the industry represents a much larger share of the regional economies of many provinces including Papua, Central Sulawesi, Bangka-Belitung, West Nusa Tenggara and East Kalimantan.

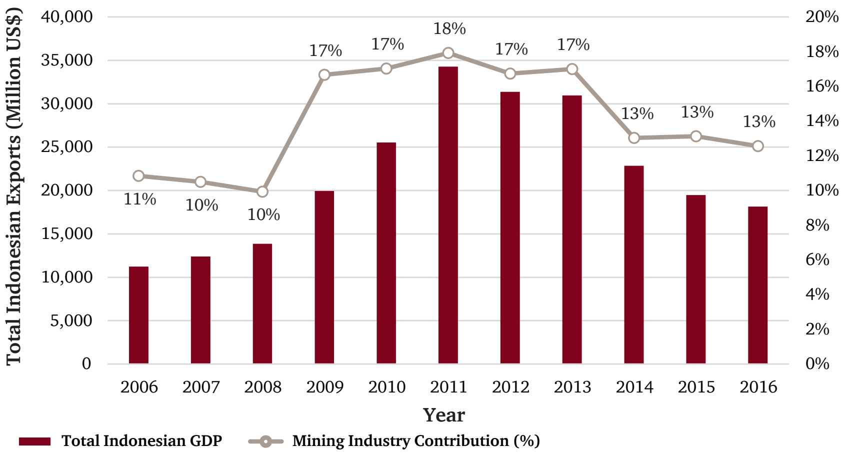
Mining industry contribution to Indonesian GDP



Source: Bank Indonesia

The mining sector contributes a higher proportion of Indonesian exports, particularly as mining products are generally priced in US dollars, however, the contribution of the sector to Indonesian exports has also fallen off in the last few years. The implementation of the ban on exports of unprocessed (or not-sufficiently processed) minerals in January 2014 and the introduction of a significant (and progressively increasing) export duty on mineral concentrates, have resulted in an ongoing decline in mineral production over recent years. The mining industry's contribution to total Indonesian export revenues during 2014-2016 was however consistent at 13% (down from 17% in 2013). The Government, however, hopes that the total contribution of the mineral sector will increase once mineral processing and refining facilities are in place, generating higher value products and when the relaxation of the export ban on low-grade nickel ores and washed bauxite takes effect in 2017.

Mining products as a % of total Indonesian exports



Source: Bank Indonesia

Photo source :
PT Aneka Tambang (Persero) Tbk

2.0 Regulatory Framework

2.1. Introduction

Mineral and coal mining activities are governed under the Law on Mineral and Coal Mining No. 4 of 2009 (the "Mining Law"). This law replaced the previous Mining Law 11/1967, which provided the framework for all of Indonesia's pre-2009 mining concessions including all of the existing CoWs and CCoWs.

The introduction of the Mining Law in 2009 represented a significant change from the previous Indonesian mining regulatory regime. Contractually-based concessions are no longer available for new mining projects. Both the well-regarded CoW/CCoW framework for foreign investors and the Mining Rights (*Kuasa Pertambangan*, or "KP") framework for Indonesian investors were replaced by a single area-based licensing system based on specified mining areas.

Since its introduction in 2009, the Mining Law has faced many challenges. Some of the issues that are still being dealt with include foreign ownership restrictions, domestic processing requirements and CoW/CCoW conversions to the new licensing system. Although it has been eight years since the Mining Law was introduced, the industry is still transitioning towards compliance with the current Mining Law.

During 2016 there has been talk of a new mining law being drafted with the aim of addressing many of these issues. At the time of writing there is not yet any indication of when the draft mining law may be finalised.

The key objective of the Mining Law is to support sustainable national development, therefore it imposes the following requirements on investors in conducting their mining activities:

- Good mining practices;
- Increase the value add of mining products;
- Improve society;
- Cautious on environmental impact; and
- Good governance and bookkeeping.

To support the above, the Mining Law is dependent on a significant number of implementing regulations to provide detailed guidelines on how it will be administered. Most of the fundamental implementing regulations have been issued, although some clarifications are still required. At the time of writing, nine Government Regulations ("GRs") (including amendments) have been issued in respect of:

- Mining Areas (GR 22/2010);
- Mining Business Activities (GR 23/2010 as amended by GR 24/2012, GR 1/2014, GR 77/2014 and GR 1/2017);
- Reclamation and Mine Closure (GR 78/2010);
- Mineral and Coal Mining Direction and Supervision (GR 55/2010); and
- Types and Tariffs of Non-tax State Revenue Applicable in the Ministry of Energy and Mineral Resources (GR 9/2012). Please note that GR 9/2012 was not issued specifically as an implementing regulation of the Mining Law, however it provides guidance on the rates of production royalty that an IUP/IUPK holder should pay. Please refer to discussion in Section 2.6 "Royalties and fiscal regime" of this Guide regarding this GR.

A number of Ministerial Regulations ("PerMen") have also been issued by the Minister of Energy and Mineral Resources ("MoEMR"). Some of the key regulations relate to:

- Mining Services (PerMen 28/2009, as amended by PerMen 24/2012);
- DMO (PerMen 34/2009);
- Benchmark Price on Metal Minerals and Coal (PerMen 7/2017);
- Benchmark pricing on Non - Metal Minerals (PerMen 17/2010);
- Increasing Mineral Value Added through Processing and Refining Activities (PerMen 5/2017, as amended by PerMen 28/2017);
- Mine Reclamation & Closure (PerMen 7/2014);
- IUP Area Tender Procedures and Special IUP Areas in Metal Minerals and Coal Mining (PerMen 28/2013);
- Determination of Mining Areas (PerMen 37/2013);
- Detailed Procedures for Granting Operation Production IUPs and IUPKs (PerMen 32/2013 as amended by PerMen 32/2015);
- Procedures and Requirements for the Granting of Recommendations for the Export of Processed and Refined Minerals (PerMen 6/2017);
- Divestment Procedure and Mechanism of Price Determination for Divestment Shares (PerMen 9/2017);
- Coal Price Determination for Mine Mouth Power Plants (PerMen 9/2016 as amended by PerMen 24/2016);

- Mining Area Stipulation Procedures (PerMen 12/2011 as amended by PerMen 25/2016);
- Authority Delegation for Mining Licence Issuance (PerMen 25/2015);
- Change of Capital Investment (PerMen 27/2013); and
- Procedures for the Issuance of IUPK-OP as the Continuation of Operations of CoW/CCoW (PerMen 15/2017).

The Director General of Minerals and Coal ("DGoMC") has also issued a number of regulations/circular letters with some of the key ones in respect of:

- Royalty calculations;
- Benchmark price (including Adjustment Costs and Benchmark Prices for certain types and uses);
- DMO Credits;
- Affiliates;
- Procedures and Requirements for Issuing Recommendations for Registered Coal Exporters; and
- Production Costs for Determining the Coal Price for Mine Mouth Power Plants.

In addition to the above regulations, the Minister of Finance ("MoF") also issued PMK No.13/PMK.010/2017 regarding "Stipulation of Exported Goods Subject to Export Duty and Rates of Export Duty" to support the implementation of PerMen 6/2017. Please refer to Section 2.5 "Mandatory in-country processing and export restrictions" of this Guide for further discussion regarding PMK No.13/PMK.010/2017.


Photo source : PT Bukit Asam (Persero) Tbk

The hierarchy of the current regulatory framework is illustrated in the diagram below:

Mining Law
No.4/2009

Government Regulations

- **Mining Areas** GR 22/2010
- **Mining Business Activities** GR No. 23/2010, as amended by GR 24/2012, GR 1/2014, GR 77/2014 and GR 1/2017
- **Mine Reclamation & Closure** GR 78/2010
- **Mineral and Coal Mining Direction and Supervision** GR 55/2010
- **Royalty Rates** GR 9/2012

MoEMR Regulations

- **Mining Services** PerMen 28/2009, as amended by PeMen 24/2012
- **DMO** PerMen 34/2009
- **Benchmark Pricing** PerMen 7/2017 PerMen 17/2010
- **Increasing Mineral Value Added Through Processing and Refining Activities** PerMen 5/2017, as amended by Permen 28/2017
- **Mine Reclamation and Closure** PerMen 7/2014
- **IUP Tender Procedures** PerMen 28/2013
- **Determination of Mining Areas** PerMen 37/2013
- **Detailed Procedures for Granting Operation Production IUPs / IUPKs** PerMen 32/2013, as amended by PerMen 32/2015
- **Procedures and Requirements for the Granting of Recommendation for the Export of Processed and Refined Minerals** PerMen 6/2017
- **Divestment Procedures and Mechanism of Price Determination** PerMen 9/2017
- **Coal Price Determination for Mine Mouth Power Plants** PerMen 9/2016 as amended by PerMen 24/2016
- **Mining Area Stipulation Procedures** PerMen 12/2011 as amended by PerMen 25/2016
- **Authority Delegation for Mining Licence Issuance** PerMen 25/2015
- **Change of Capital Investment** PerMen 27/2013
- **Procedures for the Issuance of IUPK-OP as the Continuation of CoW/CCoW** PerMen 15/2017

DGoMC Circulars

- **Royalty Calculations** No. 32.E/35/DJB/2009
- **Adjustment Costs for Coal Benchmark Prices** No. 515.K/32/DJB/2011 No. 999.K/30/DJB/2011 No. 644.K/30/DJB/2013
- **Coal Benchmark Price for Certain Types and Uses** No.480.K/30/DJB/2014
- **DMO Credits** No. 376.K/30/DJB/2010
- **Affiliates** No.376.K/30/DJB/2010
- **Procedures and Requirement for issuing Recommendation for Registered Coal Exporter** No. 714.K/30/DJB/2014
- **Coal Benchmark Price for Mine-Mouth Power Plant** No. 953.K/32/DJB/2015

2.2. Mining areas

Mining can only be conducted in areas designated by the Central Government as open for mining. As such, the Central Government is required to designate the mining areas (referred to in Bahasa Indonesia as *Wilayah Pertambangan* – "WP"). WPs are categorised as follows:

- Commercial mining business areas (*Wilayah Usaha Pertambangan* – "WUP") representing mining areas for larger scale mining;
- State reserve areas (*Wilayah Pencadangan Negara* – "WPN") representing areas reserved for the national strategic interest; and
- People's mining areas (*Wilayah Pertambangan Rakyat* – WPR") representing mining areas for small-scale local mining.

In determining the WPs, the Central Government (with the assistance of provincial and regional governments) has carried out a detailed mapping exercise and is preparing a map of areas open for mining. The areas identified as mining areas will not necessarily be available exclusively for mining and may include other uses such as forestry. Under the regulation, the map may be updated every five years.

On 24 December 2013, the MoEMR issued PerMen 37/2013 providing technical criteria to determine the WPs as follows:

- Having the spread of rock formations of the relevant mining product;
- The mining product's indicative data is available;
- The mining product's potential data is available; and
- There is mineral or coal reserve data.

At the time of writing, this mapping process was still ongoing and, since the final map of designated areas must be approved by Parliament, this process may take some time.

It should be noted however, that one key positive step taken by the Government is the establishment of a "clean and clear" list of mining licence areas which have been verified by the DGoMC and declared to be valid and free of competing claims. This list, which can be accessed on the DGoMC website, indicates that between January–March 2017 only approximately 30% of the nearly 3,600 existing mining licences have applied for and been granted "clean and clear" status. There are indications that the MoEMR may revoke IUPs which fail to obtain the "clean and clear" status.

2.3. Mining licences

Within the designated mining areas (or WPs), mining licences may be issued to one or more parties as follows:

- An IUP is a general licence to conduct mining business activities in a WUP area;
- An IUPK is a licence for conducting mining activities in a specific WPN area in which mining business activities can be carried out; and
- An *Izin Pertambangan Rakyat* ("IPR") is a licence for conducting a mining business in a WPR area of limited size and investment. IPRs are not available to foreign investors.

The comments in this guide are directed primarily at IUPs and IUPKs. For further information on the IPR requirements please contact one of our advisers.

Ownership of mining licences

An IUP may be issued to the following entities:
- A business entity (established under the laws of Indonesia);
- A cooperative; or
- An Indonesian individual (including a partnership).

The business entity must be an Indonesian legal entity. This includes (1) Indonesian companies wholly-owned by Indonesian nationals i.e. a Limited Liability Company ("PT"); (2) Domestic Investment companies (*Penanaman Modal Dalam Negeri*, or PMDN); and (3) Indonesian companies with foreign shareholding (*Penanaman Modal Asing*, or "PMA"). Under the previous Mining Law 11/1967, a CoW/CCoW could be held by either foreign or domestic investors, whilst a KP could only be issued to domestic investors.

The Mining Law therefore removes some of the distinctions between Indonesian and foreign investors in the mining sector, and is consistent with the current Negative List on Foreign Investment issued by *Badan Koordinasi Penanaman Modal* ("BKPM"), or the Indonesian Investment Coordinating Board, which allows 100% foreign investment in the mining sector, subject to the share divestment rules discussed below.

One mining licence per company

A key feature of the Mining Law is that a privately held company can only hold one licence (i.e. one IUP/IUPK) and only companies listed on the IDX and companies granted non-metal mineral and/or rock WIUPs are entitled to hold more than one licence. The most recent regulations seem to have relaxed this requirement and in certain circumstances an IUP or IUPK can be transferred to an IUP/IUPK holding entity although details of the procedures for such transfers still require further clarification.

As a transitional rule, a privately held company which held multiple KPs prior to the new Mining Law may convert these to IUPs and may continue to hold them within the same company. Any new licence applications will however, need to be made through a separate company. It is thought that the new transfer rules set out in GR 24/2012 may be intended to facilitate the restructuring of companies holding multiple IUPs pursuant to the transitional provisions.

For further details of how this restructuring could be beneficial please contact one of our advisers.

Exploration and Production licences

A mining company obtains an IUP or IUPK for two separate phases of mining activities as follows:
- Exploration: An Exploration IUP/IUPK is granted for the performance of general surveys, exploration and feasibility studies within a WUP/WPN area; and
- Operation Production: An Operation Production IUP/IUPK is granted for performing construction, mining, processing, refining, hauling and selling within the WUP/WPN area.

Under GR 77/2014, if an IUP-OP holder does not undertake transport and sales activities these activities could be performed by another entity which holds a special IUP for transport and sales and if an IUP-OP holder does not undertake processing and refining activities these activities could be performed by either:
- Another IUP-OP holder which has processing and refining facilities; or
- Another entity which holds a special IUP for processing and refining.

Specific licences

Entities which do not themselves own mines, but rather intend to engage solely in trading, processing and refining activities are still required to obtain a special IUP-OP. However, these licences are distinguished by the specific activities which the holders intend to perform:

- Transport and Sales IUP-OP (for companies engaged in the coal/minerals transportation and trading business);
- Processing and/or Refining IUP-OP.

PerMen 32/2013 (as amended by PerMen 32/2015) formalises the requirements for those wishing only to apply for these Transport and Sales IUP-OPs and Processing and/or Refining IUP-OPs and imposes a number of new restrictions on these activities. In PerMen 32/2015, these requirements are waived for companies domiciled within an industrial area who perform mining activities for non-commercial purposes.

To obtain a Processing and/or Refining IUP-OP, a company must first obtain an In-principle Licence (or *Izin Prinsip*). Only when an In-principle Licence has been obtained, a company can submit an application to upgrade the In-principle Licence to a Processing and/or Refining IUP-OP. Interestingly, obtaining the Processing and/or Refining IUP-OP does not mean that commercial operations may commence. The relevant issuing authority must evaluate whether the company meets the operational feasibility requirements before approving commercial production.

The key restrictions, and rights and obligations of each type of specific IUP-OP are outlined below:

	Transport and Sales IUP-OP	Processing and/or Refining IUP-OP
Rights	• Conduct the purchase of mining commodity products from holders of IUP-OP, IUPK-OP, Processing and/or Refining IUP-OP, IPR, and/or other Transport and Sales IUP-OP that have "clean and clear" certificate; • Conduct transportation and sale of minerals or coal purchased • Establish and or utilize the facility and infrastructures of transportation and sales such as stockpiles, docks, or special ports according to the provisions of laws and regulations.	• Buy and transport mining commodities that will be processed and/or refined in accordance with the cooperation agreement document approved by relevant authority; • Transport and sell mining commodities that has been processed and/or refined; • Make cooperation agreement with other party ifor the utilisation of by-products of processing and/or refining for domestic industrially raw materials; • Conduct blending of mining commodities product to meet buyer specification; • Obtain related licenses in accordance with the provisions of laws and regulations; and/or • Utilize the facilities of transportation infrastructure facilities and docks or ports
Obligations	The obligations of holders of Transport and Sales IUP-OP and Processing and/or Refining IUP-OP are broadly similar, as follows: • Submit annual work program and budget; • Submit monthly, quarterly and annual activity reports; • Sell coal/minerals with reference to Government benchmark prices; • Comply with any onshore value adding requirements e.g. in country processing; • Prioritize the fulfillment of domestic needs; • Submit the report when establishing the facility of transportation and facility of loading that will be used;	

	• Support the development and empowerment of community in region that is exposed to activity impact; • Prioritize the utilisation of local workers, goods and service; • Obey the provisions of law and regulations in the field of traffic and road transport when using the public road facilities; and • Responsible for the work and environment safety and health caused by activity of transportation and sales business;	
Restrictions	• Sell minerals or coal to the holders of Transport and Sales IUP-OP issued by the same issuing authority, e.g. the holder of Transport and Sales IUP-OP issued by regent/mayor is prohibited to sell mineral or coal to a holder of Transport and Sales IUP-OP issued by the same regent/mayor however it can sell mineral or coal to a holder of Transport and Sales IUP-OP issued by the governor or MoEMR; • Conduct transportation and sales of mining products that come from parties (e.g. holder of IUP-OP, IUPK-OP, Processing and/or Refining IUP-OP, etc.) which do not have clear and clean certificate; • Transfer its IUP to another party; • Approval of the relevant issuing authority is required before any transfer of the shares in an IUP-OP holder occurs.	• Conduct the processing and/or refining of mining products that come from parties (e.g. holder of IUP-OP, IUPK-OP, Processing and/or Refining IUP-OP, etc.) which do not have "clean and clear" certificate; • Transfer its IUP to other party; • Approval of the relevant issuing authority is required before any transfer of the shares in an IUP-OP holder occurs. However, it appears that no such approval is required for a share transfer when the company is holding only a Principle Licence.

Based on the transitional provisions of PerMen 32/2013, the Transport and Sales IUP-OP holder can cooperate with CoW/CCoW holders provided that they are in compliance with the provisions in PerMen 32/2013 – noting that any existing agreement with a CoW/CCoW holder should have been adjusted in accordance with the provisions in PerMen 32/2015 by 18 November 2015.

Temporary Licences

In situations where the mining of coal and/or minerals is ancillary to some other main activity the following temporary licences are available:

- Temporary Transport and Sales Licence: granted to a mining company to allow the sale of coal and/or minerals extracted during the exploration phase; and
- Temporary IUP for Sales Licence: granted to a company which is not in the mining business (e.g. road construction) which excavates coal and/or minerals as part of its activities. This licence is required regardless of whether the company intends to sell or use the coal and/or minerals.

Both temporary licences have associated restrictions, among others:

- The licence can be issued only once, cannot be extended, and is granted for a specific quantity of coal and/or minerals;
- The licence holder must pay production royalties on the coal and/or minerals sold; and
- The coal and/or minerals must be sold domestically.

The licences are granted by the relevant authority in accordance with the location from which the coal and/or minerals are excavated (see the table below in the section "Authority to issue an IUP/IUP-OP/Specific Licence").

Authority to issue an IUP/IUP-OP/Specific Licence

An IUP may be issued by either a regional government (Mayor, Regent or Governor) or the Central Government (MoEMR) depending on the location of the proposed mine and its associated infrastructure. IUPs may only be issued to PMA companies by the Central Government. The IUPKs for converted CoWs/CCoWs may only be granted by the Central Government.

Through PerMen 25/2015, the MoEMR delegated the authority to issue licences to PMA companies to the Investment Coordinating Board as follows:

- IUP Exploration;
- IUP – Operation Production including extensions;
- Cancellation of IUP relinquished to the Government;
- IUP – OP for Transport and Sales including extensions;
- IUP – OP for Processing and Refining including extensions;
- Temporary Licence for Transport and Sales;
- IUP-OP for Sales;
- In-principle Licence for Processing and Refining; and
- Business Licence for Mining Services including extensions.

The issuance of Exploration IUPs is performed as follows:

Exploration IUP	
Grantor	**Project location**
BKPM	If the licence is issued to a PMA company or converted from a CoW/CCoW.
MoEMR	Where the area covers more than one province.
Governor	Where the area covers more than one regency, but is within one province.
Mayor/Regent	Where the area is within one city or regency.

The authority to issue an IUP-OP follows the usual geographical distinctions (per the previous table) and depends upon the location of the mine infrastructure such as a processing plant, hauling road, stockpile and port facilities and the environmental impact of the project as depicted in the table below:

IUP-OP		
Grantor	**Project location**	**Environmental impact**
BKPM	For licences issued to a PMA company or converted from a CoW/CCoW.	For licences issued to a PMA company or converted from a CoW/CCoW.
MoEMR	Where the mining area, processing and refining and port facilities are located across more than one province	Where the environmental impact extends across more than one province (with the recommendation of the Mayor/Regent and Governor)
Governor	Where the mining area, processing and refining and port facilities extend across more than one regency, but within one province.	Where the environmental impact extends across more than one regency, but within one province (based on the recommendation of the Mayor/ Regent).
Mayor/Regent	Where the mining area, processing and refining and port facilities are within one city or regency.	Where the environmental impact is within one city or regency (based on the recommendation of the MoEMR and Governor).

It is uncertain which test will prevail for the granting of an IUP-OP in circumstances where there is an inconsistency between the project location and the extent of the environmental impact. Since many mining projects will have mining, processing, hauling and port facilities within different regencies or even within different provinces, it can be expected that the Governors and MoEMR will have greater control over the issue and renewal of IUP-OPs than was the case under the previous KP licensing system.

Specific Licences (Transport and Sales IUP-OP and Processing and/or Refining IUP-OP)	
Grantor	**Project location**
BKPM	For licences issued to a PMA company.
MoEMR	Where transport & sales and processing & refining activities extend across more than one province. *For Processing & Refining IUP-OPs:* • If the raw commodities are imported. • If the source mine and the refining facilities are located in different provinces. • If the mining licence for the source mine supplying the raw commodities was itself issued by the MoEMR.
Governor	Where the transport & sales and processing & refining activities extend across more than one regency, but are within one province. *For Processing & Refining IUP-OPs:* • If the source mine is located in a different regency to the processing facilities • If the mining licence for the source mine supplying the raw commodities was itself issued by the Governor.
Mayor/Regent	Where the transport & sales and processing & refining activities are within one city or regency. *For Processing & Refining IUP-OPs:* • If the mining licence for the source mine supplying the raw commodities was itself issued by the Regent/Mayor.

Authority to issue an IUPK

An IUPK should be issued by the Central Government regardless of the geographical coverage of the operations. State-owned companies are to be prioritised for the development of a WPN, but in the event that this option is not taken up, the IUPK can be offered to private investors via a tender process.

Licence terms and extensions

The mining licences are issued and extended as follows:

	Exploration IUP	IUP-OP	Extensions of IUP-OP
Coal	7 years	20 years	10 years x 2
Metallic minerals	8 years	20 years	10 years x 2
Non-metallic minerals	3 years	10 years*)	5 years x 2*)
Rocks	3 years	5 years	5 years x 2

**) Certain non-metallic minerals companies may be granted a Production IUP-OP of 20 years, extendable twice for a maximum of 10 years.*

Once the second extension of an IUP-OP expires, the relevant Mining Business Licence Area (*Wilayah Izin Usaha Pertambangan*, or "WIUP") is to be returned to either the central or regional government. If the WIUP relates to metallic minerals and coal it could be determined either as a WPN or WIUP/WIUPK (*Wilayah Izin Usaha Pertambangan Khusus*). The offer for a WIUP would be via tender, whilst the offer for a WIUPK would be via priority or tender (noting that the previous IUP-OP holder would have the right to match the tender offer).

Specific Licences

	In-principle Licence	Special IUP-OP	Extensions of Special IUP-OP
Transport and Sales IUP-OP	Not Applicable	3-5 years	Maximum 3 years for each extension
Processing and/or Refining IUP-OP	3 years (with one extension for 1 year)	Maximum 20 years (including 2 years for construction)	Maximum 10 years for each extension

IUPK

	Exploration IUPK	Production IUPK	Extensions of Production IUPK
Coal	7 years	20 years	10 years x 2
Metallic minerals	8 years	20 years	10 years x 2

Under GR 1/2017:

- Applications for extension of most mineral and coal IUP-OPs shall be submitted to the MoEMR, governor, or regent/mayor as applicable no earlier than five years and at the latest one year prior to the expiration of the IUP-OP;
- Applications for extensions of non-metal mineral or rock IUP-OPs shall be submitted to the MoEMR, governor, or regent/mayor as applicable no earlier than two years and at the latest six months prior to the expiration of the IUP-OP; and
- Applications for extensions of IUPK-OPs shall be submitted to the MoEMR no earlier than five years and at the latest one year prior to the expiration of the IUPK-OP.

Previously, GR 23/2010 stipulated that all applications for extensions of the IUP-OP and the IUPK-OP shall be submitted no earlier than two years and at the latest six months prior to the expiration of the IUP-OP/IUPK-OP. The above changes introduced by GR 1/2017 will be well received by the mining industry as it should allow greater certainty, planning and investment by mining companies in the years leading up to the expiry of a mining business licence.

Licence areas

A key aspect of GR 23 is that the size of the Exploration IUP for coal and metallic minerals must be reduced after three years of exploration (shorter for non-metallic minerals and rocks). The maximum area for the production phase is reduced again when the Production IUP/IUPK is issued.

Exploration IUP		Downsizing after 3 years of exploration (under GR 23)	Production IUP
Coal	5,000ha – 50,000ha	Must be reduced to a maximum of 25,000ha	Max 15,000ha
Metallic minerals	5,000ha –100,000ha	Must be reduced to a maximum of 50,000ha	Max 25,000ha
Non-metallic minerals	100ha – 25,000ha	12,500ha (applies after 2 years)	Max 5,000ha
Rocks	5ha to 5,000ha	2,500ha (applies after 1 year)	Max 1,000ha

Exploration IUPK		Downsizing after 3 years of exploration (under GR 23)	Production IUPK
Coal	Max 50,000ha	Must be reduced to a maximum of 25,000ha	Max 15,000ha
Metallic minerals	Max 100,000ha	Must be reduced to a maximum of 50,000ha	Max 25,000ha

An IUP or IUPK is issued for a particular type of mineral or coal. If other minerals are discovered in the licence area the relevant government authority shall issue further IUPs or IUPKs for those different minerals. The exploration IUP holder will be given priority to acquire a licence to mine the additional mineral(s) before the relevant government authority grants a mining licence to another investor.

Tender requirements for new mining licences

New IUPs and IUPKs must be issued through a competitive tender process rather than direct appointment. A company may bid for an IUP, but for IUPK licences, State-owned companies have precedence. The tender process is intended to create transparency and fairness for all potential investors and represents a significant change from the system adopted under the old mining law where the relevant government authority could directly grant a KP upon application.

GR 23/2010 (as amended by GR 24/2012) and PerMen 28/2009 (as amended by PerMen 24/2012) set out the tender process and selection criteria for a WIUP or WIUPK.

Tender procedures

In brief, the tender procedures are as follows:

a. The tender must be announced at least three months prior to its commencement

b. The tender should be conducted for all WIUPs, whilst WIUPKs are to be offered by the central government to state-owned or district-owned enterprises. The tender process for WIUPKs will only be conducted when there is more than one state-owned or district-owned enterprise in contention, or no state-owned or district-owned enterprises accepting the offer. The WIUPK is then to be offered via a tender process to state-owned or district-owned enterprises, or to national enterprises where there are no other bidders

c. The tender process and establishment of a tender committee is to be managed by the MoEMR in the case of WIUPKs or by the MoEMR/Governor/Regent/Mayor in the case of WIUPs, depending upon the location of the WIUP, the composition of the tender committee should satisfy the requirements regarding the minimum number and level of competence of committee members and the requirement to include representatives from certain government agencies

d. The type of business entity allowed to participate in the WIUP tender process is based on the size of WIUP acreage, as follows:

WIUP			WIUPK
≤1,000 ha	1,001 – 5,000 ha	> 5,000 ha**	
District-owned enterprise (Local) national enterprise Cooperation and individual (including firms and partnerships)	District-owned enterprise State-owned enterprise National enterprise* Cooperation	District-owned enterprise State-owned enterprise National enterprise* Foreign held entities	District-owned enterprise State-owned enterprise Private enterprise entities

Note:
**) A national enterprise is defined as a fully Indonesian-owned company*
***) For a WIUP exceeding 5,000 hectares, foreign investors wishing to take part in the tender process must use an Indonesian legal entity (i.e. a PMA company)*

e. The bidders are required to meet specified administrative, technical and financial conditions

f. There are two stages, pre-qualification and final tender:
   i. During the pre-qualification stage, the evaluation of bidders is based on the administrative, technical and financial requirements
   ii. Every bidder who passes the pre-qualification stage then submits an offer price. The tender committee may then visit the location of the WIUP being offered. The evaluation of bidders is based on the weighted average results, with 40% from the pre-qualification result and 60% of the offer price. The offer price should not be less than the compensation price (i.e. the compensation for mining/geological information and investment for each WIUP and WIUPK). The compensation price will be determined based on other regulations

g. For three working days after the announcement of the winner, the other bidders may submit an objection if they believe the tender process was not in accordance with the regulations, or there was any misconduct. The MoEMR, governor or regent/mayor (as the case may be) should provide a response within five working days.

Photo source : PT Agincourt Resources

A bidder must also place a cash deposit with a state-owned bank at the time of application of 10% of the value of compensation for data and information of a new mining licence, or 10% of the total cost of the data or investment in the case of a licence which has expired. A successful bidder will be required to pay the tender value within five working days of being announced as the tender winner.

Transfer restrictions

Under the Mining Law, the transfer of an IUP/IUPK to another party is generally prohibited. However, GR 24/2012 provides an exception whereby IUP/IUPKs can be transferred if the transferee is at least 51% held by a company which already holds an IUP/IUPK. It is not yet clear whether this rule is intended for transfers to any IUP/IUPK holder or whether it is limited to a minimum 51% owned subsidiary of the existing IUP/IUPK holder.

The intention of this rule may be to facilitate the reorganisation of IUP/IUPK interests by entities holding multiple IUP/IUPKs pursuant to the transitional rules in GR 23/2010. Further information will be required regarding the full extent of this amendment. There is also some concern that it goes beyond the powers granted under the Mining Law which may require consideration.

Under the Mining Law, the transfer of ownership and/or shares of an IUP/IUPK company on the IDX can only be done after the commencement of a certain phase of the exploration activities. The transfer should be communicated to the relevant government authority and should not contravene the provisions of the prevailing legislation.

The Mining Law does not appear to regulate the transfer of shares outside the IDX.

2.4. Control of production and control of mineral and coal sales

Mineral mining production limitation regulations

Due to the non-renewable nature of coal and mineral resources, which are essential for national development, and to guarantee sufficient supplies to fulfil national needs, the Central Government considers that it is important to limit national coal and mineral production as necessary. The MoEMR, Governor, or Head of Regency will determine the policy for production limitations.

Sanctions apply for non-compliance, which include warnings, suspension of activities, or the revocation of mining licences in extreme cases.

DMO

This policy is intended to guarantee the supply to meet increasing domestic demand, especially for coal.

The Central Government has the authority to control production and export of each mining product. The regional government is obliged to comply with the production and export controls imposed by the Central Government.

Details of the DMO procedures were issued in PerMen 34/2009 on 31 December 2009.

The DMO applies to all types of coal and minerals. Broadly, mining companies must comply with the DMO requirements by selling their minerals/coal production to domestic consumers.

Neither PerMen 34/2009 nor GR 23/2010 set a specific DMO percentage, rather the decision for each particular year is to be made by the MoEMR, based on the following procedures:

1. Domestic users submit their forecast requirements by no later than March of the preceding year
2. The MoEMR reviews and calculates the domestic requirements submitted to them and the production plans of the mining companies
3. The MoEMR must then issue a decree on the minimum DMO percentage by no later than June of the preceding year. The decree must also list the domestic users and their respective needs, and
4. The mining company must then submit its work program and budget for the relevant year to the authority that issued its licence (MoEMR, Governor or Mayor/Regent) and the DGoMC, stating its compliance with the DMO percentage.

There are provisions for a minimum floor price for DMO sales, which will be subject to Ministerial Regulation. However, PerMen 34 does provide that the minimum price will be subject to the same minimum price for exports (see the following comments on “Coal and Mineral Price Benchmarking”).

PerMen 34/2009 also introduces a “cap and trade” system, whereby mining companies that exceed their DMO obligations may sell/transfer DMO credits to a mining company that is unable to meet its DMO commitment.

The mechanism for trading DMO credits has been clarified in DGoMC Circular Letter No. 5055/30/DJB/2010 (dated 29 November 2010) which provides that DMO credits can be transferred between mining companies with the approval of the DGoMC, including credits held by traders on behalf of mining companies. The pricing mechanism for DMO credits is to be determined on commercial terms.

At the date of writing, the DMO has only been applied to coal. The Government reportedly set a coal DMO of 121 million tonnes for 2017 (approximately 29% of forecasted total production for 2017), which represents an increase of approximately 9% from the coal DMO target for 2016. It is not yet clear how the DMO for 2017 would be allocated to coal mining companies, as the official Ministerial decree has yet to be issued. However, past history has shown that the percentage required will be applied to the production volumes of all producers. As the Government aims to accelerate the completion of its 35GW electrification programme, it is expected that the DMO for coal set by Government will continue to increase in the coming years.

Coal and mineral price benchmarking

GR 23/2010 (amended by GR 1/2017), as further implemented by PerMen 7/2017 (superseding PerMen 17/2010) provides the framework which authorises the MoEMR to set the mineral and coal sales benchmark prices.

The Concluding Provision of PerMen 7/2017 stipulates that from the effective date of PerMen 7/2017, the provisions in PerMen 17/2010 that regulate the benchmark price for minerals and coal are revoked. By way of comparison, the benchmark price for minerals as regulated in PerMen 17/2010 provided for benchmark prices for metallic minerals, non-metallic minerals and rocks whereas the benchmark prices for minerals as regulated in PerMen 7/2017 only provides for benchmark prices for metallic minerals.

It is unclear whether the provisions regarding benchmark prices for non-metallic minerals and rocks still refer to PerMen 17/2010 or the intention of the Concluding Provision of PerMen 7/2017 is in fact to remove the provisions regarding the benchmark prices for non-metallic minerals and rocks. This would need further clarification from the Ministry of Energy and Mineral Resources. For the purpose of this Guide, we have assumed that the benchmark prices for non-metallic minerals and rocks are still regulated by PerMen 17/2010.

Broadly, the MoEMR, through the DGoMC, will be responsible for setting the benchmark prices for coal and metallic minerals. The Governor, and the Regent or Mayor, will be responsible for setting the benchmark prices for non-metallic minerals and rocks.

PerMen 7/2017 stipulates that the benchmark price is set at sale point Free on Board ("FOB"). This is slightly different to PerMen 17/2010 which stipulated that the benchmark price is set at the FOB vessel point of sale. PerMen 17/2010 also highlighted various terms of minerals and coal sales (i.e. FOB vessel, FOB barge, and Cost Insurance Freight or "CIF"). Under PerMen 17/2010, certain costs are accepted to adjust the benchmark price if the delivery takes place at a point other than FOB vessel (i.e. FOB barge or CIF). The allowable adjustments would include the costs of barging, surveyors, insurance and transshipment. For metallic minerals, the types of costs allowable as adjustments to the benchmark price included treatment costs and refinery costs. In PerMen 7/2017, there are no specific provisions regarding the terms of sale for minerals and coal or the allowable adjustments to the benchmark prices. It is therefore unclear whether such adjustments to minerals and coal benchmark prices are still allowable under PerMen 7/2017.

The benchmark price serves as the floor price for the Government Royalty calculation. If the actual sales price is higher than the benchmark price, the Government Royalty will be based on the actual sales price. If actual sales are below the benchmark price, the Government Royalty should be calculated based on the benchmark price.

The benchmark price for metallic minerals, as determined by the DGoMC on behalf of the MoEMR, may include the following commodities:

a. Nickel, in the form of nickel ore; ferronickel; mixed hydroxyde precipitate; mixed sulfide precipitate; nickel metal shot; nickel pig iron; nickel ingot; and/or nickel-matte;
b. Cobalt, in the form of: cobalt ore; cobalt concentrate; cobalt ingot; and/or cobalt sulfide;
c. Lead, in the form of: lead ore; lead concentrate; lead ingot; and/or lead bullion;
d. Zinc, in the form of: zinc ore; zinc ingot; zinc concentrate; and/or zinc oxide;
e. Bauxite, in the form of: bauxite ore; aluminum ingot; chemical grade alumina; and/or smelter grade alumina;
f. Iron, in the form of: iron ore; iron concentrate; iron sand; iron sand pellet; sponge iron; and/or pig iron;
g. Gold, in the form of gold metal;
h. Silver, in the form of silver metal;
i. Tin, in the form of tin ingot;
j. Copper, in the form of: copper ore; copper concentrate; and/or copper metal;
k. Manganese, in the form of: manganese ore; and/or manganese concentrate;
l. Chromium, in the form of: chromium ore; and/or chromium metal;
m. Titanium, in the form of: ilmenite concentrate; and/or titanium concentrate; and
n. Other certain Metallic Minerals.

The benchmark price for minerals and coal are determined based on the benchmark price formula which considers certain factors, including the value/content of metallic mineral; minerals reference prices (*Harga Mineral Acuan* or "HMA"); corrective factors; treatment costs and refining charges. While for determination of the coal benchmark prices, examples of these factors include the calorific value of coal; coal reference price (*Harga Batubara Acuan* or "HBA"); moisture content; sulphur content; and ash content.

Where coal is sold on a term basis, the HBA used as the reference in determining the price of coal in the sales contract is calculated based on 50% of the HBA in the month of contract signing plus 30% of the HBA in the month prior to the signing of the contract plus 20% of the HBA two months prior to the signing of the contract. This formula was introduced in PerMen 7/2017. The previous PerMen 17/2010 required the use of the average HBA for the three months prior to signing.

The benchmark price will be updated monthly and determined in accordance with market prices (based on a basket of recognised global and Indonesian coal indices in the case of coal). Various regulations have been issued by DGoMC, setting out:

- The formula to be used to calculate the benchmark price and the cost adjustments applicable for steam (thermal) and coking (metallurgical) coal.
- Guidance for the calculation of the benchmark price for specific coal types (e.g. fine coal, reject coal, and coal with specific impurities) and specific uses (e.g. own use in the coal mining process, coal value adding processes performed at the mine mouth, and for Community Development ("CD") near the mine area).

The coal benchmark prices for specific types of coal would be based on the benchmark prices after taking into account some adjustment factors determined by the DGoMC, whilst the prices for coal for specific uses will generally be based on the production costs determined by the DGoMC, plus a margin.

Mine mouth power plants

PerMen 9/2016 as amended by PerMen 24/2016 sets out guidance regarding coal supply and pricing for mine mouth power plants.

Under PerMen 24/2016, the coal price for mine mouth power plants is calculated based on basic coal price plus exploitation fee/royalty. The basic coal price is determined based on agreement between the coal mine owner and the power plant company and is calculated based on the production cost formula plus a margin (from 15% to 25%) and by considering an escalation factor. The escalation factor is adjusted on an annual basis based on the changes in the USD/Rupiah exchange rate, fuel prices, consumer price index and regional minimum wage. The margin is determined based on agreements between the coal mine owner and the power plant company within the range provided for in the PerMen. The basic coal price must be communicated to the MoEMR. The basic coal price is valid for the duration of the Power Purchase Agreement. Transport costs are excluded except for the transportation of coal from the mine to the power plant's stockpiling facility.

Mines supplying mine-mouth power plants must be listed on the Clean-and-Clear list and must have the reserve allocation and coal quality required by the power plant. It also requires the mine owner to hold a minimum of 10% of the equity of the power plant company. The distance between the mine and the power plant must be a maximum of 20 kilometres.


Photo source : PT Vale Indonesia Tbk

2. 5. *Mandatory in-country processing and export restrictions*

Obligations to increase added value and to meet minimum level of in-country processing and refining requirements

Holders of coal IUPs and IUPKs are required to carry out processing to increase the added value to the coal they produce, either directly or in cooperation with other companies, IUP holders and IUPK holders.

- "Processing" by a holder of a coal IUP-OP or coal IUPK-OP covers the following activities:

Coal upgrading	Coal briquetting	Coke making
Coal liquefaction	Coal gasification, including underground coal gasification	Coal slurry/coal water mixture

- "Processing" by a holder of a coal Processing IUP-OP covers the following activities:

Coal blending	Coal upgrading	Coal briquetting	Coke making
Coal liquefaction	Coal gasification	Coal slurry/coal water mixture	

Holders of mineral IUPs and IUPKs are required to carry out in-country processing and refining to increase the value added to the minerals they produce, either directly or in cooperation with other companies, IUP holders and IUPK holders. PerMen 5/2017, as amended by PerMen 28/2017 specifically sets out the requirements for in-country mineral processing and refining.

Minerals of which the added value can be increased include:
- Metallic minerals
- Non-metallic minerals, or
- Rocks.

Processing covers activities to improve the quality of minerals or rocks without changing their physical and chemical properties, such as conversion into metallic mineral concentrates or polished rocks. Refining is defined as activities to improve the quality of metallic minerals through an extraction process and by increasing the purity of the mineral to produce a product with different physical and chemical properties from the original, such as metals and alloys.

The increase in added value of minerals shall be carried out through the following activities:
- Processing and refining for metallic minerals
- Processing for non-metallic minerals, or
- Processing for rocks.

Holders of an IUP-OP, IUPK-OP or Processing and Refining IUP are required to meet specific minimum in-country processing and refining requirements for various types of metal minerals, non-metallic minerals, certain rocks, by-products or residues from the refining of metal mineral mining commodities (in the form of copper, tin, lead and zinc) and by-products or residues from the refining of lead concentrates in slag form. These specific minimum in-country processing and refining requirements are detailed in Attachments I to IV of PerMen 5/2017 (see Appendix A of this Guide for the minimum in-country processing and refining requirements applicable to metallic minerals prior to export).

The obligation to meet minimum in-country processing and refining requirements as set out in PerMen 5/2017 would not be applicable to the holders of IUP-OP and IUPK-OP whose mined products are directly used in the domestic interest and for export of minerals for research and development purposes provided that recommendations from the DGoMC on behalf of MoEMR and export approval from the Director General of Foreign Trade ("DGFT") are obtained.

Processing and refining can be done in cooperation with other IUP and IUPK holders as well as holders of Processing and/or Refining IUPs. This cooperation may be in the form of:
(a) Sales and purchases of ore/concentrates, or
(b) Processing and/or refining activities.

The cooperation plans must be submitted to the MoEMR with attention to the DGoMC (or Governor) for approval. A holder of an IUP-OP or IUPK-OP that supplies ores, concentrates, or mineral intermediate products to other processing and/or refining parties must submit its sales planning to the MoEMR with attention to the DGoMC (or Governor).

Restrictions placed on exports of processed and refined minerals

Upon payment of export duties under the relevant laws and regulations, the fulfilment of the minimum domestic processing and refining requirements, and after obtaining export approval from the Ministry of Trade ("MoT"), holders of IUP-OP, IUPK-OP and Processing and/or Refining IUPs may export certain approved quantities of their processing products for a period of five years from 11 January 2017.

There are specific rules applicable to export of nickel and bauxite, as follows:

- Holders of a nickel IUP-OP, nickel IUPK-OP, nickel Processing and/or Refining IUP and other parties that are engaged in nickel processing and/or refining must utilise nickel with a content of $< 1.7\%$ for at least 30% of the nickel processing and/or refining capacity of their facility. Only when this requirement has been fulfilled, may they export certain approved quantities of nickel with a content of $< 1.7\%$ for a period of five years from 11 January 2017, provided, however, that they have constructed or are in the process of constructing a refining/smelting facility, either individually or jointly with other parties, and pay export duties under the relevant laws and regulations.

- Holders of a bauxite IUP-OP, bauxite IUPK-OP, bauxite Processing and/or Refining IUP and other parties that are engaged in bauxite processing and/or refining may export certain approved quantities of washed bauxite with an Al_2O_3 content of $\geq 42\%$ for a period of five years from 11 January 2017, provided, however, that they have constructed or are in the process of constructing a refining/smelting facility, either individually or jointly with other parties, and pay export duties under the relevant laws and regulations.

Export approval from the MoT is granted based on a recommendation from the MoEMR. As set out in PerMen 6/2017, to obtain a recommendation, holders of IUP-OPs, IUPK-OPs and Processing and/ or Refining IUPs must submit an application for recommendation to the MoEMR with attention to the DGoMC. A number of documents must be submitted with this application for export recommendation, e.g. an integrity pact to conduct the development of an in-country refining facility; a "clean and clear" IUP certificate; a statement on the full payment of non-tax state revenue obligations for the last one year; plan for the development of an in-country refining facility which has been verified by an independent appraiser; latest reserve report; etc. Please refer to PerMen 6/2017 for the detailed requirements of documents to be submitted together with an application for export recommendation. The application for export recommendation shall be submitted in accordance with the application format set out in PerMen 6/2017.

The DGoMC shall evaluate the application for export recommendation and based on this evaluation, the DGoMC on behalf of the MoEMR will approve or reject the application within 14 working days of full receipt of the application.

The export recommendations by the DGoMC on behalf of the MoEMR are valid for one year, and extensions may be given for a period of one year for each extension.

In order to obtain an extension of the recommendation, a company must have achieved not less than 90% of the plan for physical progress of the refining facility construction. In the event that the percentage of physical progress of the refining facility construction is not achieved, the DGoMC on behalf of the MoEMR shall issue a recommendation to the MoT for revocation of the provided export approval.

In February 2017, the MoF issued PMK No.13/ PMK.010/2017 to support the implementation of PerMen 6/2017. This PMK stipulates the rates of export duty for the various forms of processed metallic minerals.

Photo source : PT Vale Indonesia Tbk

Under PMK No.13/PMK.010/2017, the export duty rates are linked to the physical progress of the refining facility development, as set out in the export recommendation issued by the MoEMR, as per the following four stages:

- Stage I – level of physical progress of development up to 30% of the total development;
- Stage II – level of physical progress of development more than 30% and up to 50% of the total development;
- Stage III – level of physical progress of development more than 50% and up to 75% of the total development; and
- Stage IV – level of physical progress of development more than 75% of the total development.

The export duty rates under PMK No.13/PMK.010/2017 are as follows:

No	Types of Mineral	Export Duty Rate				
		Stage of physical progress of refining facility development				Minerals with certain criteria
		Stage I	Stage II	Stage III	Stage IV	
1	Copper concentrate with concentration > 15% Cu	7.5%	5%	2.5%	0%	N/A
2	Iron concentrate (hematite, magnetite) with concentration > 62 % Fe and < 1% TiO_2	7.5%	5%	2.5%	0%	N/A
	Laterite iron concentrate (geothite/ laterite) with concentration > 50% Fe and concentration of (Al_2O_3+SiO_2) > 10%	7.5%	5%	2.5%	0%	N/A
	Iron sand concentrate (magnetite-ilmenite lamellae) with concentration > 56% Fe and 1% < TiO_2 < 25%	7.5%	5%	2.5%	0%	N/A
	Iron sand concentrate pellet (magnetite-ilmenite lamellae) with concentration > 54% Fe and 1% < TiO_2 < 25%	7.5%	5%	2.5%	0%	N/A
3	Manganese concentrate with concentration > 49% Mn	7.5%	5%	2.5%	0%	N/A
4	Lead concentrate with concentration > 56% Pb	7.5%	5%	2.5%	0%	N/A
5	Zinc concentrate with concentration > 51% Zn	7.5%	5%	2.5%	0%	N/A
6	Ilmenite concentrate with concentration > 45% TiO_2	7.5%	5%	2.5%	0%	N/A
7	Other titanium concentrates with concentration > 90% TiO_2	7.5%	5%	2.5%	0%	N/A
8	Nickel with concentration < 1.7% Ni	N/A				10%
9	Washed bauxite with concentration > 42% Al_2O_3	N/A				10%

Export restrictions for mineral CoW holders

PerMen 5/2017 stipulates that CoW holders may export certain approved quantities of their processing products for a period of five years from 11 January 2017, provided that:

- They convert the CoW into an IUPK-OP. This change is subject to approval by the MoEMR. After an application for a change of the form of mining business is submitted by a CoW holder, the MoEMR shall approve/reject such application within 14 working days upon full receipt of the application.
- They pay export duties under the relevant laws and regulations and fulfil the minimum domestic processing and refining requirements stipulated under PerMen 5/2017.

Pursuant to the amendment of PerMen 5/2017 by PerMen 28/2017, an approval for the conversion of a CoW into an IUPK-OP may be granted by the MoEMR:

a. For a period until the expiry date of the CoW – when an IUPK-OP is granted based on this condition, the CoW area is changed to a WIUPK in accordance with the relevant laws and regulations and the IUPK-OP shall follow the prevailing regulations.
b. For a specific period in connection with adjustment for the continuation of operations – when an IUPK-OP is granted based on this condition, the provisions under the CoW and other agreements between the Government and CoW holders shall remain valid. After the expiry of the specific period covered by this IUPK-OP, there is an option to continue using the provisions under the CoW or to follow the prevailing laws and regulations, depending on whether a settlement can be reached to adjust the terms of the CoW to that of an IUPK-OP.

The above provisions under PerMen 28/2017 are not very clear and leave much to further interpretation. However, press reports subsequent to the issuance of the regulation indicated that PerMen 28/2017 was issued in connection with the Government's efforts to allow certain CoW holders to resume exports of mining products while still negotiating with the Government for the conversion of the CoW into an IUPK-OP.

There has been significant debate between the Government and the mining sector regarding the commerical viability of the in-country processing requirements, including the imposition of the export duty. In particular, CoW holders have questioned the applicability of the regulations to them, given the *lex specialis* status of the CoWs. Questions have also been raised by the industry regarding the economic feasibility of processing certain types of minerals, given current and forecast global and domestic demand and supply considerations; inadequate supporting infrastructure in some areas of the country for downstream processing facilities; and the level of the export levy and its impact on profitability. Nevertheless, the Government has repeatedly indicated its commitment to enforcing these requirements.

Photo source : PT Bukit Asam (Persero) Tbk

Investment considerations for building in-country refining facilities

In the event that a mining company intends to build a smelter in Indonesia, some key considerations for investors considering investments in processing/refining facilities, and associated infrastructure are as follows:

a. Whether it is favourable to include the processing/refining facilities and infrastructure within the company holding the IUP-OP (i.e. the mining company) or under a separate company holding a Processing and/or Refining IUP-OP?
b. If a separate company is to be established, what would be the most beneficial arrangement with the mining company? Whether a trading or a processing service arrangement would be preferable.
c. Whether any tax facilities are available, such as an income tax holiday or import facilities.
d. The relevant tax considerations in relation to the Engineering, Procurement and Construction (EPC) contract.
e. How financing can be arranged in the most tax efficient manner.
f. The right model for cooperation between shareholders (mining companies, offtakers, financial investors, domestic, foreign, etc.).

PwC Indonesia recommends that investors contact our specialist mining team should they require further advice. Please see Appendix F for the contact details of PwC Indonesia's mining specialists.

Letter of Credit ("L/C") requirement for exports of mineral resources

Pursuant to the issuance of PerMenDag 4/2015 (as amended by PerMenDag 67/2015) which is intended to obtain more accurate information on foreign exchange revenue from exports, the MoT now requires the use of an L/C for the export of mineral products (e.g. nickel oxide, gold concentrate, gold bars, pure tin solder, copper bars, etc.).

In brief, the L/C requirements are as follows:

a. The price stated in the L/C should not be lower than the global market price
b. The payment should be made to a domestic foreign exchange bank (*bank devisa*)
c. The L/C mechanism should be declared in the export declaration (PEB)
d. The L/C documentation is subject to audit by a surveyor appointed by MoT, and
e. No exports will be allowed if they fail to satisfy the L/C requirements.

Further implementing regulations will be issued by the DGFT.

Exporters of mineral products should closely examine the procedures and requirements to avoid unnecessary sanctions, including the suspension of export/import activities. However, it remains unclear how the rules can be effectively applied for inter-company sales, non-sales exports, exports through pipelines, and exports under trustee arrangements, among others.

On 30 March 2015, the MoT issued PerMenDag 26/2015 which allows an exporter unable to implement the L/C terms to apply to the MoT for deferral (this is however subject to a post-audit by the MoT and penalty sanctions). The approval from the MoT will consider the following:

a. The terms adopted in sales contracts for the Export of Certain Commodities between the exporter and overseas customer which was drawn up before PerMenDag 4/2015 became effective (e.g. whether it uses a Telegraphic Transfer or L/C), and
b. The ability of the exporter to adjust the means of settlement using an L/C within a certain period of time, and
c. Written confirmation of stamp duty on both points above.

A post-audit would be performed by the MoT on the above documents. The revocation of L/C terms deferral and other sanctions may apply if the audit identifies the above documents, and the exports are inappropriate.

The L/C can be paid via an export financing institution of the Government.

2.6. *Royalties and fiscal regime*

Royalties

All IUP/IUPK holders are required to pay production royalties at rates which vary depending on the mining scale, production level, and mining commodity price. Currently, a range of percentages of sale proceeds applies for different types of coal and mineral mining.

Holders of an IUPK will be required to pay an additional royalty of 10% of net profit. The Central Government is entitled to receive 40% of this additional royalty while the balance is to be shared between the relevant province and regencies. Since this additional royalty is determined based on the net profit it is expected that the government will have a greater monitoring role over capital expenditure and mining operating costs in the case of IUPKs.

The current production royalty rates for key Indonesian commodities are set out in the following table. For rates applicable under a CoW/CCoW reference should be made to the relevant agreement (see Chapter 3.0 and Appendix E for further details on CoW/CCoW terms).

IUP Royalty Rates	
Commodity	**Production royalty rate**
Coal - Open Pit - Underground	 3% - 7% 2% - 6%
Nickel	4% - 5%
Zinc	3%
Tin	3%
Copper	4%
Iron	3%
Gold	3.75%
Silver	3.25%
Iron Sand	3.75%
Bauxite	3.75%

The Government has been looking to increase the production royalty rates for IUPs, in particular for coal, as the current rates are significantly lower than that under a CCoW (i.e. a 13.5% production share). However, this has not yet been implemented in any official regulations.

Fiscal regime

There are no specific articles outlining the details of tax or other fiscal provisions in the Mining Law. However it does provide that tax facilities should be provided in accordance with the prevailing laws except as otherwise stated in the IUP/IUPK.

The *lex specialis* concept embedded in some CoWs/CCoWs may be possible if enduring fiscal terms can be agreed in the IUP/IUPK. The ability of a term in an IUP/IUPK to override Law No. 36/2008 (Income Tax Law or "ITL") would however be problematic and likely to result in further uncertainty. It appears that all IUPs issued to date contain no specific tax concessions.

Refer to Chapter 4.0 for further details in relation to mining specific taxation matters.

2.7. *Divestment of foreign shareholding*

Under GR 77/2014, the maximum shareholding which a foreign investor can acquire in a company which holds an IUP/IUPK depends on the type of mining licence the company holds and whether this company carries out processing and refining activities. The applicable maximum shareholdings are set out as follows:

Mining Licence	Carry Out Processing and/or Refining Activities	Maximum Foreign Ownership (%)
Exploration IUP and Exploration IUPK	Not Applicable	75
IUP-OP and Production & Operation IUPK ("IUPK-OP")	No	49
IUP-OP and IUPK-OP	Yes	60
IUP-OP conducts underground mining	Not Applicable	70

Pursuant to the amendment of GR 77/2014 by GR 1/2017, foreign shareholders must upon five years of production divest their shares in stages, such that by the tenth year of production, foreign shareholders shall have a maximum 49% shareholding.

A summary of the divestment rules for mining companies under GR 1/2017 is as follows:

Mining Licence	Year of Production - Divestment %				
	6th	7th	8th	9th	10th
IUP and IUPK	20%	30%	37%	44%	51%

Divestments are to be made to (in order of preference) the Central Government, Provincial Government or Regency/Municipal Government, *Badan Usaha Milik Negara* ("BUMN") and *Badan Usaha Milik Daerah* ("BUMD") or national private business entity (in the form of a Limited Liability Company).

Previously under GR 77/2014, IUP-OP and IUPK-OP holders which conduct underground mining can, after the fifth year of production, have a 70% maximum foreign shareholding whereas IUP-OP and IUPK-OP holders which carry out processing and/or refining activities can, after the fifth year of production, have a 60% maximum foreign shareholding. Additionally, IUP-OP and IUPK-OP holders which conduct underground mining or which carry out processing and/or refining activities can divest over a period up to the 15th year of production. Under GR 1/2017, these provisions are no longer applicable and divestment must follow the requirements under GR 1/2017 as explained above. GR 1/2017 will ultimately result in all foreign investors losing the majority stake in the mines in which they have invested, regardless of whether they are carrying out underground mining or smelting activities.

The following provisions of GR 1/2017 are not very clear and/or may have multiple potential interpretations, however PerMen 9/2017 provides further guidance clarifying the provisions:

- GR 1/2017 stipulates that foreign shareholders shall offer their divestment shares within 90 calendar days of the fifth year of the issuance date of an IUP-OP. This implies that the time when production is measured from is the issuance date of the IUP-OP rather than the actual date of commencement of production (which means the construction period is counted). PerMen 9/2017 clarifies that the initial production date for the purpose of divestment is the date of commencement of production activities.

- GR 1/2017 removed a provision under GR 77/2014 which stated that divestment requirements do not apply to the holders of an IUPK Processing and/or Refining. PerMen 9/2017 clarifies that holders of IUPK Processing and/or Refining are not subject to the divestment requirements.
- GR 1/2017 removed a provision under GR 77/2014 which stated that mining companies whose shares are listed on the IDX are considered to be held 20% domestically at a maximum. PerMen 9/2017 clarifies that divestment may be carried out through an IPO on the IDX in the event that none of the Central Government, Provincial Government or Regency/Municipal Government, BUMN, BUMD or a national private business entity are interested in taking the divestment shares. PerMen 9/2017 does not however provide a maximum ownership that can be considered as domestically held as under GR 77/2014.

Although based on the hierarchy of regulations, GR 1/2017 ranks above PerMen 9/2017, it is expected that in practice the provisions of PerMen 9/2017 would apply, as they seek to clarify the GR.

In addition to the above, GR 1/2017 and PerMen 9/2017 stipulate the following:

- Holders of IUP-OP and IUPK-OP for which shares must be divested, are prohibited from providing loans to the Indonesian party for the purpose of acquiring the divestment shares. This provision is likely intended to prevent the foreign shareholder from maintaining control through nominee arrangements.
- Holders of IUP-OPs and IUPK-OPs are prohibited from pledging the shares which are obliged to be divested.
- In the case of the issuance of new share capital which dilutes the Indonesian shareholder's ownership percentage, the entities holding an IUP-OP and IUPK-OP should in the first instance offer the new shares to the existing Indonesian shareholder, or to other Indonesian participants (Central Government, Provincial Government, BUMN, BUMD, or national private business) if the existing Indonesian shareholder is not interested to exercise its rights.

Transitional provisions

The transitional divestment provision under GR 77/2014 stipulates that a CoW or CCoW holder which has been in the production phase for less than five years prior to the issuance of GR 77 is subject to the new divestment requirements. CoW and CCoW holders who have been in the production phase for more than five years prior to the issuance of GR 77/2014 must carry out the divestment based on the following criteria:

- 20% of shares held must be divested no later than 15 October 2015, and
- No later than five years from the issuance of GR 77, the CoW and CCoW holder must comply with the divestment requirement, i.e. by 15 October 2019.

GR 1/2017 made no change to this transitional divestment provision. This could potentially create confusion in interpreting this transitional provision because the explanation of this transitional provision is not consistent with the new divestment requirements under GR 1/2017, i.e. the explanation of this transitional provision provides examples of the application of old divestment requirements under GR 77/2014, for example a CoW holder which conducts underground mining production may divest over a period up to the 15th year of production.

As stipulated in GR 1/2017 and PerMen 9/2017, CoW and CCoW holders are required to comply with the divestment requirements in these regulations. This will continue to be an ongoing debate between the Government and CoW and CCoW holders since these companies are likely to argue that the provisions in the CoW/CCoW should override GR 1/2017 and PerMen 9/2017.

Additional requirements regarding the conversion of capital investment status

GR 77/2014 reiterates the requirements for the conversion of a PMDN company to a PMA company or a change in the shareholders of a PMA company.

The changes from a PMDN company to a PMA company, or vice versa, will require approval from the MoEMR. IUP holders (including Transport & Sales IUP-OP and Processing and/or Refining IUP-OP) are prohibited from changing their investment status prior to obtaining Ministerial approval. This is discussed further below.

The divestment procedures including the timeline, divestment price, approval processes and the payment mechanism should follow the requirements of PerMen 9/2017.

Divestment via IPO

GR 77/2014 stipulated that mining companies whose shares are listed on the IDX are considered to be held 20% domestically at a maximum. Pursuant to the amendment of GR 77/2014 by GR 1/2017, this provision has been removed in GR 1/2017. Therefore, GR 1/2017 is silent regarding the maximum ownership that can be considered domestically held for IDX-listed mining companies.

PerMen 27/2013 stated that divestment via the Indonesian capital market will not be treated as satisfying the divestment requirements. Pursuant to the revocation of PerMen 27/2013 by PerMen 9/2017, this provision has been removed. Instead, PerMen 9/2017 stipulates that divestment can be carried out through offering shares on the IDX in the event that none of the Central Government, Provincial Government or Regency/Municipal Government, BUMN, BUMD or national private business entities are interested in taking divested shares. This implies that divestment via the Indonesian capital markets can be treated as satisfying the divestment requirements.


Photo source : PT Aneka Tambang (Persero) Tbk

Changes in capital investment structure

Any changes in the capital investment structure of an entity holding an IUP or an IUPK (including a Transport & Sales IUP-OP and a Processing and/ or Refining IUP-OP) requires approval from the MoEMR, governor or regent/mayor (in accordance with the level of the issuing authority for the IUP). Approval is required for changes in:

a. Investment and financing sources
b. Entity status from PMA to PMDN or from PMDN to PMA
c. The articles of association
d. The board of directors or board of commissioners, and
e. Share ownership.

Pricing of shares subject to divestment

PerMen 9/2017 stipulates that the divestment share price is determined based on the "fair market value", without considering the value of mineral or coal reserves at the time the divestment is conducted. This pricing mechanism could be a significant concern for foreign investors given that it is likely to result in a price lower than the fair market value, which is generally understood to include the net present value of the cash flows generated through exploitation of the reserves over the remaining life-of-mine.

The regulated divestment share price would become:

a. The maximum price to be offered to the central, provincial/ regional governments; or
b. The minimum price to be offered to BUMN and BUMD or a national private business entity.

The Government (via the MoEMR) may engage an independent valuer to evaluate the divestment share price. If agreement cannot be reached on the divestment share price, the divested shares shall be offered based on the divestment share price calculated based on the evaluation performed by the Government.

2.8. Reclamation and mine closure

On 20 December 2010, the Government released GR 78/2010 dealing with reclamation and post-mining activities for both IUP-Exploration and IUP-OP holders. This regulation updates PerMen 18/2008 issued by the MoEMR on 29 May 2008. On 29 February 2014, the MoEMR issued PerMen 7/2014 (the implementing regulation for GR 78/2010) detailing the requirements and guidelines for the preparation of reclamation and post-mining plans.

An Exploration IUP holder, among other requirements, must include a reclamation plan in its exploration work plan and budget and provide a reclamation guarantee in the form of a time deposit placed at a state-owned bank. The reclamation plan for the exploration phase is required to be prepared before undertaking any exploration activities. Upon submitting an application for an IUP-OP, the reclamation plan for the production phase and the post mining plan shall also be prepared by the IUP/IUPK holder, and this plan should cover a five-year period (or the remainder of the mine life, if shorter).

An IUP- OP holder, among other requirements, must provide:

- A five-year reclamation plan;
- A post-mining plan;
- A reclamation guarantee which may be in the form of a joint account or time deposit placed at a state-owned bank, a bank guarantee, or (if meeting certain eligibility criteria) an accounting provision; and
- A post-mining guarantee in the form of a time deposit with a state-owned bank.

The requirement to provide reclamation and post-mining guarantees does not release the IUP holder from the requirement to perform reclamation and post-mining activities.

PerMen 7/2014 also sets out the procedures for the preparation of the reclamation and post-mining activities report.

The transitional provisions in GR 78/2010 and PerMen 7/2014 make it clear that CoW/CCoW holders are also required to comply with this regulation.

The reclamation and mine closure guarantees may only be withdrawn upon approval from the MoEMR, the Governor, the Regent or the Mayor, as applicable.

2.9. *Mining services*

IUP or IUPK holders can no longer subcontract all activities, but must actually remove the coal/minerals ore from the ground themselves. A detailed list of the types of Mining Services Business distinguishes between certain defined Mining Services Business and Non-Core Mining Services. Broadly, the requirements are directed at ensuring the use of local businesses and restricting the use of affiliate companies.

Apart from mandatory in-country processing, which can be fulfilled by engaging another party with a Processing and/or Refining IUP-OP licence, an IUP/IUPK holder can only engage a Mining Services Company for the purposes of consultation, planning and testing, overburden stripping and transportation. Under PerMen 24/2012, an IUP holder may outsource the construction of an underground mine to a mining services company specialising in tunneling work, and the IUP holder can also use equipment owned by a mining services company through a rental arrangement. A detailed list of Mining Services is further detailed in the attachments to PerMen 28/2009 as amended by PerMen 24/2012.

Classification of Mining Services and Mining Service Companies

Companies wishing to provide services to an IUP/IUPK holder must obtain the following licences:

Mining Service Sub-categories and licensing requirements	
Mining Service Business	**Non-Core Mining Service**
Expansive list in PerMen 28/2009 as amended by PerMen 24/2012.	Any service business other than a Mining Service Business that provides services in support of mining business activities.
Licence: Mining Services business Licence/ *Izin Usaha Jasa Pertambangan* ("IUJP").	Licence: Registration Letter/*Surat Keterangan Terdaftar* ("SKT").

Mining Services must be provided by an Indonesian entity, with a clear preference for the use of Local and/or National Companies. In this regard, PerMen 28/2009 as amended by PerMen 24/2012 provides the following classifications for service providers:

Local Company	A wholly Indonesian owned company/entity which operates and is domiciled only in one regency/province.
National Company	An Indonesian legal entity where all shares are owned by Indonesian nationals and which operates in Indonesia or offshore.
Other Company	An Indonesian legal entity where some/all of its shares are owned by a foreign party.

Further entrenching the domestic content obligation is the requirement for the mining service company to use local goods, local subcontractors and local labour.

Restrictions on the use of affiliates/subsidiaries

Further restrictions are placed on the ability to use subsidiaries and affiliates of the IUP/IUPK holder as subcontractors, namely the requirement to obtain approval from the DGoMC. Subsidiaries and affiliates are further defined (pursuant to DGoMC Regulation no. 376.k/30/DJB/2010, dated 10 May 2010) as entities that have a direct ownership relationship with the IUP/IUPK holder, i.e. where:

a. The IUP/IUPK holder directly owns at least a 25% shareholding in the affiliated mining service company;
b. The IUP/IUPK holder is a direct shareholder and owns voting rights in the affiliated mining services company of more than 50%, based on an agreement granting direct financial and operational control; and/or
c. The IUP/IUPK holder has the authority to appoint or replace financial and operational directors or others at a similar level in the mining contractor company.

Approval will only be granted in circumstances where there are no other mining companies of the same kind in the Regency/Province, the IUP/IUPK holder has put the services out to tender and no Local or National service providers have either the technical or financial capability required to carry out the services. The IUP/IUPK holder must provide a guarantee that pricing will be based on arm's length principles.

Prohibition against receiving fees from a mining services company

The IUP/IUPK holder is prohibited from receiving any fees from the mining services company. This appears to have been introduced to eliminate practices where by the mining licence owner assigns all mining operations to a third party and receives compensation based on a share of profits or of the quantity of coal/minerals produced.

Transitional provisions for existing Mining Services arrangements

Mining companies which had already engaged mining services companies before the enactment of PerMen 28/2009 were required to comply with the regulation no later than three years from the effective date of PerMen 28/2009 (i.e. 30 September 2012).

All existing IUPs will continue to be valid until their expiration but must comply with the provisions of PerMen 28/2009 as amended by PerMen 24/2012.

2.10. *Penalty provisions and dispute resolution*

Penalty provisions

The Mining Law also regulates the consequences of infringement of the law by the IUP/IUPK holder (an illegal miner), as well as the regional government.

A breach of the Law can be punished by both administrative and criminal sanctions, including the revocation of an IUP/IUPK and prison terms.

Dispute resolution

Disputes regarding IUPs/IUPKs should be settled through court procedures and domestic arbitration in accordance with the prevailing laws and regulations.

2.11. *Transitional provisions*

KPs

All existing KPs were required to have been converted to IUPs by 30 April 2010 based on GR 23/2010. There are no transitional provisions concerning the conversion of KPs in the Mining Law. Although the conversion itself is relatively straightforward the impact of the implementing regulations, in particular PerMen 28/2009, mean that a number of historical mining service structuring arrangements are no longer permitted under the Mining Law.

GR 23/2010 confirms that companies that held multiple KPs can continue to hold these under the Mining Law, upon conversion to IUPs.

Divestment

For details on the Transitional Provisions relating to Divestment, please refer to Section 2.7 "Divestment" of this Guide.

Photo source :
PT Bukit Asam (Persero) Tbk

CoWs/CCoWs/Coal Co-Operation Agreements ("CCA")

All existing CoWs/CCoWs/CCAs ("contracts") will continue until their expiry date and may be extended without the need for a tender (where further extensions are still available under the contracts).

However, the extended licences will be granted under the IUPK system, rather than under the CoW framework. If it has been extended once, the second extension would also be granted without the need for a tender. Both extensions require the companies to apply to the MoEMR at the earliest two years or at the latest six months prior to the expiry of the contract. Before issuing the IUPK, the MoEMR should have already issued approval for the relevant mine area as a WIUPK OP. Failure to fulfil these requirements may result in the mine area being opened for tender.

Detailed guidance on the application for the extension of IUPK OPs is outlined in GR 77/2014, as amended by GR 1/2017 and PerMen 15/2017.

Although the terms of existing contracts will be honoured, the Law specifically provides that holders of existing contracts must, within five years of enactment of the Law, comply with the obligation under the Law to conduct onshore processing and refining of ore.

Contract holders who have already commenced some form of activity are required, within one year of the enactment of the Mining Law, to submit a mining activity plan for the entire contract area. If this requirement is not fulfilled, the contract area may be reduced to that allowed for IUPs under the new Law.

Further, the Mining Law indicates that the provisions of existing contracts must be amended within one year to conform with the provisions of the new Law, other than terms related to state revenue (which is not defined but presumably includes State Tax Revenue and Non-Tax State Revenue such as royalties). At the time of writing, more than eight years after the issuance of the Mining Law, the negotiation process between the Government and contract holders regarding amendments to the contracts is still ongoing. It is not stated in the Mining Law which provisions existing contracts must conform to, but this could include alignment with the Mining Law's provisions on divestment obligations, re-sizing of the mining areas, reduced production periods, prohibitions on using affiliated mining contractors and the like. Many of these matters have been raised by the Government in contract renegotiations with contract holders.

The transitional provisions were among the most controversial aspects of the Mining Law, with debate in Parliament continuing on this point right up to the final passage of the Law. Unfortunately, the outcome was two possibly conflicting provisions meaning that, state income treatment aside, it is not clear how fully existing contract rights will be honoured. Resolution of this question will obviously be of major interest to those investors holding contracts, and is likely to be a continuing deterrent to additional investment by existing contractors, until the Government's interpretation of these transitional clauses is clearly understood, and contract renegotiation efforts are completed.

Whilst the Government has commenced discussions with most contract holders, in an attempt to expedite the negotiations, Presidential Decree No. 3/2012 was issued on 10 January 2012 to establish a team, headed by the Coordinating Minister for Economic Affairs and comprised of a number of ministers, to negotiate the terms of the contracts and bring them into line with the Mining Law. However, after the fifth anniversary of this Decree, contract renegotiations are still ongoing with most contract holders. It is understood that the negotiations have been focusing on issues such as the size of the concession areas, taxes and royalties, the use of mining service contractors, benchmark pricing, mine closure and reclamation, onshore processing and minimum divestment requirements.

In January 2017, PerMen 5/2017 was issued which effectively represents an attempt by the Government to require CoW holders to convert to IUPKs as PerMen 5/2017 stipulates that COW holders will only receive export permits after conversion. This may be regarded by CoW holders as a breach of the terms of their contracts, particularly considering that under the transitional provision of the Mining Law, it is clearly stated that all existing CoWs will be honoured until their expiry dates. In February 2017, the Government issued PerMen 15/2017 which sets out the procedures for granting an IUPK-OP as a continuance of a CoW/CCoW. In Article 8 of this PerMen 15/2017, it is stated that the provisions under the CoW and other agreements between the Government and CoW holders become an inseparable part of the granting of the IUPK-OP and will remain valid until the period as determined in the IUPK-OP. There is no further explanation provided in PerMen 15/2017 regarding this matter, for example whether all or only part of the provisions under the CoW will remain valid or what other agreements are being referred to (this presumably includes the documents signed by the Government and CoW holders as a result of the contract renegotiations referred to above). It remains to be seen how CoW holders will react to these changes.

Photo source :
PT Bukit Asam (Persero) Tbk

Contracts of Work

3.1. General overview and commercial terms

Contracts of Work

The CoW system for regulating mining operations has played a key role in the success of Indonesia's mining industry. The CoW system, which was introduced in 1967, has been gradually refined and modernised over the past forty years to reflect changing conditions in Indonesia and abroad. To date, there have been seven generations of CoWs. A comparison of the various generations of CoWs is provided in Appendix E.

As discussed earlier, the Mining Law does not provide for CoWs under the new licensing framework, however the transitional provisions state that existing CoWs will be honoured until the stipulated expiry date, but from that point they can only be extended under the new IUPK licensing framework. Hence, the following discussion is only applicable to CoWs which existed prior to the Mining Law, and before any amendment following the Government's renegotiation process to align CoWs with the Mining Law. Any new mining activity can only be conducted under the IUP framework of the Mining Law.

CoWs were regulated under MoEMR Decision Letter No. 1614/2004. In essence, a CoW is a comprehensive contract between the Government and an Indonesian company. The company could be 100% foreign-owned. However, if the company was 100% foreign-owned, it may have been subject to divestment requirements at a later date. As a practical matter, most CoWs have some level of Indonesian ownership.

The CoW sets out the company's rights and obligations with respect to all phases of a mining operation, including exploration, pre-production development, production and mine closure. A CoW applies to a specifically defined geographical area (the contract Area).

The CoW company is the sole contractor for all mining in the CoW area, other than for oil and gas, coal and uranium. The CoW company has control, management and responsibility for all its activities, which include all aspects of mining such as exploration, development, production, refining, processing, storage, transport and sale.

The CoW outlines a series of stages with defined terms:

Stage	Term (Years)	Available Extension[1]
General survey [1]	1	6 months – 1 year
Exploration [2]	3	1 – 2 years
Feasibility study	1	1 year
Construction	3	-
Production	30	20 years or other period as approved by the Government

Note:
1) Depends on the CoW generation. For the detail, refer to Appendix E.
2) For first generation, the maximum period for general survey until feasibility study was 18 months, and can be extended for a maximum of six months

Some of the important considerations that are covered by a CoW include: expenditure obligations; import and export facilities; marketing; fiscal obligations; reporting requirements; records, inspection, and work programme; employment and training of Indonesian nationals; preference given to Indonesian suppliers; environmental management and protection; regional cooperation in relation to infrastructure; provision for infrastructure for the use of the local population and local business development. It is a tribute to the Government and to the industry that these important matters can be appropriately addressed in a concise legal contract.

The CoW covers all tax, royalty, and other fiscal charges, including: dead rent in the contract Area; production royalties; income tax payable by the company; employees' personal income tax; withholding taxes on dividends, interest, rents, royalties and similar payments; VAT; stamp duty; import duty; and land and buildings tax.

Coal Co-operation Agreements and Coal contracts of Work

CCoWs were regulated under MoEMR Decision Letter No. 1614/2004. Since November 1997, coal mining was brought more in line with general mining through the CoW structure. There have been two generations of CCAs (first and second generation contracts) and one generation of CCoW which is typically referred to as the third generation CCoW.

The first generation of CCA was regulated under the Presidential Decree No. 49/1981 dated 28 October 1981 regarding the Principal Regulation for Coal Co-operation Agreement between PT Tambang Batubara Bukit Asam (now PT Bukit Asam (Persero) Tbk or "PTBA"), the state-owned mining company, and the contractor. Presidential Decree No. 49/1981 was replaced by Presidential Decree No. 21/1993 dated 27 February 1993 which regulated the second generation of CCA. The third generation of CCoW was issued pursuant to Presidential Decree No. 75/1996 dated 25 September 2006.

Coal Co-operation Agreements

The key difference between the CCA and the CoW system is that under a CCA, the foreign mining company acted as a contractor to the Indonesian state-owned coal mining company, PTBA. Legislation has since been enacted and CCAs amended to transfer the rights and obligations of PTBA under the CCAs to the Government, represented by the MoEMR.

Under the CCA, the coal contractor is entitled to an 86.5% share of the coal produced from the area, and the contractor bears all costs of mine exploration, development and production. The Government (previously PTBA) retains entitlement to the remaining 13.5% of production. However, in accordance with Presidential Decree No. 75/1996 dated 25 September 1996, the contractors pay the Government's share of production in cash, which represents 13.5% of sales after the deduction of selling expenses.

For the first generation of CCA, equipment purchased by the coal contractor became the property of the Indonesian Government (previously PTBA), although the contractor has exclusive rights to use the assets and is entitled to claim depreciation. For the second and third generations of CCA and CCoW, the equipment purchased by the contractor remains the property of the contractor.

Foreign shareholders that own 100% of a first generation CCA are required to offer shares to Indonesian nationals or companies so that, after ten years of operating, foreign ownership in the company is reduced to a maximum of 49%.

Coal contracts of Work

Under the CCoW, the mining company is, in effect, entitled to 100% of the coal production however, a royalty of 13.5% of sales revenue is paid to the Government.

The CCA and CCoW outline a series of stages with defined terms:

Stage	Term (Years)	Available Extension (Years)
General survey	1	1 year
Exploration	3	2 years for third generation but not specifically mentioned in other generations
Feasibility study	1	1 year for third generation but not specifically mentioned in other generations
Construction	3	-
Production	30	-

Pre-contract of Work Expenses

The shareholder of the contract company would typically incur significant expenditure before the contract company is incorporated and the contract is signed. This pre-incorporation expenditure may be transferred from the shareholder to the contract company as deferred pre-operating costs, and will be amortised starting from the period in which production commences. These expenses are subject to audit by a public accountant and approval by the Minister and the Director General of Taxation ("DGT").

Exploration and Development

The stages coincide with decision points for the relinquishment of part of the contract Area. This section deals with the general survey, exploration, feasibility and construction stages.

Upon signing the contract, the company is required to lodge a US Dollar security deposit in the state-owned bank account, which is released upon completion of the following:

- Satisfactory completion of the General Survey period (50%); and
- Submission of a general geological map to the Ministry within 12 months of completion of the Exploration Stage (50%).

For the seventh generation of CoW or third generation of CCoW, the security deposit is released upon completion of the following:

- Satisfactory completion of the General Survey period (25%);
- End the first year of exploration (25%); and
- Submission of a general geological map within 12 months of completion of the Exploration Stage (50%).

During the preproduction stage, all of the companies signing the contract are required to submit detailed quarterly progress reports to the MoEMR. Under the contracts, the companies have responsibility for all of the financing requirements of the project and details are to be reported to the MoEMR.

For a company holding a contract, obligations are imposed throughout the life of the contract with respect to environmental restoration, the employment and training of Indonesian nationals, preference to Indonesian suppliers, and the provision of infrastructure for the use of the local community.

The company also has the following obligations under the contract:

contracts of Work	Coal Co-operation Agreements/ Coal contracts of Work
• General Survey Stage The company is obliged to spend an agreed amount during the General Survey stage. At the end of the period, the company must submit a report detailing the items and amount of expenditure and is required to relinquish at least 25% of the original contract Area.	• General Survey Stage The company is obliged to spend an agreed amount during the General Survey stage. At the end of the period, the company must submit a report detailing the items and amount of expenditure and is required to relinquish at least 25% of the original contract Area for second and third generations and 40% for first generation.

contracts of Work	Coal Co-operation Agreements/ Coal contracts of Work
• Exploration Stage In the Exploration stage, the company is obliged to spend an agreed amount per year on exploration activities. At the commencement of this stage, the company must submit an annual program and budget to the MoEMR. At the end of the Exploration stage, the company is required to file with the MoEMR: - A summary of its geological and metallurgical investigations and all data obtained; and - A general geological map of the contract Area. On or before the second anniversary of the commencement of the Exploration stage the company is required to have reduced the contract Area to not more than 50% of the original contract Area.	• Exploration Stage In the Exploration stage, the company is obliged to spend an agreed amount per year on exploration activities. At the commencement of this stage, the company must submit an annual program and budget to the MoEMR. At the end of the Exploration stage, the company is required to file with the MoEMR: - A copy of drill holes, pits and assays of the samples; and - A copy of geophysical or geological maps of the contract Area. On or before the second anniversary of the commencement of the Exploration stage the third generation company is required to have reduced the contract Area to not more than 25% of the original contract Area. First and second generation contractors are required to have reduced the contract Area to not more than 20% to 40% of the original contract Area.
• Feasibility Study Stage At the end of the Feasibility Study stage the company is required to submit a feasibility study, including environmental impact studies, to the MoEMR and to design the facilities. At the end of the Feasibility Study, the company is required to have reduced the contract Area to not more than 25% of the original contract Area.	• Feasibility Study Stage At the end of the Feasibility Study stage the company is required to submit a feasibility study, including environmental impact studies, to the MoEMR and to design the facilities. At the end of the Feasibility Study, the third generation CCoW company is required to have reduced the contract Area to not more than 25,000 ha.
• Construction Stage The company undertakes the construction of the facilities.	• Construction Stage The company undertakes the construction of the facilities.
• Dead Rent Throughout the life of the CoW, the company is required to pay dead rent. This is an annual amount based on the number of hectares in the CoW area and the stage of the CoW.	• Dead Rent Throughout the life of the contract, the company is required to pay dead rent. This is an annual amount based on the number of hectares in the approved area and the stage of the mining.

Production

During the production phase, the company is required to provide the following Exploitation reports to the MoEMR:

- Fortnightly statistical report;
- Monthly statistical report;
- Quarterly report concerning progress of operations;
- An annual report; and
- Other reports to various departments.

The company may export its production, but is encouraged to meet domestic demand first. Sales to associates are required to be at arm's length prices. Sales contracts exceeding three years are subject to Government approval.

The contract also requires contractors to provide the following reports to the MoEMR:

- Monthly statistical report;
- Quarterly report concerning progress of operations; and
- An annual report for the third generation of CCoWs.

The contract company may choose to operate the mine itself or it may sub-contract the operations of the mine, but outsourcing mining operations should now be considered in light of the rules contained in the Mining Law and PerMen 28/2009 as amended by 24/2012, which may be applicable to contracts.

Because a company can be party to only one contract (either a CoW, CCA or CCoW), it is common for mining groups to have more than one company in Indonesia. Group overheads can be borne by yet another company formed to service the group contract companies. This can provide operational efficiencies, but its tax implications should be considered further.

Other financial obligations

Royalties

Royalties are payable quarterly to the Government based on the actual volume of production or sales, according to the provision set out in the contract. However, in practice, currently the royalty is to be paid to the Government prior to shipment as required under the prevailing export administrative procedures.

Dead rent and Land and Buildings Tax (*Pajak Bumi dan Bangunan* or PBB)

The company is required to pay dead rent and PBB as set out in the contract. Dead rent is an annual charge based on the number of hectares in the Mining Area. PBB is certain percentage from the mining area.

3.2. *Fiscal regime under CoW, CCoW and CCA*

All generations of CoW, CCoW and CCA (collectively referred to hereafter as the contract(s)) except for the second generation CCA are based on the taxation and other laws and regulations in place at the time when the agreements were signed. In many circumstances, this means that the regulations affecting mining companies operating under such contracts differ from the current regulations which often creates difficulties in interpreting the agreements as well as doing business with other companies. Potential investors in mining properties covered by earlier generation contracts should seek professional assistance to examine such issues.

Many earlier generation contracts also include divestment requirements for foreign shareholders.

3.3. *Termination of the contract*

If at any time during the term of a contract the company believes the contract Area is unworkable, it may terminate the contract. The procedures for terminating the contract may be summarised as follows (this matter is not specifically mentioned in first and second generation CCoWs):

- Submit written notice to terminate the contract, attaching a closure plan, related documents, maps, plans, worksheets and other technical data and information.

Provided that the data and fulfilment of the company's obligations are considered acceptable to the MoEMR, the MoEMR will issue confirmation within six months from the date on which the company submitted the notice. Otherwise, the contract is automatically considered to be terminated, and the company shall be relieved of its obligations.

A general summary of the implications of termination of the contract at the various stages of the contract is set out below. All sales, removals or disposals of property will be subject to the tax rules set out in the contract:


Photo source : PT Bukit Asam (Persero) Tbk

a. General Survey and Exploration Period
    - The company has a period of six months to sell or remove its property, otherwise the property becomes the property of the Government; and
    - The company is required to provide any information gained from the work it has performed to the Department of Mines and Energy.
b. Feasibility Study Period
    - The company is required to offer all property located in the contract Area to the Government at market value;
    - The offer is valid for 30 days. If the Government accepts the offer, it is required to settle within 90 days; and
    - If the Government does not accept the offer, the company then has six months to sell or remove its property, otherwise the property reverts to the Government without any compensation to the company.
c. Construction Period
    - The conditions are identical to those for the Feasibility period except that, if the Government does not accept the offer, the company has 12 months to remove or sell its property.
d. Operating Period or Expiration of the contract
    - The company is required to offer all property located in the contract Area to the Government at market value;
    - The offer is valid for 30 days. If the Government accepts the offer, it is required to settle within 90 days; and
    - If the Government does not accept the offer, the company then has twelve months to sell or remove its property, otherwise the property reverts to the Government without any compensation to the company.

Upon the termination of the contract, any property that is used for public purposes such as roads, schools and hospitals with associated equipment immediately becomes the property of the Government without any compensation to the company.

3.4. *Transfer of the contract*

Purchase and sale of shares in a contract Company

Due to the difficulties involved in transferring a direct interest in a contract, it is common for such interests to be transferred indirectly through the transfer of shares in the company holding the contract, or through transferring the shares of holding companies above the company holding the contract.

However, the shareholders of the contract company cannot transfer shares prior to the commencement of the operating period, without the written consent of the Government.

The shareholders in the contract company also require the prior written consent of the MoEMR for a transfer of shares of the contract company after the commencement of the operating period. Under the terms of the contract, such consent shall not be unreasonably withheld or delayed.

Consent is not required in the case of a transfer of shares to:

- Indonesian Participants (as defined), or
- An affiliate or subsidiary of the shareholder.

Purchase and sale of direct interests in the contract

The contract does not allow the CoW/CCA/CCoW companies to transfer or assign all or part of their interest in the contract without the prior written consent of the Government. On such a transfer, the company is not relieved of any of its obligations under the contract, except to the extent that the transferee or assignee assumes and performs such obligations.

Unincorporated joint ventures

As alluded to above, transfers of partial interests in contracts are rare events, and require some degree of negotiation with the MoEMR. For this reason, joint venture ownership and operation is equally unusual. The contract and the income tax legislation are silent as to the tax treatment of joint ventures. The tax treatment of a joint venture is one of a number of matters to be negotiated with the MoEMR in conjunction with the transfer of an interest in the contract that creates the joint venture.

Farm-ins

The contract and the income tax legislation of general application do not address farm-ins per se. As a commercial matter, a typical farm-in to a mineral property involves an eventual transfer of an interest in the property. Accordingly, the farm-in arrangement, and the tax treatment thereof, will be considered by the Minister in conjunction with his consideration of approval of the transfer. A farm-in can usually be effected more easily through a transfer of shares in the offshore investing company.

3.5. CoW and CCoW renegotiation

As discussed above, pursuant to the Mining Law of 2009, it is intended for the terms of existing mining contracts (CoWs and CCoWs) to be brought into line with the provisions of the Mining Law. Accordingly, the Government has approached many (if not all) CoW and CCoW holders to commence negotiations to amend the terms of contracts.

The key areas in which the Government is seeking to negotiate are as follows:

a. The size of mining areas: the Government is looking for CoW and CCoW holders to make additional relinquishments to bring the acreage closer to that of licences issued under the Mining Law (please refer to the Licence Areas section on page 35 for more details)
b. contract extensions: the CoW and CCoW will be extended as per IUPK (please refer to Transitional Provisions for CoWs/CCoWs/CCAs section on page 58 for more details)
c. The amount of royalties: the Government proposes to increase the royalty rates
d. Obligations to process raw materials in Indonesia: the CoW and CCoW holders were required to increase the level of value-added processes carried out in-country (please refer to the Mandatory in-country processing and export restrictions section on page 42 for more details);
e. Divestment: foreign shareholders are required to divest up to 51% of their interest in the CoW and CCoW company (please refer to the Divestment of foreign shareholding section on page 50 for more details);
f. Utilisation of local goods and services: further restrictions on the use of affiliated service companies and promoting the use of local service contractors (please refer to the Restriction on the use of affiliates/subsidiaries section on page 56 and Service providers to the mining industry section on page 95 for more details), and
g. Tax provisions (except for Corporate Income Tax ("CIT") rate): tax provisions are to follow the prevailing regulations.

Up to December 2016, it has been reported that the Government has signed contract amendments with nine CoW and 22 CCoW holders. The amended contract terms are generally consistent with the agreed terms in earlier negotiated memoranda of understanding.

Meanwhile, reports indicate there are still 25 CoW and 47 CCoW holders who have not agreed with several terms in the proposed amendments and five CCoWs which have been terminated or are in the process of termination.

Given that contracts are specific to each contract holder, the outcomes from the negotiations will vary, however one of the key sticking points has been the Government's refusal to agree to any change which would reduce the amount of State Revenue collected under the contract. Accordingly, the holders of earlier generation CoWs and CCoWs, which lock in a higher rate of tax, are reluctant to agree to any significant changes if the tax and royalty rates cannot be reduced. Similarly, the maximum size of mining areas under the Mining Law are significantly smaller than some CoWs and CCoWs, which is also proving a hurdle to aligning existing contracts with the Mining Law.

It is still not clear that more than eight years on from the issuance of the Mining Law any significant progress has been made in finalising the renegotiated terms especially for the first and third generation CCoW holders. The industry will be keen to see the Government's approach to this, and hopes for a strong commitment to respecting contract sanctity.

Photo source :
PT Aneka Tambang (Persero) Tbk

4.0 Tax Regimes for the Indonesian Mining Sector

4.1. *General overview of Indonesian tax systems*

On an annual basis, PwC Indonesia publishes the Indonesian Pocket Tax Book. This publication provides a general guide to the prevailing Indonesian Tax Laws and regulations and is available on PwC Indonesia's website (www.pwc.com/id).

4.2. *Tax regime for an IUP/IUPK company*

General

The Mining Law stipulates that any tax facilities for a mining project should be provided in accordance with the prevailing laws except as otherwise stated in the IUP/IUPK. This indicates that tax concessions outside of the prevailing Tax Law/regulations may still be available.

However, it appears that there is a strong intention on the part of the Government to apply the prevailing Tax Laws/regulations to IUP/IUPK holders. Therefore, in practice, special tax provisions with overriding status (*lex specialis*) may not be available for an IUP/IUPK, as is the case for already issued IUPs.

A company holding an IUP/IUPK is required to register for tax and obtain a tax registration number. The tax registration number is called Nomor Pokok Wajib Pajak ("NPWP"). The IUP/IUPK company is also required to register for tax at the local tax office within whose jurisdiction the mine operates which includes Value-Added Tax ("VAT") obligations (if applicable and not centralised in the head office) and Withholding Tax ("WHT").

CIT

Under the prevailing ITL, the Government may issue a GR governing taxation of mining business. As at the date of this publication a GR on mining taxation has not been issued. Thus, unless specifically stipulated the prevailing tax rules are likely to apply.

Below are some of the main tax considerations which will be relevant to a mining investor.

CIT Rate

Under the prevailing ITL/regulations a company is subject to CIT on its net taxable profit. The net taxable profit is calculated based on gross income minus allowable expenditure.

CIT rate is 25% of net taxable profit. A 5% income tax reduction is applicable for companies listed on the IDX, subject to meeting certain requirements.

General expenses

Broadly, deductible expenses are those incurred to generate, maintain and collect taxable income and generally include the amount paid or accrued for all expenditure attributable to the company's operations in a year which typically has a useful life of less than one year.

Certain expenditure may not be tax deductible under the ITL such as certain donations and benefits-in-kind provided to employees. Some types of benefits-in-kind provided at the mining site may be deductible if the mine is located in a remote area and approval from the DGT is obtained.

Specific operating expenses of a mining operation may include supplies, contracted services, insurance, royalties on intellectual property, processing expenses, repairs and maintenance, etc. These should be deductible in the year in which they are incurred.

Selling, general and administrative expenses are generally tax deductible in the year in which they are incurred.

Income

Gross income usually represents sales of mining products and any other income earned by the mining company.

Exploration and development expenses

Exploration and development expenses may include camp construction, drilling, access roads, project communication facilities, etc.

On-site exploration expenses are generally deductible in the year incurred, provided that the expenses meet the general deductibility criteria.

Major exploration and mine development expenses should generally be capitalised and amortised upon spending rather than production.

Tax losses carried forward

Tax losses can be carried forward for up to five years under the prevailing ITL and are recouped on a first-in-first-out basis. Tax losses cannot be carried back.

Non-interest bearing loans

It is common for a shareholder to not charge interest on loans to subsidiaries during the exploration and development stage. However, care should be taken to structure the loan terms and conditions to ensure that the transfer pricing rules are observed. Non-interest bearing loans from Shareholders are only allowed if certain requirements are met.

Depreciation of fixed assets

Fixed assets are categorised into four categories depending on the nature of the asset and its expected useful life. The rate at which assets can be depreciated will depend upon the category of the asset. Assets are generally depreciated over 4, 8, 16 or 20 years and taxpayers may apply a diminishing balance or straight line approach to depreciation.

Reclamation reserve

For accounting purposes, a mining company is usually required to maintain a reclamation reserve in its accounts for environmental management and reclamation work during the contract period and at the end of the life of the mine. During exploration the reclamation reserve should be in the form of a time deposit with a local bank.

The reclamation reserve should be deductible provided that it is calculated in accordance with prevailing energy/mineral resources sector laws/regulations. If the actual cost exceeds the reserve the balance is generally deductible.

Amortisation of intangible assets

Intangible assets may include pre-operating costs, patents, rights, licences, etc. Intangible assets can be amortised over an effective life of either 4, 8, 16 or 20 years using either a diminishing balance or straight line approach.

For costs incurred for the acquisition of mining rights with a beneficial life of more than one year these costs should be amortised based on a production unit method not exceeding 20% per annum.

Mine closure

The prevailing ITL is not clear on whether a provision for mine closure (e.g. mine infrastructure demobilisation costs) is deductible. Since mine closure costs are usually spent in the later stages of a mine's life when the company is earning little or no income, proper planning is crucial to ensure the utilisation of deductions from these costs. The current regulations on reclamation reserves are silent on the matter of mine closure reserves therefore mine closure reserves are unlikely to be deductible, until the costs are spent or funded.

Thin Capitalisation Rule

On 9 September 2015, the MoF issued the “thin capitalisation” rule under PMK No.169/PMK.010/2015 (PMK 169). PMK 169 is effective for fiscal year 2016 onwards. The thin capitalisation rule provides a maximum ratio between debt to equity (DER) of 4:1. PMK 169 excludes CCoWs/CoWs where the respective contract specifies the applicable DER.

PMK 169 disallows deductions on interest expenses in the following circumstances:

- Entirely if equity is zero or negative;
- Partly, according to the portion of the loan exceeding the DER;
- Partly, according to the portion of the loan associated with final tax income (e.g. land and/or buildings rental); and
- Entirely for non-reporting offshore private loans (to be further clarified in a subsequent DGT regulation).

PMK 169 defines interest to include discounts or premiums, arrangement fees, interest on leasing, compensation for loan guarantees, and the related foreign exchange. Even when the DER is within the permitted level, the ITL requirements should still be complied with, meaning a challenge on interest deductions would still be possible if, for example, the loan was used to generate Indonesian bank interest income, the loan was used to finance benefits in kind, the interest rate was not arm’s length or the related party loan leverage was beyond industry practice.

Transactions with related parties

Payments to affiliates may be deductible if they are directly attributable to mining operations. However the amount of the deduction is limited to that which would have been paid to a non-related party for the same service.

The DGT has increased its audit focus on related party transactions. Taxpayers must disclose a significant amount of detail in their CIT return regarding the levels of related party transactions that exist and must also be able to justify the use of a particular pricing methodology. The DGT has started performing transfer pricing audits. As a result, taxpayers with related party transactions must carefully consider their transfer pricing positions.

The application of the mineral/coal benchmark prices to related party transactions for tax purposes is unclear. The benchmark pricing regulations currently only apply for the basis of performing the Government Royalty calculation (i.e. they do not technically apply to CIT). However, given that the major coal indices are used as the basis for setting the benchmark price, this price is generally used as the reference point by the DGT in determining the arm’s length price.

Bookkeeping in US Dollars

For tax purposes, a PMA company may request authorisation to maintain bookkeeping in US Dollars and in English. The company must request approval no later than three months after establishment or three months before the commencement of the US Dollar accounting year (for an established company.)

Following the recent adoption of accounting standards concerning the use of an appropriate functional currency (consistently with International Financial Reporting Standards) wholly-Indonesian owned entities, in addition to PT PMAs, can now elect to use the US Dollar rather than the Indonesian Rupiah as their bookkeeping currency for tax purposes where a currency other than the Rupiah is their functional currency. The same deadlines for application apply.

For tax purposes however, the US Dollar is the only alternative to the Indonesian Rupiah.

Article 22 Income Tax Collection

On 9 June 2015, the MoF issued PMK No.107/ PMK.010/2015 (PMK 107) which included transactions subject to Article 22 Income Tax. PMK 107 became effective on 8 August 2015.

PMK 107 requires a party which purchases coal and minerals from an entity (or individual) holding an IUP to collect and remit Article 22 Income Tax at 1.5% of the purchase price at the time of purchase. PMK 107 also stipulates that Article 22 Income Tax at 1.5% is applicable to export of coal and minerals by IUP companies (remitted upon export).

Furthermore, the sale of gold bars, other than where sold to Bank Indonesia or where processed into jewellery for export, is also subject to Article 22 Income Tax at 0.45%. This is collected by the gold producer.

The Article 22 Income Tax constitutes a CIT prepayment (cash flow concern only).

Tax Allowances

The Government provides several tax allowances in GR 18/2015 along with PMK No. 89/ PMK.010/2015. On 15 April 2016 the Government issued GR 9/2016 which amended the list of businesses eligible to apply for tax allowances, across a wide range of industry sectors and geographical regions as set out in GR 18/2015. GR 9/2016 came into effect on 9 May 2016. GR 9/2016 does not change the criteria for the eligible mining sectors.

The tax allowances consist of:

- A reduction in net taxable income of up to 30% of the amount invested in the form of qualifying fixed assets (including land), prorated at 5% for 6 years and provided that the assets invested are not being misused or transferred out within a certain period;
- Accelerated depreciation and amortisation;
- Withholding taxes on dividends paid at non-residents at 10%; and
- An increased loss carry forward period from five years to a maximum of ten years.

In relation to the mining sector tax incentives are available, subject to the satisfaction of certain criteria, for:

- Basic iron and steel manufacturing;
- Gold and silver processing and refining;
- Certain brass, iron ore, uranium, thorium, tin, lead, copper, aluminium, zinc, manganese and nickel processing and refining activities;
- Coal gasification; and
- The use of coal for energy liquefaction.

Apart from the processing and refining of copper, silver and gold, these income tax incentives are generally only applicable to activities undertaken outside Java.

GR 9/2016 sets detailed requirements under each designated business sector and/or region which relate to the investment value, number of Indonesian workers and the size of the business area. This regulation only sets out new high level criteria as a requirement for enjoying the tax incentives and leaves the detailed requirements to be determined by the relevant ministers.

GR 18/2015 as amended by GR 9/2016 confirms that taxpayers who obtain this tax incentive cannot use the other tax facilities such as those for Integrated Economic Development Zones (Kawasan Pengembangan Ekonomi Terpadu/KAPET) or Tax Holidays.

Tax Holidays

The government provides tax holidays through PMK No.159/PMK.010/2015 which provides a CIT reduction from 10% up to 100% of the CIT due for 5 - 15 years from the start of commercial production. The period can be extended to 20 years if the investment is deemed to be in the national interest.

For the mining sector, the tax holiday is available for the upstream metal industry. The tax holiday is applicable to the relevant pioneer industry taxpayers established on or after 15 August 2011 which have new capital investment plans of at least Rp 1 trillion, meet the 4:1 DER and commit to placing a time deposit equal to 10% of the planned investment value in Indonesian banks.

Many smelter companies expect to be eligible for the tax holiday facility. However, by including the smelter business in the tax allowance, the Government wishes to encourage investors in smelters to (only) apply for the tax allowance (and not the tax holiday). At the time of writing, we were not aware of any tax holiday facility having been granted for a smelter company.

VAT

The delivery of goods and services in Indonesia is generally subject to VAT except for the delivery of certain pre-determined types of goods and services. The current VAT rate is 10%.

The prevailing VAT Law stipulates that supplies of gold bars, coal and natural resources taken directly from source are not subject to VAT. This VAT position may change according to the level of processing of the mining product in question. In respect of coal, there are a number of private rulings from the DGT indicating that washing or crushing activities do not constitute processing (although briquetting activities do). Further issues may arise in this respect once the detailed requirements of the Mining Law in respect of in-country processing are stipulated.

In the event that a company delivers a non-VAT-able mining product (e.g. gold bars and coal), any Input VAT incurred on the import and/or domestic purchase of goods/services will not be creditable/refundable and so effectively becoming an additional cost (which should be deductible).

During pre-production, only Input VAT incurred on purchases of capital goods is creditable. Furthermore since during pre-production the company will not have any Output VAT, a VAT overpayment is likely.

For most companies, a VAT refund is only available at the end of the year. However, companies that incur VAT during pre-production may still apply for refunds in respect of VAT on capital goods on a monthly basis. However, if they fail to commence production (defined as the delivery of VATable goods/services) within three years (may be extended to five years) from the date on which they credit the Input VAT, they must repay the VAT refund by the end of the month following the failure to enter production. This timing requirement obviously presents a problem for long-term mining projects which may take several years to enter into production.

WHT

Taxpayers, including mining companies, are obliged to withhold tax on payments for dividends, interest, royalties and most types of services.

WHT is payable on dividends, interest and royalties paid to Indonesian companies at the rate of 15%. However, in the case of dividends, provided that the dividend is sourced from retained earnings and the Indonesian corporate shareholder owns at least 25% of the mining company's shares, the dividend will not be subject to income tax including WHT.

A 2% WHT is applicable on payments for most types of services made to Indonesian resident entities.

If the payments are made to a non-resident the WHT rate is 20%. A tax treaty may provide outright relief on services payments and reduce the WHT on payments of dividends, interest and royalties (generally to 10% or 15%). The DGT regulated procedures are to be followed to access the benefits of a tax treaty including a pre-determined disclosure form, and measures to prevent tax treaty abuse.

Land and Buildings Tax (*Pajak Bumi dan Bangunan* or "PBB")

The DGT issued PER 47/2015 regarding Procedures for the Imposition of PBB within the Mining Sector for Minerals and Coal Mining, which revoked PER 32/2012. PER 47/2015 became effective on 1 January 2016.

In general, PBB in the mining industry covers land and/or buildings located in mining areas including locations in the mining licence area and outside the mining licence area which are used for mining activities. It is applicable to both onshore and offshore activities.

Details of land and buildings defined as PBB objects include:

a. Land consisting of:
   - Land surface which includes: (1) onshore areas (such as reserve production areas, unproductive areas, emplacement areas, security areas, etc); and (2) offshore areas;
   - Subsurface areas used in the exploration and production stages; and

b. Building structures permanently attached to the land and/or areas of water and used for mining activities.

The PBB rate is 0.5% of the taxable sale value of the PBB object. The taxable value for mining is stipulated as being a proportion of the sale value of the PBB object at 40% of the sale value for PBB objects.

The sale value of the PBB objects are determined by the DGT on behalf of the MoF and are updated periodically depending on the economic development of the Region in question.

Specifically for land and buildings used for mining, the sale value should also take into account the net income from the mining activity (gross income less production costs). PER 32 provides a detailed explanation of how this calculation should be performed.

Photo source :
PT Bukit Asam (Persero) Tbk

4.3. *Tax regime for a CoW/CCoW/CCA company*

One of the key features of a CoW/CCoW/CCA (contract) is its *lex specialis* status – that is, the terms in the contract override the general law. For example, when certain specific tax rules are set out in a contract these tax rules generally take precedence over the prevailing Tax Laws.

Generally, the tax rules in a contract reflect those in force at the time when the contract is signed although there may be some exceptions. Typically, a contract fixes the tax rules for the duration of the contract (with the exception of second generation contracts where they generally follow the prevailing tax regulations).

Taxation matters that are not governed in the contract should follow the prevailing Tax Laws and regulations (as discussed above).

The advantage of having *lex specialis* tax rules in a contract includes tax stability throughout the life of the project or at least up to the end of the contract term.

The disadvantage of *lex specialis* status is that the mining company may not always be able to access favourable changes in the ITL such as a reduction in income tax rates or the introduction of tax incentives. Despite this, the *lex specialis* tax rules have historically been favoured by investors particularly for big long-life mining projects because it provides stability in various aspects of mining operations including tax.

The mining tax regime included in a contract is relatively straightforward. However, in some cases, the language in the contract may be interpreted widely which can result in disputes between the mining company and the DGT.

The transitional provisions of the Mining Law (Article 169) provide that existing contracts will remain effective until the expiration date. However, the contracts should be adjusted within one year to conform with the Mining Law except for provisions on state revenue (note that the exception is not applicable if there are efforts to increase the state revenue). Currently, the circumstances in which the government can seek to amend the tax/non-tax state revenue provisions in a contract remain unclear. The Government has been involved in negotiations with individual contract companies regarding revisions to the contract terms, but as yet there have not been any wholesale changes to contracts. Rather, any changes have been made on a case by case basis. At present, there is still no guidance on how Article 169 of the Mining Law will be implemented, although it is understood that the Government tends to require the CoW/CCoW companies to follow the prevailing Tax Law except for the corporate income tax rate (which may be higher than the prevailing rate).

The major recent development is in relation to the DGT's formal view on the CIT rate that should be applicable for third generation CCoWs and sixth/seventh generation CoW companies. As a background, the relevant CoW/CCoW companies would expect to apply the CIT rate of 25% in accordance with the prevailing Income Tax Law. However, the DGT issued SE 44/2014 confirming its view that these companies are subject to CIT at the rate of 30% (i.e. the CIT rate indicated in the Income Tax Law applicable upon the signing of the contract).

Note that the tax treatments described in this booklet are generic and variations may exist between the various generations of contracts. Appendix E summarises the typical tax treatments in the particular generations of contracts. Not all generations of contracts have specific tax rules and as such those contacts may simply require the tax treatments to follow the prevailing Income Tax Law. In assessing the applicable tax regime, a detailed review of the contract is necessary because different rules may exist between two contracts of the same generation.

Tax registration

A company holding a contract is required to register for tax and obtain a NPWP.

The contract company should register for tax at the local tax office where the mine operates. These include the obligations for VAT (if applicable and not centralised at head office) and WHT.

Bookkeeping in US Dollars

For tax purposes, a contract company may opt to apply bookkeeping in US dollars and in English language. The company only needs to notify the DGT of the US dollar bookkeeping, no later than a month before the commencement of the US Dollar accounting year.

Irrespective of the currency and the language used, the company may settle their corporate income tax liabilities in Rupiah or US Dollars, and file tax returns in Indonesian language. With respect to CIT, relevant tax returns should be presented in US Dollars side by side with Rupiah in the annual CIT return.

CIT

Similarly to an IUP/IUPK company, a contract company is subject to income tax on its net taxable profit. In the contract, the expenditure described below is normally allowed to be deducted from the gross income.

The mineral CoWs typically have *lex specialis* CIT rules. In respect of a CCA/CCoW, the first and most of the third generation contracts include *lex specialis* CIT provisions whilst the second and remaining third generation CCoWs do not. Where *lex specialis* tax rules do not apply the company must follow the prevailing income tax rules for the CIT calculation.

CIT rate

Where a contract includes a specific CIT rate these contract companies may not be entitled to the reduced 25% CIT rate under the general tax law which is applicable from the 2010 income year onwards (the rate was reduced from the previous 30%).

The CIT rate applicable to the third generation CCoW and sixth/seventh generation CoW companies has been a longstanding issue not least because these CCoWs/CoWs typically provide a *lex specialis* tax framework linked to the 1994 Income Tax Law (i.e. with a 30% maximum CIT rate) but the relevant provision in the contract could be subject to a different interpretation.

On 24 November 2014, the DGT issued SE 44/2014 which states that, in the DGT's view the 30% CIT rate continues to apply. The DGT had also imposed interest penalties on some taxpayers who applied the 25% CIT rate. Taxpayers continue to challenge the DGT's interpretation given their view of the spirit of the tax rate provisions in the contract, which they believe alows them to access any reductions in CIT rates.

Exploration and development expenses

On-site exploration expenses are generally deductible in the year the expenses are incurred provided the expenses relate to the contract area.

Mine development expenses should generally be capitalised and amortised in accordance with the amortisation rules in the contract.

Reclamation reserve

As per the prevailing tax rules however, some generations of contracts may require reference to the previous Income Tax Law and/or a deposit with a state-owned bank in order for the reclamation provision to be deductible.

Operating expenses

Generally as per the prevailing law.

Selling, general and administration expenses

Generally as per the prevailing law.

Asset revaluation

Generally as per the prevailing law.

Employee benefits/ facilities

The contracts normally provide concessional tax treatment on benefits provided to employees who reside in the contract Area. The cost of most benefits provided to employees located in the contract Area is deductible but is not taxed in the hands of the employees

Pre-contract expenses

The shareholder(s) of the contract company may generally incur expenditure before the contract company is incorporated and the respective mining contract is signed.

A contract normally allows these pre-incorporation expenses to be transferred from the shareholder(s) to the contract company. The pre-incorporation expenses are recognised as deferred pre-operating costs and may be claimed as deductions by way of amortisation starting from commencement of production.

Most contracts require these pre-incorporation expenses to be audited by a public accountant and approved by the DGT. The implementation of this rule is not entirely clear.

There are also a number of transactional tax issues to be addressed in relation to the transfer of pre-incorporation expenses from the shareholder(s) to the company in particular the VAT and WHT obligations (although VAT may be exempt under the contract).

Depreciation of fixed assets

Fixed assets are generally deductible through depreciation. Different generations of contracts include different depreciation rules but most offer an accelerated rate.

Mining infrastructure such as buildings, roads, bridges and ports are generally depreciable. Public infrastructure such as roads, schools and hospitals are usually deductible through depreciation under the contract's rules.

Fixed assets should be classified into several different categories based on their useful life. Accelerated depreciation rates may be available for fixed assets located in the contract Area. Earlier generations of CCoW/CCA usually provide an investment allowance deduction (i.e. hypothetical depreciation) and have a fixed depreciation rate based on the straight line method irrespective of the type of assets.

For certain contracts, if the mine life is shorter than the asset's fiscal useful life, the remaining book value may be fully depreciated at the end of the mine life.

Interest expenses

Most CoWs/CCoWs provide specific rules on DER. If such rules are not available in the contract, the company should follow the DER as stipulated in PMK 169.

Carried forward tax losses

Under a contract, tax losses can be carried forward for the period stipulated in the contract. This may be more or less than the five years carry forward allowed under the prevailing Income Tax Law. Tax losses cannot be carried back.

Amortisation of intangible assets

Intangible assets may include pre-operating costs, patents, rights, licences, etc.

Expenses incurred prior to production (with a useful life greater than one year – some contracts do not require this) may be capitalised and amortised once production commences. These expenses may also include expenses incurred by the contract company's shareholder(s) prior to the formation of the company (i.e. pre-incorporation expenses).

PBB

PBB for CoW and CCoW are usually specifically governed under the contract.

Sales Tax

Before the enactment of the VAT Law in 1984, Indonesia adopted a Sales Tax. Under the *lex specialis* rules Sales Tax is still applicable to the Generation 1 CCA companies. Sales Tax is imposed at 5% maximum on certain services provided to the contractors, and payable on a self-remittance basis (similarly to WHT).

From 1 January 2013, PMK No.194/PMK.03/2012 provides that Generation 1 CCA contractors should also not collect VAT on these services.

VAT

With the exception of the above CCA contractors, CoW/CCoW companies are subject to VAT on the utilisation of services and goods. However, some contracts may adopt a VAT regime different to the prevailing VAT regulations. For example, Input VAT may be creditable despite the fact that coal or gold bars are being produced, which are exempt from output VAT.

During pre-production the company will not have any Output VAT due to there being no deliveries of mining products. Therefore VAT overpayment is likely as the company should pay its Input VAT to vendors for purchases of taxable goods/ services.

Until 2004, mining companies were designated as VAT Collectors meaning that the mining company should collect and pay the VAT charged by vendors (i.e. Input VAT) directly to the State Treasury, rather than to the respective vendors. Some contract companies continue to act as VAT collectors as required by the relevant contract.

Subject to the tax rules in the contract, the company may claim a refund on the Input VAT paid but must undergo a tax audit.

All VAT payments are denominated in Rupiah. If the company keeps its books in US Dollars, outstanding VAT receivables could give rise to foreign exchange issues if long outstanding.

WHT

CoW/CCoW companies are obliged to withhold tax from payments of dividends, interest, royalties and most types of services. The WHT rate will depend on the tax rules stipulated in the contract, the type of payment and whether the recipient is a resident or non-resident.

However, pursuant to PMK No.39/PMK.11/2013 the MoF requires CoW/CCoW companies to apply the prevailing WHT rates on certain services (although this is often disputed by CoW/CCoW companies under the *lex specialis* principles).

Imports of Capital Equipment

Most contracts provide an exemption from Import Duty, VAT and Income Tax on imports of capital equipment for up to a year after the commencement of commercial production.

If no import facility is available under a contract, reliefs or exemptions may be available under the prevailing law.

On 30 December 2016, the MoF issued PMK No.259/ PMK.04/2016 (“PMK 259”) which revokes PMK No.110/ PMK.010/2005. PMK 259 provides certain requirements for the transfer or re-export or destruction of goods imported by CoW/CCoW companies that obtain exemption from the Import Duty and VAT upon importation of the goods. In general, any transfer/ re-export/ destruction of goods imported with exemptions within five years need to obtain a recommendation from BKPM and approval from the Customs Office. Failure to meet these requirements may lead to the Import Duty and VAT becoming payable plus the associated penalties. This regulation is effective from 3 February 2017.

4.4. *Other taxation considerations*

Non-Tax State Revenue

Royalties

Royalties are payable quarterly to the Government based on the actual volume of production or the sales price. For CoW/CCoW holders this is based on the terms of the contract. However, based on the prevailing regulations and current practice the royalty should be paid prior to shipment.

The prevailing royalty rates applicable to IUP/ IUPK holders are set out in Section 2.

Dead Rent

Throughout the life of the contract the company is required to pay dead rent. This is due annually and the amount is normally calculated based on the number of hectares in the contract/licence area and the stage of the mining operations (e.g. different rates for general survey, exploration, and exploitation stage).

Regional Tax

A mining company may be liable for a number of Regional Taxes and Retributions. The rates range from 1.5% to 35% of a wide number of reference values determined by the relevant regional Government. contracts may limit the additional types and rates of Regional Tax introduced after the signing date of the contract. A summary of the types of regional taxes that may apply is included at Appendix B.

Transfers of Mineral Interests

Purchase and sale of mining interests

The direct transfer of a contract is subject to a number of restrictions which make such transfers uncommon. As set out below, the assignment of a contract would create a number of difficult tax issues. The transfer of ownership (in whole or in part) is therefore generally achieved through the disposal of an interest in the company holding the contract.

The prevailing ITL stipulates that gains arising from the transfer of a mining interest, financing participation or capital investment in a mining company are subject to Income Tax.

The prevailing ITL also stipulates that the Government will issue a separate GR on the calculation of Income Tax for the mining sector. The GR may cover the Income Tax on the transfer of a mining interest. However to date, no mining sector specific GR has been issued in respect of the calculation of Income Tax.

Technically, the transferor might include the proceeds of the sale of the mining interest as income for Income Tax purposes, whilst the transferee is entitled to deduct the purchase price in accordance with the rules for deducting the cost of intangible assets.

There are several tax issues which need to be resolved in respect of the assignment of a contract. This includes the tax implications of the transfer of the tangible assets (such as mine infrastructure equipment, etc.) and intangible assets (such as Deferred Exploration Expenditure) to the buyer without creating any additional tax costs. Therefore, specific advice should be sought on the tax impacts arising from the sale of mining rights.

Purchases and sales of shares in an IUP/IUPK or contract company

This approach is common for the acquisition of mine properties in Indonesia.

The sale of shares is a taxable event. For a domestic seller, Income Tax is imposed on the profits earned from the sale. For a non-tax resident seller, a 5% income tax on gross proceeds is due unless relief is available under a tax treaty or the company being sold is a listed company in Indonesia (in this case, a 0.1% final tax is due on the sale proceeds).

The prevailing ITL provides for a long-arm capital gains tax provision. The DGT can treat the sale of a conduit or special purpose company established in a tax haven country which has an Indonesian PE or subsidiary as the sale of an interest in an Indonesian company. In this case, the DGT can impose 5% final income tax on the gross sale proceeds.

The implementation and further development of this new rule should be closely monitored, since to date there has still been no clear definition of what will constitute a tax haven, or what the implications will be if the indirect ultimate shareholder of the tax haven company is resident in a jurisdiction with which Indonesia has a tax treaty.

Investment Structuring

As a general rule of thumb, a tax efficient investment structure would create significant tax savings for the life of mine, which in turn would increase the economic value of the mine. A favourable structure would also be effective for project financing purposes. Care must therefore be taken in structuring the initial investment in the mining industry. Some relevant contract and IUP/IUPK issues to be aware of include:

- A company can only hold one contract or one IUP/IUPK. This ring fencing rule, together with the fact that there is no group relief for Income Tax purposes, requires careful planning, particularly for the use of service companies within one group, inter-company charges, inter-company borrowing, etc;
- The use of a tax efficient shareholding structure to maximise profit repatriation/ dividends would enhance the project feasibility (note that under some tax treaties the WHT on dividends may be reduced from 20% to 15% or 10%);
- Sales of shares in contract or IUP/IUPK companies that are not listed on the IDX by foreign investors are taxed at 5% income tax on gross proceeds, unless protected by a tax treaty. The investment may be structured to reduce the tax on exit;
- A typical concession in some of the contracts of a reduced WHT rate for dividend tax payments to founder foreign shareholder(s);
- The use of tax efficient project financing strategies or intra-group financing considering the thin capitalisation rules and the fact that debt forgiveness is subject to tax in Indonesia (this issue is common in unsuccessful exploration projects); and
- The best investment structure and arrangements for the mineral processing and refinery businesses.

Professional advice should be obtained at an early stage of the investment process. This includes the investment structuring considerations and financial/tax due diligence on the target mining company.

5.0

Accounting Considerations

The accounting considerations section below discusses certain accounting issues that are commonly faced by a mining company operating in Indonesia. The discussion in this Guide does not attempt to cover all accounting issues applicable for a mining company operating in Indonesia. Please contact one of our advisers listed in Appendix F to discuss further.

5.1. Exploration and evaluation

Exploration costs are incurred to discover mineral resources. Evaluation costs are incurred to assess the technical feasibility and commercial viability of the resources found. Exploration starts when the legal rights to explore have been obtained. Expenditure incurred before obtaining the legal right to explore is generally expensed; an exception to this would be separately acquired intangible assets such as payment for an option to obtain legal rights.

The accounting treatment of exploration and evaluation ("E&E") expenditures (capitalising or expensing) can have a significant impact on the financial statements and reported financial results, particularly for entities at the exploration stage with no production activities.

Statement of Financial Accounting Standard ("SFAS") No. 64 "Exploration for and evaluation of mineral resources" sets out the accounting for E&E expenditures. Under SFAS No. 64, an entity shall determine an accounting policy specifying which expenditures are recognised as exploration and evaluation assets and apply the policy consistently. In making this determination, an entity considers the degree to which the expenditure can be associated with finding specific mineral resources. An entity may change its accounting policies for exploration and evaluation expenditures if the change makes the financial statements more relevant to the economic decision-making needs of users and no less reliable, or more reliable and no less relevant to those needs. An entity shall judge

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relevance and reliability using the criteria in SFAS No. 25 “Accounting Policies, Changes in Accounting Estimates and Errors”.

Expenditures incurred in exploration activities should be expensed unless they meet the definition of an asset. An entity recognises an asset when it is probable that economic benefits will flow to the entity as a result of the expenditure. The economic benefits might be available through commercial exploitation of mineral reserves or sales of exploration findings or further development rights. It is often difficult for an entity to demonstrate that the recovery of exploration expenditure is probable.

Evaluation activities are further advanced than exploration and hence are more likely to meet the criteria for recognising an asset. However, each project needs to be considered on its merits. The amount of evaluation work required to conclude that a viable mine exists will vary for each area of interest.

Management needs to develop a consistent and transparent accounting policy that is applied through the various phases of exploration and evaluation activity, highlighting the cut-off point before capitalisation of costs commences. Costs incurred after probability of economic feasibility is established are capitalised only if the costs are necessary to bring the resource to commercial production. Subsequent expenditures should not be capitalised after commercial production commences, unless they meet the asset recognition criteria.

Exploration and evaluation assets can be measured using either the cost model or the revaluation model. In practice, most companies use the cost model. Depreciation and amortisation of E&E assets usually does not commence until the assets are placed in service. Exploration and evaluation assets recognised should be classified as either tangible or intangible according to their nature.

Exploration and evaluation are reclassified from the Exploration and Evaluation account when evaluation procedures have been completed. Exploration and evaluation assets for which commercially-viable reserves have been identified are reclassified to development assets. Exploration and evaluation assets are tested for impairment immediately prior to reclassification out of Exploration and evaluation and when impairment indicators are identified, which include but not limited to:

- Rights to explore in an area have expired or will expire in the near future without renewal;
- No further exploration or evaluation is planned or budgeted;
- A decision to discontinue exploration and evaluation in an area because of the absence of commercial reserves; and
- Sufficient data exists to indicate that the book value will not be fully recovered from future development and production.

5.2. Development

Development expenditures are costs incurred to obtain access to proved and probable reserves and to provide facilities for extracting, treating, gathering, transporting and storing the minerals.

Development expenditures are capitalised to the extent that they are necessary to bring the property to commercial production. They should be directly attributable to an area of interest or capable of being reasonably allocated to an area of interest. Costs which could meet these criteria include:

- the purchase price for development assets, including any duties and any non-refundable taxes;
- costs directly related to bringing the asset to the location and condition for intended use such as drilling costs or removal of overburden to establish access to the ore reserve; and
- the present value of the initial estimate of the future costs of dismantling and removing the item and restoring the site on which it is located, where such obligations arise when the asset is acquired or constructed.

Allocation of expenditure includes direct and indirect costs. Indirect costs are included only if they can be directly attributed with the area of interest. These may include items such as road construction costs and costs to ensure conformity with environmental regulations. Costs associated with re-working engineering design errors or those attributed to inefficiencies in development should not be capitalised.

General or administrative overheads relating to the whole entity, rather than to specific phases of operations, are expensed as incurred. Time charges from head office staff may be capitalised where there is a clear and direct allocation of their time to development specific activities.

Entities should also consider the extent to which "abnormal costs" have been incurred in developing the asset. SFAS 16 requires that the cost of abnormal amounts of labour or other resources involved in constructing an asset should not be included in the cost of that asset. Entities will sometimes encounter difficulties in their mining plans and make adjustments to these. There will be a cost associated with this, and entities should develop a policy on how such costs are assessed as being normal or abnormal.

Expenditures incurred after the point at which commercial production has commenced should only be capitalised if the expenditures meet the asset recognition criteria.

Pre-production sales

There may be a long commissioning period for a mine, sometimes longer than twelve months, during which production is gradually increased towards design capacity. An entity may have revenue from saleable material produced during this phase. Where the test production is considered necessary to the completion of the asset, the proceeds from sales are usually offset against the asset cost instead of being recognised as revenue. Judgment is required to determine whether all revenues earned during the commissioning period should be deducted from the cost of developing the mine.

5.3. Production

Revenue recognition

Revenue recognition can present challenges for mining entities. Production often takes place in joint ventures, and entities need to analyse the facts and circumstances to determine when and how much revenue to recognise. Extracted mineral ores may need to be moved long distances and need to be of a specific type to meet the smelter or refinery requirements. Entities may exchange product to meet logistical, scheduling or other requirements.

The following are common challenges on revenue recognition in the mining industry:

a. Provisional pricing arrangements
   Sales contracts for certain commodities often incorporate provisional pricing - as at the date of delivery of the mineral ore, a provisional price may be charged. The final price is generally an average market price for a particular future period. Revenue from the sale of provisionally priced commodities is recognised when the risks and rewards of ownership are transferred to the customer (which would generally be the date of delivery) and revenue can be reliably measured. At this date, the amount of revenue to be recognised will be estimated based on the forward market price of the commodity being sold. In most cases, the relevant forward market price should provide a reliable basis for measuring the value of the sale at the date of delivery. If so, the sale should be recognised at this time. At each subsequent period end the provisionally priced contracts are marked to market using the most up-to-date market prices with any resulting adjustments usually being recognized within revenue.

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b. Agency arrangements
It is important to identify whether a mining entity is acting as a principal or an agent in transactions as only when the entity is acting as a principal will it be able to recognise revenue based on the gross amount received or receivable in respect of its performance under a sales contract. Entities acting as agents do not recognise revenue for any amounts received from a customer to be paid to the principal. Whether an entity is acting as a principal or agent is dependent on the facts and circumstances of the relationship, which should be assessed carefully and thoroughly to determine the appropriate accounting treatment.

c. Tolling arrangements
Many companies involved in the industry provide value-added services to companies that mine ore or unprocessed mineral product. These companies may be involved in smelting, washing, refining or transporting product on behalf of a mining company. The mining company may have agreed the sale with the end user or be selling to a smelting or refining company who will then sell to an end user.

For example, a custom smelter may operate on either a purchase or toll basis. On a purchase basis, the smelter is entitled to a charge based on the final sale price of the metal produced. On a toll basis, the smelter is entitled to a treatment (toll) charge, which is usually fixed by contract or based on a formula relating to the selling price of the metal.

Revenue recognition by the mining company might then be at one of the following points:
- When they ship the metal to the smelter;
- When the metal arrives at the smelter;
- At the end of the period in which the smelter has to make provisional payment; or
- When the smelter advises the producer of the final metal quantities and, in some instances, sales price.

The appropriate point of revenue recognition from the mining company's perspective is determined based on the transfer of risks and rewards. When intermediaries are used, such as in a smelting arrangement, an assessment of whether such an arrangement also constitutes a lease must also be considered.

Stripping costs during the production phase

An entity usually obtains two kinds of benefits from its stripping activity. These are extraction of ore in the current period in the form of inventory and improved access to the ore body for future periods. As a result, two different kinds of assets are created. If the stripping activity in the current period does not provide an identifiable benefit, the associated costs are expensed in the current period.

To the extent that the benefits from the stripping activity are realised in the form of inventory produced, the associated costs are recorded in accordance with the principles of SFAS 14: Inventories.

To the extent that the benefits are realised in the form of improved access to the ore body in the future, the associated costs are recognised as a 'stripping activity asset' if all of the following conditions are met:
(a) It is probable that the future economic benefit associated with the stripping activity will flow to the entity;

(b) The entity can identify the component of the ore body for which access has been improved; and
(c) The costs relating to the stripping activity associated with that component can be measured reliably.

Identifying components of the ore body is a complex process involving management judgment. It might be difficult to separately identify costs to produce inventory and to improve access to the ore body. In such cases, costs are allocated between the inventory produced and the stripping activity asset with reference to a relevant production measure. Allocation of costs cannot be based on a sales measure.

Stripping assets are initially measured at cost and subsequently measured at cost less depreciation, amortisation and impairment losses. While rare in practice, the stripping activity assets may also be carried at revalued amount if the existing asset of which it is a part is carried at its revalued amounts. The stripping activity asset is typically depreciated based on the Units of Production ("UoP") method, unless another method is more appropriate.

5.4. Closure and rehabilitation

The mining industry can have a significant impact on the environment. Closure or environmental rehabilitation work at the end of the useful life of a mine or installation may be required by law, the terms of operating licences or an entity's stated policy and past practice.

An entity that promises to remedy damage or has done so in the past, even when there is no legal requirement to do so, may have created a constructive obligation and thus a liability under SFAS. There may also be environmental clean-up obligations for contamination of land that arises during the operating life of the mine or installation. The associated costs of remediation/restoration can be significant. The accounting treatment of closure and rehabilitation costs is therefore critical.

A provision is recognised when an obligation exists to perform the rehabilitation. The local legal regulations should be taken into account when determining the existence and extent of the obligation. An obligation might arise if an entity has a policy and past practice of performing rehabilitation activity. A provision is recorded if others have a reasonable expectation that the entity will undertake the restoration. Obligations to decommission or remove an asset are created at the time when the asset is put in place. Mining infrastructure, for example, must be removed at the end of its useful life, typically upon the closure of the mine.

Closure provisions are measured at the present value of the expected future cash flows that will be required to perform the decommissioning. The cost of the provision is recognised as part of the cost of the asset when it is put in place and depreciated over the asset's useful life. The total cost of the fixed asset, including the cost of closure, is depreciated on the basis that best reflects the consumption of the economic benefits of the asset (typically UoP). Provisions for closure and restoration are recognised even if the closure is not expected to be performed for a long time, for example more than 50 years. The effect of the time to expected closure will be reflected in the discounting of the provision. The discount rate used is the pre-tax rate that reflects current market assessments of the time value of money.

Closure provisions are updated at each balance sheet date for changes in the estimates of the amount or timing of future cash flows and changes in the discount rate. The accretion of the discount on a closure liability is recognised as part of finance expense in profit or loss.

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6.0 Additional Regulatory Considerations for Mining Investment

Investment Law

Law No. 25/2007 ("Investment Law") is the most recent investment law which introduces an integrated one-stop service to simplify business licensing. Under the Investment Law, the BKPM is given the power to coordinate the implementation of the investment policy.

The obligations for Limited Liability companies set out in the Investment Law include:

- Prioritising the use of Indonesian citizen manpower
- Creating a safe and healthy working environment
- Implementing corporate social responsibility, and
- Environmental conservation.

Investors exploiting non-renewable natural resources must also allocate funds for site restoration that fulfil the standards of environmental feasibility. Sanctions for non-compliance with certain aspects of the Investment Law, (which includes corporate social responsibility) include the restriction, freezing or revocation of business activities/ licences.

The Central Government provides protection from nationalisation unless such nationalisation is required by law. In this case, the Central Government will provide compensation based on the market value. In addition, investors are also given the right to freely transfer and repatriate foreign currency in the form of, amongst others, royalties, dividends, loan repayment, sales of investments and management and technical service fees.

On February 2016, the Government announced the Tenth Economy Package Policy focusing on changes to the Negative List of Investment. Under this Economic Policy Package, there will be some changes to the conditions for foreign investment in mining sectors. However, until the issuance of this Mining Guide, the government is yet to issue the Presidential Regulation on the amendment of the Negative List of Investment.

Forestry Law

Geographically, Indonesia has resource-rich soil, which includes forest resources. The use of forest resources is therefore strictly governed by the Central Government, especially protected forests. It is common that mining concession areas overlap with forestry areas (either a protected or productive forest), which means that mining activities will be impacted by the rules applicable to such forests.

Law No. 41/1999 (Forestry Law) as amended by Law No. 19/2004 allows 13 open-pit mines in protected forests, as long as the mining companies had contracts prior to the introduction of the Forestry Law (as governed under Presidential Decree No.41/2004).

Under GR No. 24/2010 as amended by GR No. 61/2012 and GR No. 105/2015 and Minister of Forestry Regulation No. P-16/Menhut-II/2014 dated 10 March 2014, utilisation of Forest Areas for non-forestry activities is permitted in both production forest areas and protected forest areas subject to a "borrow–and-use" permit from the Minister of Forestry. "Borrow and use" permit is non-transferrable and cannot be used as a guarantee to other party.

"Protected forest" areas are open for mining activities provided that mining is performed through underground mining (not an open pit), subject to a number of conditions. For areas designated as "Production forest" areas, underground and open pit mining may be permitted. Mining is prohibited in areas designated as "Conservation forests".

Use of a forest area for mining will require compensation to be made, by way of either land compensation or compensation payments. No compensation is payable for certain limited survey and exploration activities (unless for a trial purpose to determine a mine's economic feasibility). The borrow-and-use permit holder will also be required to pay certain non-tax State Revenue and undertake reforestation activities upon ceasing its use of the land.

Approval for the use of forestry areas is generally granted by the Minister of Forestry. However, approval for the use of forestry areas for mining operations in a WPN that have a significant impact cover a significant area, and have strategic value, can only be granted by the Minister of Forestry after initial approval is obtained from Parliament.

Energy Law

Given the importance of energy resources, it is necessary for the Central Government to create an energy management plan to fulfil the national energy needs in the long run. Law No. 30/2007 established the National Energy Council as a government body to design and formulate the national energy policy, to determine the national energy general plan, to determine the steps to be taken in an energy crisis and in emergency conditions, and to monitor the implementation of policy in energy fields with cross-sectoral characteristics.

Environmental Laws and Regulations

There is a difficult balance to be found between protecting the environment and preserving natural resources, and maintaining a viable mining industry. Environmental protection in Indonesia is governed by various laws, regulations and decrees, and non-compliance may result in fines and penalties and revocation of licences and/or permits in extreme cases.

The environmental law was recently updated by Law No. 32/2009 ("Environmental Law"). It requires the Central Government and regional governments to prepare a strategic environmental analysis and ensure that the principles of sustainable development have been integrated into the development of a particular region.

Both the Mining Law and the Environmental Law in conjunction require mining companies exploiting natural resources that have an environmental or social impact to create and maintain an environmental impact planning document (Analisis Mengenai Dampak Lingkungan or "AMDAL"), which consists of an environmental impact assessment, an environmental management plan and an environmental monitoring plan. An environmental management effort document, Upaya Pengelolaan Lingkungan ("UPL") and Upaya Pengawasan Lingkungan ("UKL") generally need to be prepared in any situation where the AMDAL document is not required.

The sanctions applied for breaches of the Environmental Law range from three to 15 years of imprisonment and/or a fine from Rp 100 million to Rp 750 million. The Environmental Law also stipulates the minimum penalties which apply, depending on the nature of the breach.

The environmental quality requirements (which concern emissions and waste water temperature levels) have been the subject of recent industry concerns due to the time lag required to implement new processes and technologies, and increased production costs.

New Listing Rules for Mining Companies

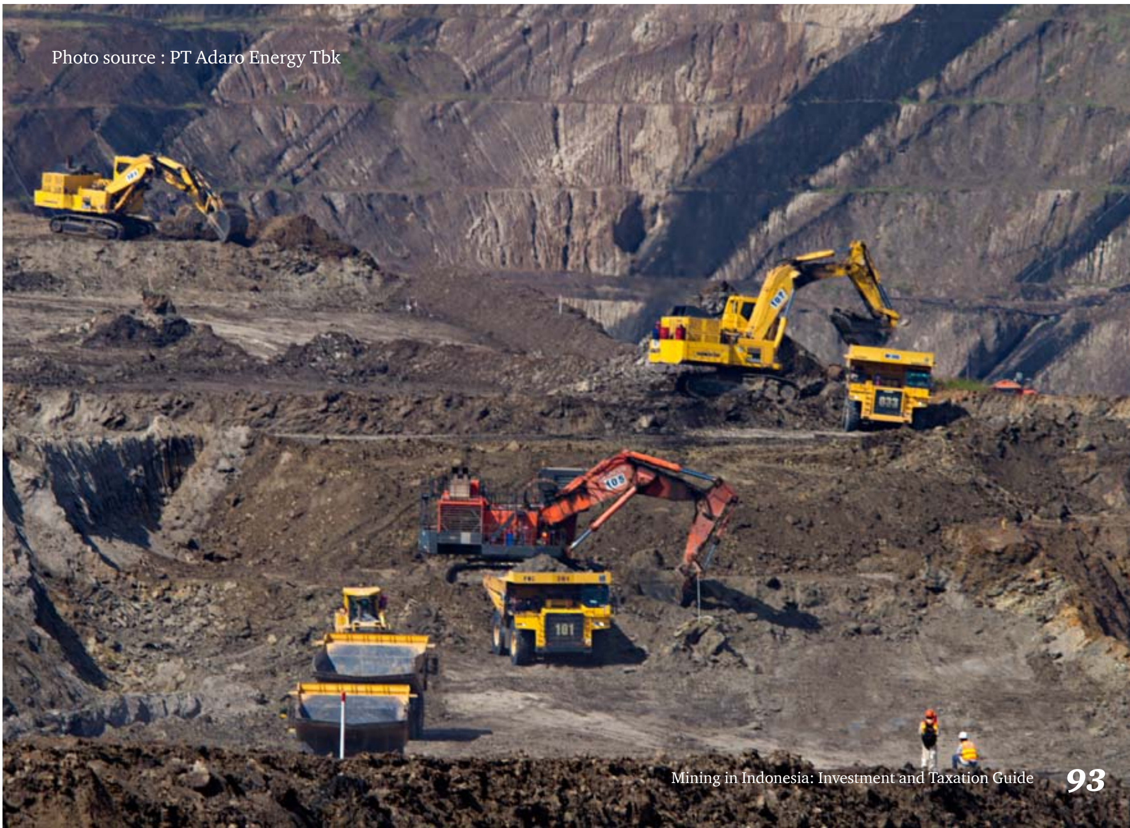
Pursuant to the issuance of IDX Decision No. KEP00100/BEI/10-2014, the listing rules for mining (mineral and coal) companies were simplified. The new rules cover mining companies (and prospective companies) with a mining business licence, or holding companies which (or which will) consolidate 50% of a mining subsidiary's income, where the mine:

- Has commenced sales, or
- Is already in the production phase but has not commenced sales, or
- Is not yet in production.

To qualify for listing, the prospective issuers must fulfil the following conditions (among others):

- Net tangible assets and deferred exploration costs must be at least Rp 100 billion for listing on the Main Board and Rp 5 billion for the Development Board
- One or more of the company's directors must have technical expertise and at least five years' work experience in the mining sector within the past seven years
- The issuer must maintain proven and probable reserves certified by a competent authority (in some other jurisdictions this is referred to as either a "Competent Person report" or a "Qualified Person report")
- Have a clean and clear certificate, and
- Have undertaken a feasibility study within three years of the date the listing request is submitted.

Other requirements are detailed in the IDX Regulations. Mineral and coal companies whose shares were listed on the IDX before the issuance of this Decision should have fulfilled the requirements regarding directors' qualifications by 1 July 2015.



Bank Indonesia Regulation on the Obligation to Use Rupiah

Bank Indonesia ("BI") Regulation No. 17/3/PBI/2015 on the Obligation to Use Rupiah for Transactions in Indonesia was effective as of 1 July 2015, with the stated aim of stabilising the Rupiah exchange rate.

The MoEMR issued a media release on 1 July 2015 (No. 40/SJI/2015) to outline the agreement between the MoEMR and BI concerning this regulation as it pertains to the oil & gas, mining and power industries following various discussions with the private sector. The media release refers to three categories of transaction as follows:

- Category 1: transactions that are able to be made directly in Rupiah, for example leases of offices/houses/vehicles, salary payments for Indonesian employees and payments for various support services, where a transition period of up to six months will be given;
- Category 2: transactions where time is required to implement the provisions of the regulation, for example fuel purchases, import transactions through local agents, long-term contracts and multi-currency contracts, where transactions in fixed-term contracts shall continue to be in foreign currency with the possibility of future amendment;
- Category 3: transactions for which it is fundamentally difficult to fulfill the provisions of the regulation, for example salary payments for expatriates, drilling services and the lease of ships, where businesses may continue to use foreign currency.

Investors should continue to monitor this issue as further procedures for the implementation of the BI regulation are expected to be issued by the MoEMR and BI in due course.

Bank Indonesia Regulation on Reporting on Foreign Exchange Trading

Bank Indonesia Regulation No. 16/22/PBI/2014 regarding Reporting on Foreign Exchange Trading and Reporting on the Application of Prudential Principles in Foreign Loan Administration for Non-bank Corporations includes a requirement for companies to report their foreign currency loans to Bank Indonesia on a quarterly basis. Further, the fourth quarter report needs to be verified by an independent public accountant. Failure to comply with the reporting obligations triggers administrative sanctions of Rp 10 million.

The prudential principles under Bank Indonesia Regulation No. 16/21/PBI/2014 and Circular Letter No. 16/24/DKEM as amended by Circular Letter No. 17/18/DKEM are as follows:

a. Minimum hedging ratio is 25% of the negative difference between current assets and current liabilities that will be due within three months and that will be due within three months and six months of the end of a quarter;
b. Minimum liquidity ratio is 70%, calculated by comparing the company's current assets and current liabilities that will be due within three months at the end of the reporting quarter; and,
c. Minimum credit rating of BB or equivalent from certain credit ratings agencies approved by the Indonesian Financial Services Authority.

Other Regulations Related to Mining Operations

Other relevant regulations applicable to Indonesian mining operations include regulations regarding the use of groundwater, technical guidelines to control air pollution from fixed sources, water quality and pollution, used oil regulations and storage of production chemicals. Failure to comply may lead to fines, penalties and in extreme cases, the revocation of the licence/permit.

Corporate Social Responsibility

contractors are required to comply with relevant laws and regulations on Corporate Social Responsibility ("CSR") and Community Development.

Under the Law no. 40/2007 ("Corporation Law") Article 74, PT companies that have a resources business must implement CSR, which must be budgeted for in the companies' expenditure plans. The details of such responsibilities will be further regulated under government regulations. As at the date of writing, no government regulations had been issued.

Service Providers to the Mining Industry

Mining companies typically have four phases of operations - exploration and evaluation, development, production, and closure and rehabilitation. PerMen 24/2012 allows certain activities to be carried out by external parties which may include:

- Exploratory drilling and sampling
- Infrastructure construction
- contract mining and overburden removal
- Hauling and barging

Under the Mining Law and PerMen 28/2009 as amended by 24/2012, only Indonesian incorporated companies may provide services to mining licence holders in Indonesia.

We outline below some of the guidance associated with the most significant mining services described above:

	Exploratory drilling and sampling company	Construction company	contract mining and overburden removal company	Hauling and barging company
Regulation	Investment Law PR 39/2014 Mining Law PerMen 28/2009 PerMen 24/2012	Investment Law PR 39/2014 Mining Law PerMen 28/2009 PerMen 24/2012	Investment Law PR 39/2014 Mining Law PerMen 28/2009 PerMen 24/2012	Investment Law PR 39/2014 Mining Law PerMen 28/2009 PerMen 24/2012

	Exploratory drilling and sampling company	Construction company	contract mining and overburden removal company	Hauling and barging company
Investment licence issuer	BKPM	BKPM	BKPM	BKPM
Business licence issuer	MoEMR	Construction Services Development Agency BKPM MoEMR	MoEMR	Minister of Transportation MoEMR or governor or city mayor (depending on service area)
Period of Business licence	3 years and extendable	Unlimited from the Investment Coordinating Board 3 years and extendable based on approval from MoEMR	3 years and extendable	Unlimited from Minister of Transportation 3 years and extendable based on approval from MoEMR
Maximum Foreign Ownership	• Oil and gas survey services (49%) • Geological and geophysical survey (49%) • Geothermal survey (95%)	• Generally for non-small scale EPC services is 67% and for construction contracting and consulting is 55%. • For certain construction, different requirements may apply, such as for platform construction the maximum foreign ownership is 75%, for spherical tank and offshore piping installation the maximum foreign ownership is 49% whilst for onshore piping, vertical/horizontal tank construction is reserved for domestic investors only. • Small and medium scale construction contracting and consulting (only for local small scale companies) A construction company can be in the form of a representative office. In this case, a joint operation with local construction company is required.	Same requirements as a construction company Small and medium scale excavating and earth moving work and site preparation for mining (only for local small scale companies).	Ferry, river and lake transport and transport facilities (49%) Special goods, cargo and heavy equipment transport (49%) Support business in terminals (49%) Domestic and international sea transport (49%) Land transport rental (local investors only) Up to 100%, if formed as a general mining services company.
Tax	Prevailing tax laws	Prevailing tax laws (with a final deemed profit tax regime)	Prevailing tax laws	Prevailing tax laws

Processing

Under the Mining Law, mining companies will be required to process their minerals within Indonesia.

	Downstream processing
Regulation	Law 25/2007, Presidential Regulation 36/2010, Law 4/2009, PerMen 5/2017
Investment licence issuer	Investment Coordinating Board
Business licence issuer	MoEMR/Governor/Mayor depending on the location
Maximum foreign ownership	Up to 100%
Tax	Prevailing tax laws


Photo source : PT Vale Indonesia Tbk

Mining Infrastructure

The establishment of a greenfields mining project is capital intensive, and in the case of Indonesia often involves substantial investment in mine infrastructure (access/haulage roads, railways, conveyors, captive power plants, camp and recreation facilities, washing and crushing facilities and ship loaders) given the often remote locations and distance from water/ transhipment facilities.

We outline as follows some of the investment guidance associated with the most significant infrastructure described above:

As a separate business

	Special Port/ Terminal	Road	Power Plant	Railways
Regulation	Law 17/2008 Law 25/2007 GR No. 61/2009 GR No. 64/ 2015 Presidential Regulation No. 39/2014	Law 38/2004 GR 34/2006 GR 30/2009 GR 15/2005 GR 44/2009 GR 43/2013 Law 25/2007 Presidential Regulation No. 39/2014	Law 30/2009 GR 3/2005 GR 10/1989 GR 26/2006 GR 14/2012 Law 25/2007 Presidential Regulation No. 39/2014	Law 23/2007 GR 56/2009 Law 25/2007 Presidential Regulation No. 39/2014
Investment licence issuer	BKPM Port business will be performed by the company by entering into the concession rights or agreement with the Port Authority	BKPM	BKPM	BKPM

	Special Port/ Terminal	Road	Power Plant	Railways
Business licence issuer	Port Operating Licence is granted to the Port Authority, which is formed by the Ministry of Transportation not the company itself. Sea Port Operating Licence is issued by: • Minister for Main Ports and Hub Ports • Governor or Mayor/Regent for Feeder Ports • Lake/River Port Operating Licences are issued by the Mayor/Regent	Minister of Public Works Based on concession rights agreement with the government	MoEMR, Governor or Mayor depending on the business/ transmission area and electricity facility location	Ministry of Transportation, Governor or Mayor depending on the railway coverage
Period of business licence	Based on concession rights or agreement with Port Authority	Based on concession rights or agreement with the relevant Minister	30 years	Railways Infrastructure operational licence: based on concession agreement with the relevant Minister, Governor or Mayor Railways Facility operational licence: 5 years and extendable
Transferable licence?	No	Yes, based on agreement with the Ministry	Not regulated	Not regulated

	Special Port/ Terminal	Road	Power Plant	Railways
Maximum foreign ownership	• Supply of harbour facilities (49% but can be up to 95% during concession period under a PPP scheme) • Loading/ unloading (49% but can be up to 60% for investor from ASEAN countries) • Supply of reception facilities (49%) • Supply & business of sea harbour (49%)	Toll road 95%	• Development & installation of electricity supply (95%) • Development & installation of electricity utilisation (95%) • Maintenance and operation of electricity equipment (95%) • Development of electricity equipment technology (up to 100%) • Electricity consulting (95%) • Nuclear power plant (up to 100%) • Electricity transmission and electricity distribution (95% but can be up to 100% under PPP scheme) • Power plant below 1MW reserved for domestic investment • Power plant below between 1 - 10MW (49%) • Power plan > 10 MW(95% but can be up to 100% under PPP scheme)	Rail transport Not specified (100%)
Land rights	Land rights are given to the Port Authority. The company performs business based on concession rights or agreement with the Port Authority	Based on concession rights given by the Government	Legal title transferred to company in the form of Hak Guna Bangunan (Right to Use Land for Erecting Buildings) for a total period of 80 years	Depends on concession rights given by the Government

	Special Port/ Terminal	Road	Power Plant	Railways
Fee to government	Stipulated in the concession rights agreement	Not stipulated in the regulations	Non tax state revenue collected from electricity transmission and distribution facility	Not stipulated in the regulations
Tax	Prevailing tax laws	Prevailing tax laws	Prevailing tax laws	Prevailing tax laws
Other issues	Law 17/2008 stipulates that implementing regulations will be further defined in the GR. No specific regulations on port operations in place to date	Only able to engage in toll road business	None	None

As part of mining business

	Special Port/ Terminal	Road	Power Plant	Railways
Regulation	Law 17/2008 Law 4/2009 Presidential Regulation No. 61/2009	Law 38/2004 GR 34/2006 GR 8/1990 GR 40/2001 GR 15/2005 Law 4/2009	Law 30/2009 GR 3/2005 GR 10/1989 Law 4/2009	Law 23/2007 GR 56/2009 Law 4/2009
Business licence issuer	Minister of Transport	Mayor/Regent if within a regency Governor if cross-regency within a province MoEMR if cross-province	Mayor/Regent for transmission within a regency Governor for transmission inter-regency within a province Minister for national transmission	Minister, Governor or Mayor depending on the railways coverage
Period of business licence	Five years and extendable	No specific regulations limiting period of operating licence	MoEMR, Governor or Mayor depending on the business/ transmission area and electricity facility location	Ministry of Transportation, Governor or Mayor depending on the railway coverage
Land rights	Right to Use	Right to Use	Right to Use	Right to Use
Other issues	Allowed only if the nearest available port cannot assume the special port activities	Yes, based on agreement with the Ministry	Not regulated	Not regulated

Appendices

Photo source : PT Aneka Tambang (Persero) Tbk

Minimum in-country processing and refining requirements for metal minerals prior to export

No	Commodity		Minimum Limit			
	Ore	Mineral	Processing		Refining	
			Products	Quality	Products	Quality
1.	Copper (fusion process)	Chalcopyrite Digenite Bornite Cuprite Covelitte	Copper Concentrates	≥15% Cu	Copper Cathode	Cu Metal ≥ 99% Cu
					Copper Telluride	a. Cu Metal ≥ 99%; b. Te Metal ≥ 9%; c. TeO_2 ≥ 98%; d. Te $(OH)_4$ ≥ 98%; and/or e. Copper telluride alloy > 20% Te
	Copper (leaching process)	Chalcopyrite Digenite Bornite Cuprite Covelitte	-	-	Metal	a. Cu Metal ≥ 99%; b. Au Metal ≥ 99%; c. Ag Metal ≥ 99%; d. Pd Metal ≥ 99%; e. Pt Metal ≥ 99%; f. Se Metal ≥ 99%; g. Te Metal ≥ 99%; h. TeO_2 ≥ 98%; i. $Te(OH)_4$ ≥ 98%; and/or j. Rare metals and rare earth elements (refer to the requirement for rare-earth metal terms for tin).
2.	Nickel and/or cobalt (fusion process) a. Saprolite b. Limonite	Pentlandite Garnierite Serpentinite Carolite	-	-	Nickel Matte, Metal Alloys and Nickel Metal	a. Ni Mate ≥ 70% Ni; b. FeNi ≥ 8%Ni; c. Nickel Pig Iron (NPI) 2% ≤ Ni < 4% with Fe ≥ 75%; d. Ni Metal ≥ 93%; and/or e. NiO ≥ 70% Ni.
	Nickel and/or cobalt (leaching process) Limonite				Metal, Metal Oxide, Metal Sulfide, mix hydroxide/sulfide precipitate, and hydroxide nickel carbonate	a. Ni Metal ≥ 93%; b. Mix Hydroxide precipitate (MHP) ≥ 25% Ni c. Mix sulfide precipitate (MSP) ≥ 45% Ni; d. Hydroxide Nickel Carbonate (HNC) ≥ 40% Ni; e. NiS ≥ 40% Ni; and/or f. Co Metal ≥ 93% g. CoS ≥ 40% Co; h. Cr Metal ≥ 99%; and/or i. Cr2O3 ≥ 40%.

No	Commodity		Minimum Limit			
			Processing		Refining	
	Ore	Mineral	Products	Quality	Products	Quality
	Nickel and/or cobalt (reduction process) a. Saprolit b. Limonit				Metal Alloys	a. Sponge FeNi 2% ≤ Ni < 4% with Fe ≥ 75%; b. Sponge FeNi ≥ 4% Ni; c. Luppen FeNi 2% ≤ Ni < 4% with Fe ≥ 75%; d. Luppen FeNi ≥ 4% Ni; e. Nugget FeNi 2% ≤ Ni < 4% with Fe ≥ 75%; and/or f. Nugget FeNi ≥ 4% Ni.
3.	Bauxite	Gibbsite Diaspora Boehmite	-	-	Metal Oxide/ Hydroxide and metal	a. Smelter grade alumina ≥ 98% Al_2O_3 b. Chemical grade alumina ≥ 90% Al_2O_3 c. Alumina Hydrate ≥ 90% $Al(OH)_3$ d. Proppants: 1) Al_2O_3 ≥ 72% (Granulated); 2) Able to rupture at a pressure 7.500psi, the size of fraction: -20+40 mesh ≤ 5.2%; -30+50 mesh ≤ 2.5%; or -40+70 mesh ≤ 2.0%. 3) Apparent Specific Gravity (ASG) 3.27. and/or e. Al Metal ≥ 99%

No	Commodity		Minimum Limit			
	Ore	Mineral	Processing		Refining	
			Products	Quality	Products	Quality
4.	Iron	Hematite Magnetite	Iron concentrates *)	≥ 62% Fe and ≤ 1% TiO_2	Sponge, metal and metal alloys	a. Sponge iron ≥ 72% Fe; b. Sponge ferro alloy ≥ 72% Fe; c. Pig iron ≥ 75% Fe; and/ or d. Ferro alloy ≥ 75% Fe
		Goethitee Hematite Magnitite (Laterite iron)	Laterite iron concentrates **)	> 50% Fe and (Al_2O_3 + SiO_2) > 10%		
		Lamela magnetite-ilmenite (iron sand)	Iron sand concentrates ***)	≥ 56% Fe; and 1% < TiO_2 ≤ 25%	Metal	a. Sponge iron > 72% Fe; and or b. Pig iron > 75% Fe.
			Pellet iron sand concentrates ****)	≥ 54% Fe; and 1% < TiO_2 ≤ 25%		
			Ilmenite concentrates *****)	≥ 45% TiO_2	Metal oxide, metal chloride, and metal alloys	a. Synthetic TiO2 ≥ 85%; b. TiCl4 ≥ 87%; and or c. Titanium alloy ≥ 65% Ti.
5.	Tin	Cassiterite	-	-	Metal	Metal Sn ≥ 99.90%
			Zircon concentrates	Refer to the requirements for zirconium and zircon.		Refer to the requirements for zirconium and zircon.
			Ilmenite Concentrate	TiO_2 ≥ 45%	Metal oxide, metal chloride, and metal alloys	a. Synthetic TiO2 ≥ 85%; b. TiCl4 ≥ 87%; and or c. Titanium alloy ≥ 65% Ti.
			Rutile concentrates	TiO_2 ≥ 90%	Metal chloride and metal alloys	a. $TiCl_4$ ≥ 98%; and/or b. Titanium alloy ≥ 65% Ti.
			Monazite and xenotime concentrates	-	Metal oxide, metal hydroxide, and rare earth metal	a. Rare earth metal oxide (REO) ≥ 99%; b. Rare earth metal hydroxide (REOH) ≥ 99%; and/or c. Rare earth metal ≥ 99%.

No	Commodity		Minimum Limit			
	Ore	Mineral	Processing		Refining	
			Products	Quality	Products	Quality
6.	Manganese	Pyrolusite Psilomelane Braunite Manganite	Manganese concentrates	≥ 49% Mn	Metal, Metal alloys and Manganese Chemical	a. Ferro Manganese (FeMn), Mn ≥ 60% b. Silica Manganese (SiMn), Mn ≥ 60% c. Manganese Monoxide (MnO), Mn ≥ 47.5% MnO_2 ≤ 4%; d. Manganese Sulfate ($MnSO_4$) ≥ 90%; e. Manganese Chloride ($MnCl_2$) ≥ 90% f. Manganese Carbonate Synthetic ($MnCO_3$) ≥ 90%; g. Kalium Permanganat ($KMnO_4$) ≥ 90%; h. Manganese Oxide (Mn_3O_4) ≥ 90%; i. Manganese Dioxide Synthetic (MnO_2) ≥ 98%; j. Manganese Sponge (Direct Reduced Manganese) Mn ≥ 49%, MnO_2 ≤ 4%; and/or k. Electrolytic Manganese Dioxide MnO_2 ≥ 90% and K < 250 ppm

No	Commodity		Minimum Limit			
			Processing		Refining	
	Ore	Mineral	Products	Quality	Products	Quality
7.	Lead and Zinc	Galena Sphalerite Smithsonite Hemimorphite (calamine)	Zinc concentrates	≥ 51% Zn	Metal, Metal oxide/hydroxide	a. Bullion ≥ 90% Zn; b. ZnO ≥ 98%; c. ZnO_2 ≥ 98%; and/or d. Zn $(OH)_2$ ≥ 98%.
					Gold metal and/or silver	a. Au Metal ≥ 99%; and/or b. Ag Metal ≥ 99%.
			Lead concentrates	≥ 56% Pb	Metal, metal oxide/hydroxide	a. Bullion > 90% Zn; b. PbO ≥ 98%; c. $Pb(OH)_2$ ≥ 98%; and/or d. PbO_2 ≥ 98%;
					Gold metal and/or silver	a. Au Metal ≥ 99%; and/or b. Au Metal ≥ 99%.
8.	Gold	a. Native b. Associated minerals	-	-	Precious metal	Au Metal ≥ 99%
9.	Silver	a. Native b. Associated minerals	-	-	Precious metal	Ag Metal ≥ 99%
10.	Chromium	Chromite	-	-	Metal and alloys	a. Cr Metal ≥ 99%; and/or b. Chromium alloys ≥ 60% Cr

No	Commodity		Minimum Limit			
	Ore	Mineral	Processing		Refining	
			Products	Quality	Products	Quality
11.	Zirconium		-	-	Zircon chemical, zircon sponge, zirconia, zircon metal, and hafnium	a. Zirconium Oxychloride (ZOC) $ZrOCl_2{\cdot}_8H_2O \geq$ 90%; b. Zirconium sulfate (ZOS) $Zr(SO_4)_2{\cdot}_4H_2O \geq 90\%$; c. Zirconium Basic Sulfate (ZBS) $Zr_5O_8(SO_4)_2.xH_2)$ $\geq 90\%$; d. Zirconium Basic Carbonate (ZBC) $ZrOCO_3.xH_2O) \geq 90\%$; e. Ammonium Zirconium Carbonate (AZC) $(NH_4)_3ZrOH(CO_3)_3.$ $2H_2O \geq 90\%$; f. Zirconium Acetate (ZAC) $H_2ZrO_2(C_2H_3O_2)_2 \geq$ 90%; g. Kalium Hexafluoro Zirconate (KFZ) K_2ZrF_6 $\geq 90\%$; h. Zirconium Sponge ≥ 85%; i. Zirkonia (ZrO_2+HfO_2) $\geq 99\%$; j. Zirconium ≥ 95% Zr; and/or k. Hafnium ≥ 95% Hf.
			Ilmenite	$TiO_2 \geq 45\%$	Metal oxide, metal chloride and metal alloy	a. TiO2 synthetic ≥ 85%; b. TiCl4 ≥ 87%; and or c. Titanium metals alloy ≥ 65%.
			Rutile	$TiO_2 \geq 90\%$	Metal chloride and metal alloy	a. TiCl4 ≥ 87%; and or b. Titanium metals alloy ≥ 65% Ti.
12	Antimony	Stibnite	-	-	Antimony metal	a. SB ≥ 99%; and/or b. $Sb_2O_5 \geq 95\%$.

Remarks:

*) This represents iron concentrates which contains hematite/magnetite mineral with iron component of Fe ≥ 62%.

**) This represents iron concentrates which contains goethite/laterite mineral with iron component of Fe ≥ 51% and alumina (Al_2O_3) and silica (SiO_2) components of ≥ 10%.

***) This represents iron concentrates which contains lamella magnetite-ilmenite mineral with iron component of Fe ≥ 58% and compound concentration Titanium oxide of $1\% \leq TiO_2 \leq 25\%$.

****) This represents iron concentrates in the form of pellet which contains lamella magnetite-ilmenite mineral with iron component of Fe ≥ 56% and compound concentration Titanium oxide of $1\% \leq TiO_2 \leq 25\%$.

*****) This represents iron concentrates which contains lamella magnetite-ilmenite mineral with compound concentration Titanium oxide of $TiO_2 \geq 50\%$.

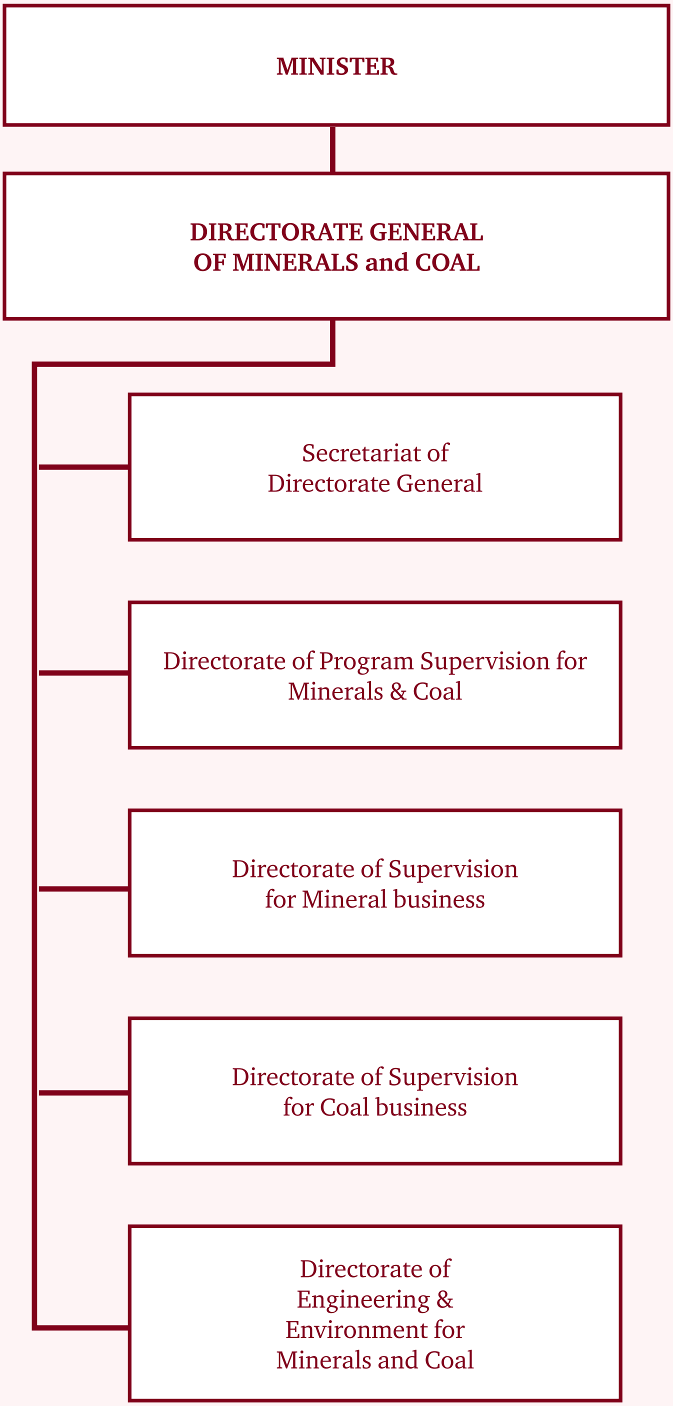
Regional Taxes

This table represents a selection of the various regional taxes relevant to the mining industry.

Type of Regional Tax		Maximum Tariff	Current Tariff	Imposition Base
A. Provincial Taxes				
1	Taxes on motor vehicle and heavy equipment	10%	Non-public vehicles	
			1%-2% for the first vehicle owned	Calculated with reference to sales value and a weight factor (size, fuel, type, etc.). Government table will be published annually to enable calculation.
			2% - 10% for the second and more vehicle owned	
			0.5% - 1% for public vehicles	
			0.1% - 0.2% for heavy equipment vehicle	
2	Title transfer fees on motor vehicle, above-water vessels and heavy equipment	20%	Motor vehicles	
			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 subsequent title transfer	
3	Tax on motor vehicle fuel	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)
4	Tax on the collection and utilisation of underground water and surface water	20%	Tariff on surface water only	Purchase value of water (determined by applying a number of factors).

Type of Regional Tax		Maximum Tariff	Current Tariff	Imposition Base
B. Regency and Municipal Taxes				
5	Catering	10%	10%	Purchase value
6	Tax on street lighting	10%	3% utilisation by industry	Sales on electricity
			1.5% personal use	
7	Tax on non-metal mineral and rock (formerly C-Category mined substance collection)	25%	Set by region	
8	Tax on groundwater	20%	Set by region	Purchase value
9	Duty on the acquisition of land and buildings rights	5%	Set by region	Land and buildings sale value

Ministry of Energy and Mineral Resources



IMA (Indonesian Mining Association)

IMA was founded on 29 May 1975, as a non-governmental, non-political, non-profit organization established in accordance with the laws of the Republic of Indonesia. The headquarters and registered office of the association are located in Jakarta. The association serves as a link between the Government and the mining industry, organizing lectures, seminars and training activities for the members, organizing periodic conferences on mining in Indonesia, publishes proceedings and mining information, and representing the Indonesian mining industry at national and international meetings. IMA is a founding member of the ASEAN Federation of Mining Associations and currently provides the secretariat for the Federation.

IMA Purpose

The aims and objectives of the association are to support the government in its policies to encourage the development of the mining industry and to utilise non-confidential and non-proprietary information to promote the exploration, mining, mineral beneficiation and metallurgical aspects in Indonesia through:

1. Studying problems relating to such aspects of the mining industry at the national level and possible solutions to these problems.
2. Studying modern methods in the mining industry, which have been adopted in other countries for application in Indonesia.
3. Fostering a mutual respect between the members of the association, both private and government (it being understood that no decision or action of the association shall affect any contracts to which any of the members are parties).
4. Advancing new ideas relative to such aspects of the mining industry.
5. Fostering a spirit of scientific research among the members of the association.
6. Establishing contact and cooperation with similar professional organisations outside Indonesia.
7. Disseminating objective information and analysis concerning such aspects of the mining industry.
8. Maintenance of a high standard of professional conduct on the part of the Association members.
9. Promotion of the development of the infrastructure necessary to support the mining industry in Indonesia.
10. Familiarisation of the general public and educational institutions with current developments and problems in the mining industry.
11. Giving assistance to and encouraging potential university graduates in preparing for a career in the mining industry.

APBI-ICMA (Indonesian Coal Mining Association)

ASOSIASI PERTAMBANGAN **BATUBARA** INDONESIA
INDONESIAN **COAL** MINING ASSOCIATION

APBI-ICMA was founded on 20 September 1989 as a response to the challenges of the coal mining industry in Indonesia.

The APBI-ICMA is a non-government, non-profit and non-political organisation that embraces both upstream (exploration and exploitation) and downstream (marketing and distribution, utilisation and mining services) aspects of the coal industry in Indonesia.

The association aims to create an environment for its members to discuss common concerns, exchange ideas and work towards a common goal for the coal mining industry.

The APBI-ICMA also acts as a partner to relevant government Institutions and provides the industry's views on how to encourage a favourable environment for investment and competition.

The APBI-ICMA works collaboratively with all stakeholders to enhance investment in the economic health of the coal mining industry to deliver greater benefits to government, investors, communities, employees, customers and the environment.

Summary of CCoW generations

No	Item	First Generation	Second Generation	Third Generation	Remarks
1	**Dead rent – in US$ per hectare per annum except stated otherwise**				
	a. General Survey	0.01 – 0.03	0.05 – 0.10	0.025 – 0.05	Second Generation's dead rent follows the prevailing dead rent tariff
	b. Exploration	0.08 – 0.20	0.20 – 0.70	0.10 – 0.35	
	c. Feasibility	0.20	1.00	0.50	
	d. Construction	0.20	1.00	0.50	
	e. Operation	1.00	2.00 - 4.00	1.50 – 3.00	
2	Production royalty rate (%)	13.5%	13.5%	13.5%	Calculated based on coal sales price minus certain marketing/ selling
3	**CIT**				
	a. Tax Rates	35% for the first ten years of Operating Period; 45% thereafter	25%*)	Incremental CIT rate to 30% (or lower rate subject to a GR)	
	b. Depreciation rates				
	Non-building assets:				
	i. Straight line	12.5%	5% - 25%*)	10% - 50% (for tangible assets located in the contract Area); otherwise 5% - 25%	
	ii. Declining balance	Not Applicable	10% - 50%*)	20% - 100% (for tangible assets located in the contract Area); otherwise 10% - 50%	
	Building assets:				
	i. Straight line	12.5%	5% - 10%*)	10% - 20% (for tangible assets located in the contract Area); otherwise 5% - 10%	
	ii. Declining balance	Not Applicable	Not Applicable*)	Not Applicable	

No	Item			First Generation	Second Generation	Third Generation	Remarks
	c. Amortization rates (%)						
		a. Straight line		12.5%	10% - 25%*)	10% -50%	Under most CCoWs costs incurred prior to commercial operation may be deferred and amortised
		b. Declining balance		Not applicable	10% - 50%*)	20% - 100%	
	d. Accelerated Depreciation						
		Non-building assets:		25%	Not Applicable*)	Not Applicable	Accelerated depreciation can be claimed only within any of the first four year of the life of the assets
		Building assets:		10%	Not Applicable*)	Not Applicable	
	e. Investment allowance			20% of total investment	Not Applicable*)	Not Applicable	At the rate of 5% a year
	f. Deductible expenses:						
		Operating Expenses:					
		i.	Cost of materials, supplies, equipment and utilities	✓	✓	✓	
		ii.	Expenses for contracted services	✓	✓	✓	
		iii.	Premiums for insurance	✓	✓	✓	
		iv.	Damage/ losses not compensated for under insurance	✓	✓	✓	
		v.	Payments of royalties or other payments in respect of patent, design, technical information and services	✓	✓	✓	
		vi.	Losses from obsolescence or destruction of inventory	✓	✓	✓	Provision is not deductible
		vii.	Rentals	✓	✓	✓	

No	Item		First Generation	Second Generation	Third Generation	Remarks
	viii.	Dead rent, surface rent, production royalties, stamp duty, and other levies	✓	✓	✓	
	ix.	Sales tax	✓	Silent	Silent	
	x.	Uncredited VAT	Silent	✓	✓	
	xi.	Expenses for treatment, washing, processing, repairs and maintenance, handling, storing, loading, transporting and shipping	✓	✓	✓	
	xii.	Expenses for commission and discounts	✓	✓	✓	
	xiii.	Expenses for environment/ reclamation	Silent	✓	✓	
	xiv.	Expenses incurred prior to the establishment of the company by a shareholder	Silent	x	✓	For Third Generation, these are deductible provided the expenditures have been audited by independent auditor and approval from the DGT has been obtained
	Sales, General & Administation					
	i.	Salaries and wages	✓	✓	✓	
	ii.	Costs of specified benefits-in-kind in the contract area	✓	x	✓	For Second Generation, these are not deductible unless the holder obtains remote area approval from the DGT
	iii.	Research expenses	✓	✓	✓	For Second Generation, this should be performed in Indonesia
	iv.	Travel expenses	✓	✓	✓	Only for business purposes
	v.	Technical fees	✓	✓	✓	

No	Item	First Generation	Second Generation	Third Generation	Remarks
	vi. Management fees and other fees for services performed abroad	✓	✓	✓	
	vii. Communication and office expenses	✓	✓	✓	
	viii. Dues and subscriptions	✓	✓	✓	
	ix. Advertising and other selling expenses, public relations, marketing	✓	✓	✓	
	x. Legal and auditing expenses	✓	✓	✓	
	xi. General overhead expenses	✓	✓	✓	
	xii. Exploration expense	✓	✓	✓	
	xiii. Other relevant expenses	✓	✓	✓	
	xiv. Reserve for reclamation	Silent	✓	✓	For Third Generation, subject to a deposit placed in a State Owned bank, audited by a public accountant and approved by the DGT
	g. Interest deductibility				
	Maximum debt to equity ratio	1.5 to 1	4 to 1[*)] refer to PMK-169	Not Applicable	
	Maximum debt to equity ratio for Investments <=US$200m	Not Applicable	Not Applicable	5 to 1	
	Maximum debt to equity ratio for Investments >US$200m	Not Applicable	Not Applicable	8 to 1	

No	Item	First Generation	Second Generation	Third Generation	Remarks
	h. Tax loss carried forward	Four years (losses before the fifth anniversary of the Operating Period can be utilised in any year)	Five years	Eight years	
4	**WHT rates**				
	i. Dividends, interest and royalties	10%	15% for domestic taxpayer, 20% for foreign taxpayer	15% for domestic taxpayer, 20% for foreign taxpayer	For Second and Third Generation, reduced tax rate is available under a tax treaty. However please note that the WHT rates under CCoWs may be irrelevant based on PMK-39.
	ii. Dividends (founder shareholders)	10%	Silent	7.5%	
	iii. Rental, technical fees, management fees and other service fees (domestic/ foreign)	10%	2% to 20%	15% of deemed net income/ 20%	
	iv. Employee income tax	Applicable*)	Applicable*)	Applicable*)	
5	**VAT rates**				
	i. VAT on coal sales	Not Applicable*	Exempted*)	10% on domestic sales; 0% on export sales	Third Generation CCoW VAT obligations are grandfathered to the 1994 VAT Law. VAT paid should be creditable/refundable
	ii. VAT on domestic purchases	Not Applicable*	10% paid to vendor*)	10% collected by the mining company	Input VAT cannot be credited/refunded by Second Generation CCoW holders, but this is deductible for CIT purposes
	iii. VAT on import	Not Applicable*	10% paid to Custom Office*)	Could be exempted in accordance with the prevailing regulations	
	iv. VAT on offshore services	Not Applicable	10% on self-assessment basis*)	10% on self assessment basis	

No	Item	First Generation	Second Generation	Third Generation	Remarks
6	**Sales Tax rates**	2 - 2.5% on domestic services provided to contractor; and 0 - 5% on goods (for one contractor only)	Not Applicable	Not Applicable	Sales tax was repealed in 1984, when VAT was introduced. List of services (and goods) provided in PMK-194.
7	**Import of capital goods:** **a. Import duty** **b. Article 22 Income Tax**	Exempted	a. Exempted/ reduced rates up to the 10th anniversary of the Operating Period, in accordance with prevailing regulations; b. Could be exempted in accordance with the prevailing regulations	a. Exempted/reduced rates up to the 10th anniversary of the Operating Period, in accordance with prevailing regulations; b. Could be exempted in accordance with the prevailing regulations	Exemption from import duty is subject to either CCoW or BKPM Master List approval
8	**Other taxes & levies**				
	a. Regional taxes (e.g. motor vehicles and street lighting levy)	Regional Development Tax (IPEDA): maximum of US$100,000 a year	Applicable *)	Follows the prevailing Regional Tax Law at a rate not exceeding the prevailing rate at the signing date	
	b. Land and building tax	Silent	0.5% x 40% of the sale value of PBB objects*) (refer to PER-47)	Preproduction period: equal to deadrent; Operating production period: deadrent plus 0.5% x 30% of gross revenue from the mining operations	
9	**Stamp duty**	1/1000 of the total loan amount	Rp3,000/ Rp6,000*)	Silent	

Note:
*) follows the prevailing tax laws and regulations

Photo source : PT Aneka Tambang (Persero) Tbk

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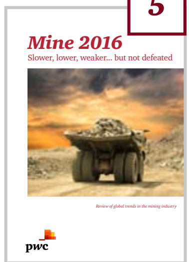

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