Government Amends Mining Sector Rules

The Government recently amended Government Regulation No. 23 of 2010 on mining (the "**Old Regulation**") through the issuance of Government Regulation No. 24 of 2012 (the "**Amended Regulation**"). Effective as of 21 February 2012, the Amended Regulation introduces a number of significant changes to Indonesia's mining regime, as discussed below.

Increase in Percentage Divestment Obligation

Under the Old Regulation, a foreign investor that holds a mining license ((*Izin Usaha Pertambangan* / "**IUP**") or special mining license ((*Izin Usaha Pertambangan Khusus* / "**IUPK**") is required to divest at least 20% of the mining company's issued capital to an Indonesian entity/entities after the company has been in production for at least five years.
However, under Article 97(1) of the Amended Regulation, the divestment percentage is significantly increased to at least 51% of the shares held by the foreign investor.

As in the case of the Old Regulation, the Amended Regulation sets five years since the commencement of production as the point in time when the divestment obligation arises. However, the Amended Regulation goes further by introducing a deadline of 10 years within which the divestment process must be completed, once again counting from the date of commencement of production.

In addition, the Amended Regulation sets minimum percentages that must be divested each year from the sixth to the tenth, as shown in the following table:

No.	Years	Minimum Indonesian Ownership
1.	6th year	20%
2.	7th year	30%
3.	8th year	37%
4.	9th year	44%
5.	10th year	51%

It should be noted that the Amended Regulation requires the Indonesian shareholding to be maintained in accordance with the above percentages should the company increase its capital.

As in the case of the Old Regulation, the Amended Regulation provides that the shares to be divested must first be offered to the central government. Should the central government be unwilling or unable to purchase them, they should then be offered to the relevant provincial or regency/municipal government. If no offers are forthcoming, the next step is to offer them to state- and local government-owned enterprises. During each of these stages, those involved are given 60 days from the date of the offer to declare an interest. Should no declaration of interest be made by a state-related party, the shares may be offered to private Indonesian companies, who are given 30 days to express an interest in purchasing them after the initial offer date.

The foreign-owned shares may not be divested to any other class of purchaser other than those listed above. Should no expression of interest in the shares be forthcoming from a qualified potential purchaser, the entire process will have to be repeated the following year

Of particular importance to mining investors that hold IUPs or IUPKs, the divestment requirements of the Amended Regulation apply to mining licenses granted both prior and subsequent to its issuance. This differs markedly from the position of contracts of work and coal contracts of work signed prior to the enactment of the Mining Law (No. 4 of 2009), which, under the principle of sanctity of contract, remain in effect until expiry and are therefore immune to changes brought about by government regulation.

Transfer of Mining Licenses Purportedly Allowed, Despite Statutory Prohibition

Although Article 93(1) of the Mining Law 2009 clearly prohibits the transfer of a mining license to a third party, Article 7A of the Amended Regulation provides that both an IUP and IUPK may be transferred provided that the transferee is at least 51% owned by the transferor, in other words, an affiliate of the transferor.

Thus, the Amended Regulation appears to be attempting to make an exception to a prohibition that is specifically established by statute. As a government regulation is subordinate to a statute under the Indonesian hierarchy of laws, it is difficult to see how this purported exception could withstand a challenge in the Supreme Court by an interested party.

Furthermore, the Amended Regulation has nothing to say as regards the requirements and procedures for carrying out such a transfer.

IUPs for FDI Companies

Generally, IUPs may be granted by the Government to (i) enterprises, (ii) cooperatives, and (iii) individual persons. Enterprises in this context include private enterprises, state-owned enterprises and local government-owned enterprises. The Amended Regulation provides clearer guidance as to what constitutes a private enterprise by defining it as (i) an enterprise whose shares are owned by domestic investors; or (ii) an enterprise whose shares are owned by foreign investors (or what it generally referred to as a foreign direct investment (FDI) company).

The Amended Regulation then provides that should an applicant for an IUP be an FDI company, the IUP will be issued by the Minister of Energy and Mineral Resources (rather than a provincial governor or regent/mayor, as the case may be).

Conclusion

For the most part, the changes introduced by the Amended Regulation represent a further ramping up the Government's long-standing efforts to ensure greater Indonesian rights over Indonesian resources. There is no doubt that the new divestment rules will have a detrimental effect on the interests of foreign-owned mining companies and potentially make Indonesia a less attractive investment destination for international miners. As such, it is likely to meet strong resistance from industry lobby groups.

As regards the purported deviation from the Mining Law introduced by the Amended Regulation, this is clearly vulnerable to an application for judicial review, meaning that it could be struck down by the Supreme Court as being in conflict with a statute.

The Ministry of Energy and Mineral Resources, which is responsible for the application of the Amended Regulation, will soon be launching a public information campaign on the new rules, and perhaps more information on the issue will emerge during this process.

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