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CONTEXTUAL REPORT

EITI INDONESIA REPORT
2015



COORDINATING MINISTRY FOR ECONOMIC
AFFAIRS REPUBLIC OF INDONESIA

EITI Extractive
INDONESIA Industries
Transparency
Initiative



**COORDINATING MINISTRY FOR ECONOMIC AFFAIRS
REPUBLIC OF INDONESIA**

EITI INDONESIA REPORT 2015 CONTEXTUAL REPORT

VOLUME TWO

KAP HELIANTONO & REKAN





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AMDAL	Analisa Mengenai Dampak Lingkungan
APBN	Anggaran Pendapatan dan Belanja Negara
APBN-P	Anggaran Pendapatan dan Belanja Negara Perubahan
ASM	Artisanal and Small-Scale Mining
ASR	Abandonment and Site Restoration
BAPPENAS	Badan Perencanaan Pembangunan Nasional
BBM	Bahan Bakar Minyak
BEI	Bursa Efek Indonesia
BI	Bank Indonesia
Binwas	Pembinaan dan Pengawasan
BKPM	Badan Koordinasi Penanaman Modal
BL	Bina Lingkungan
BLUD	Badan Layanan Umum Daerah
BO	Beneficial Owner
BP MIGAS	Badan Pelaksana Kegiatan Usaha Hulu Minyak dan Gas Bumi
BPH Migas	Badan Pengatur Hilir Minyak dan Gas Bumi
BPK	Badan Pemeriksa Keuangan
BPKP	Badan Pengawasan Keuangan dan Pembangunan
BPS	Badan Pusat Statistik
BPT	Branch Profit Tax
BUMD	Badan Usaha Milik Daerah (Local State-Owned Enterprise)
BUMN	Badan Usaha Milik Negara (State-Owned Enterprise)
BUMN-K	Badan Usaha Milik Negara-Khusus
BUT	Badan Usaha Tetap
C&D	Corporate and Dividend
CAD	Canadian Dollar
CAGR	Compound Annual Growth Rate
CNC	Clean and Clear

Cq.	Casu Quo (dalam hal ini, lebih spesifik lagi)
CR	Cost Recovery
CSR	Corporate Social Responsibility
CV	Commanditaire Venootschap (Persekutuan Komanditer)
DBH	Dana Bagi Hasil
DHPB	Dana Hasil Produksi Batubara
DIPA	Daftar Isian Pelaksanaan Anggaran
Distamben	Dinas Pertambangan dan Energi
Ditjen	Direktorat Jenderal
DJA	Direktorat Jenderal Anggaran
DJP	Direktorat Jenderal Pajak
DJPK	Direktorat Jenderal Perimbangan Keuangan
DMO	Domestic Market Obligation
DPD	Dewan Perwakilan Daerah
EBTKE	Energi Baru Terbarukan dan Konservasi Energi
EITI	Extractive Industries Transparency Initiative
EP	Eksplorasi dan Produksi
ESDM	Energi Sumber Daya Mineral
ETBS	Equity To Be Split
FTP	First Tranche Petroleum
GPFG	Government Pension Fund Global
H₂S	Hydrogen Sulfide
ICP	Indonesian Crude Price
IMF	International Monetary Fund
Inpres	Instruksi Presiden
IP	Izin Prinsip
IP/PPI	Indonesia Participating/Pertamina Participating Interest
IPO	Initial Public Offering
IPP	Izin Pinjam Pakai
IPPKH	Izin Pinjam Pakai Kawasan Hutan
IPR	Izin Pertambangan Rakyat
IUP	Izin Usaha Pertambangan

IUPK	Izin Usaha Pertambangan Khusus
JOB	Joint Operation Body
K/L	Kementerian/Lembaga
KA	Kerangka Acuan
Kab.	Kabupaten
KAP	Kantor Akuntan Publik
Kemenkeu	Kementerian Keuangan
KESDM	Kementerian Energi dan Sumber Daya Mineral
Kg	Kilogram
KI	Kredit Investasi
KIP	Komite Informasi Pusat
KK	Kontrak Karya
KKKS	Kontraktor Kontrak Kerja Sama
KKS	Kontrak Kerja Sama
KMK	Keputusan Menteri Keuangan
Korsup	Koordinasi dan Supervisi
KP	Kuasa Pertambangan
KPJM	Kerangka Pengeluaran Jangka Menengah
KPK	Komisi Pemberantasan Korupsi
KSO	Kerja Sama Operasi
LAKIP	Laporan Akuntabilitas Kinerja Instansi Pemerintah
LKPP	Laporan Keuangan Pemerintah Pusat
LNG	Liquid Natural Gas
LO	Liaison Officer
LSM	Lembaga Swadaya Masyarakat
MA	Mahkamah Agung
MBLB	Mineral Bukan Logam dan Batuan
MBOEPD	Thousand Barrels of Oil Equivalents Per Day
MBOPD	Thousand Barrels of Oil Per Day
MDM	Migas Data Management
Mendagri	Menteri Dalam Negeri
Menhut	Menteri Kehutanan

Migas	Minyak dan Gas Bumi
Minerba	Mineral dan Batubara
MK	Mahkamah Konstitusi
MMBO	Million Barrels of Oil
MMBOE	Million Barrels of Oil Equivalents
MMBTU	Million British Thermal Units
MMSCFD	Million Standard Cubic Feet Per Day
MMSTB	Million Stock Tank Barrels
MSCF	Thousand Standard Cubic Feet
MSG	Multi-Stakeholder Group
MTEF	Medium-Term Expenditure Framework
NJOP	Nilai Jual Objek Pajak
NPWP	Nomor Pokok Wajib Pajak
OP	Operasi Produksi
OPEC	Organization of the Petroleum Exporting Countries
P3B	Persetujuan Penghindaran Pajak Berganda
PBB	Pajak Bumi dan Bangunan
PBB	Performance Based Budgeting
PBI	Peraturan Bank Indonesia
PBK	Penganggaran Berbasis Kinerja
PDB	Produk Domestik Bruto
PDRB	Produk Domestik Regional Bruto
PDRD	Pajak Daerah dan Retribusi Daerah
PEL	Penyajian Evaluasi Lingkungan
Pemda	Pemerintah Daerah
Pemkab	Pemerintah Kabupaten
Pemkot	Pemerintah Kota
Pemprov	Pemerintah Provinsi
PEP	Politically Exposed Person
Permen	Peraturan Menteri
Permendag	Peraturan Menteri Perdagangan
Permenhut	Peraturan Menteri Kehutanan
Perppu	Peraturan Pemerintah Pengganti Undang-Undang

Perpres	Peraturan Presiden
Perusda	Perusahaan Daerah
PETI	Pertambangan Tanpa Izin
PHK	Pemutusan Hubungan Kerja
PHT	Penjualan Hasil Tambang
PI	Participating Interest
PIL	Penyajian Informasi Lingkungan
PKBL	Program Kemitraan dan Bina Lingkungan
PKP2B	Perjanjian Karya Pengusahaan Pertambangan Batubara
PLTU	Pembangkit Listrik Tenaga Uap
PMA	Penanaman Modal Asing
PMK	Peraturan Menteri Keuangan
PN	Pengadilan Negeri
PNBP	Penerimaan Negara Bukan Pajak
PN TABA	Perusahaan Negara Tambang Arang Bukit Asam
POD	Plan of Development
POJK	Peraturan Otoritas Jasa Keuangan
POR	Pay Out Ratio
PP	Peraturan Pemerintah
PPATK	Pusat Pelaporan dan Analisis Transaksi Keuangan
PPID	Pejabat Pengelola Informasi dan Dokumentasi
PPh	Pajak Penghasilan
PPN	Pajak Pertambahan Nilai
PPN	Perencanaan Pembangunan Nasional
PSC	Production Sharing Contract
PSDH	Provisi Sumber Daya Hutan
PSO	Public Service Obligation
PTFI	PT Freeport Indonesia
PTK	Pedoman Tata Kerja
PTSP	Pelayanan Terpadu Satu Pintu
Raperda	Rancangan Peraturan Daerah

Renja	Rencana Kerja
Renstra	Rencana Strategis
RKA	Rencana Kegiatan dan Anggaran
RKAB	Rencana Kerja dan Anggaran Belanja
RKP	Rencana Kerja Pemerintah
RPJM	Rencana Pembangunan Jangka Menengah
RPJMN	Rencana Pembangunan Jangka Menengah Nasional
RPJPN	Rencana Pembangunan Jangka Panjang Nasional
RRR	Reserve Replacement Ratio
RUU	Rancangan Undang-Undang
RUPS	Rapat Umum Pemegang Saham
SAP	Standar Akuntansi Pemerintahan
SBI	Sertifikat Bank Indonesia
SDA	Sumber Daya Alam
SDM	Sumber Daya Manusia
SE	Surat Edaran
SIB	Surat Instruksi Bersama
SIMPONI	Sistem Informasi Penerimaan Negara Bukan Pajak Online
SITC	Standard International Trade Classification
SK	Surat Keputusan
SKK Migas	Satuan Kerja Khusus Pelaksana Kegiatan Usaha Hulu Minyak dan Gas Bumi
SPOP	Surat Pemberitahuan Objek Pajak
SSP	Surat Setoran Pajak
SUN	Surat Utang Negara
TAC	Technical Assistance Contract
TKDN	Tingkat Komponen Dalam Negeri
Tekmira	Teknologi Mineral dan Batubara
TSP	Tanggung Jawab Sosial Perusahaan
UNDP	United Nations Development Programme
USD, US\$	United States Dollar

UU	Undang-Undang
WAP	Weighted Average Price
WIUP	Wilayah Izin Usaha Pertambangan
WIUPK	Wilayah Izin Usaha Pertambangan Khusus
WK	Wilayah Kerja
WP	Wilayah Pertambangan
WPN	Wilayah Pencadangan Negara
WPR	Wilayah Pertambangan Rakyat
WUP	Wilayah Usaha Pertambangan
WUPK	Wilayah Usaha Pertambangan Khusus
YP2IP	Yayasan Pusat Pengembangan Informasi Publik

IN TERMS OF COMPLIANCE WITH THE EITI STANDARD 2016, THIS YEAR THERE ARE AT LEAST TWO SIGNIFICANT BREAKTHROUGHS REGARDING THE TRANSPARENCY OF THE EXTRACTIVE INDUSTRY OF THE GOVERNMENT OF INDONESIA.





EXECUTIVE SUMMARY

The discussion topics in this Contextual Report are written based on the EITI standard 2016 and inputs from the Implementation Team. The discussion includes the governance, licenses and contracts, the extractive industry contribution, the role of state owned enterprises, corporate social responsibility and the management of state revenues derived from extractive industry.

In terms of compliance with the EITI standard 2016, this year there are at least two significant breakthroughs regarding the transparency of the extractive industry of the Government of Indonesia. First, the availability of cadastral information for oil and gas sector and mineral and coal accessible at <http://geoportal.esdm.go.id>. Second, the preparation of the Presidential Regulation plan on Beneficial Ownership which is led by the Financial Transaction Reports and Analysis Center (PPATK) together with other related ministries.

Contextual report 2015 is presented in 8 (eight) sections that can be an important reference for the public to understand the extractive industry in Indonesia.

First section of this report explain the definition of the extractive industry. Extractive industry is all activities that take natural resources directly from the earth in the form of mineral, coal, oil and gas. As a country with abundant natural resources, extractive industry becomes one of the main industries in Indonesia. Hence, the governance of extractive industry is worthy of attention. One of the efforts made by Indonesian government to manage extractive industry well is an EITI Standard implementation. EITI, which stands for the Extractive Industries Transparency Initiative is a global standard covering provision that enhances transparency and accountability of resources management by requiring oil, gas and mining companies to disclose their payment to the government,

and the government to disclose its revenue from the companies. The implementation of the EITI standard in Indonesia is expected to benefit the government, companies and the society.

The legal basis of EITI implementation in Indonesia is Presidential Regulation Number 26 Year 2010. The regulation orders the establishment of Transparency Team that consist of Steering Team and Implementation Team. The team is tasked with the carrying out of transparency of national and local extractive industry revenues by collecting revenue data related to extractive industry from both government and companies, conducting the reconciliation and publishing the data to the public.

Second section of contextual report discusses about the governance of the extractive industry related to legal provision of the extractive industry, permit system through licenses and contracts and changes as well as improvements of the governance of the extractive industry that are underway at the time of writing of this report. This section assists the society to understand the regulation and management system of the extractive industry in Indonesia.

The governance of the extractive industry in Indonesia is guided by the 1945 Constitution of the Republic Indonesia Article 33 paragraph 3: "Land and water and the natural riches contained therein shall be controlled by the State and shall be made use of for the people", which in its development has been applied in the Law which has undergone several amendments. Currently, the applicable law in the extractive industry is Law No. 22/2001 regarding Oil and Gas and Law No. 4/2009 regarding Mineral and Coal Mining. This section exhibits list of regulations as well as the hierarchy of fiscal policy and law applicable in the extractive industry.



The discussion about the governance includes the discussion about related regulations, such as Forestry Law, national energy policy, contract transparency and Beneficial Ownership transparency.

This section also discusses the current government efforts in improving the governance of the extractive industry. The Government has applied an Indonesia's Integrated One Stop Service Program (PTSP) to simplify the licensing process, including the license related to the extractive industry. In mineral and coal mining sector, the Government has established policies to accelerate full implementation of the Law No 4/2009 and the Law No. 23/2014 in order to improve the governance of mineral and coal mining in Indonesia. Several actions taken by the Government among others are reconciliation of National IUP since 2011 and the establishment of coordination & supervision conducted by KPK in mineral and coal mining sector since 2014.

Current issues and challenges related to the governance of the extractive industry are also discussed in this section. They are the declining of exploration activities in oil and gas sector as well as mineral and coal sector, issues related to regulations of the gross split scheme, current status of the revision of Oil and Gas Law and Mineral and Coal Law, debates and the development of regulations related to the value added enhancing of minerals, the implementation of divestment regulation, the conversion of contracts to license regime and the accuracy of non-tax state revenue payment and reporting. These topics are prepared based on the guidance of the Implementation Team and Scope of EITI Report 2015 of Indonesia.

Third section of contextual report discusses about the process of licenses and contracts of oil and gas in Indonesia, including types of license/contract and tenders in 2015. In Indonesia's oil and gas mining, there are three types of contracts: (1) Production Sharing Contract (PSC); (2) Joint Operation Body (JOB); and (3) Production Sharing Contract with Gross Split Scheme. The process of determination and auction procedures of the working area (Wilayah Kerja/WK) in oil and gas mining is described in this section along with the information of WK's offering in 2015 and the discussion about compulsory offering of 10% Participating Interest (PI) to Local Owned Enterprises and local companies. The current issue that has also become a challenge for the Government of Indonesia (Ministry of Energy and Mineral Resources) related to licensing and contract in oil and gas mining is a transition period of oil and gas blocks concerning contract extensions/cooperation agreements which will expire in 2024 and have not been extended and its relation to the achievement of national targets of oil and gas production.

The next discussion covered by this section is about the license issues in mineral and coal mining sector. Based on the Law No. 4/2009 on Mineral and Coal Mining and the Law No. 23/2014 on Local Government, the concession mechanism is the granting of licenses through Mining Business License (IUP) with the permit granting authority owned by the Minister of EMR and the Governor (Head of Provincial Region). However, contracts / agreements (KK

or PKP2B) which have been issued before the stipulation of the Law No. 4/2009 remains in effect until the contract / agreement expires.

One of the mandates of the Mineral and Coal Law of 2009 is that the Government is obliged to determine the allocation of Mining Areas (WP) that is the basis of the determination of Mining Business Area (WUP) / People's Mining Area (WPR) / Country Reserves Area (WPN). The determination of WUP / WPR / WPN becomes the basis for granting licenses (Mining Business License Area (WIUP) / People's Mining License (IPR) / Special Mining Business License Area (WIUPK)) through the auction mechanism. The process of determination up to the auction of WIUP is also described in this section. There is no IUP auction in 2015 because the government is still in the process of reforming the national IUP since the enactment of the Mineral and Coal Law of 2009. Directorate General of Mineral and Coal issues Circular Letter No. 08.E / 30 / DJB / 2012 concerning moratorium on issuance of IUP by Local Government and still valid until now.

Fourth section of the contextual report discusses the overview of extractive industry and the contribution of extractive industry to the Indonesian economy. The discussions include the ranking of reserves and production of Indonesia's extractive industry at the global level, production data and value, concentration areas of production, development projects in the upstream oil and gas sector, description of mineral and coal mining exploration activities, and extractive industry contribution to economic growth (GDP) in Indonesia, state revenue, total exports and employment.

The contribution of the extractive industry to total GDP by 2015 is 8% of the total national GDP. Although the contribution at the national level is below 10%, the mining sector has a relatively large contribution in some provinces, for example in East Kalimantan in which mining sector accounts for 45% of total GDP. In addition, mining sector in Papua Province and Riau Province accounts for 32% and 30% of total GDP of the respective province.

The extractive industry contribution is significant to state revenues and exports. Extractive industry accounted for 15% of total state revenues. In the period of 2012-2014 the contribution of state revenues from the extractive industry is quite high at around 30% of the total state revenues. However, due to the declining of oil price, from about US\$ 100 / barrel to only US\$ 50 / barrel, industry revenues declined by around 50% in 2015 (2012: 30%, 2015: 15%).

There is a decrease in the contribution of mining export value by about 4%, from 28% in 2014 to 24% of the value of national exports in 2015. The decrease is due to the decline of natural gas exports since the government prioritizes the use of natural gas for national consumption. The decline in oil price does not significantly affect the value of national exports because oil production is largely consumed domestically. The contribution of manpower in the mining and quarrying sector accounts for about 1.3 million workers (or 1.15% of total workforce) by 2015.

Fifth section of this report discusses 4 (four) State-Owned Enterprises (SOEs) engaged in the extractive industry, namely PT Pertamina, PT Aneka Tambang, PT Bukit Asam and PT Timah. All SOEs are in the form of Persero and three SOEs, namely PT Aneka Tambang, PT Bukit Asam and PT Timah have been listed on the Indonesia Stock Exchange (IDX). The Government of Republic of Indonesia holds 65% of common stock and Dwiwarna share with veto rights in three state-owned enterprises of mineral and coal as well as 100% of PT Pertamina shares. The role of the Government in the management of those SOEs is represented by the Ministry of SOEs, Ministry of Finance and Ministry of Energy and Mineral Resources, each of which has authority in terms of operational / managerial, capital and formulation, determination and implementation of policies in the field of energy and mineral resources.

In connection with the financial relationship between SOEs and the central government, in 2015 the Government increases the amount of paid-up capital to PT Aneka Tambang (Persero) Tbk by Rp 3.5 trillion. The additional capital from the Government is used to construct the Halmahera Feronikel Plant. In 2015, three state-owned enterprises engaged in the extractive industry contributed to the Rp 6.86 trillion dividend received by the Government of the Republic of Indonesia. PT Aneka Tambang (Persero) Tbk does not pay dividends because of its financial condition.

As mandated in the Law No. 19/2003, the establishment of SOEs is not only intended to seek profit but also to organize the public benefit and also to provide guidance and assistance to small entrepreneurs, cooperative and community groups. Therefore, similar with other state-owned enterprises, the four SOEs in the extractive industries also have an obligation to implement the Partnership and Community Development Program (PKBL) and conduct public services. One form of public service is the fuel (BBM) subsidy by PT Pertamina (Persero). PT Pertamina receives a mandate from the Government to distribute subsidized fuel. Based on the EITI 2015 reporting form, Pertamina has disbursed a 3 kg LPG and BBM subsidy equivalent to 47,555 billion Rupiah.

The government plans to form a holding company of SOEs for efficiency and synergy and increase the assets of SOEs. In relation to the extractive industry, the Government will establish a holding of oil and gas and mining companies. Holding of oil and gas SOEs is a combination of PT Pertamina (Persero) and PT Perusahaan Gas Negara. Meanwhile, the holding of mining SOEs will consist of PT Inalum (Persero), PT Aneka Tambang (Persero) Tbk, PT Timah (Persero) Tbk and PT Bukit Asam (Persero) Tbk.

Sixth section of the contextual report discusses environmental responsibility and corporate social responsibility for extractive industry companies in Indonesia. Furthermore, this section also mentioned about the people's mining and illegal mining / mining

without permission (PETI). Companies engaged in the extractive industry have environmental responsibility and social responsibility as set out in various regulations. The Company is obliged to provide the amount of funds used as collateral for environmental restoration / reclamation costs called the Abandonment Fund and Site Restoration (ASR) for oil and gas companies, and Reclamation and Post-Mining Guarantee Reserves for mineral and coal companies.

Until 2015, the ASR funds collected in the accounts of a number of state banks amounted to US\$ 775 million (with an average increase rate of 35% since 2011). Based on the Supreme Audit Board (BPK) audit in the first semester of 2017, it is known that SKK Migas has not recorded the receivable of ASR from 8 PSC Contractors totaling Rp72.3 billion. SKK Migas requested the 8 PSC Contractors to settle the ASR reserve bill and was paid Rp48.3 billion. SKK Migas has authority over the management of such ASR funds, such as billing authority and approval for the disbursement and use of such funds. Until now there is no information that can be accessed by the public about the total amount of national reclamation and post-mining funds paid by mineral and coal companies. To improve transparency, reclamation and post-mining guarantee reserves data filling is included in the reporting form of 2015, in which the amount of reclamation and post-mining guarantees of companies included in the reconciliation scope can be seen in the EITI Reconciliation Report 2015.

In relation to corporate social responsibility (CSR), any company incorporated as a limited liability company is required to hold a CSR program (based on Limited Liability Company Law). However, the amount of CSR is not regulated. As for SOEs, it is mandatory to organize Partnership and Community Development Program (PKBL) with a maximum amount of 4% of profit after previous yearly tax.

Furthermore, this section discusses the people's mining license. The definition of Artisanal and Small-Scale Mining (ASM) is largely a mining activity carried out individually, in groups, by families or cooperatives in a traditional and minimal or non-technological manner. The Law No. 4/2009 on mineral and coal mining does not recognize ASM but regulates the People's Mining to accommodate the legality of traditional mining undertaken by the people. This section also briefly discusses the unauthorized mining.

Seventh section of the contextual report discusses state revenue management in the extractive industry beginning with the planning, budgeting and audit process. This section provides information on methods of allocating revenue from the extractive industry to local government.

All non-tax state revenues from the extractive industry are received in cash, unless some revenues from the upstream oil and gas sector related to production sharing contracts. Such revenues received by the Government of Indonesia in

the form of in-kind. They are the government's oil and gas lifting and DMO (minus DMO costs) related to production sharing contract. The management of in-kind revenues from the upstream oil and gas is under the authority of SKK Migas. Tax revenues from the extractive sector are entirely in cash. Since 2015, tax revenue from the oil and gas sector can be paid in in-kind. However, there has been no realization to date. The state revenues from the extractive industry are deposited in the state treasury and recorded in the Central Government Financial Statement (LKPP).

This section also discusses the planning and budgeting process along with the audit implementation process and the allocation mechanism of state revenue between the central government and the local government. The public may access financial notes, LKPP and LKPP audit

results by the Supreme Audit Board (BPK) on the Ministry of Finance and BPK web pages. For an overview of the extractive industry in the future, the public can access the EMR Ministry Strategic Plan for 2015-2019 on the Ministry of Energy and Mineral Resources web page.

The allocation of state revenues from extractive industry between the central and the local government is regulated in revenue sharing funds (DBH) in accordance with the Law No. 33/2004 on Financial Proportionality. The local government share of petroleum and natural gas revenue is 15% and 30%, respectively. From the oil and gas sharing scheme, the Local Government receives an earmarked of 0.5% for primary education. In addition, there are also DBH sharing schemes for the special autonomous regions of Aceh Province, West Papua Province and Papua Province which get an additional 55% for petroleum revenues



and an additional 40% for natural gas revenues. Papua and West Papua Provinces are required to allocate such revenues for education sector of at least 30% and for health and nutrition improvement of at least 15%, while the Aceh Province is required to allocate at least 30% for education. The Local Government obtains 20% of revenues from the general mining. Realization and budget allocation of DBH can be seen in appendix of LKPP or the Directorate General of Fiscal Balance web page. This section exhibits 10 major recipient areas of DBH from oil and gas as well as mineral and coal.

Payments from extractive industry companies to local governments are also discussed in this section, especially about the types and rates of payments. Several associations, including the Indonesia Mining Association (IMA) and the Indonesian Mining Services Association (Aspindo) have filed a judicial review to the Constitutional Court for the imposition of motor vehicle tax (PKB) and

tax on change of motor vehicle ownership (BBNKB) for heavy equipment commonly used by mining companies. The Constitutional Court decided that heavy equipment used in mining activities is not an object of PKB and BBNKB because it is not a motor vehicle.

Eighth section is a recommendation section. The Implementation Team requires the EITI Report to include recommendations to improve transparency and governance levels in the extractive industry. In this report, there are two recommendations:

1. There is an agreement on adequate technical procedures that clearly illustrates how local governments can access data to be able to project the amount of revenue sharing funds for oil and gas.
2. EITI Secretariat to send a letter to the PPID ESDM to open PKP2B and KK contracts in the upstream mineral and coal sector.



01

INTRODUCTION

BENEFITS OF IMPLEMENTING EITI FOR THE GOVERNMENT ARE IMPROVING THE EFFECTIVENESS AND THE EFFICIENCY OF THE EXTRACTIVE INDUSTRY GOVERNANCE IN THE COUNTRY, SO THAT ALL CITIZENS CAN BE BENEFITED FROM NATIONAL AND LOCAL REVENUE OF NATURAL RESOURCES.



1.1 Definition of the Extractive Industry

Extractive activities are all activities that take natural resources directly from the earth in the form of mineral, coal, oil and gas. Extractive industry is divided into two activities, i.e. upstream activities and downstream activities. Upstream activities are activities that are based on exploration and exploitation activities. Exploration activities are activities aimed at obtaining information on geological conditions to find and obtain reserve estimates. While exploitation activities are series of activities aimed at producing oil, gas, coal and other minerals consisting of drilling/mining activities, construction of transportation facilities, storage, processing for separation and purification.

Downstream activities are processing activities consisting of purifying, enhancing quality and enhancing added value process, then process of transportation, storage and/or commerce. This report focuses on upstream activities. The extractive industry in this report only covering oil, gas, mineral and coal mining in accordance with the definition of the extractive industry in Presidential Regulation Number 26 Year 2010.

1.2 What is Extractive Industries Transparency Initiative (EITI)?

Extractive Industries Transparency Initiative is a global standard covering provision that enhances transparency and accountability of resources management by requiring oil, gas and mining companies to disclose their payment to the government, and for the government to disclose its revenue from the companies. EITI aims to provide information disclosure to the public to strengthen the system and build trust, both to the government and to related companies¹.

EITI has two basic concepts as illustrated in Figure 1.

- **Transparency:** Companies engaged in the extractive industry disclose their payments to the Government and the Government discloses its revenue. The figures are reconciled by the Independent Administrator Team which is subsequently reported and published in the Annual Report of EITI along with a contextual report of extractive industry.
- **Accountability:** The establishment of Multi-Stakeholder Group (MSG) consisting of government representatives, representatives of private companies/state-owned enterprises and representatives of non-governmental organizations, who are required to engage in supervising the reconciliation process and engage in the discussion on issues arising from the problem found in the EITI report. The existence of MSG Team is expected to improve the transparency and accountability of a country's extractive industry.

The EITI Standard is supervised by an international board consisting of representatives from the government of EITI implementing countries, supporting countries, non-governmental organizations, industry and companies².

1.3 Benefits for Indonesia as an EITI Compliant Country

Benefits of implementing EITI for the Government are improving the effectiveness and the efficiency of the extractive industry governance in the country, so that all citizens can be benefited from national and local revenue of natural resources. The improvement of the effectiveness and the efficiency of the extractive industry governance can also mitigate conflicts related to the extractive industry, so that economic and political condition can be more stable. The stability of a country's economic and political condition can improve the investment climate and provide a positive signal for investors. The disclosure of information on contracts between the Government and companies can increase support for fairer enactment of contracts so that the Government may obtain more reasonable share of revenue.

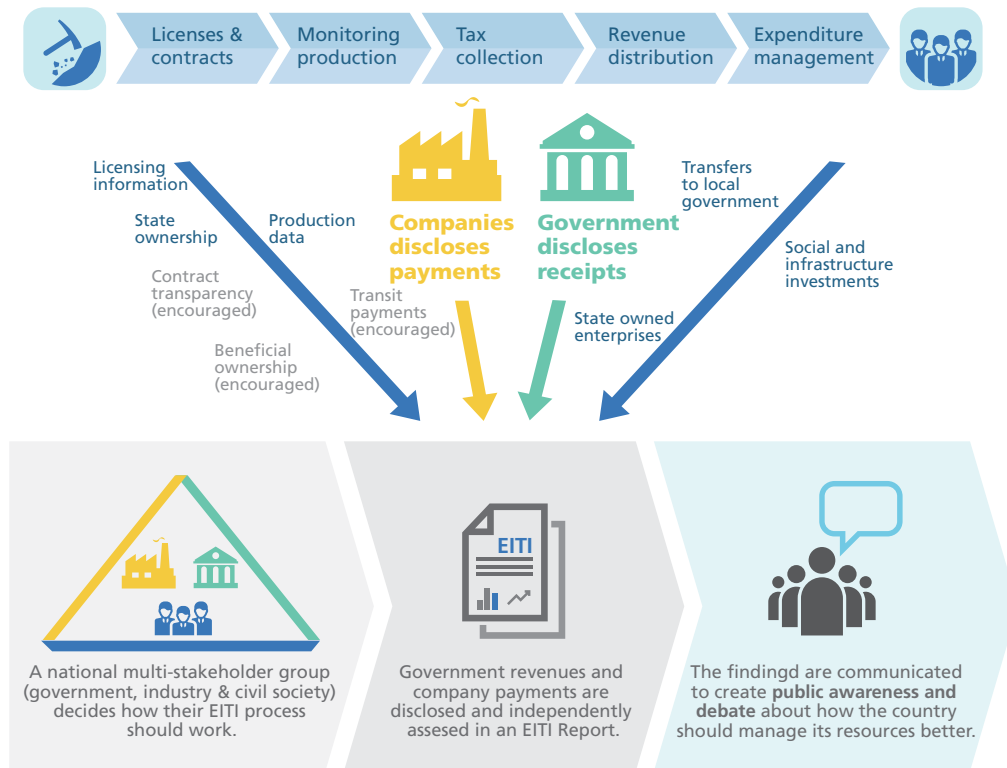
The benefits for companies participating in EITI are gaining clear information regarding companies responsibilities in complying all provisions and policies imposed by the Government related to the extractive industry and trust from the public. Meanwhile, the benefit for the society is to receive reliable information, so that the society can demand for accountability in managing national and local revenue derive from extractive industry. In addition, access to information related to extractive industry owned by the society enables the society to monitor and demand for companies responsibilities, such as pending payments, to be met. Active participation from the society in implementing EITI enhances clean management of natural resources, so that the society can receive better benefits.

A country must pass through 4 stages of registration before becoming an EITI candidate country and needs to publish an EITI report within 18 months after getting accepted as an EITI candidate country. Subsequently, to become an EITI compliant country, an EITI candidate country will go through a validation process for 2.5 years from becoming an EITI candidate country. According to the EITI website in August 2017, there are 52 EITI implementing countries including 38 countries that have not been assessed related to the compliance with the EITI Standard 2016 and 5

1 <https://eiti.org/eiti>

2 <https://eiti.org/about/board>

Figure 1. The EITI Standard



Source: EITI Standard

suspended countries as they either unable to meet the EITI Standard 2016 or encounter political instability. In addition to the 52 EITI implementing countries, there are 3 countries that have announced their commitment to join and implementing EITI.

The EITI Standard can be obtained from <https://eiti.org/standard/overview>

1.4 EITI in Indonesia

EITI in Indonesia is regulated by Presidential Regulation Number 26 Year 2010 regarding Transparency of National/ Local Extractive Industry Revenues which is decided by President of the Republic of Indonesia, Susilo Bambang Yudhoyono in April 23, 2010. The presidential regulation establishes the definition of the extractive industry and national and local revenues derived from the extractive industry. Furthermore, the regulation instructs to the establishment of Transparency Team and explains the structure and task of the Team.

Transparency Team is under and directly responsible to the President. The Team is tasked to carry out the transparency of national and local revenues derived from the extractive industry. In carrying out its duties, the Transparency Team has the authority to

request information, additional data, input and/or ask for consultation from the central government, local government and companies engaged in the extractive industry.

The Transparency Team consists of Steering Team and Implementation Team, each chaired by Coordinating Minister for Economic Affairs and Deputy of Coordinating Energy and Mineral Resources, Coordinator for Economic Affairs. The Steering Team is in charge of formulating general policies, providing direction to the Implementation Team, determining the work plan of the Transparency Team and evaluating the implementation of national and local revenues transparency. This team reports at least once a year to the President. The members of the Steering Team consist of the Minister of Energy and Mineral Resources, the Minister of Finance, the Minister of Home Affairs, the Head of the Financial and Development Supervisory Board and Prof. Ir. Dr. Emil Salim, President's Advisor on Economy and Environment, as a representative from the society.

Meanwhile, the Implementation Team is responsible to the Steering Team and is responsible for formulating the Transparency Team work plan for 3 years, preparing the report format, selecting a reconciliator, disseminating the results of the report reconciliation, preparing the Report of the Steering Team to the President and

carrying out anything else assigned by the Steering Team. This team is a multistake group and its members consist of representatives of the Coordinating Ministry for Economic Affairs, Ministry of Energy and Mineral Resources, Ministry of Finance, Ministry of Home Affairs, Financial and Development Supervisory Board, Special Unit for Upstream Oil and Gas (SKK Migas), PT

Pertamina (Persero), regional governments, associations of mineral and coal mining companies and oil and gas and representatives from non-governmental organizations (NGOs).

Indonesia officially became an EITI candidate in October 2010 and has published four EITI reports, namely:

Table 1. Published EITI report

Report	Publish Year	Scoping Year	Type of Report
First	2013	2009	Reconciliation Report
Second	2014	2010-2011	Reconciliation Report
Third	2015	2012-2013	Contextual Report and Reconciliation Report
Fourth	2017	2014	Contextual Report and Reconciliation Report

Source: EITI Indonesia

Figure 2. The Implementation of EITI in Indonesia



Source: Modification Result

02

THE GOVERNANCE OF EXTRACTIVE INDUSTRY

SEVERAL INTENSIVE REGULATIONS AND DEREGULATIONS ARE CARRIED OUT BY THE GOVERNMENT OF INDONESIA IN THE PERIOD OF 2015-2017, INCLUDING THE SIMPLIFICATION OF POLICIES IN OIL AND GAS MINING AND MINERAL AND COAL MINING SECTORS.

This section includes a discussion of the legal framework in governing the extractive industry in Indonesia, the duties and functions of relevant government agencies in the extractive industry and contracts and licensing of extractive industry. In addition, the last part of this section discusses the changes and improvements in extractive industry governance that are being implemented at the time of writing.

2.1 The Overview of Upstream and Downstream Activities

2.1.1 Oil and Gas Sector

Figure 3 describes upstream to downstream oil and gas business activities, which upstream business activities are activities that are based on exploration and exploitation business activities. While downstream activities are business activities that focus on business activities of management, transportation, storage and/or commerce.

The operational of upstream and downstream activities of oil and gas regulated under the Law No. 22/2001 is managed by the following institutions based on sector of activity:

- Upstream activities of oil and gas are managed by a special unit for upstream oil and gas (Satuan Kerja Khusus Pelaksana Kegiatan Usaha Hulu Minyak dan Gas Bumi / SKK Migas) pursuant

to the Presidential Regulation No. 9/2013, whose duties and responsibilities are under the Vice Minister of Energy and Mineral Resources, the Vice Minister of Finance and the Head of Investment Coordinating Board.

- Downstream activities of oil and gas are managed by regulatory agency for downstream oil and gas (Badan Pengatur Hilir Minyak dan Gas Bumi/ BPH Migas) pursuant to the Law No. 22/2001 article 46 and 47.

2.1.2 Mineral and Coal Sector

Similar to the oil and gas industry, the minerals industry has business activities that can be categorized in the primary industry (upstream) and secondary industry (downstream). Upstream mineral and coal activities rely on exploration activities to locate and determine resource values (hypothetical-inferred-indicated-measured) and reserves (probable-proved). If the result of the exploration meets a particular feasibility (especially technical and economic feasibility), then it will be continued into exploitation (mining) activities to produce minerals.

Meanwhile, the processing business activities to increase the added value of mining materials are secondary industry activities (minerals downstream

Figure 3. Upstream and downstream activities in oil and gas sector

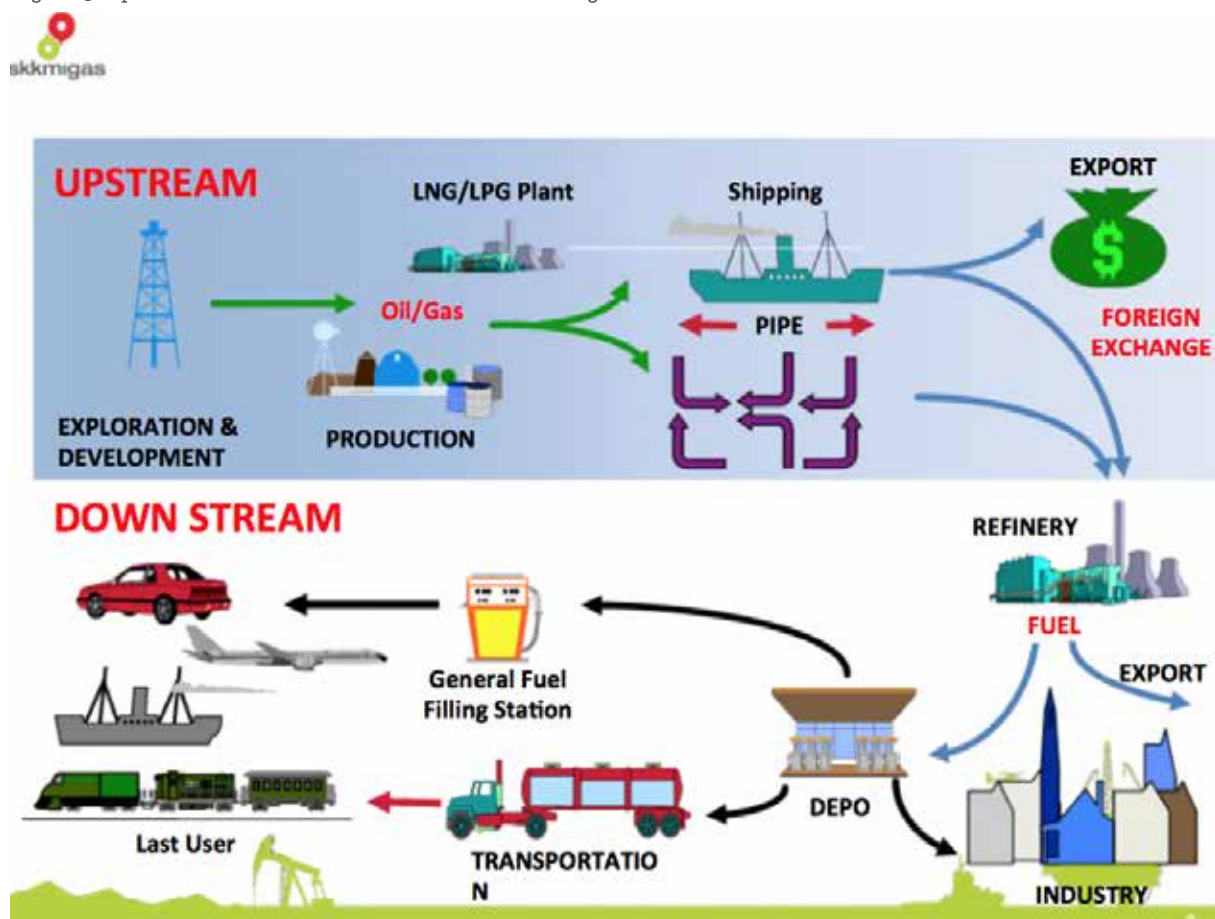
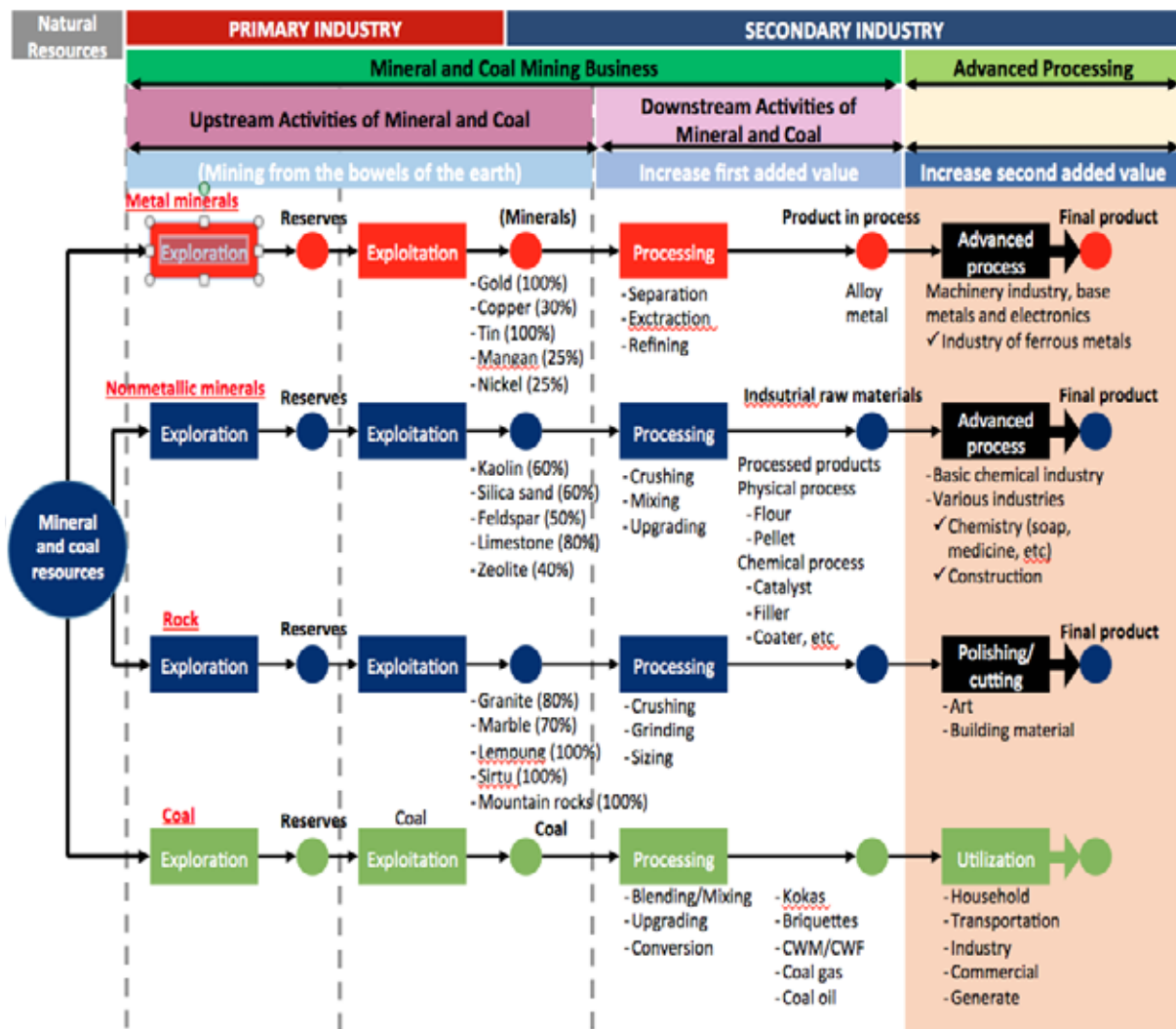


Figure 4. The chain of mineral and coal mining activities



Source: Badan Penelitian dan Pengembangan ESDM, KESDM

business), which the first added value is to produce products to become raw materials / products for advanced minerals industry to produce the final products. Unlike minerals, the final product of coal mining is a source of energy (fuel), especially for industry, such as fuel for power plant / electricity industry, fuel for steel and cement industry and other industry activities instead of finished goods products. Figure 4 illustrates the chain of mineral and coal mining activities.

2.2 The Mandate of the 1945 Constitution of the Republic of Indonesia

The 1945 Constitution of the Republic of Indonesia article 33 regulates the basic principles of Indonesia's economic activity. The following is the content and explanation of article 33 which is the 4th amendment of the 1945 Constitution:

Table 2. The content and explanation of the 1945 Constitution article 33

Article (paragraph)	Content	Explanation
Article 33 (1)	"The economy shall be organized as a common endeavour based upon the principles of the family system."	Indonesian economy is based on family system and not based on other system, such as liberal or socialist.

Article (paragraph)	Content	Explanation
Article 33 (2)	"Sectors of production which are important for the country and affect the life of the people shall be under the powers of the State."	State controls over the sectors of production, which are important and affect the life of the people, such as oil and other minerals.
Article 33 (3)	"The land, the waters and the natural resources within shall be under the powers of the State and shall be used to the greatest benefit of the people."	The natural wealth of the entire territory of Indonesia both in the earth and on earth must be used to prosper the people of Indonesia as a whole.
Article 33 (4)	"The organization of the national economy shall be conducted on the basis of economic democracy upholding the principles of togetherness, efficiency with justice, continuity, environmental perspective, self-sufficiency, and keeping a balance in the progress and unity of the national economy."	The implementation of the Indonesian economy prioritizes the principles of togetherness, efficiency, fairness, continuity and environmental perspective as well as promoting the national economy.

Source: The 1945 Constitutional

With the addition of the fourth paragraph in the 1945 Constitution article 33, the role of the state in regulating the economy is clearly not limited only as a regulator. The Government shall become a direct player when negative externalities, failures in the market mechanism, and/or economic and social inequality arise.

The fourth paragraph of the 1945 Constitution article 33 also relevant with the first and second principles of the EITI Standard 2016³. They are :

1. We share a belief that the prudent use of natural resource wealth should be an important engine for sustainable economic growth that contributes to sustainable development and poverty reduction, but if not managed properly, can create negative economic and social impacts.
2. We affirm that management of natural resource wealth for the benefit of a country's citizens is in the domain of sovereign governments to be exercised in the interest of their national development .

Related to the EITI Standard, the 1945 Constitutional article 28F also regulates about transparency, which is stated as follows:

"Every person shall have the right to communicate and to obtain information for the purpose of the development of his/her self and social environment, and shall have the right to seek, obtain, possess, store, process and convey information by employing all available types of channels"

Which is then regulated in the Law No. 14 Year 2008 on Public Information Disclosure. The issuance of the Law No. 14/2008 is based on the following considerations:

- a. that information is a basic need of every person to develop their personality as well as their social environment, and is a significant part of the national security;
- b. that the right to obtain information is a human right and transparency of public information is a significant characteristic of a democratic state that holds the

sovereignty of the people in high esteem, to materialize good state management;

- c. that transparency of public information is a facility to optimize public supervision on the organizing of the state and other public agencies and everything that affects the interest of the public;
- d. that public information management is an effort to develop an informative society.

With the issuance of the Law of Public Information Disclosure, the public has the right of obtaining information and the state must fulfill the right through all institutions as a form of good governmental implementation. Government through agencies or ministries and institutions shall provide data and information to the public. Regarding to this matter, the government obliges to provide public data without having to announce it⁴.

The 1945 Constitutional article 33 becomes the legal basis which further regulates several provisions in the extractive industry in Indonesia, namely the Law No. 22/2001 concerning Oil and Gas and the Law No. 4/2009 concerning Mineral and Coal Mining as well as the derivative rules which will be discussed briefly in this section.

2.2.1 Legal Framework of Oil and Gas Mining

The Law of Oil and Gas

The formation of the Law No. 22 Year 2001 on Oil and Gas aimed at National Development that is directed to the creation of welfare for the people. The making process of the Law also considers national and international development that can create oil and gas business activities that are independent, capable, transparent, competitive, efficient and environment-oriented, and encourage the development of national potential and involvement.⁵

The Law No. 22/2001 on Oil and Gas affirms the State's control over oil and gas activities which the operational arrangement is carried out by

3 The EITI Standard 2016, look in the Box 1 :The EITI Principles, page 10.

4 <http://www.mongabay.co.id/2014/10/06/soal-sda-pemerintah-masih-sulit-buka-data-indikasi-apa/>

5 Hadi Setia Tunggal, SH. Himpunan Peraturan Perundang-Undangan Minyak dan Gas Bumi, Pertambangan Mineral dan Batubara, Panas Bumi, dan Ketenagalistrikan, (Jakarta: Harvarindo, 2010) h.37

the government as an owner of mining and processing authority of oil and gas in Indonesia. The Government is represented by SKK Migas and BPH Migas in upstream and downstream activities of oil and gas sector. Both SKK Migas and BPH Migas are tasked to ensure⁶:

- a. The conservation of resources and reserves;
- b. The management of oil and gas data;
- c. The application of good technical norms;
- d. The quality of processes products;
- e. The safety and security of the workplace;
- f. The management of good governance on environment to prevent environmental damage;
- g. The prioritization of the usage of local manpower, goods and services;
- h. The development of local society and
- i. The development and application of oil and gas technology.

Characteristics of production sharing contract according to the Law of Oil and Gas, among others:

- the term of contract maximum 30 years and can be extended to maximum 20 years. The term of exploration is 6 years and can be extended to maximum 4 years;
- oil and gas produced shall remain in the hand of the government until the point of transfer;
- the management control of operations shall be done by SKK Migas;
- there is a duty to supply domestic needs (DMO);
- capital and risk are borne by the contractor.

The Law of Oil and Gas also regulates about basic provisions that need to be included in the contract, including the term of contract.

The following descriptions illustrate some important rules in the Law of Oil and Gas:

Implementing Regulations for the Law of Oil and Gas

Ring Fencing Principle

Oil and gas upstream industry follows the principle of Ring Fencing (The Regulation of the Minister of Finance No. SE-75/1990), which means that one working area for one business entity or permanent establishment and having one tax identification number. The principle also regulates the procedures of cost recovery stated that cost incurred in one working area is not allowed to be charged to the other working area to relieve the tax from another working area.

Cost Recovery

Cost Recovery is operational cost reimbursement from production results. Operation costs are costs incurred by the contractor in conducting exploration, exploitation and other permitted expenses. Government Regulation Number 79 Year 2010 and the amendment, Government Regulation No. 27 Year

2017, stipulate the requirements of operating costs that can be returned, namely: 1) directly related to the operation of the contractor's working area, 2) using the fair price, 3) the implementation of petroleum operations accordingly with good business practice and engineering principles and 4) operating activities in accordance with the work plan and budget approved by SKK Migas. GR No. 79/2010 and its amendment, GR No. 27/2017 article 13 provides a list of cost recovery that cannot be returned by the government (negative list).

In June 2017, the President of the Republic of Indonesia issued Government Regulation No. 27/2017 on Amendment to Government Regulation Number 79/2010 on Operating Cost that can be Recovered and Treatment for Income Tax in the Upstream Oil and Gas Business Sector, this GR was issued in order to increase the discovery of national oil and gas reserves, drive the investment climate and provide legal certainty to upstream oil and gas business activities. Here are some significant clauses on this revision GR:

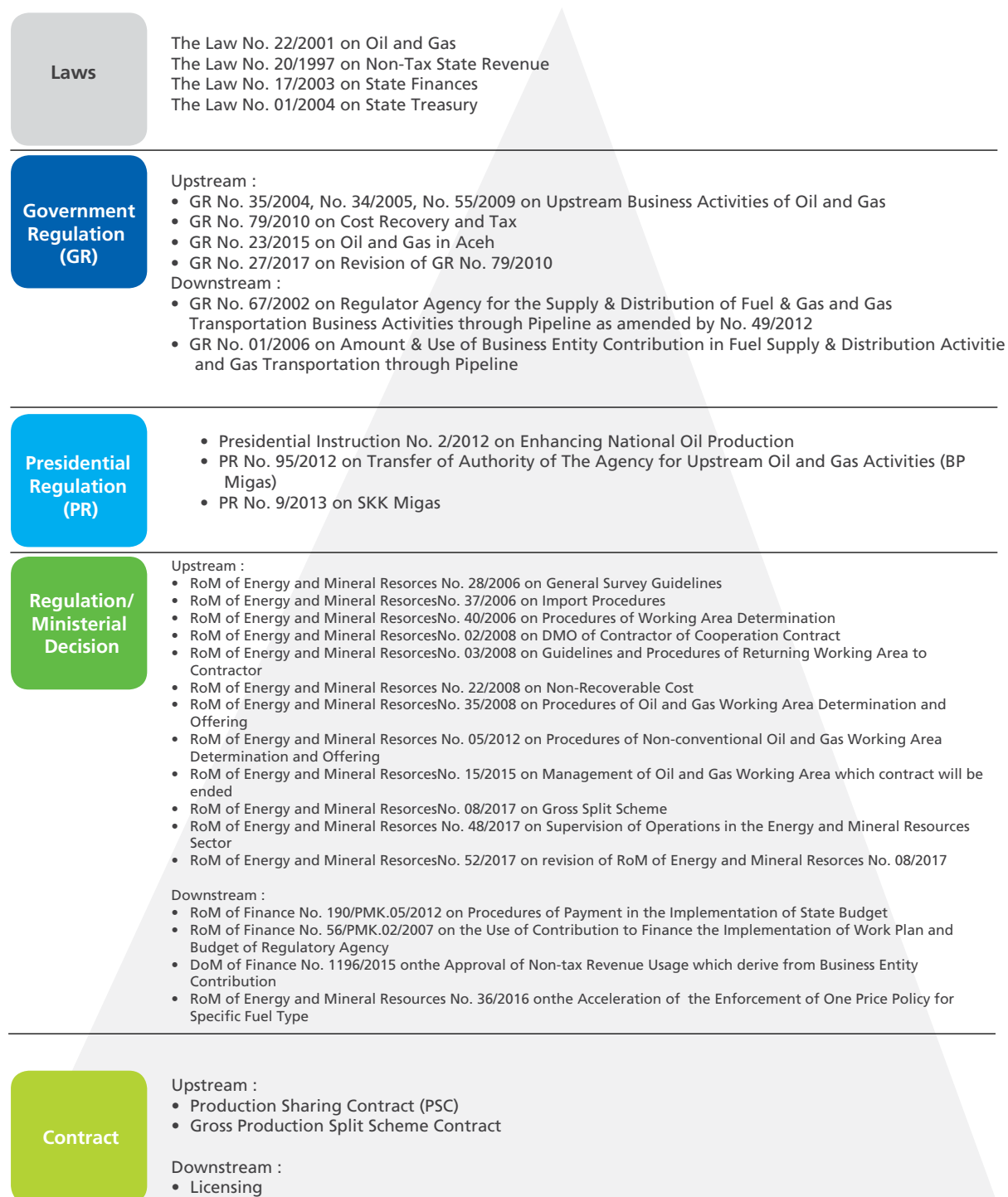
- Article 13 revokes certain non-refundable cost in GR No. 79/2010, such as: environmental development costs during the exploitation period, cost recovery incentives and employee income tax paid as an income tax allowance.
- GR No. 79/2010 article 23 which stated that cost of LNG production process is a refundable cost
- GR No. 27/2017 article 10A introduces dynamic production sharing concept (sliding scale) in Cooperation Contract which established by the Minister of Energy and Mineral Resources and other incentives.

Income Tax and Uniformity Principle

One of the emphasis on the provisions of GR No. 79/2010 is the concept of uniformity principle which is an approach in calculating income tax based on the calculation of income and cost of earnings that follow provisions in the production sharing contract. Hence, the calculation of the contractor's income tax is different from the general income tax calculation. The main differences lie in:

- Recognition of income calculated using Indonesia Crude Price (ICP) and gas contract price;
- The arrangement of the deductible cost in tax is similar to the recoverable cost arrangement under this contract and GR;
- Tax losses from the oil and gas sector may be suspended (carried forward) until the cooperation contract expires, whereas, according to the Tax Law, the tax loss can only be compensated within 5 years;
- The basic calculation of cost recoverable depreciation expenses can be different from the general tax regulation

Figure 5. Oil and gas law hierarchy (upstream to downstream)



Prioritization of Domestic Consumption (Domestic Market Obligation - DMO)

The Contractor shall deliver a certain amount of oil and gas from the Contractor's portion for domestic consumption (DMO) throughout the production period following the provisions of the cooperation contract, generally the maximum DMO to be delivered is 25% of the contractor's lifting. The Government will pay the quantity of DMOs submitted by the contractor based on the price specified in the production sharing contract. Payment Procedures of Domestic Market Obligation Fee, Over Lifting and / or Under Lifting of the Contractor in Upstream Oil and Gas Business Activities are regulated in the Regulation of the Minister of Finance No. 139 / PMK.02 / 2013 dated October 17, 2013 and its amendment, the Regulation of the Minister of Finance No. 230 / PMK.02 / 2015 dated December 18, 2015.

Natural Gas Pricing (The Regulation of the Minister of Energy and Mineral Resources No. 40/2016)

In order to encourage the acceleration of economic growth and enhancement of the competitiveness of national industries, the Government regulates the determination of natural gas prices by considering: i) the ability of domestic consumers to purchase natural gas; ii) domestic and national price of natural gas; iii) economy of the field; and iv) the added value of domestic natural gas utilization. In the event that the price of natural gas is higher than US\$ 6 / MMBTU, the Minister may specify the price of certain natural gas for the fertilizer, petrochemical, oleo chemical, steel, ceramic, glass and rubber gloves industries.

Participation of Regional Owned Enterprises)

GR No. 35/2004 Article 34-35 stated that the contractor is obliged to offer 10% participating interest (PI) to Regional Owned Enterprises where WK is located since first time plan of development (POD) is approved by the Minister of Energy and Mineral Resources (EMR). If interested, Regional Owned Enterprises pay 10% of the investment that has been invested by the contractor within the working area. In the event that a Regional Owned Enterprises is incapable, the contractor shall offer it

to a national company. Terms of 10% Participating Interest Offer in the Working Area of Oil and Gas is stipulated in the Regulation of the Minister of Energy and Mineral Resources Number 37 Year 2016.

Production Sharing Contract (PSC)

PSC is a form of Cooperation Contract in Upstream Business Activities based on the principle of production sharing. This contract is signed by the Government and the Contractor in which the Contractor shall bear the risks and costs of upstream oil and gas business activities. When a commercial reserve is found and can be developed, it will be used to recover the investment spent by the Contractor. The calculation is as follows: the production will be reduced by First Tranche Petroleum (FTP) then the total production after deducting the FTP will be reduced by the recoverable cost consisting of Investment Credit Current Year Operating Cost Depreciation and Unrecovered Cost. The rest will be shared between the Government and the Contractor in accordance with the PSC agreement. Generally the division of the Government and the contractor after tax is 85:15 for petroleum and 70:30 for natural gas.

The production sharing contract system has undergone several changes as The Law of Oil and Gas changes. The main differences between generations are as follows:

- Some PSCs currently have flexibility over percentages for production sharing.
- Current PSCs have also included DMO for natural gas..
- SKK Migas and the Contractor are entitled to FTP amounting to 20% of production..
- The percentage of production sharing in the contract assumes that the Contractor is subject to Tax after the Income Tax amounting to 20% (not deducted from the "Tax Treaty").
- Any change in PSC entity must be approved by SKK Migas directly and indirectly.
- Transfer of participating interest to non-affiliates can be approved if (regulated in the GR No. 79/2010 and revised by GR. No. 27/2017):
 - it has the approval of SKK Migas
 - the Contractor has met its firm commitment (3 years of ownership)

Table 3. Generation of PSC

Generation of PSC	Description
First Generation (1965 – 1975)	Cost recovery is limited to 40% of total revenue; investment credit of 10% for the contractor; DMO of 25% at the price of 0,2 cent US dollar per barrel.
Second Generation (1976 – 1988)	Unlimited cost recovery; investment credit of 25% for the contractor; DMO remains at 25%, however, in the first 5 years are paid according to the prevailing price, then valued at the price of 0,2 cent US dollar per barrel.
Third Generation (1988 – 1994)	There are additional terms regarding FTP (First Tranche Petroleum) or the part of the revenues that need to be set aside before deducting cost recovery and incentives offering for frontier, marginal and deep sea areas. FTP is set at 15 -20 %. This number has also become a limitation for cost recovery that can be paid by the government, which is 50 – 85% of total revenue. Investment credit is set at 17 – 20 % and DMO is set at 25% at the full price for the first 5 years. Then after 5 years, DMO is paid 10% of the normal price.

Generation of PSC	Description
Fourth Generation (1994 - 2008)	To stimulate investment in remote and frontier areas (especially provinces in the eastern region), the Government introduced a 65/15 after-tax proceeds for contract in these areas.
Fifth Generation (2008 - Now)	Production sharing after tax is negotiable; there are several limitation for cost recovery (stated in the list of non-recoverable cost in the RoM of Energy and Mineral Resources No. No. 22/2008 which is revised by GR No. 79/2010 on Cost Recovery and Tax and GR No. 27/2017 on the Revision of GR No. 79/2010); and incentives offering in other areas such as through investment credit.
Sixth Generation (2017 - Now)	The last generation that has just been issued by the Ministry of Energy and Mineral Resources on January 13, 2017 is the RoM of Energy and Mineral Resources No.8/2017 on PSC with Gross Production Split Scheme which is then revised with the RoM of Energy and Mineral Resources No. 52/2017

Source: PWC Oil and Gas Guide 2017

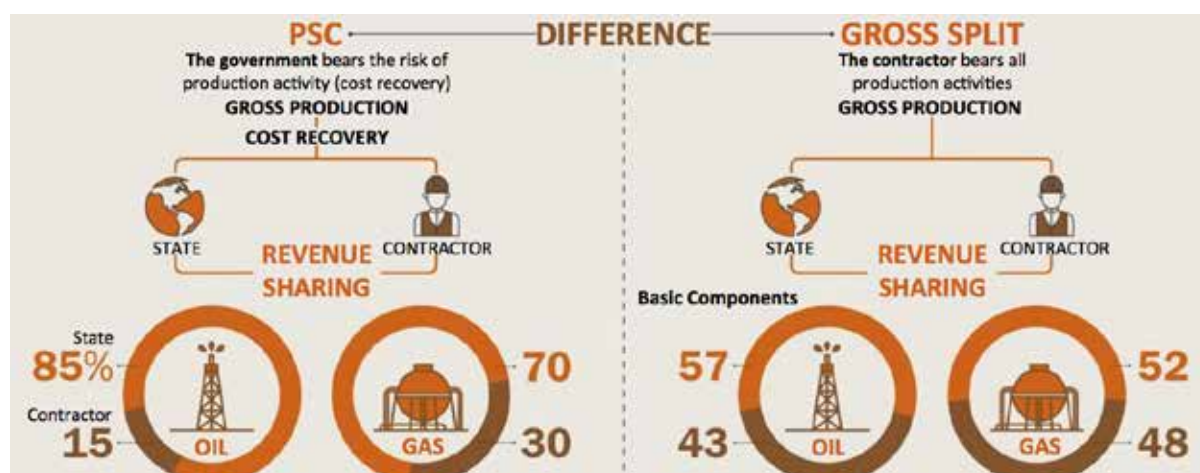
Gross Split Scheme

One of the government's efforts to increase investment in the oil and gas sector and to simplify the calculation of the division between the Contractor and the Government is the issuance of the Regulation of the Minister of Energy and Mineral Resources No. 8/2017 on Gross Split Scheme. The scheme is expected to increase the efficiency and effectiveness of production sharing contracts. This regulation provides incentives for exploration and exploitation activities since the contractor is free to determine the costs incurred. With this scheme, the contractor can focus on cost efficiency and reduce the flow of bureaucracy over the approval process of the costs incurred.

The concept of the gross split scheme is based on the calculation of the gross production without considering the cost recovery mechanism. The main principles to keep in mind are:

- The ownership of natural resources remains in the hands of the State until the point of hydrocarbon transfer
- Control over the operation of upstream oil and gas activities remains in the hands of SKK Migas
- All capital and risks are borne by the contractor
- PSC with a gross split scheme establishes at least 17 regulatory items (including decision making, financing obligations, dispute resolution, etc.)

Figure 6. The difference between PSC and Gross Split Scheme



Source: <http://katadata.co.id/berita/2017/08/31>

The illustration of the gross split mechanism is as follows:

$$\text{Contractor Take} = \text{Base Split} \pm \text{Variable Components} \pm \text{Progressive Components}$$

$$\text{Government Take} = \text{Government Share} + \text{bonuses} + \text{Contractor's Income Tax}$$

The definition of the above formula is explained in the following Table:

Table 4. Gross split mechanism

Article	Definition	Arrangement
Article 5	Base Split	For petroleum, the government is entitled to 57% and the contractor is entitled to 43%. For natural gas, the government is entitled to 52% and the contractor is entitled to 48%.
Article 6	Variable Components	The correction unit can be seen in the Appendix of the Regulation of the Minister of Energy and Mineral Resources No. 8/2017 which is determined based on the following parameters: Working Area status, field location, reservoir depth, availability of supporting infrastructure, reservoir type, CO ₂ content, H ₂ S content, oil density, the level of domestic components during field development and production stages.
Article 6	Progressive Components	The price of petroleum and cumulative production of oil and gas
	Bonus Components	Bonuses consist of : <ul style="list-style-type: none"> • Signature Bonus is a payment from the winner of the working area tender to the government as stated in the PSC before signing the Cooperation Contract. • Production Bonus is a payment in a certain amount from the contractor to the government after reaching a certain amount of cumulative production as regulated in the contract.

Source: The Regulation of the Minister of Energy and Mineral Resources No. 8/2017

In the beginning, the Regulation of the Minister of Energy and Mineral Resources No. 8/2017 received an unfavorable response from oil and gas industry players because it was considered less profitable, especially for marginal wells including old wells located in frontier areas and gas projects⁷. Therefore, in August 2017, the Ministry of Energy and Mineral Resources issued the Regulation of the Minister of Energy and Mineral Resources No. 52/2017 on Revision of the Regulation of the Minister of Energy and Mineral Resources No. 8/2017 which revised several articles in the Regulation of the Minister of Energy and Mineral Resources No. 8/2017 in order to provide incentives for wells that have low economic levels and when oil prices are very low. The revisions are expected to stimulate the investment climate and have a positive impact on state revenues. Here are some key points in the revised gross split rule:

- There are additions of production sharing for the contractor to 6% from the initial of 3% in secondary production stages (reservoir of water/gas injection) and to 10% from the initial of 5% in tertiary production stages that use Enhanced Oil Recovery (EOR).
- An addition of production sharing amounting to 1% up to maximum 5% applicable when a field of oil and gas contains high content of Hydrogen Sulfide (H₂S).

- An addition of production sharing for working area without available supporting infrastructure (new frontier). An addition is amounting to 4% for onshore working area and 2% for offshore working area.
- An addition of production sharing for progressive components, that is gas production. If gas production cumulatively under 30 MMBOE, then the contractor will receive an addition of production sharing amounting to 10%.
- A change in an addition of production sharing for ICP component. An addition of 11,25% will be added when the price is under US\$ 40/barrel.

In terms of taxation, the revisions of the gross split regulation still receive several notes from various parties, especially on taxation certainty, the cost recovery balance of the previous contract and the ownership of the assets by the state while the purchasing process is done by the company⁸. It is expected that the government will issue a technical regulation to regulate some unresolved issues. Section 2.6.2 discusses further on business players comments on the gross split scheme regulation.

⁷ Katadata.co.id. "Sembilan Poin Penting Aturan Gross Split". <http://katadata.co.id/berita/2017/08/31/sembilan-poin-penting-revisi-aturan-gross-splitdiakses-pada-tanggal-1-November-2017>

⁸ Out-Law.com. 2017. "Ammendments to Indonesia's new gross split PSC Regime" <https://www.out-law.com/en/articles/2017/september/amendments-to-indonesias-new-gross-split-psc-regime-a-change-for-the-better-but-some-uncertainties-remain/Diakses-pada-tanggal-1-November-2017>

2.2.2 Legal Framework of Mineral and Coal Mining

The Law of Mineral and Coal Mining

Since 2009, mineral and coal mining activities are regulated by the Law No. 4/2009 (The Law of Mineral and Coal Mining) which replaces the Law No. 11/1967. There are some basic differences between the two laws. Contract-based mining concessions (contract of work/KK, coal-mining business working agreement/ PKP2B and mining authorization/KP) have ceased to exist for new mining projects (after 2009), replaced by a single licensing system. This business license is known as Mining Business License (Izin Usaha Pertambangan/IUP). IUP granting can be done by the central government (represented by the Investment Coordinating Board); ministry of Energy and Mineral Resources and Governor or Regent/Mayor, depends mainly on the coverage of the mining area and other criteria. Special IUP can only be issued by the central government. Since the enactment of the Law No. 23/2014, the Regent / Mayor does not have the authority to issue IUP.

Since it was enacted in 2009, the Law has met many challenges in its implementation. Such as restrictions on foreign ownership, domestic mine processing

obligations and transfer of concessions from KK and PKP2B systems to IUP licensing form.

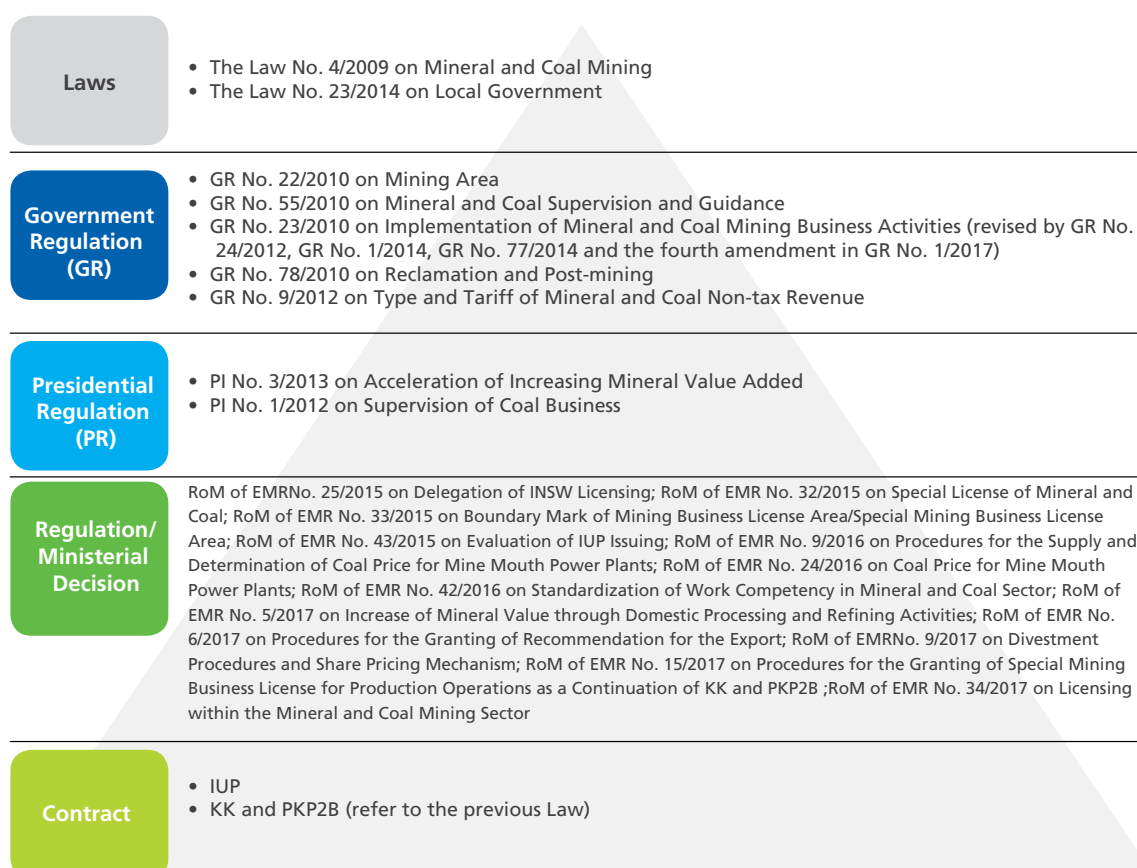
In its implementation, the Law No. 4/2009, has been supported by a number of regulations / implementation guidance in the form of Government Regulation, the Regulation of the Minister of Energy and Mineral Resources, the Regulation of the Minister of Finance and Regulation issued by Director General of Mineral and Coal. Figure 7 shows the hierarchy outline of the Laws and regulations governing the mining sector of minerals.

Implementation Regulation for the Law of Mineral and Coal Mining

Divestment Obligation of Foreign Ownership

GR No. 77/2014 regulates the maximum amount of foreign ownership by the type of license for processing and refining of mining products. The period of IUP divestment that has been in production is done gradually since the end of the fifth year after the production period up to the 10th or the 15th year, depending on the licensing criteria. Based on GR No. 1/2017, all Mining Business License (IUP) and Special Mining Business License (IUPK) of foreign investment after 5 years of production, are obliged to

Figure 7. Legal framework hierarchy of mineral and coal mining



divest their shares gradually, so that in the tenth year the shares are at least 51% owned by the Indonesian side. It is not distinguished whether to refine the mineral by itself or not and not to distinguish the type of IUP stage.

Table 5. Maximum amount of foreign ownership based on the type of license

Type of License	GR No. 77/2014		GR No. 1/2017
	Doing Processing and Refining	Maximum Percentage of Foreign Ownership	Maximum percentage of foreign share ownership
IUP and IUPK of Eksploration	N/A	49%	49%
IUP and IUPK of Production Operation	No	49%	
IUP and IUPK of Production Operation	Yes	60%	
IUP-Production Operation of Underground mining	Yes	70%	

Source: GR No. 77/2014 and GR No. 1/2017

Table 6 is a list of regulations regarding the divestment.

Table 6. List of regulations regarding the divestment in mineral and coal mining

Regulation	Description
GR No. 23/2010	Article 97: the holder of IUP and IUPK, after 5 years of production, must divest its shares up to the minimum 20% owned by Indonesian side.
GR No. 24/2012 (first amendment of GR No. 23/2010).	Article 97: Foreign investment IUP and IUPK, after 5 years of production, must divest its shares gradually per year: 6th year, 20% b. 7th year, 30% c. 8th year, 37% d. 9th year, 44% e. 10th year, 51%
GR No. 1/2014 (second amendment of GR No. 23/2010).	Article 97: No revision
GR No. 77/2014 (third amendmend of GR No. 23/2010)	Article 97: addition: holders of IUP and IUPK of production operation doing processing activities, after 5 years: a. 6th year, 20% b. 10th year, 30% c. 15th year, 40%; Underground mining (and/or open mining) a. 6th year, 20% b. 10th year, 25% c. 15th year, 30%
GR No. 1/2017 (fourth amendment of GR No. 23/2010).	Foreign investment IUP and IUPK, after 5 years of production, must divest its shares gradually so that in the tenth year at least 51% owned by Indonesian side.

Source: GR No. 23/2010, GR No. 24/2012, GR No. 1/2014, GR No. 77/2014 and GR No. 1/2017

Limitation of Export and Enhancement of Value Added

As mandated in the Law No. 4/2009, the company is obliged to undertake the processing and refining of crude minerals in the country in order to increase the value added. This is reinforced through the technical regulations concerning the implementation of minerals business activities and the Regulation of the Minister of Energy and Mineral Resources concerning the increase of value added. The regulation on value added enhancement is intended to raise Indonesia's domestic revenues and protect the sustainability of Indonesia's mineral production, where only high quality minerals can be exported without going through processing and restricting small-scale mines that are generally aimed at obtaining short-term profits.⁹

In January 2017, the Government issued GR No. 1/2017 and RoM of EMR No. 5/2017 (as amended by RoM of EMR No. 28/2017) which provides leeway (to holders of IUP-OP, IUP-OP Processing and Refining) to export raw materials and semi-finished products for the next 5 years period starting from 11 January 2017, subject to export tax payment requirements and new minimum requirements for processing and refining in the country, pursuant to RoM of EMR No. 5/2017 (as amended by RoM of EMR No. 28/2017).

⁹ Sujatmiko (Kementerian ESDM), Indonesia's Effort In Maintaining Sustainable Mineral Development, presentation module of Seventh Multi-year Expert Meeting on Commodities and Development Geneva, 15-16 April 2015, h. 7

Table 7. List of regulations regarding limitation of export and enhancement of value added

Regulation	Description
UU No. 4/2009	Article 103: 1. Holders of IUP and IUPK - Production Operation must do processing and refining domestically. 2. Holders of IUP and IUPK - Production Operation are allowed to process and refine mineral from other IUP and IUPK holders. Article 161: holders of IUP or IUPK - Production Operation that accommodate, utilize, processing and refining, transporting, selling of minerals and coal not from holders of IUP, IUPK or other legal permits shall be punished with imprisonment for a maximum of 10 years and fined Rp 10.000.000.000.
GR No. 1/2014	Article 112C (Supplementary Articles): 1. Holders of KK shall conduct refinery of mine products domestically 2. Holders of IUP - Production Operation shall conduct processing and refining of mine products domestically 3. Holders of K who have refining the mine products, may conduct overseas sales with a certain amount 4. Holders of IUP - Production Operation that has been conducting processing, may conduct overseas sales with a certain amount 5. Further provisions on the implementation and refinement as well as the minimum restrictions on processing and refining is regulated by the Ministerial Regulation
GR No. 1/2017	The provision number 3 is deleted and the provision number 5 is amended in article 112C 3. Holders of KK who have conducted refinement, may sell overseas with a certain amount: REMOVED 5. Further provisions of the implementation of processing and refining, minimum processing and refining and overseas sales by the Ministerial Regulation: AMENDED
RoM of EMR No. 5/2017	Article 17 1. Holders of KK of Metallic Minerals may only sell refined products overseas after fulfilling the minimum refining limits. 2. Holders of KK/IUP - Production Operation for metallic minerals may execute the sale of processing proceedings abroad in a certain quantity for a maximum of 5 years from the enactment of the Regulation of the Minister after making changes to the form of his mining concession into IUPK of Production Operation and pay out taxes in accordance with the provisions of legislation and meet the minimum limit of processing
RoM of EMR No. 6/2017	Article 2: 1. Holders of IUP - Production Operation, IUPK - Production Operation, IUP - Production Operation specifically for processing and / or refining, IUP - Production Operation specifically for transportation and sales and KK may conduct overseas sales: a. Metallic Minerals that have met the minimum requirements of Refinement; and / or b. Non-Metallic or Rocks Minerals that meet the minimum processing limits Article 11: Director General on behalf of the Minister shall supervise: a. implementation of mineral sales overseas; b. progress of domestic refining facilities consisting of: 1. physical progress of the facility; and 2. The amount of construction cost. This RoM is to abolish the RoM No. 5 Year 2016

Source: Law No. 4/2009, GR No. 1/2014, GR No. 1/2017, RoM of EMR No. 5/2017, RoM of EMR No. 6/2017

Prioritization of Domestic Needs (Domestic Market Obligation/DMO)

GR No. 23/2010 Chapter VII sets out the priority of domestic needs for each mineral and coal company, Here the DMO's main provisions in the GR:

- The number of DMOs shall be stipulated by the Minister of EMR, both for the processing industry and for domestic direct use.
- Holders of IUP and IUPK - Production Operations are allowed to export minerals and coal that have been produced after the fulfillment of domestic mineral and coal needs.

Table 8. List of regulations regarding DMO of mineral and coal

Regulation	Description
RoM of EMR No. 34/2009	The Regulation of the Minister of EMR concerning Prioritization of Domestic Mineral and Coal Needs
GR No. 23/2010	Chapter VII, Article 84: Prioritization of domestic needs; Control of mineral and coal production and selling

Source: GR No. 23/2010, the RoM of EMR No. 34/2009

Table 9. List of regulations regarding benchmark of mineral and coal selling price

Regulation	Description
RoM No. 17/2010	Procedures of determining benchmark selling price of mineral and coal
RoM No. 7/2017 (replace RoM No. 17/2010)	Procedures of determining benchmark selling price of metallic mineral and coal
The Regulation of the Director General of Mineral and Coal No.515. K/32/DJB/2011; No. 999.K/30/DJB/2011; No.644.K/DJB/2013	Regulation of determination and adjustment of coal selling price benchmark
The Regulation of the Director General of Mineral and Coal No.480.K/30/DJB/2014	Benchmark price for certain type and use of coal

Source: The Regulation of the Minister of EMR No. 17/2010 and No. 7/2017

Benchmark of Selling Price

The Regulation of the Minister of EMR No. 17/2010 (hereinafter substituted with The Regulation of the Minister of EMR No. 7/2017) regulates the benchmark price of metallic mineral sales every month for holders of IUP - Production Operation and IUPK - Production Operation based on a formula that refers to the market mechanism and / or in accordance with the prevailing market prices in the international market. This price benchmark will be used by the government as the lowest benchmark to calculate the royalties paid to the government. If the selling price is higher than the reference price then the price used is the selling price, and if the selling price is lower than the reference price then the price used is the reference price.

The reference price that is regulated by the Regulation of the Minister of EMR No. 17/2010 is the price of metallic minerals, non-metallic minerals and rocks. Meanwhile, the reference price that is regulated by the Regulation of the Minister of EMR No. 7/2017 (which annuls the Regulation of the Minister of EMR No. 17/2010) is the price of metallic minerals only. Non-metallic minerals and rocks reference prices are still referring to the Regulation of the Minister of EMR No. 17 / 2010.

Reclamation and Post-mining

GR No. 78/2010 regulates reclamation and post-mining activities for holders of IUP-Exploration and IUP- Production Operation (This regulation replaces ESDM Regulation No. 18/2008). Furthermore, the Ministry of Energy and Mineral Resources issues RoM of EMR no. 7/2014 (as the implementing regulation of Government Regulation No. 78/2010) which regulates in more detail the provisions of the reclamation and post-mining preparation plans.

Exploration IUP holders are required to have a reclamation plan in their exploration work plan within their budget, as well as placing a deposit fund in a Government Bank (as a guarantee). Reclamation plans should be prepared before starting exploration activities. At the time of submission of IUP-Production Operation, the applicant must include a reclamation plan during production and post-mining plan at least covering the period of 5 years (or whichever is shorter than the remaining life of the mining permit). The obligation to place reclamation and post-mining guarantee fund does not eliminate the obligations of mining permit holders to realize reclamation and post-mining activities.

Table 10. List of regulations regarding reclamation and post-mining

Regulation	Description
Law No. 4/2009	Article 96: 1c. IUP and IUPK holders are required to carry out the management and monitoring of the mining environment, including reclamation and post-mining activities Article 100: 1. IUP and IUPK holders are required to provide reclamation and post-mining guarantee funds
GR No. 78/2010	Article 2: 1. Holders of IUP and IUPK - Exploration must carry out reclamation 2. Holders of IUP and IUPK - Production Operation shall implement reclamation and post-mining activities Article 7: 1. Reclamation plan shall be prepared for a period of 5 years. 2. the reclamation plan is contained the plan for each year Article 16: 1. The minister, the governor or regent / mayor shall approve the post-mining plan within a period of no later than 60 days from the IUP / IUPK of Production Operation issued
RoM of EMR No. 7/2014	Article 16: 2d. Post-mining plans include post-mining programs, including: 1. reclamation of ex-mining land and outside mine land; 2. social, cultural and economic development; 3. maintenance of reclamation result; and 4. monitoring Article 45: Holders of IUP and IUPK - Production Operations shall be required to conduct post-mining within 30 days after mining, processing and / or refining activities ends in accordance with the approved post-mining plan. Article 66: even when IUP and IUPK of Production Operations expired, does not eliminate the obligations of IUP and IUPK holders

Source: Law No. 4/2009, GR No. 78/2010, RoM of EMR No. 7/2014

Authority of Local Government

The local government has the authority to issue IUP, depending on the scope of its mining business area and criteria. In addition, local governments may issue

local regulations on local taxes and retribution, such as taxes on non-metallic minerals and rocks, taxes on heavy equipment, taxes on groundwater use, taxes on land and building acquisitions, and so on.

Table 11. List of regulations regarding authority of local government in mineral and coal sector

Regulation	Description
Law No. 4/2009	Article 6 concerning the authority of the central government Article 7 concerning the authority of the provincial government Article 8 concerning the authority of the regency / municipal government This Law explains that regency / municipal governments have the authority to grant IUP and people's mining license (IPR)
Law No. 28/2009	Article 60 paragraph 1 The non-metallic and non-rock mineral tax rate (MBLB) shall be set at the maximum of 25%. Paragraph 2, the MBLB rate shall be determined by a local regulation
Law No. 23/2014	Article 14 paragraph 1 The implementation of governmental affairs in the sector of forestry, marine and energy and mineral resources shall be divided between central and provincial government. Annex CC of EMR sector regulates in more detail the distribution of governmental affairs of energy and mineral resources based on sub-affairs: geology, minerals and coal, oil and gas, renewable energy, and electricity. This law explains that the regency / municipal government does not have the authority to grant IUP or IPR, authority is transferred to the provincial government (Governor) with the Regent's recommendation for the issuance of Mining Business License Area (WIUP). On April 7, 2015, the Director General of Mineral and Coal sent Circular No. 04 E / 30 / DJB / 2015 to Governors and Regents / Mayors throughout Indonesia related to the enactment of the Law No. 23/2014 on Local Government, it is mentioned that the supervisory authority will be carried out by the Central Government
Law No. 2/2015 (concerning Government Regulation in Lieu of law No. 2/ 2014)	Partial changes in some articles are deleted
RoM of EMR No. 43/2015 concerning Evaluation of IUP issuance	CHAPTER III: announcement of IUP Clear and Clean status and certification of Clear and Clean Article 21: 1. Governor shall submit the evaluation result to issuance of IUP to Minister since signing of license document from regent / mayor

Source: Law No. 4/2009, Law No. 28/2009, Law No. 23/2014, Law No. 2/2015, RoM of EMR No. 43/2015

2.3 Fiscal Policy on Oil & Gas and Mineral & Coal

2.3.1 Fiscal Policy on Oil and Gas Sector

Tax and Rate Policies on Oil and Gas Mining Sector

The government's revenue from the oil and gas mining industry is in the form of in-kind and cash that will be explained in the following sections. Table 12 summarizes the income tax, land and building tax and VAT policies in the Oil and Gas Mining Industry.

Table 12. Tax policy on oil and gas sector

Type of Tax	Description
Income Tax	The income tax rate follows the applicable tax rate at the time of signing the production sharing contract. GR No. 79/2010 with the implementing regulations of the RoM of Finance No. 70/2015 amending the RoM of Finance No. 79/2012 specifies the calculation of taxable income of the Oil and Gas Industry. Table 13 details the tax rate over time.
Land and Building tax	The land and building tax object of the oil and gas sector is based on the concept of the earth (surface and body of the earth) and / or buildings within the working area or the likes relates to oil and gas mining. The procedure for the imposition of land and building tax of Oil and Gas is regulated in the Regulation of the Directorate General of Taxation No. PER-45 / PJ / 2013 and RoM of Finance No. 267/2014 for PSC which is still in Exploration stage.
VAT	Oil and gas production taken directly from the source is exempt from VAT
Dividend Tax	The existence of dividend tax relief (Branch Profit Tax - BPT) results in a distribution gap between the Contractors and the Government that is different (the Government's share is smaller) from the percentage of production sharing referred to in the production sharing contract. Currently, to close the gap, PSC contract signed after GR No. 79/2010 generally includes a clause to reduce the contractor's share of pre-tax production sharing (stabilization clause) if the contractor receives a dividend tax relief in accordance with an international tax treaty less than 20%. This is to keep the share of the Government after tax revenue by 85% (for oil) and 70% (for gas) or as specified in the production sharing contract.
Indirect tax, such as Land and Building Tax, VAT and Local Tax and Retribution	For the right oil and gas cooperation contract prior to the issuance of GR No. 79/2010, the concept of assume and discharge arranged in Cooperation Contract. In the concept, oil and gas companies are exempted from payment of indirect taxes because it is assumed that oil and gas production shared between the contractor and the government has included the payment of such taxes so that its obligations are imposed on the state oil and gas revenues; For the oil and gas cooperation contract after the issuance of GR No. 79/2010, oil and gas companies are required to pay the indirect tax directly to the state treasury but can regard it as cost recovery. Chapter VA Article 26 A-E in the GR 27/2017, which is the amendment of GR No. 79/2010, regulates about tax facility regarding petroleum operation in the stage of exploration and exploitation where there is an exemption of import duty, VAT (for certain goods/services), Income Tax Article 22 on import goods and reduction of land and building tax.
Import Duty and Import Tax	The contractor shall be exempt from collection of import duty and tax related to import of goods used in petroleum operations in exploration and exploitation activities
Other Taxes	Following the rate based on the tax rules in general

Source: various sources

Table 13 illustrates the income tax rate in accordance with the prevailing tax rate at the time of issuance of the PSC generation.

Table 13. Income tax rate of the company and government share based on the generation of PSC¹⁰

Year of PSC	Income Tax Rate – General	Income Tax Rate - Dividend	Comprehensive Tax Rate	Government Share - before tax (Oil)	Government Share - after tax (Oil)	Government Share - before tax (Gas)	Government Share - after tax (Gas)
Before 1984	45%	20%	56%	65.91%	85%	31.82%	70%
1984-1994	35%	20%	48%	71.15%	85%	42.31%	70%
1995-2007	30%	20%	44%	73.21%	85%	46.43%	70%
2008	30%	20%	44%	55.36%	75%	28.57%	60%
2009	28%	20%	42.4%	37.5%	64%	28.6%	58.86%
2010	25%	20%	40%	40%	64%	31.5%	58.86%
2013	25%	20%	40%	41.70%	65%	33.30%	60%

Source: Modification of PWC Report

The following are the implementing regulations concerning the procedure of tax payment for the oil and gas mining sector.

Regulation of the Minister of Finance No.70/2015 concerning Procedures on Paying and Reporting State Revenue from Upstream Activities of Oil and Gas.

On March 31, 2015, the Minister of Finance issued RoM of Finance No. 70/2015 to change the previous regulation, RoM of Finance No. 79/2012 as the implementing regulation of GR No. 79/2010. RoM of Finance No. 70/2015 regulates the Procedure of Paying and Reporting State Revenue from Upstream Activities of Oil and/or Gas and Income Tax Calculation for the purposes of Payment of Income Tax of Oil and / or Gas in the Form of Volume of Oil and / or Gas. Some important points in RoM of Finance No. 70/2015 are:

- State revenue is formally defined as the Government Share and “Corporate and Branch Profit Tax” is changed to “Corporate and Dividend Tax (C & D Tax).
- The contractor and SKK Migas shall calculate the final lifting which is the right of the state and the right of Contractor from each working area at the end of the year to be settled through over lifting or under lifting mechanism.
- Income Tax for Contractor of Cooperation Contract consists of Monthly C & D Tax and Annual C & D Tax.
- If required, C & D Tax may be paid in-kind based on ICP for oil or weighted average price for gas of the month in which the tax maturity is due.

Based on the provisions of Article 15A and 15B in the RoM of Finance No. 70/2015, the payment of tax in

cash may be made after 3 (three) months since the issuance of this regulation, then the payment of the Income Tax (C & D Tax) previously deposited to the Oil and Gas Account (Directorate General of Budget) is now deposited to account of State Treasury by using the Tax Payment Letter (SSP) which has been stipulated in accordance with the provisions of the Laws and Regulations. This transfer of payment of Income Tax shall come into force since July 2015 which originally to the Directorate General of Budget moves to the Directorate General of Taxation.

Tax payments in the form of “in-kind” regulated by Article 9A, 9B, 9C and 9D in RoM of Finance No. 70), that are a) the payment deadline is the same with cash payment b) Contractor and SKK Migas shall record payment in the form of a hand over official record and signed by both parties, c) The Tax Payment Slip must be completed based on the minutes of delivery of the goods including the date of handover. In the RoM of Finance No. 70/2015 there is an attachment of the Handover Official Record format and a special Tax Payment Slip for C & D Taxes in the form of “in-kind”. Based on information from SKK Migas, in 2015 there is no “in-kind” tax payment transaction.

Implementation Regulation of Land and Building Tax on Oil and Gas Sector

The Regulation of the Minister of Finance No. 76/2013 on the Administration of Land and Building Tax of the Mining Sector for Mining of Petroleum, Natural Gas and Geothermal regulates the following:

- For PSCs signed before GR No. 79/2010, the land and building tax payment process is through the transfer mechanism from the Director General of Budget to the Director General of Taxes.
- For PSC signed after GR No. 79/2010, the transfer mechanism is not enforceable. The contractor

¹⁰ Modification from PWC. Investment and Taxation Guide Oil and Gas Indonesia. 2017. Page 75

must pay the land and building tax and can be included in the cost recovery.

As the arrangement to regulate the land and building tax mechanism for the PSC, the Directorate General of Taxes (DGT) issues SE-46/2013 to provide further clarification on how to fill the Tax Object Notification Form of land and building tax on offshore tax objects. It is explained in the SE-46/2013 that Tax Object Sale Value should only be in areas “exploited” by the Contractor. On December 20, 2013, the DGT published PER-45/2013 on compliance and computation procedures for the PSC. Some of the underlined points are:

- Definition of Offshore Territory: The definition does not refer to the definition of “offshore area” which is debated in SE-46/2013, that is the term “utilization” is meant to reduce the calculation of the Offshore land and building tax.
- Introducing the concept of “zone”: is a zone used for oil and gas activities including the use of areas outside the work area.

On December 31, 2014, the Minister of Finance issued the Regulation of the Minister of Finance No. 267 Year 2014 concerning granting land and building tax incentives for the PSC which is still in exploration stage. Reduction is given to the “sub-surface” component and may increase to 100% of the land and building tax payable on that component. This incentive applies for 2015 onwards where the Contractor can meet the following requirements:

- For PSCs signed after December 20, 2010 (effective date of Government Regulation No. 79/2010)
- Has filed a tax object notification of land and building tax to the DGT
- Provide a recommendation letter from Minister of EMR stipulating that land and building tax object is still in exploration stage.

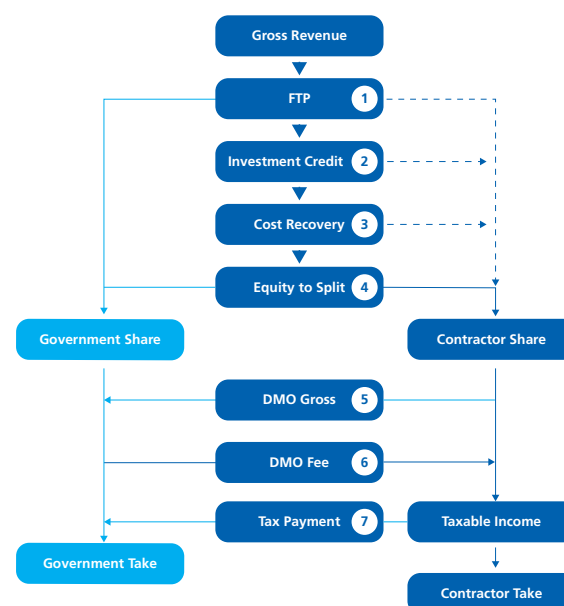
This reduction is awarded every year for a maximum of six years from the signing of the PSC contract and can be extended for up to four years (according to the recommendation letter from the Minister of EMR).

In 2017, the government issues a new regulation to revise Government Regulation No.79/2010. The new regulation, GR No. 27/2017 article 38A letter c, states that “Cooperation Contracts as referred to letter a and letter b may choose to follow the terms of the Cooperation Contract or make an overall adjustments with the provisions of this Government Regulation by adjusting the Cooperation Contract in the longest period 6 (six) months since the enactment

of this Government Regulation. Hence, in case a Cooperation Contract is adjusted to GR No. 27/2017 then the Land and Building Tax to be enacted are:

- Article 26A (4) of GR No. 27/2017: Land and building tax deduction of 100% (one hundred percent) of the land and building tax payable on oil and gas listed in the notification of tax due during the exploration period.
- Article 26B (1) letter d of GR No. 27/2017: During the exploitation, the maximum deduction of land and building tax is 100% of the land and building tax payable on oil and gas listed in the notification of tax due.

Figure 8. Cash flow in production sharing contract



Cash Flow in Production Sharing Contract

Figure 8 illustrates the cash flow of the state revenue calculation applied to the production sharing contract.

1. First Tranche Petroleum (FTP) is a partial allowance of lifting in accordance with the Cooperation Contract before cost recovery. FTP is usually shared between the government and the contractor in accordance with the proportion of production sharing in the Cooperation Contract. However, there are PSCs that have a FTP share only for the government.

2. Investment Credit (KI) is an incentive given by the government as an additional return on capital directly related to oil and gas production facilities. KI is calculated from total lifting after deducting FTP and before CR.
3. Cost Recovery (CR) is a mechanism of operating cost reimbursement by the government to the Cooperation Contract Contractor (KKKS) as stipulated in the Cooperation Contract and in accordance with the prevailing regulations. CR is paid from lifting that is valued by Weighted Average Price (WAP). The CR component consists of unrecovered costs from previous years, current year operating costs and depreciation expenses. GR No. 79/2010 and its amendment, GR No. 27/2017 article 13 regulates the types of non-refundable operating expenses in CR and income taxes.
4. Equity to be Split (ETBS) is the amount of gross lifting that has been reduced by FTP, KI (if any) and CR. ETBS will be shared between the government and the contractor according to the percentage of equity in each PSC
5. Domestic Market Obligation (DMO) Gross is the obligation to deliver contractor's part in the form of oil and / or natural gas to fulfill domestic needs.¹¹
6. DMO Fee is the remuneration paid by the government to the contractor for the delivery of oil and / or natural gas for domestic needs using the price specified in the Cooperation Contract.¹²
7. Income Tax is determined based on the prevailing laws and regulations in the taxation sector at the time the PSC contract is signed

In-kind government revenues in accordance with the production sharing contract scheme are as follows:

- FTP of the government
- Equity Share of the government
- DMO net (DMO gross minus DMO fee paid to the contractor)
- "In-kind" Tax Payments (not yet implemented in 2015)

Government revenue in cash in accordance with the production sharing contract scheme, other than tax revenues are as follows:

- Signature bonuses are imposed on the contractor 30 days after PSC is approved by the Government by the amount in accordance with the terms of the production sharing contract, which is currently ranging from 1 to 41 million US Dollars. Referring to the Regulation of Minister of Energy and Mineral Resources No.30 Year 2017, the amount of signature bonus shall be determined based on the value of the signature bonus contained in the auction result notification issued by the Director General to the Auction Winner or contained in the Ministerial Decision on the determination of the management of the oil and gas Working

Area to be expired, which will be set forth in the Contract Cooperation.

- Production bonus is the amount of money to be paid to the Government if an oil / gas Working Area reaches a certain production or achieves a specified cumulative production in the amount specified in the production sharing contract.
- After the issuance of GR No. 79/2010, state revenue is formally defined as the Government Share and Corporate and Branch Profit Tax

2.3.2 Fiscal Policy on Mineral and Coal Sector

Government revenue from the minerals mining industry is entirely received in cash.

Taxation Policy on Mining Industry

Table 14 summarizes the income tax, land and building tax and VAT in the minerals mining industry

Table 14. Taxation policy on mineral and coal mining industry

Type of Tax	Description
Corporate Income Tax	IUP The income tax rate is 25% of taxable income Reduction by 5% if the company is listed on the stock exchange KK/PPK2B The income tax rate follows the prevailing tax rate at the time of signing the contract
Land and Building Tax	The object of the land and building tax on minerals is the earth and / or buildings within the area used for mineral and coal mining activities. Included in the object of the land and building tax is the earth body in the exploration period. The procedure of imposing land and building tax in mineral and coal mining sector is regulated in the Regulation of the Directorate General of Taxes No. PER-47 / PJ / 2015.
VAT	Mining production is discharged from PPN. Processed material is subject to 10% PPN – the same rate imposed on any other industries.
Other Taxes	Follows applicable tax rate

Source: various sources

¹¹ GR No. 35/2004 on Upstream Oil and Gas Business Activities

¹² RoM of Finance No. 139/2013

Non-Tax Revenue Policy on Mineral and Coal Mining

The Government of Indonesia applies several fees and charges that must be paid by the IUP and contractor holders of KK and PKP2B in the form of:

- landrent,
- exploitation / production charge (royalty),
- sales revenue share (PHT),
- forestry fee
- borrow-to-use forestry permit (IPPKH)

Land Rent

Land rent is fee imposed on IUP area, effective as of the issuance of IUP. Land rent uses US Dollar basis per hectare of exploitation/ exploration area. The amount of rate is differentiated based on phase of operations and permit status (renewed or otherwise), or as stipulated in KK and PKP2B.

$$[\text{Total Area (Hectare) of KP/KK/PPK2B} \times \text{Rate (Rp/USD)}]$$

Land rent for IUP is calculated based on the Government Regulation No. 9/2012 as follows:

Table 15. Rate of land rent

Type of IUP	Unit	Rate
IUP and IUPK – exploration of metallic mineral and coal	Per ha/ year	USD 2.00
IUP and IUPK – production operation	Per ha/ year	USD 4.00
People's Mining License (IPR) of non-metallic mineral and rocks	Per ha/ year	USD 1.00
People's Mining License (IPR) of metallic mineral and coal	Per ha/ year	USD 2.00

Source: GR No. 9/2012

For IUP holders, land rent is paid once every year, at most 30 days since the formal issuance of IUP, or subsequently on the date of IUP issuance. For KK and PKP2B holders, land rent is paid two times every year, on January and July.

Royalty

Royalty or exploitation/production fee is charged on mining commodities of holders of Exploration IUP or Production IUP. This fee applies for each commodity sold (transaction/ shipment). The amount of royalty is calculated using a certain rate multiplied with sales volume and selling price. DG Minerals and Coal determines the selling price.

$$[\text{Volume of Production Sold} \times \text{Percentage of Rate (\%)} \times \text{Selling Price (USD)}]$$

Rate pursuant to GR No. 9/2012

Table 16. Royalty of mineral for KK and IUP

Commodities	Unit	Royalty
Nickel	Per Ton	5% of selling price
Tin	Per Ton	3% of selling price
Copper	Per Ton	4% of selling price
Bauxite	Per Ton	3.75% of selling price
Gold	Per Kilogram	3.75% of selling price
Iron ore	Concentrate	3.75% of selling price
Silver	Per Kilogram	3.25% of selling price

Source: GR No. 9/2012

Table 17. Royalty of coal for PKP2B and IUP

Open Cut Mining Operation

Calories	Unit	Royalty
≤ 5,100	Per Ton	3% of selling price
> 5,100 – 6,100	Per Ton	5% of selling price
> 6,100	Per Ton	7% of selling price

Underground Mining Operation

Calories	Unit	Royalty
≤ 5,100	Per Ton	2% of selling price
> 5,100 – 6,100	Per Ton	4% of selling price
> 6,100	Per Ton	6% of selling price

Source: GR No. 9/2012

In accordance with Circular Letter of the Directorate General of Mineral and Coal No. 04 / E / 84 / DJB / 2013, IUP, KK and PKP2B contract holders shall promptly pay royalty payments to the state treasury in advance, before the mining commodities are shipped or transported according to the mode of transportation accompanied by calculations and supporting data. If the royalty payment is proportional, the royalty redundancy / redemption is paid before the next shipment / transport.

Sales Revenue Share (PHT)

Sales revenue share (PHT) is fee imposed on PKP2B holders. PHT is 13.5% Coal Production Fund Contribution less royalty rate.

The state's share of revenue generated from PKP2B model consists of coal PHT at between 6.5%-8.5% and royalty between 5%-7%, depending on the calorific value of coal. PHT and royalty amount to 13.5%.

Forestry Fee

All companies engaged in the extractive industry sector and operating in forest areas established by the government (based on GR No. 12/2014 and the RoM of Forestry No. P68 / Menhut II / 2014) are required to pay the Forest Resource Rent Provision (PSDH), Reforestation Funds DR) and Stumpage Value Compensation.

IPPKH (Borrow-to-Use Forestry Permit)

Based on GR No. 33/2014, IPPKH rate imposed on mining companies are as follows:

- For open mining, the rate is Rp3,500,000 per hectare multiplied by the land area and the multiplier number, depending on the specification per section of mining area, as well as Rp1,750,000 per hectare for the mine buffer area. IPPKH is paid in the first year and after three years of planting during land reclamation.
- For closed mining, the rate is Rp4,000,000 per hectare multiplied by the size of the land and the multiplier number, depending on the specification per section of mining area, as well as Rp2,000,000 per hectare for the mine buffer area. IPPKH is paid in the first year and after three years of planting during land reclamation.

2.4 Duties and Functions of Relevant Government Agencies in the Extractive Industry

The following section describes government agencies and their duties and functions in the extractive industry:

2.4.1 Ministry of Energy and Mineral Resources

The Ministry of Energy and Mineral Resources has the role of organizing affairs in energy and mineral resources in government to assist the President in organizing state government.

In performing its roles, the Ministry of Energy and Mineral Resources performs the following functions:

1. Formulating and stipulating policies in guiding, controlling and supervising of oil and gas, electricity, minerals and coal, new energy, renewable energy, energy conservation, and geology sectors;
2. Implementing policies in guiding, controlling and supervising of oil and gas, electricity, minerals and coal, new energy, renewable energy, energy conservation, and geology sectors as well as managing Non-Tax State Revenue in the energy and mineral resources sector in accordance with laws and regulations;
3. Implementing technical guidance and supervision of the implementation of policies in guiding, controlling and supervising oil and gas, electricity, minerals and coal, new energy, renewable energy, energy conservation, and geology sectors;
4. Implementing research and development in energy and mineral resources sector;
5. Implementing human resources development in energy and mineral resources sector;
6. Implementing substantive support to all elements of the organization within the Ministry of Energy and Mineral Resources;
7. Guiding and providing administrative support within the Ministry of Energy and Mineral Resources;
8. Managing state properties which are the responsibility of the Ministry of Energy and Mineral Resources; and
9. Supervising the execution of duties within the Ministry of Energy and Mineral Resources.

The Ministry of EMR has four directorates, each focuses on:

- Oil and Gas
- Mineral and Coal
- Electricity
- New, Renewable Energy and Energy Conservation.

Some agencies are also within the organizational structure of the Ministry of Energy and Mineral Resources, namely: Secretariat General, Inspectorate General, Geological Agency, Research Agency and Human Resource Development Agency.

Directorate General of Oil and Gas

The Directorate General of Oil and Gas has the role of formulating and implementing policies and technical standardization in the oil and gas sector.

In performing its duties, the Directorate General of Oil and Gas shall perform the following functions:

1. Formulating policies in oil and gas sector.
2. Implementing policies in oil and gas sector.
3. Preparing norms, standards, procedures and criteria in oil and gas sector.
4. Providing technical guidance and evaluation in oil and gas sector.

5. Implementing administration of the Directorate General of Oil and Gas.

Directorate General of Mineral and Coal

The Directorate General of Mineral and Coal is in charge of formulating and implementing policies and technical standardization in the mineral and coal sector. In addition to formulating policies, the Directorate General of Mineral and Coal is also responsible for:

1. Improving the security of mineral and coal supplies in the country.
2. Encouraging the economy of coal prices for coal energy development.
3. Encouraging the improvement of domestic capability in mineral and coal management.
4. Increasing the value added of minerals.
5. Improving guidance, supervision, management and control of mining activities in an efficient, effective, competitive, sustainable and environmental ways.

Special Unit for Upstream Oil and Gas Business Activities (SKK Migas)

SKK Migas is an institution established by the Government of the Republic of Indonesia through Presidential Regulation (Perpres) No. 9 Year 2013 on the Implementation of Oil and Gas Upstream Activity Management. This institution was formed following Constitutional Court (MK) decree stating that the Regulatory Agency for Upstream Oil and Gas Business Activities (BP Migas) under the Law No. 22/2001 contradicted the 1945 Constitution. The consequence of this decision was the transfer of BPMIGAS' roles and responsibilities to the Government, or the Ministry of EMR in this regard. SKK Migas is intended as a temporary institution until a permanent body is established and is assured by the law, i.e. the new Oil and Gas Law.

SKK Migas is assigned to manage the upstream oil and gas business activities under a Cooperation Contract. The establishment of this institution is purposed that the exploitation of the state's oil and gas natural resources will be able to generate maximum benefits and revenue to the state for the greatest welfare of the people. In performing those roles, SKK Migas performs the following functions:

1. to provide inputs for the consideration of the Minister of EMR at its discretion in preparing and offering the bidding round of Working Areas and Cooperation Contract;
2. to execute Cooperation Contracts;
3. to review and submit the plan of field development to be the first production in a Working Area to Minister of EMR for obtaining approval;
4. to grant approval for development plan other than as referred to in previous point;

5. to grant approval for the work programs and budget;
6. to conduct monitoring and to administer report to Minister of EMR on the performance of the Cooperation Contracts; and
7. to appoint sellers of oil and/or gas of the state entitlement that may generate maximum profits to the state.

Regulatory Agency for Downstream Oil and Gas Business Activities (BPH Migas)

Based on the Law No. 22/2001 Articles 46 and 47, on 30 December 2002 BPH Migas was established to ensure sufficient domestic oil and gas supplies and safe operation activities for refinery, storage, transportation and distribution of oil and gas products (Article 5 paragraph 2 of the Law No. 22 Year 2001). BPH Migas is also responsible for the supervision of the distribution and transportation of fuel through pipelines operated by the company (Business Entity).

BPH Migas organizes and develops several:¹³

- Business licenses in the downstream sector
- Type, standard and quality of fuel
- Utilization of transportation and fuel storage facilities
- Exploitation of gas for domestic needs
- Strategies on crude oil reserves
- National fuel reserves
- Master plan for national gas transmission and industrial network
- Safety, occupational and environmental health and community development
- Price setting, including gas selling price for household and small scale customer
- Utilization of local resources.

Based on Article 23 Paragraph 1 and Article 23 paragraph 2 of the Law No. 22 Year 2001, downstream business activities as referred to in Article 5 number 2 may be executed by the Business Entity after obtaining permission from the Government. The business license required for petroleum business and / or natural gas business activities is distinguished on:

- a. Business License for Processing
- b. Business License for Transportation
- c. Business License for Storage
- d. Business License for Trading

In accordance with Article 23 paragraph 3 of the Law No. 22 / 2001, any business entity may be granted more than one business license as long as it is not contrary to prevailing laws and regulations.

Oil and gas downstream business activities covers:

- Management Business Activities are activities of refining, obtaining parts, enhancing quality,

and enhancing the value added of oil and natural gas for commercial purposes that produces BBM, BBG, holahan, LPG and / or LNG but not including field processing

- Transportation Business Activities are activities of transporting petroleum, natural gas, BBM, BBG, and / or processed products by land, water and / or air including the transportation of natural gas through pipes from one place to another for commercial purposes.
- Storage Business Activities are activities of receiving, collecting, storing and discharging petroleum, BBM, BBG, and / or processed products in the above and / or below ground surface and / or water surface for commercial purposes.
- Commercial Business Activities are activities of purchasing, selling, exporting, importing petroleum, BBM, BBG and / or processed products, including natural gas through pipes.

2.4.2 Ministry of Finance

Policies of the Ministry of Finance have direct implication on the upstream activities of extractive industry, especially in taxation, customs, and excise. In terms of the managing state wealth and Indonesia state budget, the ministry is responsible to manage state revenues from extractive industry, acts on behalf of the government to stipulate investment policy as well as dividend for and from extractive SOEs, and to manage distribution of natural resources-generated state revenues to subnational government.

Directorate General of Taxes (DGT)

Role: Organizing the formulation and implementation of policies in the taxation sector in accordance with laws and regulations.

Functions:

1. Formulating policies in the field of taxation
2. Implementing policies in the field of taxation
3. Preparing norms, standards, procedures and criteria in the field of taxation
4. Providing technical guidance and supervision in the field of taxation
5. Implementing monitoring, evaluation and reporting in the field of taxation
6. Implementing administration of the Directorate General of Taxes; and
7. Implementing other functions provided by the Minister of Finance

Legal basis: Presidential Regulation No. 28 Year 2015 on the Ministry of Finance and RoM of Finance No. 234 / PMK.01 / 2015 on the Organization and Working Procedure of the Ministry of Finance

Directorate General of Budget (DGB)

Role: Organizing the formulation and implementation of policies in the field of budgeting in accordance with laws and regulations.

Functions:

1. Formulating policies in the field of the preparation of the state revenue budget, state spending budget, state financing budget, cost standard and non-tax state revenue;
2. Implementing policies in the field of the preparation of the state revenue budget, state spending budget, state financing budget, cost standard and non-tax state revenue;
3. Preparing norms, standards, procedures, and criteria in the field of the preparation of the state revenue budget, state spending budget, state financing budget, cost standard and non-tax state revenue;
4. Providing technical guidance and supervision in the field of the preparation of the state revenue budget, state spending budget, state financing budget, cost standard and non-tax state revenue;
5. Implementing monitoring, evaluation and reporting in the field of the preparation of the state revenue budget, state spending budget, state financing budget, cost standard and non-tax state revenue;
6. Implementing the administration of the Directorate General of Budget; and
7. Implementing other functions provided by the Minister of Finance.

Legal basis: Presidential Regulation No. 28 Year 2015 on the Ministry of Finance and RoM of Finance No. 234 / PMK.01 / 2015 on the Organization and Working Procedure of the Ministry of Finance

Directorate of Non-Tax State Revenue, Directorate General of Budget (Dit. NTSR – DGB)

Role: Formulating and implementing policies and technical standardization in the field of Non-Tax Revenue (PNBP) and subsidies assigned to the Directorate of Non-Tax State Revenue

Functions:

1. Preparing policy formulation in the field of non-tax state revenue and subsidies assigned to the Directorate of Non-Tax State Revenue;
2. Preparing the implementation of policies in the field of non-tax state revenue and subsidies assigned to the Directorate of Non-Tax State Revenue;
3. Preparing norms, standards, procedures and criteria in the field of non-tax state revenue and subsidies assigned to the Directorate of Non-Tax State Revenue;
4. Providing technical guidance, monitoring and evaluation in the field of non-tax state revenue and subsidies assigned to the Directorate of Non-Tax State Revenue;

5. Conducting policy analysis in the field of non-tax state revenue and subsidies assigned to the Directorate of Non-Tax State Revenue; and
6. Implementing the administration of the Directorate of Non-Tax State Revenue.

Based on RoM of Finance No. 70/2015 regarding oil and gas income tax and land and building tax, part of the functions of Directorate General of Budget have been transferred to Directorate General of Taxes since July 2015.

Directorate General of Fiscal Balance (DGFB)

Role: Organizing the formulation and implementation of policies in the field of allocation and management of balance funds and other transfers to local government, and local taxes and retributions in accordance with laws and regulations.

Functions:

1. Formulating policies in the field of allocation and management of balance funds and other transfers to local government, and local taxes and retributions;
2. Implementing policies in the field of allocation and management of balance funds and other transfers to local government, and local taxes and retributions;
3. Preparing norms, standards, procedures and criteria in the field of allocation and management of balance funds and other transfers to local government, and local taxes and retributions;
4. Providing technical guidance and supervision in the field of allocation and management of balance funds and other transfers to local government, and local taxes and retributions;
5. Implementing monitoring, evaluation and reporting in the field of allocation and management of balance funds and other transfers to local government, and local taxes and retributions;
6. Implementing the administration of the Directorate General of Fiscal Balance; and
7. Implementing other functions provided by the Minister of Finance.

Legal basis: Presidential Regulation No. 28 Year 2015 on the Ministry of Finance and RoM of Finance No. 234 / PMK.01 / 2015 on the Organization and Working Procedure of the Ministry of Finance.

Directorate General of Treasury

Role: Organizing the formulation and implementation of policies in the areas of budget, cash management and investment implementation, the guidance on financial management of the Public Service Agency and financial accounting and reporting of the government in accordance with laws and regulations.

Functions:

1. Formulating policies in the areas of budget, cash management and investment implementation, the guidance on financial management of the Public Service Agency and financial accounting

and reporting of the government in accordance with laws and regulations;

2. Implementing policies in the areas of budget, cash management and investment implementation, the guidance on financial management of the Public Service Agency and financial accounting and reporting of the government in accordance with laws and regulations;
3. Preparing norms, standards, procedures, and criteria in the areas of budget, cash management and investment implementation, the guidance on financial management of the Public Service Agency and financial accounting and reporting of the government in accordance with laws and regulations;
4. Providing technical guidance and supervision in the areas of budget, cash management and investment implementation, the guidance on financial management of the Public Service Agency and financial accounting and reporting of the government in accordance with laws and regulations;
5. Implementing monitoring, evaluation and reporting in the areas of budget, cash management and investment implementation, the guidance on financial management of the Public Service Agency and financial accounting and reporting of the government in accordance with laws and regulations;
6. Implementing the administration of the Directorate General of Treasury; and
7. Implementing other functions provided by the Minister of Finance.

Legal basis: Presidential Regulation No. 28 Year 2015 on the Ministry of Finance and RoM of Finance No. 234 / PMK.01 / 2015 on the Organization and Working Procedure of the Ministry of Finance.

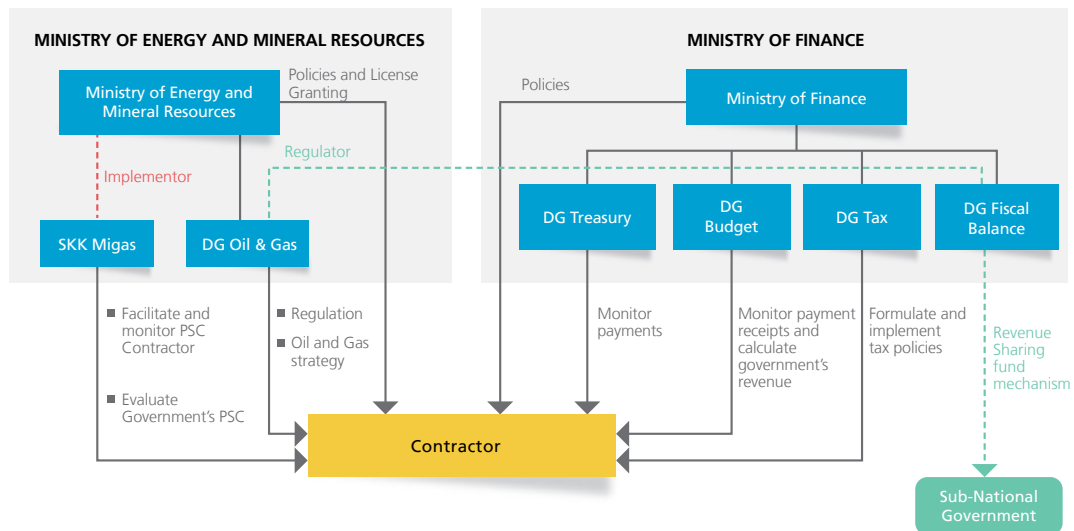
2.4.3 Ministry of Environment and Forestry

With regard to the extractive industry, the Ministry of Environment and Forestry has a role to issue exploitation licenses for extractive activities taking place in forest areas. The Ministry is also responsible to manage and control the utilization of forest in that respect.

2.4.4 Local Government

Based on the Law No. 23/2014, the management of energy and mineral resources is a government affair under the authority of the Central Government and Local Government. The division is based on the principle of accountability, efficiency, and externalities, as well as national strategic interests. The management of energy and natural resources related to oil and natural gas becomes the authority of the Central Government while the management of energy and natural resources associated with minerals and coal becomes the authority of the Central and Local Governments as the implementation of Regional Autonomy.

Figure 9. Roles and responsibilities of government agencies in oil and gas sector



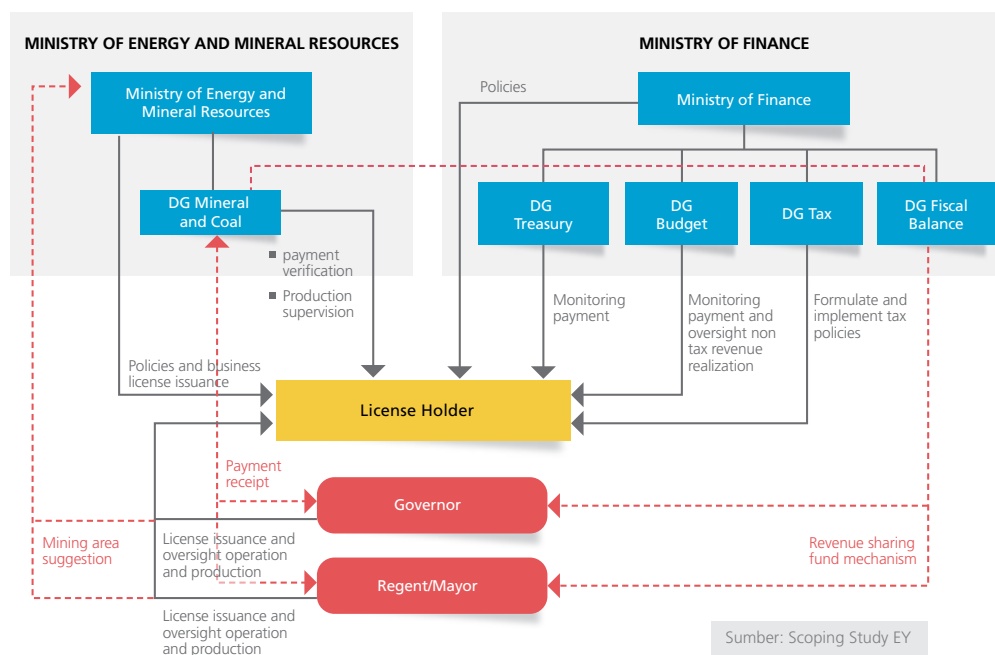
Source: Scoping Study Ernst & Young 2012 - 2013

The Provincial Government has the authority to determine the mining business license area of non-metallic minerals and rocks as well as issue mining business license related to domestic investment in one Provincial Region and sea territory up to 12 miles. In addition, the Provincial Government is authorized to issue a people's mining license, issue a special mining business license - production operation for processing and refining of mining commodities

originating from the same Provincial Region, issue a mining service license and registered certificates as well as determine benchmark price of non-metallic minerals and rocks.

The Local Government also coordinates with the Directorate General of Fiscal Balance for the allocation of percentage share of revenue sharing with the Central Government on revenues from extractive industry in the region, see section 7.2 for

Figure 10. Roles and responsibilities of government agencies in mineral and coal mining sector



Sumber: Scoping Study EY

Source: Scoping Study Ernst & Young 2012 - 2013

further explanation of transfers and payments to local government referring to the Law No. 33/2004.

Figures 9 and 10 illustrate the flow of duties and responsibilities of each agency in the extractive industry.

2.4.5 Laws and Other Regulations related to Extractive Industry

Regulations regarding Contract Disclosure

EITI Standard 2016 Requirement 2.4 requires disclosure of contract contents related to the exploration and exploitation of oil and gas and mineral and coal. Currently oil and gas production sharing contracts (PSCs) and contracts with respect to mineral and coal mining have not been publicly disclosed. Disclosure of the terms of the contract by both the government and the company is still very limited. For example, for a production sharing contract (PSC), disclosure is limited to contract date, contract period, number of firm commitments of the company and general terms of contract. One of the reasons relevant agencies cannot fully disclose the contracts is this information is considered as exempted public information (in accordance with Articles 17 and 11 of the Law No. 14/2008) as it may reveal the natural wealth of the Republic of Indonesia. General provisions of the contracts applicable to the oil and gas mining sector can be accessed at <http://eiti.ekon.go.id/en/draft-kontrak-psc/> and the general provisions of KK and PKP2B can be seen in Appendix 1.

The Law No. 14/2008 on Public Information Transparency generally regulates the obligations of the public agency to provide information to the public, unless such information is an exempted information. Exempted public information should be based on a consequential test conducted by the Information and Documentation Management Officer (PPID) at the relevant public agency. Until now the consequential test of contract disclosure has not been implemented by PPID of EMR (PPID ESDM).

The Information Commission, in accordance with the Law No. 14/2008, is in charge of resolving public information disputes. The case of public information dispute which has been decided by the Information Commission concerning the disclosure of a contract is a dispute between the Foundation of Public Information Development (YP2IP) and PPID ESDM regarding mineral and coal contracts: PT. Freeport Indonesia, PT. Kaltim Prima Coal (KPC) and PT. Newmont Nusa Tenggara (NTT). The Central Information Commission (KIP) in its decision No.197 / VI / KIP-PS-M-A / 2011 decided that copies of the contracts petitioned were open information. As for the oil and gas sector, contract with PT. Chevron Pacific Indonesia is decided as partial open information through the decision of KIP No. 356 / IX / KIP-PS-M-A / 2011.



BP Migas then filed the cancellation of the decision of the KIP in the South Jakarta District Court. This cancellation request is granted and reinforced by the Supreme Court (MA)¹⁴ Decision which rejected the appeal of KIP. One of the considerations of the Supreme Court is that BP Migas is not a public agency as defined in the Law No. 14/2008. As for the mineral and coal case, due to no appeal from EMR after 14 days since the decision, the KIP decision becomes permanent legal force. Therefore, it can be concluded that the copy of oil and gas mining contract has not been open yet. As for the case of mineral and coal mining contract, PPID ESDM has an obligation to comply with KIP decision stating that the copies of the contracts in question are open information.

Based on information from the PPID ESDM¹⁵, the public can make a requesting letter for the opening of a copy of the contract for the mineral and coal upstream contractor. This is done based on compliance with the above KIP decision.

Transparency of Beneficial Owner (BO)

Beneficial owner information is often difficult to obtain due to complex and layered ownership structure. An entity may be owned and controlled by several layers of entities with different names. This matter resulted in the identification of the beneficial owner (BO) of an entity often requiring in-depth knowledge of the business structure and the analysis of large number of corporate documents. Meanwhile, obtaining legal company documentation is not easy. Therefore, government oversight depends on information disclosed by companies or individuals.

14 Supreme Court Ruling No. 15K/Pdt.Sus-KIP/2014

15 EITI Indonesia. 2017. "Rapat Koordinasi Keterbukaan Kontrak Pertambangan". <http://eiti.ekon.go.id/rapat-koordinasi-keterbukaan-informasi-kontrak-pertambangan/> and interview with PPID ESDM. Accessed on 1 November 2017

The BO concept has not been recognized in many laws and regulations in Indonesia including the regulation in the laws and regulations related to the mining sector of oil and gas and mineral and coal. The BO disclosure arrangements are found in the rules below::

Table 18. Regulations related to beneficial ownership

Regulation	Arrangement	Definition of Beneficial Ownership
Circular Letter of DGT No. SE-04/PJ.34/2005. Guidance for determining the criteria of beneficial owner as stated in the double taxation avoidance agreement between Indonesia and other countries	<p>A foreign taxpayer showing a Certificate of Domicile from a country having a Double Taxable Avoidance Agreement (P3B) with Indonesia, may not directly enjoy the rate reduction facility.</p> <p>A domestic taxpayer of a contracting partner country may enjoy a reduction in rates if the Tax Payer is a beneficial owner of the related Dividend, Interest and Royalty.</p>	<ul style="list-style-type: none"> • “Beneficial owner” is an actual owner of the income in the form of dividends, interest and or royalties, both individual taxpayers and corporate taxpayers, who are entitled to directly receive the benefits. • “Special purpose vehicles” in the form of “conduit company”, “paper box company”, “pass-through company” and the like are not included in the above definition of “beneficial owner”.
DJP PER - 10/PJ/2017	<ul style="list-style-type: none"> • Article 2 paragraph 2 (f): the recipient of income is a beneficial owner in the case of requested in the agreement of double tax avoidance. • Article 8 (b): for the foreign taxpayer(WPLN) using a DGT-1 form and WPLN that is required as beneficial owner based on P3B, 	<p>Article 10: WPLN meets the provisions as a Beneficial Owner as referred to in Article 2 paragraph (2) letter f in the case of:</p> <ol style="list-style-type: none"> 1. For individual WPLN, not acting as an Agent or Nominee; or 2. For corporate WPLN, not acting as an Agent, Nominee, or Conduit, must meet the following requirements: <ol style="list-style-type: none"> a. Having control to use or enjoy funds, assets, or rights that generate income from Indonesia; b. No more than 50% of the corporate earnings are used to fulfill obligations to other parties; c. Assuming risks of owned assets, capital, or liabilities; and d. Not having any written or unwritten obligations to forward any or all income received from Indonesia to any other party.
The Law no. 36/2008 article 26 paragraph (1a) on Income Tax	“The domicile country of the foreign taxpayer other than those who conducting business or performing business through a permanent establishment in Indonesia referred to in paragraph (1) is the country or where the foreign taxpayer resides where he or she actually receives benefit from that income (beneficial owner)”	Not explained
Regulation of Bank of Indonesia No. 14/14/PBI/2012 and Regulation of Financial Services Authority No.22/POJK.04/2014.	Banks and financial service providers are required to request customer profile information, including Beneficial Owner identities in order to identify high risk clients including politically exposed person (PEP) for enhancing due diligence periodically.	Beneficial Owner is any individual who owns the funds, who controls the transaction of the Service User, who authorizes the occurrence of a transaction and / or who exercises control through a legal entity or agreement.

Sources: various regulations regarding beneficial ownership

The current BO definition is still highly sectoral and the understanding is diverse. Hence, the implementation is different, as shown in the example of the above mentioned rules. Therefore, it is necessary to have uniformity in understanding of BO in Indonesia. Regarding to this matter, EITI Indonesia has published a roadmap of BO (<http://eiti.ekon.go.id/en/peta-jalan-transparansi-beneficial-ownership-industri-ekstraktif/>). Figure 11 illustrates that the action plan of the BO information transparency is divided into three stages. The first stage is implemented in 2017-2018 which is the determination of the definition of BO and the existence of study or research regarding BO. The second stage is also implemented in the year 2017-2018, that is the development of the institutional framework and law of BO transparency. The third stage to be implemented in 2019 is the implementation of BO in the extractive sector. In this stage, steps will be taken to ensure the accuracy of the data and to develop the system in BO reporting.

On the other hand, currently, the transparency of beneficial ownership is not only the concern of EITI Indonesia. Government agencies are also highlighting this issue because it is closely related to their duties and functions. For example, the Directorate General of Taxes needs to know who is actually the recipient of the income. There are many cases where the one who is recorded in a letter of recognition of the property (nominee) is different from those who receive actual benefits. The Corruption Eradication Commission (KPK) and the Financial Transaction Analysis and Reporting Center (PPATK) want to prevent misuse of corporations such as for money laundering.

In order to have uniformity in BO definition and implementation in national perspective, a legal basis that underlying technical regulations in various sectors is required. The government, led by PPATK together with various ministries, has prepared a draft of BO's Presidential Regulation (PR)¹⁶. The BO's PR draft is in the finalization stage and has been approved by 6 related ministries.

Cadastre Information

EITI Standard 2016 Requirement 2.3 requires EITI implementing countries to provide lists or cadastral information for each license (mining license or contract) related to the company included in the scope of the EITI report, i.e: i. the owner of the license; ii. Coordinate point of the mining area; iii. application date, date of award and duration of license / contract; and iv. types of commodities produced (if it is in production stage).

Ministry of Energy and Mineral Resources has published a web-based information system or called by EMR One Map that capable of displaying various thematic map information of the EMR sector by online (WebGIS). This application could be accessed through this address <http://geoportal.esdm.go.id> which contains following informations:

- Oil and Gas Working Area
- Mining Business License Area
- Geothermal Working Area
- Geothermal Assignment Area
- Upstream Oil and Gas Data
- Location of Rural Electricity Project
- Potential Renewable Energy Resources
- Geological Resources
- Indonesia Forest Area

The application also contains information related to oil and gas, such as: Coordinate Point, Working Area's Name, Operator of Working Area, Status, Type of Contract, Area; and mineral and coal, such as: Coordinate Point, Province, Mine Location, Company Name, Activity Stage, Type of IUP and commodity. However, this application does not contain date of application, date of award and duration of license/contract as required in EITI standard. In order to meet the EITI standard, information on the validity date and termination of PSC and IUP contracts is accommodated in the reporting form submitted by the reporting company accessible at <http://portal-ekstraktif.ekon.go.id/license>. As for the validity date of the entire PSC contracts can be accessed at <http://skkmigas.go.id/>.

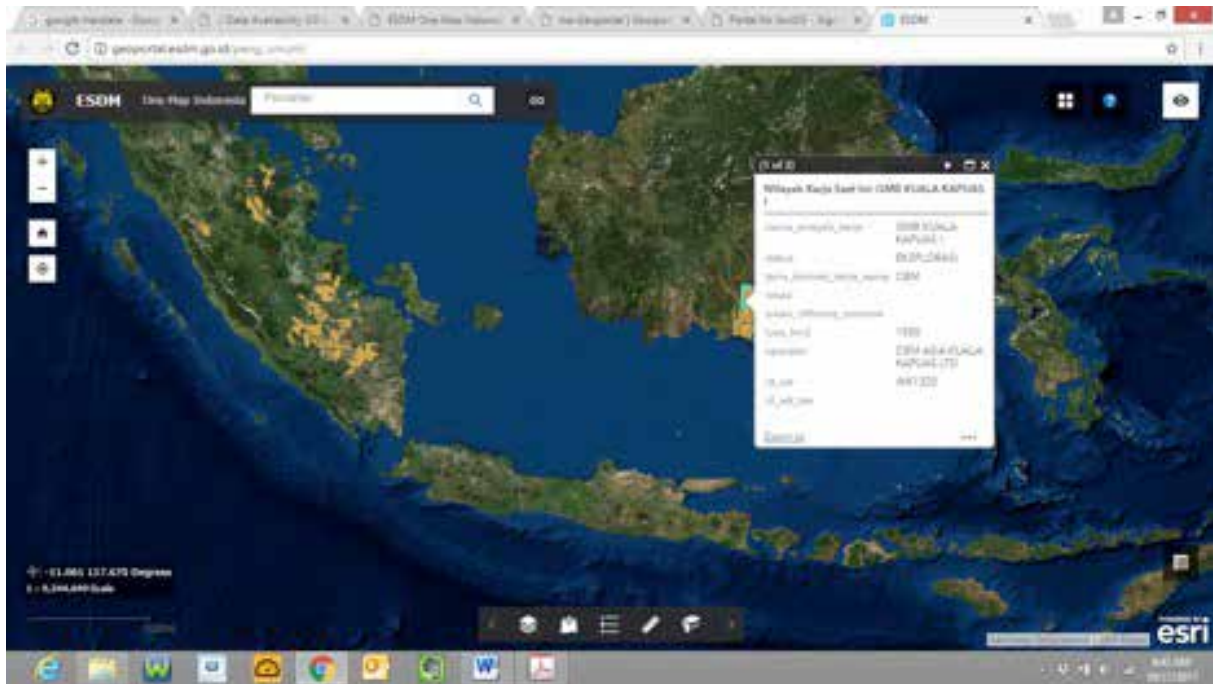
Figure 11. Roadmap of beneficial ownership transparency



Source: A Roadmap of Beneficial Ownership Transparency in The Extractive Industries in Indonesia, Kementerian Koordinator Perekonomian dan EITI Indonesia, 2016

¹⁶ EITI Indonesia. 2017. "Transparansi Beneficial Ownership", <http://eiti.ekon.go.id/transparansi-beneficial-ownership/> accessed on 1 November 2017

Figure 12. One Map Indonesia Display



Source: Geoportal of EMR

National Energy Policy

The national energy supply is dominated by fossil energy, i.e. coal, gas and oil, which is 92% (Chart 1) of the total energy mix in 2015. The dominance of fossil energy threatening national energy resistance and self-sufficiency since the fossil energy source keeps depleting while energy needs continues to increase. In order to meet the national energy needed, Indonesia will depend on import. GR No. 79/2014 on National Energy Policy provides direction of energy management that is expected to solve the problem. This GR requires the diversification of the energy mix by increasing the supply of new energy (EBT) to 23% of the national energy mix in 2025 and 31% of

the national energy mix in 2050. However, the EBT target of the energy mix that increases significantly, based on the base year percentage, does not reduce the use of fossil energy that keeps increasing from year to year.

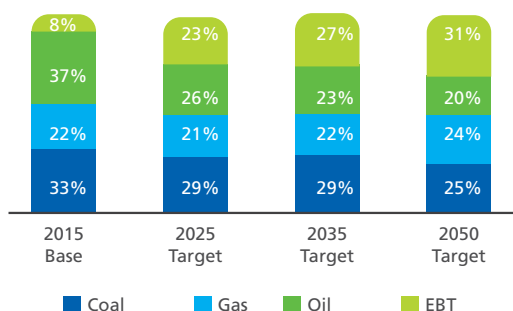
Forestry and Environmental Laws

Forestry

Extractive operations frequently take place in forest area. The legal basis used for the utilization of forest as mining area is the Law No.41/1999 that divides forest utilization into three categories: conservation forest, protected forest, and production forest. This Law stipulates that mining activities can only take place in protected and production forests. However, in protected forest, mining operations are prohibited from carrying out open pit activities.

In order to use forest area, pursuant to GR No.24/2010 a mining company needs to obtain Principle License (IP) before it can acquire Borrow-to-Use License (IPP). IP is valid for two years and can be renewed, while IPP is valid until the end of its determined period or until mining contract terminates. Exploration activities do not require IP and can apply directly for IPP.

Chart 1. Premier Energy Mix



Source: Outlook Energi Indonesia 2016, National Energy Council

Table 19. Permitted mining activities by type of forest

Type of Forest	Mining Activities	Type of License	License Issuer
Conservation Forest	Prohibited		
Protected Forest	Prohibited for open pit mining ¹⁷	Principle License (exploitation phase)	Minister of Forestry
Production Forest	Can be utilized according to license	Borrow-to-Use License (exploration and exploitation phase)	Minister of Forestry and The House of Representative (DPR), if within State Reserve Area (WPN)

Source: GR No. 24/2010

IUPs that are within the conservation forest is about 1.37 million hectares, while IUPs that are within the protected forest area is 4.93 million hectares¹⁸.

License Moratorium on Forest and Peatland Utilization

In 2011, the government enacted license moratorium on forest and peatland utilization by virtue of Presidential Instruction No. 10/2011. The moratorium is extended every two years by virtue of Presidential Instruction No. 6/2013, Presidential Instruction No. 8/2015 and the last one is Presidential Instruction No. 6/2017. However, the moratorium is not applicable for physical activities in the geothermal sector, oil and gas, power and agricultural utilization of rice and sugarcane.

Environment

To prevent adverse impacts of mining activities to the environment, the Government by virtue of Law No. 32/2009 on the environment mandates that all businesses and/or exploitation operations on natural resources to obtain Environmental Impact Assessment document (AMDAL). AMDAL covers Presentation of Environmental Information, Presentation of Environmental Evaluation and Terms of Reference (TOR) to develop Environmental Evaluation Study. Mining companies are also required to acquire environmental permit issued by Minister, or Governor or Regent/ Mayor in accordance with their respective authorities.

Reclamation and Abandonment and Site Restoration Duties

For mining companies, the Law of Mining and GR No.78/2010 are the legal instruments that govern and mandate all IUP holders to submit reclamation and post-mining plans. Following the end of exploitation phase, the mining company must execute the plans. To ensure that reclamation and post-mining plans are implemented, IUP holders must also allocated reclamation and post-mining guarantee reserves.

The main goals of reclamation and post-mining activities are to reorganize, restore and improve the quality of environment and ecosystem in mining areas and their surroundings so that they can regain their functions. The main principles of these activities are protection of surface water quality, groundwater quality, seawater quality, and quality of soil and air in mining areas, which must meet healthy level according to environmental quality standards stipulated by regulations.

For oil and gas companies, Article 36 of GR No.35/2004 regulates the obligation of contractors to set aside fund for upstream activities post-operation. This fund is reserved at the stage of exploration and must be agreed by the contractor and the regulatory body (currently SKK Migas). This obligation is further described in BP Migas Decision Letter Number KEP-0139/BP00000/2010/So concerning Operating Procedure of Abandonment and Site Restoration.

The ASR fund is an amount of money set aside to fund post-operation site restoration. The amount should be deposited by every contractor to an account co-opened by the Special Unit for Upstream Oil and Gas Business Activities (SKK Migas) and the contractor. The requirement to set aside the funding is regulated in a cooperative agreement, pursuant to GR No. 35/2004. Contractors are required to allocate the ASR fund from the exploration stage, strengthened in their work plans and budgets. The funding allocation is agreed upon by each contractor and SKK Migas.

Corporate Social Responsibility (CSR)

Regulations related to corporate social responsibility regarding the extractive industry are described in the Table below:

¹⁷ Presidential Decree No. 41/2004 allowing the 13 mining entities to do open pit mining in protected forest areas

¹⁸ KPK.2017.Presentasi KPK-Korsup Minerba – October 2017

Table 20. CSR-related regulations

Matter	Regulation	Content
Definition of CSR	Law No. 40/2007 on Limited Liability Company article 1	Social and Environmental Responsibility shall be a commitment of Corporation to take parts in sustainable economic development in order to develop life quality and beneficial environment either for a Corporation itself or site community or public.
	Law No. 25/2007 on Investment Chapter of General Provisions article 15 letter b	“Corporate social responsibility” means a responsibility mounted in every investment company to keep creating relationship which is in harmony, in balance and suiTable to the local community’s neighborhood, values, norms, and culture.
CSR-obligated Parties	Law No. 40/2007 on Limited Liability Company article 74 paragraph 1	A Corporation operating business activity in the field and/or related with natural resources shall be obliged to implement social and environmental responsibilities.
	Law No. 25/2007 on Investment article 15 letter b	Every investor shall have obligations: to implement corporate social responsibility
	Law No. 22/2001 on Oil and Gas article 11 paragraph 3 and article 40 paragraph 5	article 11 paragraph 3: The Cooperation Contract as referred to in paragraph (1) shall contain at least the basic provisions, namely: management of the living environment and development of the surrounding local community and guarantee of the community’s customary right; article 40 paragraph 5: The Business Entity or Permanent Establishment conducting Oil and Gas business activities as referred to in Article 5 shall also be responsible for developing the local environment and community.
	Law No. 32/2009 on Environmental Protection and Management article 68	Everybody undertaking business and/or activity shall be obliged to: a. provide information related to environmental protection and management truthfully, transparently and punctually; b. preserve the sustainability of environmental function; and c. abide by the provision on the quality standard of environment and/or standard criteria for environmental damage.
	GR No. 23/2010 on Implementation of Mineral and Coal Mining Business Activities article 106 paragraph (1)	Mining Permit (IUP) holders and Special Mining Permit (IUPK) holders must prepare a development and empowerment program for the communities living around the Mining Permit Areas (WIUP) and Special Mining Permit Areas (WIUPK).
	RoM of SOE No. PER-05/MBU/2007 then modified with RoM of SOE No. PER-08/MBU/2013 article 2 paragraph 1 and 2, last modified with PER-09/MBU/07/2015	1. Perum and Persero are required to implement the Partnership and Environmental Development Program by fulfilling the provisions set forth in this Regulation. 2. The public company can implement the Partnership and Environmental Development Program by referring to this Regulation as stipulated in the decision of the General Meeting of Shareholders (GMS).

Matter	Regulation	Content
The implementation of CSR	Law No. 40/2007 on Limited Liability Company article 74 paragraph 2	Social and environmental responsibilities as referred to in paragraph (1) shall be obligation of Corporation that is budgeted and calculated as expenses of Corporation that its implementation is conducted by considering compliance and regularity.
	GR No. 47/2012 on Social and Environmental Responsibility of Limited Liability Company articles 4 and 6	Article 4 : Social and environmental responsibility is performed by the Board of Directors based on the company's annual work plan after obtaining approval from the Board of Commissioners or General Meeting of Shareholders (GMS) in accordance with the articles of association of the company. The company's annual work plan contains the activities and budget plans required for the implementation of Social and Environmental Responsibility (TJSL). Article 6: The implementation of TJSL is contained in the annual report of the company and reported to the GMS.
	GR No. 23/2010 on Implementation of Mineral and Coal Mining Business Activities article 106 paragraph 4	Community development and empowerment as intended by section (1) shall be prioritized for the communities living around the Mining Business License Areas and Special Mining Business License Areas directly affected by the impact of mining activities.

Source: Various laws and other regulations related to CSR

Provisions on corporate social responsibility are spread across several laws and regulations that sometimes differ from one rule and another. These regulations also have not explained in more detail the obligations of corporate social responsibility, such as the minimum amount to be spent on CSR activities and the forms of mandatory activities. Therefore, the existence of a special law or regulation as the legal basis for regulating corporate social responsibility is indispensable. The law should include definition, parties that are required to implement CSR, form of activity, monitoring, evaluation, rewards and sanctions so that corporate social responsibility can be more measurable and effective.

Public Service

State-owned enterprises as a business entity, whose capital is derived from separated state assets, has an obligation to conduct Public Service Obligation (PSO) as mandated in Law No. 25/2009 on Public Service. The scope of public service referred to Law No. 25/2009 covers the procurement and distribution of public goods and public services as well as administrative services related to strategic sectors, among others is natural resources. In relation to Law No. 25/2009 on Public Service and Law No. 19/2003 on SOEs, PT Pertamina (Persero) as a state-owned enterprise engaged in extractive industry obtain a mandate from the government to perform public service obligations (by conducting subsidized fuel distribution).

2.5 Improving Governance Related to Extractive Industries

2.5.1 Development of Indonesia's Integrated One Stop Service (PTSP)

PTSP is an integrated service in a unified process starting from the application stage until the completion stage of the service product through one door (Article 1 No. 1 of PR No. 97/2014). PTSP aims to: (a) provide protection and legal certainty to the public; (b) shortening the service process; (c) realizing a fast, easy, cheap, transparent, definite and affordable service process; and (d) bring closer and broader service to the community (Article 2 of PR No. 97/2014). The scope of PTSP includes all licensing and non-licensing services which are the authority of the Government and Local Government (Article 4 of PR No. 97/2014).

Presidential Instruction No. 4/2015 on the Implementation of Central PTSP at the Capital Investment Coordinating Board (BKPM) instructs 18 Ministries including the Ministry of Energy and Mineral Resources to: (1) delegate all licensing and non-licensing issuances related to investment to the Head of BKPM; and/or (2) assign officials or employees of the Ministry / Non-Ministry Government Institution to Central PTSP in BKPM, until the realization of integrated investment licensing and non-licensing services by online.

Related to the extractive industry, Minister of EMR has enacted the Regulation No. 25/2015 on the Delegation of Authority to Grant Licensing of Mineral and Coal for Implementation of PTSP to Head of BKPM. The simplification of licensing in mineral and coal sector has been established with the Regulation No. 34/2017 on Licensing in Mineral and Coal Mining Sector. According to the regulation, the simplification is not only through the unification of licenses, reduction of requirements and the abolition of licenses, but also the reduction of time and efficiency of the bureaucratic process. For example, the Special Mining Operation License for Freight and Sales and IUP – Production Operation that previously separated, with the issuance of this Regulation, have become unity and only need the Registration Sign and the issuance is announced through the DG Mineral and Coal website within 8 working days since the application submitted.

Since 2015, the DG Mineral and Coal has assigned 3 Liaison Officers (LOs) to BKPM in the licensing processing mechanism: (1) the Business Entity submits the license file through Mineral and Coal LO; (2) Mineral and Coal LO verifies the completeness of the documents; (3) Mineral and Coal LO submits the licensing documents to the BKPM Monitoring Team; (4) BKPM Monitoring Team and/or Administrator Team of Mineral and Coal (The Administrator Team of Mineral and Coal is established to accelerate the process of delivering documents to and from BKPM) evaluates the documents; and (5) The result of evaluation of licensing documents is validated in BKPM.¹⁹

As for the oil and gas sector, delegation and simplification of licenses have been enacted in the Regulation of the Minister of EMR No. 40/2017 on the Delegation of Authority to Grant Licensing of Oil and Gas Business Activity to the Head of BKPM. This regulation also regulates the simplification of licenses from 104 licenses to 6 licenses, namely 2 upstream oil and gas licenses and 4 downstream oil and gas licenses. The upstream license includes general survey and utilization of oil and gas data licenses. Meanwhile, the downstream license includes the business license of the management, the storage business license, the transportation business license and the trade business license.

Several intensive regulations and deregulations are carried out by the Government of Indonesia in the period of 2015-2017, including the simplification of policies in oil and gas mining and mineral and coal mining sectors. These efforts, at least, have contributed to the upgrade of Indonesia's EODB (Ease of Doing Business) rank, in which ranked 120th in 2015, rising to 106th in 2016 and up again in 2017 to 91st.

2.5.2 Re-Organizing IUP through Clean and Clear Certificate

Since the enactment of Law No. 4/2009, mineral and coal mining in Indonesia enters a new era in the licensing scheme, in which previously under the Contract/ Agreement/ Mining Concession scheme into a scheme of Mining Business License (IUP). This law grants IUP authority to provincial and regency/ city governments²⁰ in the granting of mineral and coal mining licenses. However, as a consequence, a number of problems arise due to the shift from previous mining rules/ regulations/ policies and previous regional autonomy models, particularly in mining licensing governance in Indonesia.

Due to the large number of mining licenses issuance in the period of 2009-2013, the number of mineral and coal mining governance issues in Indonesia are becoming more complex: starting from the inappropriate process of issuing licenses resulting in license overlapping issues and prohibited location (several mining areas are located in conservation and protected forests); weak supervision and implementation of good mining practices resulting in environmental damage; lack of supervision over exploitation-production-shipments (sales)-reclamation and post-mining resulting in the lack of state revenues or even loss in state financial condition (indications of illegal exports), such as PNPB arrears and low mining tax ratio; to the misallocation of reclamation guarantee and post-mining fund.²¹

IUP re-organizing process after the enactment of Law No. 4/2009 is started by temporarily suspending the issuance of new IUP with the issuance of moratorium on the issuance of new IUP regulated by Circular Letter of DG Mineral and Coal dated March 6, 2012 No. 08.E/30/DJB/2012²² concerning Temporary Suspension of new IUP Issuance until the establishment of Mining Area, which is also addressed to Governors and Regents/ Mayors throughout Indonesia. This New IUP Issuance Moratorium is still effective until now.²³

The availability of accurate and valid data is necessary in order to formulate and develop appropriate policies to re-organize thousands of IUPs issued by the Local Governments in the decentralization period. Hence, the Ministry of EMR through Directorate General of Mineral and Coal takes the initiative to hold reconciliation of National IUP data²⁴. The mechanism used in the implementation of reconciliation is verification and

²⁰ Afterwards since Law No. 23/2014, The Regency / Municipal Government has no further authority in the granting of mineral mining licenses.

²¹ PWYP Indonesia and KPK, Coal Licenses Arrangement in Coordination and Supervision of KPK, 2017.

²² Previously the DG Mineral, Coal and Geothermal issued regulations No. 03.E/31/DJB/2009 on the date of 30 Januari 2009 on Mining Licenses before the issuance of Government Regulations as the implementation of Law No. 4/2009 which then came out in 2010, addressed to the Governors and Regents / Mayors throughout Indonesia to temporarily suspend the issuance of new IUP until the issuance of Government Regulation as the implementation of Law No. 4/2009.

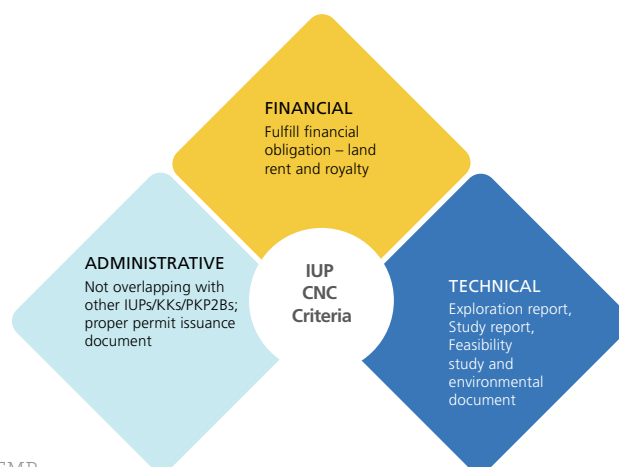
²³ Slide module of Kasubag Penyusunan Peraturan Perundang-Undangan Ditjen Minerba Kemen ESDM, Licensing Reform in the field of Mineral and Coal Mining after the enactment of Law No. 23/2014 – 3 Februari 2016.

²⁴ The legal basis for the implementation of National IUP reconciliation are: (1) Art. 36 Verse 3 and 4, along Art. 38 Verse 1 and Verse 3 Government Regulations (GR) No. 22/2010 on Mining Territory; (2) Art. 102 Verse 2 GR No. 23/2010 on Implementation of Mineral and Coal Mining Business Activities; and (3) Art. 2 Verse 1 and Art. 13 Verse 1 GR No. 55/2010 on Guidance and Supervision of the Mineral and Coal Mining Management.

Slide module of Direktur Pembinaan Program Minerba Kemen ESDM, Socialization and EITI Seminar "Perbaikan Tata Kelola Kegiatan Usaha Pertambangan Minerba" – 25 August 2016.

¹⁹ Slide module Sekretariat Stranas Pencegahan dan Pemberantasan Korupsi Direktorat Hukum dan Regulasi Kementerian PPN/BAPPENAS, Public Discussion Activity on Prevention of Corruption in the Granting of Mining Business Licenses in Indonesia – 9 October 2017.

Figure 13. CNC IUP Criteria



Source: DG Mineral and Coal, MoEMR

classification with status granting of Clean and Clear (CnC) and Non-Clean and Clear (Non CnC) IUPs. The status of CnC is granted if the IUP meets the administrative, technical and financial requirements as illustrated in Figure 13. Prior to 2014, two national IUP reconciliation phases have been implemented. Phase I was held in May-July 2011 and Phase II was held in October-November 2012²⁵.

Two important things in 2014 that have a significant impact on the upgrading of the National IUP are the establishment of KPK's Coordination and Supervision of Mineral and Coal and the enactment of Law No. 23/2014. The establishment of Coordination and Supervision (Corsup) of Mineral and Coal is part of the National Rescue Movement of Natural Resources (GN-PSDA) initiated by the KPK in early 2014. The initial coverage of Corsup is 12 provinces with the largest mining license in Indonesia²⁶. Then 19 other provinces are added²⁷ and the total become 31 + 1 provinces (North Kalimantan Province is the expansion of East Kalimantan Province). The total coverage of Mineral and Coal Corsup reaches 162 mineral and coal producing regencies/cities in Indonesia. There are five main objectives of the Corsup, they are: (1) Implementation of IUP re-organizing; (2) Implementation of financial obligations of mining business players; (3) Implementation of supervision of mining production; (4) Implementation of mine products processing and refining obligations; and (5) Supervision of the implementation of sales and shipments of mining products. Corsup is still ongoing now and as of February 2016, it turns into part of Energy Corsup with wider sector, which includes oil and gas, electricity, as well as renewable energy and energy conservation (EBTKE)²⁸.

After the enactment of Law No. 23/2014, the National IUP Re-organizing continues (especially on adjustment) with some regulations, namely Circular Letter of Minister of Internal Affairs No. 120/253/SJ dated January 16, 2015 and Circular Letter of Minister of Energy and Mineral Resources No. 04.E/30/DJB/2015 dated April 30, 2015 which emphasize that mineral and coal sector is no longer the authority of the Regency/City Government. At the end of 2015, Ministry of EMR stipulates the Regulation No. 43/2015 on Procedures for Evaluating the Issuance of Mineral and Coal Mining Business Licenses. This regulation aims to strengthen the mechanism of evaluation and control of IUP and especially through the mechanism of CnC Audit, including provisions for the Governor in order to accelerate the evaluation process of CnC and submit the result to the Minister within 90 calendar days²⁹.

The process of re-organizing the National IUP, especially the arrangement process, continues until the end of 2017. As of August 2017, there are 9,147 National IUPs with the status of CnC amounted to 6,548 and Non CnC amounted to 2,599³⁰. Public information related to the announcement of National IUP status can be accessed on the pages of the Directorate General of Minerals and Coal Ministry of Energy and Mineral Resources (<https://www.minerba.esdm.go.id/public/38696/pengumuman-cnc/>). As of October 2017, it has published the 26th IUP Reconciliation Announcement.

25 Slide module of Direktur Pembinaan Program Minerba Kemen ESDM, Socialization and EITI Seminar "Perbaikan Tata Kelola Kegiatan Usaha Pertambangan Minerba" – 25 August 2016.

26 Riau Island, Jambi, South Sumatera, Bangka Belitung, East Kalimantan, South Kalimantan, Central Kalimantan, West Kalimantan, Central Sulawesi, Southeast Sulawesi, South Sulawesi and North Maluku.

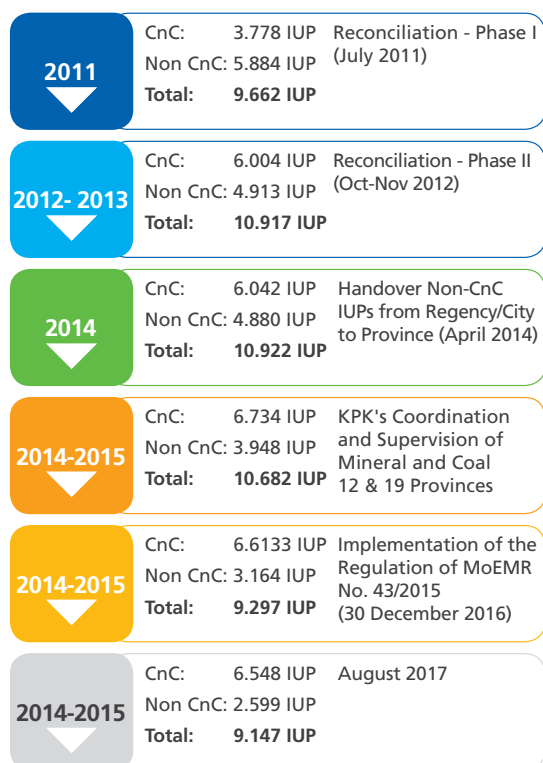
27 Aceh, North Sumatera, Riau, West Sumatera, Bengkulu, Lampung, Banten, West Jawa, Central Jawa, East Jawa, North Sulawesi, West Sulawesi, Gorontalo, East Nusa Tenggara, West Nusa Tenggara, Maluku, Papua and West Papua.

28 PWYP Indonesia and KPK, The Structuring of Coal Permits in Coordination and Supervision KPK, 2017.

29 Slide module Ditjen Minerba Kemen ESDM, Monitoring and Evaluation of Coordination Result and Mining Supervision for North Sulawesi, Gorontalo and West Sulawesi provinces – 10 June 2015.

30 Slide module Korsup Minerba KPK, National Movement – Indonesia's Natural Resources Rescue (GN-PSDA) – 9 October 2017.

Figure 14. Development of National IUP Re-organizing



Source: Performance Report (LAKIN) 2015 & 2016, DG Mineral and Coal MoEMR; Slide Korsup Minerba KPK, Gerakan Nasional - Penyelamatan SDA Indonesia (GNP-SDA) - 9 Oktober 2017(Modified)

2.6 Challenges and Issues Relating to Governance in Extractive Industries

2.6.1 The Declining of Exploration Activities in Indonesia

Oil and Gas Sector

Oil and gas needs and reserves in Indonesia are increasingly unbalanced, growth is increasing, while proven reserves and production continues to decline. Some of the issues and challenges of the Government of Indonesia need to be immediately followed up in order to increase the oil and gas reserves and attract investors to conduct exploration activities in Indonesia.

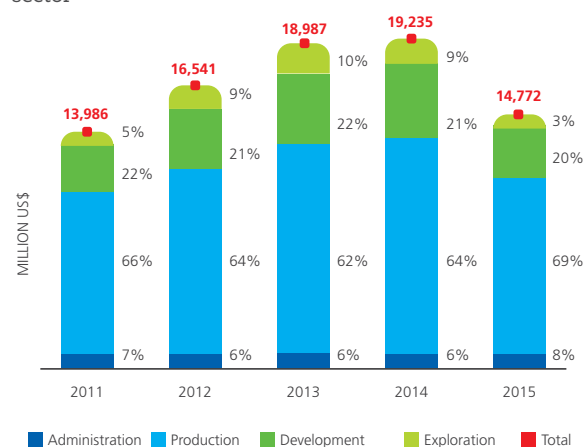
The decreasing value of upstream oil and gas investment and the declining working area of exploration threaten the resilience of Indonesia's oil and gas production. Based on Chart 2, investment in Indonesia's upstream oil and gas sector in 2015 decreased by 23% over the previous year, from US\$ 19.23 billion to US\$ 14.77 billion. Total exploration working area in 2013 reached 238 areas, reduced to 199 areas in 2016 with 37 areas of which are in the process of termination.

There are several factors that influence the decline of investor interest in the oil and gas sector, which are as follows:³¹

- The fall in world oil prices resulting in the declining of income and the money available for investment;
- The cost of exploration in the eastern part of Indonesia, mostly in the deep sea, is expensive; and
- The issue of legal certainty on investment in oil and gas sector in Indonesia, including the Tax Regulation. Since the enactment of GR No. 79/2010, legal regulation in the oil and gas sector, especially in the taxation sector, is not *Lex Specialis* anymore

With the enactment of GR No. 27/2017 that revise GR No. 79/2010 on Cost Recovery and Income Tax Treatment in the Oil and Gas Sector, there are several important points that create more attractive oil and gas investment, such as several elimination and reductions in the oil and gas taxation. However, several things that should be considered are the holders of the PSC need to be careful in calculating the economic implications of adopting the GR No. 27/2017. One of the main concerns of PSC generation before GR No. 27/2017 is the concept of "assume and discharge" since all taxes previously not written in the PSC Contract are now covered in GR No. 27/2017. In order to avoid uncertainty, some regulations issued by the Ministry of Finance/ DG Tax Decision need to be changed to be consistent with the GR No. 27/2017. We shall see and monitor how the impact of the implementation of GR No. 27/2017 if the Contractor of Cooperation Contract chooses to adopt the GR No. 27/2017.³²

Chart 2. Realization of investment in upstream oil and gas sector



Source: SKK Migas Annual Report 2016

31 Katadata.co.id. 2015. "Investasi Migas Indonesia Tak Lagi Menarik". <http://katadata.co.id/opini/2015/05/11/investasi-migas-indonesia-tak-lagi-menarik>. Accessed in 6 November 2017

32 PWC. 2017. "The New GR 79". <https://www.pwc.com/id/en/publications/assets/eumpublications/newsflash/2017/eum-newsflash-2017-62-v1.pdf>. Accessed in 7 November 2017

Currently, oil and gas investors are still waiting for the implementing regulations, especially the special tax laws in the oil and gas sector of regulations concerning the gross split scheme. The government (MoEMR) believes that oil and gas investment in Indonesia is still profitable and the new regulation of the Minister of Finance will stimulate the upstream oil and gas investment.

Mineral and Coal Sector

Indonesia has a high potential of mineral and coal prospects. However, mineral and coal exploration activities and financing, which are the key to the sustainability of the mining industry are almost nonexistent or greatly reduced. The decline in international commodity prices further exacerbated the decline in exploration activities. Indonesian mineral and coal mining companies recorded a large drop in revenues and profits as a result of falling commodity prices and focusing their business activities to raise production and lower operating costs and also to mine on deposits that are more easily mined to lower capital expenditure³³.

Other causes of the absence/lack of mineral exploration activities in Indonesia due to regulatory uncertainties in the mineral and coal mining industry leading to the investment that less attractive in this sector³⁴. According to a survey of Fraser Institute Annual Survey Mining Companies 2016, Indonesia along with the Philippines and Mongolia are the 10 lowest countries based on the Best Practice Mineral Potential Index or the index that encourages investment for exploration³⁵.

Since the enactment of Law No. 4/2009 on Mineral and Coal Mining, the Government of Indonesia has sought to enter into a new direction of mineral and coal mining governance policy that accommodates national interest principles, community benefits, business assurance, decentralized management and good mining practices in order to achieve a sustainable mining. It can be seen from the export ban regulation, the moratorium of new IUP, the IUP reorganizing through CnC mechanism and divestment regulation. These regulations are good for the long-term improvement of mineral and coal mining in Indonesia, for example by adding value added before export and to increase employment. However, in terms of time selection with declining global economic conditions, these regulations reduce the potential of mineral and coal mining³⁶.

In addition, the Government and other parties often questioning the amount of royalty, regardless of the large large amount of corporate spending for taxes and other levies. There are at least 35 items that must be paid by mining companies including taxes, non-taxes, local taxes and retribution and non-tax state revenue (PNBP) collected by other government institutions (approximately 30% of gross revenues³⁷). Moreover, Law No. 4/2009 (Article 129) regulates an additional charges of 10% for IUPK holders, imposed on net income. Hence, mining industry players are concerned about the potential impact of their long-term investment certainty with the provisions established under Law No. 4/2009.

The mining industry is generally a long-term investment and capital-intensive. Mineral deposits are generally located in remote areas with minimal infrastructure, making it very risky in many aspects such as technical, geological, market, fiscal, policy and environmental. With these characteristics, mining investors in general ask for a certainty in regulatory regime to ensure that their long-term investments are guaranteed. Fiscal stimuli, such as VAT exemption during the exploration period, certainty in divestment regulation³⁸ and coordination between central and local governments to reduce taxes and retribution expenses are expected to encourage exploration investment³⁹.

2.6.2 Regulation regarding Gross Split Scheme

The Gross Split scheme is not expected to offer only the efficiency and effectiveness of the upstream oil and gas industry but also to provide attractive incentives for investors. In 2017, contract with the new Gross Split model is implemented on PSC ONWJ, but there are some concerns from industry players in response to this scheme, among others, as follows⁴⁰:

- **Taxation:** The Contractor's share of production for each lifting period will be based only on the pre-tax basis gross split percentage. According to the regulation, it is possible that operational costs can be deducted before calculating the income tax on the Contractor, but lack of detailed explanation.
- **The role of SKK Migas:** SKK Migas continues to play a role in the supervision of the Contractor, and its supervision of Work Program and Budget is limited to guide and monitor the Contractor's commitment to its work program. With the

33 PWC. 2017. Mining Guide 2017. Page 19

34 Idem

35 Fraser Institute. Fraser Institute Annual Survey of Mining Companies 2016. Page 24. Accessible in <https://www.fraserinstitute.org/sites/default/files/survey-of-mining-companies-2016.pdf>

36 Op.cit

37 Industri.bisnis.com. 2015. "Royalti Tambang: Perusahaan Merasa Terbebani Pajak & Pungutan Lainnya". <http://industri.bisnis.com/read/20151203/44/498350/royalti-tambang-perusahaan-merasa-terbebani-pajak-pungutan-lain>. Accessed in 7 November 2017

38 PWC. 2017. "Indonesia Mining Exploration - time for a reset?". <https://www.pwc.com/id/en/media-centre/pwc-in-news/2016/english/indonesian-mining-exploration-time-for-a-reset.html>. Accessed in 7 November 2017

39 Hallatu, Alexander. "Pungutan tambang jadi rebutan pusat dan daerah". <http://perpustakaan.bappenas.go.id/lontar/file?file=digital/blob/F4121/Pungutan%20tambang%20jadi.htm>. Accessed in 7 November 2017

40 Pinsent Masons - Indonesia new Gross Split PSC, Reforminer, Quarterly Energy Notes, April 2017

reduction of control of SKK Migas on the Contractor, it can be interpreted as contradictory to Article 33 (3) of the 1945 Constitution, namely the decreasing of state power over the control of natural resources.

- **Ownership of assets and equipment:** According to the PSC scheme, all land, goods and equipment purchased by the Contractor for upstream business activities are directly owned by the state and managed by SKK Migas. However, in the Gross Split scheme, the Contractor will not receive any Cost Recovery on such expenses as in the old PSC.
- **Contract enforcement:** Regulation of the Minister of EMR No. 8/2017 Article 24 contains an ambiguous provision because it mentions that gross split will be applied to the expired working area and is not renewed, while the extended contract may choose either the previous contract model or the gross split model.
- **Simplification of bureaucracy and administration:** Articles 15 and 16 regulate the role of SKK Migas in approving the work plan and budget proposed by the contractor and approval of the field development work plan (POD). Then Article 23 regulates the role of SKK Migas in the control and supervision. These provisions raise the question of how far the role of SKK Migas in controlling the contractor operational activities consistent with the main purpose of the Gross Split scheme ministerial regulation to achieve efficiency.

2.6.3 Current Status of Revision of Oil and Gas Law and Mining Law

Oil and Gas Law

Background

The initiative of Oil and Gas Law revision began in 2008 through a decision issued by the Special Committee of Inquiry Right on BBM. Furthermore, a number of judicial reviews of the articles of Law No. 22/2001 submitted to the Constitutional Court and there are 3 demands that are granted, further strengthening the importance of the revision of the Oil and Gas Law. Three decisions of the Constitutional Court granted the demands include:

- Constitutional Court (MK) Decision No. 002/PUU-I/2003 which canceled Article 28 paragraph (2) and paragraph (3) regarding the determination of fuel price pursuant to market mechanism, article 12 paragraph (3) regarding the Minister of Energy and Mineral Resources in determining the entity entitled to exploration or exploitation, Article 22 paragraph (1) which requires the business entity to submit a quarter of its production for domestic needs.
- Constitutional Court (MK) Decision No. 20/PPU-V/2007 decides that Article 11 Paragraph (2) of the Oil and Gas Law concerning sufficient notification (without approval) to Parliament

(DPR) is contradictory to the 1945 Constitution article 33. The Constitutional Court believes that the process of cooperation contract agreement should be consulted first with DPR.

- Constitutional Court (MK) Decision No. 36/PUU-X/2012 which disincorporate BP Migas.

Main Issues in Draft of Oil and Gas Law

The completion of Oil and Gas Law revision, which has been going on since 2010 is discussed a lot in the DPR. Some of the changes proposed by the government include: (summary can be accessed at <http://www.dpr.go.id/doksetjen/dokument/minangwan-seminar-Tend-The-Realization-Tata-Management-Migas-National-Sconai-Konstitusi-1435282372.pdf>)

- The ownership of natural resources remains in the hands of the government up to the point of transfer;
- Upstream business activities are implemented based on the upstream business license from the government;
- The establishment of a Special State-Owned Enterprise (SOE) which is a SOE that obtains upstream oil and gas business license through cooperation with other parties and acts as management controller;
- Pertamina's participation as follows:
 - Pertamina is granted an independent oil and gas upstream business license. Other business entity or permanent establishment shall be granted the license through a cooperation contract with Special SOE;
 - Working area offerings are tiered and Pertamina obtains first priority;
 - iThe working area business license is granted to Pertamina for the second time extension of license;
- Establishment/designation of the aggregate enterprise consisting of i) National Oil and BBM Aggregate Enterprise and ii) National Gas Aggregate Enterprise to meet domestic needs;
- All oil and gas production from Pertamina and Special SOE shall be sold to Aggregate Enterprises with the price of economics of field development;
- The business license from the Government valid for 30 years and can be extended for 20 years;
- The exploration period is 10 years.

The DPR has drafted the Oil and Gas Law revision (<http://www.dpr.go.id/doksileg/proses2/RJ2-20150626-022308-2742.pdf>). There are eleven topics proposed in the civil society-based Oil and Gas Revision draft, including: oil and gas management planning, upstream oil and gas institutional model, regulatory body, SOE management, petroleum funds, DMOs, reserve funds, participating interest (PI), protection on impacts of oil and gas activities and reforms information systems and participation.

In addition, academic community from ITS also conveyed its aspirations by drafting an academic draft of oil and gas revision submitted to the government and DPR in November 2016 (<http://www.dpr.go.id/doksileg/proses1/RJ1-20150626-022308-6590.pdf>).

Mineral and Coal Law

Background

The reason of the Government⁴¹ proposed an Amendment to the Mineral and Coal Law is to adjust the authority of mineral and coal mining management related to the issuance of Law No. 23/2014 on Local Government (Local Government Law). Revision of the Mineral and Coal Law is also required to follow up the Constitutional Court Decision related to some parts of the articles contained in the Law which are canceled and considered contradictory to the 1945 Constitution. In addition, the existence of several obstacles in the implementation of the Mineral and Coal Law is also the reason of the government proposed changes to the Law. The revision is aimed at evaluating mineral and coal governance.

Main Issue in Draft of Mineral and Coal Law

According to the draft of Mineral and Coal Law revision⁴², there are some parts that will undergo changes. These changes include additional definitions for some terms related to mineral and coal mining as well as changes in the establishment and determination of Mining Area. The Mineral and Coal Law is also adjusted to the Local Government Law and no longer authorizes the regency/city governments in the management of mineral and coal mining. Management authority by local government will be given fully to the provincial government. Furthermore, the provisions related to the value added and share divestment are also described in more detail in Mineral and Coal Law revision.

Status of Oil and Gas Law and Mineral and Coal Law Revision

The draft of Oil and Gas Law and Mineral and Coal Law revision are still discussed in the Legislation Body (Baleg) of the DPR and will be proposed as priority of national legislation program (Prolegnas Prioritas) 2018.⁴³ The Revision of Oil and Gas Law and Mineral and Coal Law have actually been proposed in the 2010-2014 Prolegnas list and continues to be included in the 2015 - 2019 Prolegnas list. Both revisions have been listed in Prolegnas Prioritas since 2015. However, until the end of 2017 this revision is not yet completed. Meanwhile, oil and gas business players and mineral and coal business players are waiting for the revision as part of legal certainty in business. Therefore, the Government is expected to encourage the continuing completion of the Oil and Gas Law and Mineral and Coal Law revision initiated by the DPR.

2.6.4 The Debate and Progress of Regulation on Increasing Mineral Value Added

Currently, the discussion between the government and business players regarding the domestic processing and refining provisions continues. Some industry players, based on their assessment, consider that the construction of processing and refining facilities (smelters) is not easy because it requires a large amount of investment and uneconomical⁴⁴. In addition, smelter operations are not the core business of mining companies⁴⁴. Meanwhile, on the external side, the decline in global mineral commodity prices in the last 2 years and the weakening of the Rupiah resulted in a decrease in the economic level of a project and lead to delays or even the suspension of smelter projects. The situation has an impact on the uncertainty of lending to the smelter industry due to its worsening level of feasibility⁴⁵. As a result, the number of smelters build is less than the planned number. Only 5 smelters were built in 2015 out of a total of 12 planned smelters, and only 2 smelters built in 2016 out of a total of 4 planned smelters.

The government provides relaxation on a number of pre-determined stipulations related to the activities of increasing mineral value added through the Regulation of the Minister of EMR No. 5/2017 (revoked the Regulation of the Minister of EMR No. 1/2014 and revised again with Regulation of the Minister of EMR No. 28/2017) and 6/2017 (revised by Regulation of the Minister of EMR No. 35/2017). This relaxation aims to provide legal certainty and business certainty, as well as to avoid major job losses and reduced state revenues from the mineral mining sector.

In order to support the regulations, especially to support the downstream program of domestic mineral products, the Minister of Finance issues the regulation No. 13/PMK.010/2017⁴⁶ on Stipulation of Export Goods Subject to Export Duty and Export Duty Tariff. This regulation regulates export duties for metallic mineral processing products, in which the determination of export tariffs is related to phases of physical construction of the smelter, namely: physical construction up to 30% of the total construction shall be subjected to 7.5% tariff; physical construction up to 30-50% subjects to 5% tariff; construction up to 50-75% of total subjects to 2.5% tariff; and construction of above 75% subjects to 0% tariff. As for the export duty tariff of metallic mineral with certain criteria (nickel with <1.7% nickel content and washed bauxite with > 42% washed bauxite content) subject to 10% tariff. The provisions contained in the regulation of the minister of finance are valid until January 11, 2022.

41 Conception Description (Government), official DPR's website, accessible in <http://www.dpr.go.id/prolegnas/deskripsi-konsep2/id/25> on the date of 22 September 2017

42 2016's Bill on Mineral and Coal, accessed in <http://www.hukumonline.com/pusatdata/detail/1t57ode70d125d5/node/481/rancangan-uu-tahun-2016-mineral-dan-batubara> on the date of 28 September 2017

43 Halo Vale. April Edition 2014. Membangun Smelter Tidak Mudah, p. 16

44 GbgIndonesia.com. "Indonesia's Smelting Plans-Moving Slow, but Moving". http://www.gbgindonesia.com/en/energy/article/2016/indonesia_s_smelting_plans_moving_slowly_but_moving_11374.php. Accessed in 1 December 2017

45 DG Mineral and Coal. LAKIN Minerba 2016, p.53-59.

46 RoM of Finance 13/PMK.010/2017 revoking RoM of Finance 140/PMK.010/2016 which revoke RoM of Finance 75/PMK.011/2012 (Have been modified 4 times: RoM of Finance 128/PMK.011/2013; RoM of Finance 6/PMK.011/2014; RoM of Finance 153/PMK.011/2014; and PMK 136/PMK.010/2015).

Figure 15. Value added policy (Regulation of the Minister of EMR No. 5/2017 and No. 6/2017)

OPPORTUNITY OF CONCENTRATE EXPORT	CHANGE FROM KK TO IUPK – PRODUCTION OPERATION	OBLIGATION TO BUILD SMELTER	BENCHMARK PRICE DETERMINATION
<p>Export opportunity of mineral processing products (concentrates), with strict requirements and supervision</p> <ul style="list-style-type: none"> • A period of 5 years • Has/is building a smelter • Paying the out duty • Change from KK to IUPK – Production Operation 	<p>Change from KK to IUPK - Production Operation related to concentrate export</p> <ul style="list-style-type: none"> • Maximum area of IUPK – Production Operation is 25,000 Ha • State revenues in accordance with applicable regulations • Divestment of 51% shares 	<p>Domestic smelter obligation to utilize metallic mineral with certain criteria</p> <ul style="list-style-type: none"> • After fulfilling domestic needs (at least 30% of total smelter capacity), nickel with <1.7% nickel content can be exported • Washed bauxite with $\geq 42\%$ washed bauxite content can be exported • Must build a smelter and pay out duty • To conserve nickel reserves and encourage the construction of low grade nickel and bauxite smelters 	<p>The determination of benchmark prices for the sale of mineral and coal (export and domestic) is conducted by:</p> <ul style="list-style-type: none"> • Minister - for metallic minerals and coal • Governor or Regent/ Mayor - for non-metallic minerals and rocks • Benchmark prices based on market mechanisms or international market prices • Regulation of the Minister of EMR No. 7/2017

Source : DG Mineral and Coal MoEMR Presentation Slide, Kegiatan Coffee Morning Membahas Isu-Isu Strategis dan Peraturan Subsektor Minerba – 2 Februari 2017

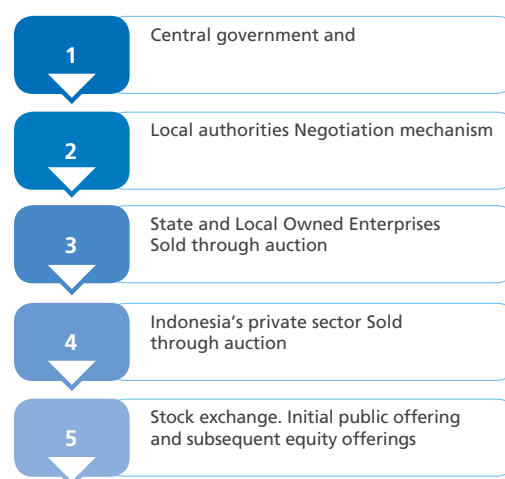
2.6.5 Implementation of Share Divestment Regulations

The obligation of shares divestment for companies holding mining licenses in Indonesia with shares owned by foreign investors is regulated by Article 112 of Law No. 4/2009 along with the implementation regulation of GR No. 1/2017 which regulates the procedures for shares divestment and divestment pricing mechanisms in mineral and coal mining activities and technical regulation of the Regulation of the Minister of EMR No. 09/2017. See Section 2.2.2 on the regulation of share divestment.

The ownership of the divested shares is offered by Foreign IUP-Production Operation and IUPK-Production Operation holders to Indonesian participants through several sequences as follows: (1) Government, through Minister with negotiation mechanism. If the Government is not interested, shares shall be offered to (2) Provincial Government and Regency/City Government in which the location of the mining business area is located, with the negotiation mechanism. Furthermore, if the Provincial Government and Regency/City Government are not interested, shares shall be offered through auction mechanism to (3) SOE and LOE. If the auction is not executed (SOE and LOE are not interested), shares shall be offered to (4) national private companies. If the auction is not executed (national private companies are not interested), then foreign holders of IUP-Production Operation and IUPK-Production Operation can offer the shares through (5) the stock exchange in Indonesia.

If the offering through the stock exchange cannot be executed, the implementation must be accumulated based on the divestment procedure regulated by the Regulation of the Minister of EMR⁴⁷. If the offering of shares up to the level of the stock exchange (Indonesia Stock Exchange) cannot be executed, the foreign holders of IUP-Production Operation and IUPK-Production Operation may repeat the offering process in the following year or register at the Indonesia Stock Exchange⁴⁸.

Figure 16 The offering sequence of foreign mining companies' share



Source: <https://resourcegovernance.org/sites/default/files/documents/memperkuat-kebijakan-divestasi-saham-tambang-di-indonesia.pdf>

47 Art. 4-10 Minister Regulation ESDM No. 09/2017.

48 Manley and Bria. 2017. "Memperkuat kebijakan divestasi saham tambang Indonesia" <https://resourcegovernance.org/sites/default/files/documents/memperkuat-kebijakan-divestasi-saham-tambang-di-indonesia.pdf> accessed in 6 November 2017

CASE EXAMPLE - PT FREEPORT INDONESIA SHARES DIVESTMENT ISSUE

In association with the shares divestment of PT Freeport Indonesia (PTFI), the Indonesian government has announced that the Government and PT Freeport have reached five basic agreements, namely: (1) The legal basis of the relationship between the Government of Indonesia and PTFI is within the framework of the Government of Indonesia granting permission to PTFI (IUPK-Production Operation), not the Contract of Work (KK); (2) PTFI shall conduct shares divestment and 51% of total shares shall owned by Indonesia; (3) PTFI shall build a smelter facility by no later than 2022, unless there is a force majeure condition; (4) Documented fiscal and legal guarantees support will be provided to PTFI for the sake of state revenue stability (Government of Indonesia), whereby aggregate state revenues will be more stable / greater than before (KK relationship); and (5) After PTFI has agreed on these four points as stipulated in IUPK-Production Operation, PTFI will get a maximum extension of 2 x 10 years until 2041.

However, the CEO of Freeport through his letter circulated publicly disagrees with the Government of Indonesia's proposal. In its letter PTFI declares its position in 5 terms, namely (1) Freeport shares divestment process, PTFI proposes that the initial divestment is done through IPO / Initial Public Offerings, then the divestment is done gradually with reference to GR No. 20/1994 on Share Ownership in Companies Established in the Framework of Foreign Investment; (2) the shares divestment calculation, PTFI requires the calculation to use fair market value and use international accounting standards based on the company's operations until 2041 - Freeport believes that it has the right to extend the contract twice until 2041⁵⁴; (3) share transfer mechanism, PTFI requires divestment process to be done by selling shares of parent company and PT Mitra Joint Venture by performing PTFI's desired calculation; (4) the right of the government, PTFI agrees that the Government of Indonesia may request all of its rights in the form of 51% of total production of all areas listed in the IUPK after the divestment process is completed, but PTFI requires the valuation of its shares to be carried at fair value and calculated up to 2041 operations; (5) PTFI will ensure easy access to data for due diligence.

Until now the negotiation between the Government of Indonesia and PT Freeport Indonesia has not reached an agreement regarding the emerged problems. The negotiation deadline initially targeted for completion in October 2017, but it is extended for another three months to January 2018⁵⁵.

The implementation of the agreement of shares divestment between foreign mining companies and the Indonesian government does not always run smoothly (please refer to Case Example Box - PT Freeport Indonesia Shares Divestment Issue).

Price of the shares divested by foreign IUP-Production Operation or IUPK-Production Operation holders to Indonesian participants is determined based on fair market value (FMV) by not taking into account mineral or coal reserves at the time of the divestment offer. This method is often interpreted as a "replacement cost" method⁴⁹.

The method of price determination without taking into account the reserves become a concern of foreign investors because the value obtained may lower than fair market value⁵⁰. Theoretically, the value of shares (FMV) is a reflection of the value that will be obtained by the company from selling future production, minus taxes (which is equivalent to the reserve value minus expenses and taxes). This interpretation is different with the FMV interpretation contained in the Regulation of the Minister of EMR No. 9/2017.

The spirit of nationalizing for the benefit as much as possible for the people of Indonesia needs to be complemented by the business point of the mining corporation that is quite complex and high risk. Investments by investors require certainty and assurance to get enough confidence that the investment will get an adequate return/return rate. Related to debates surrounding the regulation, the government should also consider reviewing the valuing mechanism in the divestment process by involving mineral and coal mining business players. Existing international mine asset valuation rules may be considered for being adopted.

The Government of Indonesia has committed to consistently complete the share divestment process, not only for PTFI, but also for all foreign mining license holders operating in Indonesia in accordance with the rules and regulations set forth under Indonesian law. In this case, the Government of Indonesia is still in progress in completing some technical regulations.

The constructive and sufficiently comprehensive recommendations from Manley and Bria (2017)⁵³ may be considered for the current ongoing foreign share divestment policy in mineral and coal sector. First, the improvement of the divestment pricing mechanism since Article 14 of the Ministerial Regulation No. 09/2017 has the potential to make the investment in

49 Idem. Page 4

50 PWC. 2017. Mining Guide 2017, p. 53

51 Reuters. 2017. "Freeport at loggerheads with Indonesia over divestment". <https://www.reuters.com/article/us-freeport-mcmoran-indonesia/freeport-at-loggerheads-with-indonesia-over-divestment-letter-idUSKCN1C42HJ> accessed in 6 November 2017

52 Katadata. "Diperpanjang 3 Bulan, DPR prediksi negosiasi Freeport tetap buntu". <https://katadata.co.id/berita/2017/10/11/diperpanjang-3-bulan-dpr-prediksi-negosiasi-freeport-tetap-buntu> accessed in 6 November 2017

53 Manley and Bria. 2017. "Memperkuat kebijakan divestasi saham tambang di Indonesia". <https://resourcegovernance.org/sites/default/files/documents/memperkuat-kebijakan-divestasi-saham-tambang-di-indonesia.pdf> accessed in 6 November 2017

the mining sector unattractive to foreign investors. Second, establish a more unambiguous regulation for the mechanism of share divestment negotiation to be conducted between foreign mining license holders and government; provincial government; and regency/city Government, as well as the mechanism of auction for shares divestment between foreign mining license holders and SOE and LOE; and national private companies. Third, establish a regulation for the buyer of the divestment shares through an auction mechanism to the national private companies to disclose publicly the true owner of the company (BO-Beneficial Owner). Fourth, the last option from the sequence of divestment offer is through IPO in Indonesia Stock Exchange. This option is interesting for further intensive review because it is more transparent compared to negotiation and auction mechanisms that have the potential for corruption. Fifth, the government policy to continue encouraging and improving the ability of good corporate governance of SOEs and LOEs as potential shareholders of the shares divestment, especially if SOEs and LOEs are not only act as shareholders but also as the operational controller of foreign mining sector.

2.6.6 Contract Shifting to IUP

Article 169 of Law No. 4/2009 regulates the mechanism of contract shifting to IUP, that are: (A) KKs and PKP2Bs shall remain valid until the termination of the Contract / Agreement; (b) The provisions in the KKs and PKP2Bs shall be adjusted not later than 1 (one) year after Law No. 4/2009 is enacted except for the components of state revenue; and (c) The exception is an effort to increase state revenue.

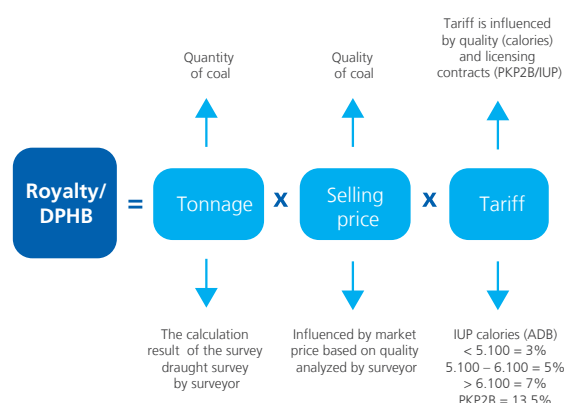
There are four strategic issues that still emerging in the process of amendment (renegotiation) of KK and PKP2B as described in Table 21, which are about: (1) Continuation of mining operations; (2) State revenue; (3) Processing and refining obligations; and (4) Divestment obligation.

Based on Mineral and Coal Achievements Report for the first semester of 2017, 21 KKs and 37 PKP2Bs have signed contract amendments⁵⁴. The amendment of the contract considers state revenue, share divestment, continuation of mining operations and processing and refining obligations.

2.6.7 Accuracy of Reporting and Payment of Mineral and Coal PNB

Based on the Article 9 of Law No. 20/1997, the determination of the amount of PNB is entrusted to the taxpayer concerned for self calculate in order to pay and report the PNB.

Figure 17. Mechanism of coal royalty calculation



Source: Article in Minerba XXIII Edition, December 2015 – Materi Sosialisasi Pengawasan Pembayaran Royalti pada Pengapalan batubara domestik dan ekspor

Self-assessment system allegedly has the potential to reduce PNB of mineral and coal. This is due to the lack of effective control, compliance and auditing, which are important components of the self-assessment system. This allegation is strengthened by the findings of BPK in Semester I – 2016 reported that the self-assessment PNB payment system has not been adequately monitored to ensure the fairness of calculations performed by the company resulted in the loss of potential revenue from the coal sector in 2012-2014⁵⁵.

The following matters, according to the management review of PNB of mineral and coal conducted by KPK, result in inaccuracy of the volume and quality calculation of mineral and coal to be sold by business players as a basis for calculating royalty obligation:

Table 21. Strategic issues in the renegotiation of mineral and coal industry contracts

Strategic Issue	Description
Continuation of mining operations	The continuation of mining operations is proposed 2 years before the end of the contract, in the form of a Special Mining Business License (IUPK) for a period of 2x10 years.
State Revenue	Corporate Income Tax is set in accordance with nail down scheme, while royalty and other taxes are set in accordance with the laws and regulations.
Obligation of processing and refining	The company is obliged to conduct refining in the country
Divestment obligation	Divestment of 51% of total shares (upstream)

Source: DG Mineral and Coal

⁵⁴ KESDM. 2017. "Capaian Sub-Sektor Mineral dan Batubara Semester I/2017" <https://www.esdm.go.id/assets/media/content/content-bahan-paparan-capaian-minerba-semester-i-2017.pdf> accessed in 31 October 2017

⁵⁵ BPK. 2016. Summary of Examination Results Semester I for year 2016, Page xxix

- The government does not re-check the volume and quality calculations of mineral and coal conducted by appointed surveyors;
- Lack of shipping/transportation process supervision of mineral and coal (limited supervision);
- There is a conflict of interest possibility in the implementation of surveyor duties (clause of the Regulation of the Minister of Home Affairs);
- No access to the surveyor reporting system for DG Mineral and Coal;
- The spread of mineral and coal export ports at various points (special ports);
- There is a difference in the Minister of Trade Regulation related to the mineral and coal trading system.

Furthermore, one of the papers in the National Seminar on Technology of Supervision and Monitoring System in Indonesia mentioned about 1) royalty reporting manual system 2) no specific reporting format for royalty payment; 3) no online-based system that can directly show the amount of production from each coal companies that increase the difficulties of controlling and supervising PNBP of mineral and coal.

In order to optimize the revenue from PNBP of mineral and coal (especially the one that relates directly to the completeness and accuracy of payment), the government and related ministries and agencies have undertaken the following measures:

- Improving IT-based reporting and payment system of PNBP (SIMPONI) since 2015;
- Establishing an intensive monitoring program of royalty payment on domestic and export shipments. Among them are by involving independent surveyors appointed by the government to verify the quantity and quality of mining products, prior to shipment, as well as the provision of prepayment, prior to shipment;
- Planning to establish and/or build 14 special mining ports spread across Kalimantan and Sumatra to facilitate monitoring (the Government has included this plan in Prolegnas 2016);
- Establishing KPK-Corsup of Mineral and Coal;
- Implementing reconciliation of production data and sales of coal between the Directorate of Coal Business Development and the Provincial Energy and Mineral Resources Office which aims to collect and verify data on the production and sale of coal companies holding the Mining Business License (IUP) of Production Operation stage under the authority of the local government, reconciliation is conducted 2 times per year;
- Since March 2017, Directorate General of Mineral and Coal together with Commission VII of DPR conduct activities of Integrated Guidance and Supervision (Binwas Terpadu) on mineral

and coal business players. Binwas Terpadu in mineral sector is scheduled to be implemented in 20 provinces, namely: East Java, Central Java, Special Region of Yogyakarta, West Java, Banten, DKI Jakarta, West Nusa Tenggara, South Sulawesi, North Sulawesi, Gorontalo, Papua, Maluku, West Sumatera, North Sumatera, South Sumatera, Riau, Bangka Belitung, South Kalimantan, West Kalimantan and East Kalimantan/North Kalimantan.

Recommendations to optimize the accuracy of PNBP revenues from mineral and coal sector have been disclosed by some parties but some efforts have not been implemented. KPK in its study recommended, among others, the implementation of an integrated data system of mineral and coal trade traffic coordinated between the Ministry of Finance and Ministry of Energy and Mineral Resources⁵⁶. Similar to the study, the World Bank and the Ministry of Finance also recommend the implementation of PNBP payer databases containing various data, making it easier to check the accuracy of the calculation of PNBP⁵⁷.

⁵⁶ KPK. 2013. "Kajian Sistem Pengelolaan Penerimaan Negara Bukan Pajak (PNBP) Mineral dan Batubara", p. 26

⁵⁷ World Bank, Ministry of Finance. 2014. "Meningkatkan Pengelolaan PNBPN dari Pertambangan Indonesia", p. 10

03

LICENSE AND CONTRACT



This section discusses licenses and contracts process in oil and gas mining and mineral and coal mining as well as types of license/contract and tender in 2015.

3.1 Oil and Gas Mining Sector

3.1.1 Applicable Contract Type

Production Sharing Contract (PSC)

The production sharing contract (PSC) system is a common contract in the upstream oil and gas industry, which places the state as the owner and holder of the right to oil and gas resources. In this contract, the provision of in-kind production sharing between the Government of Indonesia and the contractor is stipulated. The Contractor shall bear the risks and costs of exploration and development. Hence, if the

exploration fails to find oil and gas (dry hole), or find oil and gas that is not economical, the contractor shall bear all expenses of the exploration activities.

On the other hand, if the exploration is successful, in-kind production will be shared between the government and the contractor by split arrangement agreed in the Cooperation Contract. Figure 8 illustrates the flow of the PSC cash flow and the description of the PSC's fiscal instruments. Gross revenue which is the volume of oil / gas lifting multiplied by oil price (referring to ICP) / gas price (referring to contract price) and deducted by the First Tranche Petroleum (FTP), investment credit and cost recovery. The remaining (equity to be split) will be shared between the government and the contractor in accordance with the production sharing split in

the PSC. In general, the production sharing between government and contractors after tax is 85:15 for oil and 70:30 for gas (Table 13 illustrates production sharing with different presentations from several generations of PSC). With the obligation of DMO submission, the contractor may get a smaller value than the percentage of production sharing set out in the contract.

Joint Operation Body (JOB)

Several current PSCs have Joint Operation Body contracts (JOB-PSC), i.e. contracts between the government and contractors consisting of Pertamina and other contractors, whereby Pertamina owns 50% of the JOB. At JOB, operations are carried out by a joint operating body consisting of Pertamina representatives and contractor representatives in JOB contracts. Pertamina's representatives and contractor representatives jointly approve the budget and make work plans and regulations / policies. The expired JOB contract will likely be returned to the government, then the government will establish the next operator.

The production sharing contract for oil and gas mining is granted through a tender process or a direct offering in which the winner is determined by the Minister of EMR.

Production Sharing Contract with Gross Split Scheme

The explanation of the production sharing contract system with the gross split scheme has been illustrated in the section 2.2.1 Legal Framework of Oil and Gas Mining.

3.1.2 Establishing Working Area (WA)

Working area proposed by the DG Oil and Gas based on regional geological data study, general survey, market demand, or new discovery, is offered through a bidding round, or, based on a joint study carried out by an investor and the DG Oil and Gas which is directly offered.

Proposed working area should be open areas, defined as:

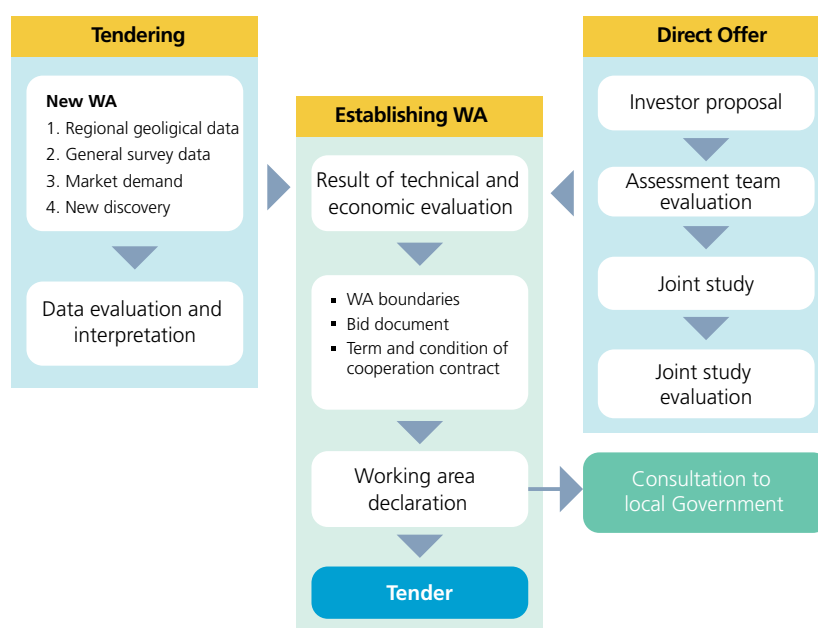
- Areas that have not been established as operating areas
- Part of operations areas set aside according to contract, or set aside based according to contractor's/Minister's proposal
- Working area whose contract is no longer valid

Working area established by the Minister of EMR can be offered through bidding and direct offer.

Bidding

Working area proposed by the DG Oil and Gas is based on regional geological data study, general survey study, market demands, and new discovery. General survey activities as a requirement to complement working area preparation as stipulated in GR No.35/2004 comprise geological survey, physics survey, geophysics survey, and geochemical survey that company can conduct on its own costs and risks, and with permit from the Minister of EMR. Using data interpretation and evaluation result, the DG Oil and Gas prepares block design and delineates boundary of working area.

Figure 18. Flow of oil and gas working area establishment



Direct Offer

Direct offer of WA comes from WA proposals submitted by Business Entity (BE) or Permanent Establishment (PE). An Assessment Team evaluates this proposal using data or supplementary documents such as boundaries of proposed WA, geological potential, reserve projection, production projection, economic feasibility study of WA, and profile of BE and PE. A company is required to present its proposal to the Assessment Team and within 14 days after the presentation, the company must submit commitment for joint study, timeline, and other prerequisites.

If the offer is accepted, the company is required to conduct a joint study and is given 7 months to complete the study, with possible one time extension for 4 months. The company is liable for all costs and risks incurred. Subsequent to the study result, DG Oil and Gas carries out economical and technical feasibility assessment. The DG may, based on assessment result, propose the joint study area as WA. The company must provide joint study bond in the amount of 1 (one) million US Dollar at the latest 14 days after the issuance of WA direct offer approval. The approval is valid for the same length of time as the joint study.

In order to establish a WA, for both direct offer and bidding, DG Oil and Gas is required to submit WA establishment proposal to the Minister of EMR. Together, Minister and the DG consult with local government, and as the last phase the Minister may establish a WA.

3.1.3 Tendering Process of Working Area

The process commences with DG Oil and Gas forming a Bidding Team (for WA offered in bidding) and Assessment Team (for WA offered in direct offer). Both teams will consist of representatives from the Ministry and SKK Migas with technical, economic, and legal competence as well as knowledge in other fields as required. The teams also invite academic experts with corresponding skills and expertise.

The bidding round starts with announced invitation and issuance of bidding documents for each WA tendered by the DG Oil and Gas. Companies that purchase the documents will be noted as candidate bidders. Companies who wish to proceed in the bidding will be required to submit their participation documents at the latest 120 days (for bidding participants) or 45 days (for direct offer participants) since the date of bidding or offer is announced. Bidding/ Assessment Team will conduct technical, financial, and performance evaluation based on the submitted documents.

1. Technical assessment encompasses:
 - Seismic survey commitment consisting of type, crooked lines, survey quantity;
 - Quantity commitment of new field wildcat well as well as plan of drilling location based on geological study, geophysics study, and technical justification;
 - Reasonable and feasible technical proposal for implementation
2. Financial assessment encompasses:
 - Value of signature bonus;
 - Ability to finance work commitment during the first three years of exploration;
 - Budget for firm commitment;
 - Last three years financial statements audited by public auditor;
 - Financial statements of holding company audited by public auditor.
3. Performance assessment encompasses:
 - Experience in oil and gas business; and
 - Compliance with laws and regulations applicable in Indonesia

There are also a number of administrative requirements, namely:

- a. Completed application form;
- b. Company profile;
- c. Last three years financial statements;
- d. Proposed work plan for 6 years of exploration;
- e. Commitment statement to pay bonuses;
- f. Statement affirming consortium establishment agreement and operator appointment;
- g. Statement of commitment and ability to perform contract;
- h. Statement from holding company on new entity to sign PSC;
- i. Copy of incorporation deed;
- j. Support letter from holding company to back the commitments;
- k. Original copy of bid bond;
- l. Statement of compliance with bid announcement;
- m. Receipt of bid document purchase;
- n. Data package license;
- o. Statement of bidder to comply with bid announcement.

Figure 19. Oil and gas working area tendering process



1. WA tendering announced on print and electronic media, or the Ministry of EMR website (www.migas.esdm.go.id or www.wkmigas.com).
2. Tendering document should contain at least: i) bidding guidelines ii) geological information and oil and gas potential iii) reserve and production estimate iv) cooperation contract concept. Interested participants must purchase bid document at DG Oil and Gas.
3. Interested participants must purchase geological and geophysical data of tendered WA from DG Oil and Gas Data Management.
4. Government holds clarification forum to explain tendering process for participants that purchase bid document.
5. Participants must submit participation document within 120 days (bidders) or 45 days (direct offer).
6. Tendering team will make technical evaluation on 3-year firm commitment, financial capacity, and company performance.
7. Minister of EMR awards contract based on recommendation from Tendering Team
8. Contract signing between SKK Migas and contractor

Source: Directorate of Upstream Business Development, Ministry of EMR

Bid participants and winners must submit the following guarantee:

Table 22. Guarantee of oil and gas working area tender

Guarantee (Bank Guarantee)	Amount	Submission Deadline	Period of Guarantee
Bid Bond (Bidding Participants)	100% of signature bonus	Same day with submission of participation documents	6 months
Performance Bond (Awarded Participants)	10% of firm commitment or >USD1,500,000; and b. 10% of the total budget of first 2 years of exploitation, or > USD1,000,000.	Same day with contract signing	3 years 2 years since signing of the contract

Source : Regulation of the Minister of EMR No. 35/2008

The flow process of WA establishment until contract signing is uploaded on Ministry of EMR website. However, the process on the website still refers to Regulation of the Minister of EMR of 2006, while by virtue of Regulation of the Minister of EMR No. 35/2008 has updated the procedure to establish and offer oil and gas working area.

In April 2017, the Ministry of EMR issued the Regulation No. 30/2017 concerning Procedures for the Imposition, Collection, and Payment / Deposit of Non-Tax State Revenues (PNBP) that is applicable to the Directorate General of Oil and Gas. The types of PNBP that is applicable to the Directorate General of Oil and Gas include:

- a. Information service regarding potential auction of oil and gas working area (Bid Document);
- b. Signature Bonus which is the obligation of the Contractor;
- c. Financial obligations on termination of Cooperation Contracts (Terminations) that have not fulfilled the firm commitments of Exploration.

PNBP is deposited to the State Treasury through Online Non-Tax State Revenue Information System abbreviated as SIMPONI. The information system is managed by Directorate General of Budget and covering PNBP Planning System, Billing System and PNBP Reporting system.

3.1.4 WA Tendered in 2015

One of the measures that the government takes to increase reserves and production of oil and gas other than accelerating exploration activities from existing contracts is by developing new contracts.

WA Offering in 2015

In 2015 the Government of Indonesia offers WA through Direct Proposal and through Tender. Please refer to <http://www.wkmigas.com/uncategorized/indonesia-conventional-oil-and-gas-bidding-round-year-2015/>.

Offered through direct proposal:

- South Bengara
- West Berau

Offered through regular tender:

- Rupert Labuhan
- Nibung
- West Asri
- Oti
- Manakarra Mamuju
- Kasuri II

Of all the WA offered, there are 7 companies that buy Bid Document and there are 2 companies that register. However, in 2015, no company wins over the WA tender. Detail of WA offerings in 2015 can be seen in Table 5.

Table 23. Oil and gas working area offered in 2015

No	Name of WA	Name of Company		
		Buying Bid Document	Submitting Bid Document	Awarded Participant
Direct Proposal				
1	South Bengara	Eni Indonesia Ltd.	-	-
2	West Berau	-	-	-
Regular Tender				
1	Rupat Labuhan	-	-	-
2	Nibung	-	-	-
3	Wesi Asri	-	-	-
4	Oti	1. Azipac Ltd 2. PT Agra Energi Indonesia	Azipac Ltd	-
5	Manakarra Mamuju	Ophir Energy Indonesia Ltd	-	-
6	Kasuri II	1. Genting Oil & Gas Limited 2. Overseas Petroleum and Investment Corporation 3. PT Agra Eneri Indonesia	PT Agra Eneri Indonesia	-

Source : DG Oil and Gas, Ministry of EMR as of 18 October 2017

No record from BPK and other sources available in the public indicating deviation of WA offering 2015 from applicable offering regulation.

3.1.5 The Rule of One Working Area for One Company

The upstream oil and gas industry adheres to the principle of "Ring Fencing" (Regulation of the Minister of Finance No. SE-75/1990), namely one Working Area is for one Business Entity or Permanent Establishment and has one NPWP. The principle of Ring Fencing also set the procedure of Cost Recovery which states that the costs incurred in one Working Area cannot be charged to other Working Areas in order to alleviate the taxes of other Working Areas.

3.1.6 Transfer of Participating Interest (PI)

The definition of Participating Interest stated in the Regulation of the Minister of Finance No. 257/2011 is Cooperation Contract Contractor's right and obligation, either directly or indirectly, on a working area.

PI transfer must be approved by Minister of EMR and take into account SKK Migas' considerations as stipulated by Article 33 of GR No.35/2004 and Articles 3 and 4 of the Regulation of Minister of EMR No. 48/2017. In addition, Article 2 (a) of the Regulation of Minister of EMR No. 48/2017 arranges that minister's approval is not only needed for transfer of share, but also changes in board of director and/or commissioner.

During the first three years of exploration, contractors may not transfer PI to parties that are not affiliated to the company. If contractors wish to disclose data for the purpose of PI transfer to other parties, the disclosure needs to be approved by the Minister of EMR through SKK Migas. Contractors are required to offer 10% PI (to replace investments equivalent of 10%) to Local-Owned Enterprises (LOE). LOE may not sell its PI, partially or entirely, for three years since the effective date of participation.

Article 5 of the Regulation of MoEMR No. 48/2017 regulates the procedure for a 10% (ten percent) participating interest transfer upon approval of the first field development to be produced in accordance with the laws and regulations concerning the 10% participating interest offering provision in oil and gas working area.

According to Article 27 paragraph (2) GR No. 79/2010, other contractor's revenue outside the Cooperation Contract generated from the transfer of participating interest shall be subject to final income tax at the rate of:

- a. 5% of gross amount for the transfer of participating interest during the exploration period or
- b. 7% of gross amount for the transfer of participating interest during the exploitation period.

According to Article 3 paragraph (1) of the Regulation of the Minister of Finance No. 257/2011, in order to share the risk during the exploration period, the transfer of Participating Interest is exempted from the imposition of Income Tax as referred to Article 2 paragraph (2) letter a, if it meets following criteria:

- a. The contractor does not transfer all participating interest owned;
- b. Participating Interest has been owned for more than 3 (three) years;
- c. The exploration has been conducted and the contractor has disbursed an investment to carry out the exploration activities; and
- d. The transfer of participating interest conducted by the contractor is not intended to make a profit.

The contractor is exempted from the income tax as long as it undertakes the transfer of participating interest obligation to the national company as stipulated in the cooperation contract.

Articles 34 and 35 of GR No. 35/2004 state that since the approval of POD-1 of working area, the contractor shall offer 10% participating interest to the Local-Owned Enterprise (LOE). The statement of interest and ability of the LOE shall be submitted within 60 days. If within 60 days the LOE does not provide a statement of interest and ability, then the 10% participating interest shall be offered to the national company. The deadline for the statement of the ability of national company is also 60 days, and if after 60 days the national company does not provide the statement then the offering is closed.

The oil and gas industry has 3 main characteristics, namely high cost, high tech and high risk. These characteristics make it difficult for national companies to compete and invest in the oil and gas sector. Hence, the regulation is needed to help their competitiveness.

List of PI transfer that took place in 2015 approved and reported by DG Oil and Gas is as follows:

Table 24. List of PI Transfer in 2015

No	Letter No.	Date	Working Area	Operator	Before PI Transfer	After PI Transfer
1	140/13/DJM.E/2015	6-Jan-15	Arguni I	Eni Arguni I Limited	Eni Arguni I Limited 100%	Eni Arguni I Limited 80%
						GDF Suez E&P Arguni I BV 20%
2	463/13/DJM.E/2015	12-Jan-15	Muara Bakau	Eni Muara Bakau BV	Eni Muara Bakau BV 55%	Eni Muara Bakau BV 55%
					GDF Suez Exploration Indonesia BV 45%	GDF Suez Exploration Indonesia BV 33,334%
						PT. Saka Energi Muara Bakau 11,666%
3	1013/13/DJM.E/2015	20-Jan-15	GMB Sijunjung	PT Inti Gas Energi	PT Inti Gas Energi 75%	PT Inti Gas Energi 75%
					PT Bukit Asam (Persero) Tbk 25%	PT Bukit Asam Metana Ombilin 25%

No	Letter No.	Date	Working Area	Operator	Before PI Transfer	After PI Transfer
4	1201/13/DJM.E/2015	26-Jan-15	West Madura Offshore	PT Pertamina Hulu Energi WMO	PT Pertamina Hulu Energi WMO 80%	PT Pertamina Hulu Energi WMO 80%
					PT Mandiri Madura Barat 20%	PT Mandiri Madura Barat 10%
						Kodeco Energy Co Ltd 10%
5	2894/13/DJM.E/2015	2-Mar-15	Cendrawasih Bay IV	Repsol Exploracion Cendrawasih IV BV	Niko Resources (Cendrawasih Bay IV) Limited 50%	Repsol Exploracion Cendrawasih IV BV 100%
					Repsol Exploracion Cendrawasih IV BV 50%	
6	2889/13/DJM.E/2015	2-Mar-15	Cendrawasih Bay III	Repsol Exploracion Cendrawasih III BV	Niko Resources (Cendrawasih Bay III) Limited 50%	Repsol Exploracion Cendrawasih III BV 100%
					Repsol Exploracion Cendrawasih III BV 50%	
7	3432/13/DJM.E/2015	12-Mar-15	Wailawi	PT Benuo Taka Wailawi	Perusda Benuo Taka 100%	PT Benuo Taka Wailawi 100%
8	3873/13/DJM.E/2015	20-Mar-15	Mahato	Texcal Mahato EP Ltd	Texcal Mahato EP Ltd 51%	Texcal Mahato EP Ltd 51%
					Bukit Energy Central Sumatera (Mahato) Pte Ltd 37,5%	Bukit Energy Central Sumatera (Mahato) Pte Ltd 25%
					Central Sumatera Energy Mahato Ltd 11,5%	Central Sumatera Energy Mahato Ltd 11,5%
						Cue Mahato Pte Ltd 12,5%
9	3882/13/DJM.E/2015	20-Mar-15	Batanghari	PT Gregory Gas Perkasa	CNOOC Batanghari Ltd 87%	PT Gregory Gas Perkasa 100%
					PT Gregory Gas Perkasa 13%	
10	4920/13/DJM.E/2015	14-Apr-15	East Jabung	Talisman East Jabung BV	Pan Orient Energy East Jabung Pte Ltd 100%	Pan Orient Energy East Jabung Pte Ltd 49%
						Talisman East Jabung BV 51%
11	6578/13/DJM.E/2015	22-May-15	South Mandar	PTTEP South Mandar Limited	PTTEP South Mandar Limited 34%	PTTEP South Mandar Limited 50,7463%
					Total E&P Indonesia South Mandar 33%	Total E&P Indonesia South Mandar 49,2537%
					Talisman South Mandar BV 33%	
12	8116/13/DJM.E/2015	23-Jun-15	Tanjung Aru/Bala-Balakang	KrisEnergy (Tanjung Aru) BV	KrisEnergy (Tanjung Aru) BV 43%	KrisEnergy (Tanjung Aru) BV 85%
					Neon Energy (Indonesia) Pty Ltd 42%	Natuna Ventures Pte Ltd 15%
					Natuna Ventures Pte Ltd 15%	

No	Letter No.	Date	Working Area	Operator	Before PI Transfer	After PI Transfer
13	8717/13/DJM.E/2015	7-Jul-15	Cendrawasih	Repsol Exploracion Cendrawasih I BV	Black Gold Cendrawasih LLC 70%	Repsol Exploracion Cendrawasih I BV 100%
					Repsol Exploracion Cendrawasih I BV 30%	
14	10456/13/DJM.E/2015	18-Aug-15	Nunukan	PHE Nunukan Company	PHE Nunukan Company 35%	PHE Nunukan Company 64,5%
					PT Medco E&P Nunukan 40%	BPRL Ventures Indonesia BV 12,5%
					BPRL Ventures Indonesia BV 12,5%	Videocon Indonesia Nunukan Inc 23%
					Videocon Indonesia Nunukan Inc 12,5%	
15	10936/13/DJM.E/2015	28-Aug-15	North Sumatera Block B	PT Pertamina Hulu Energia NSB	ExxonMobil Oil Indonesia Inc 100%	PT Pertamina Hulu Energia NSB 100%
16	10938/13/DJM.E/2015	28-Aug-15	North Sumatera Offshore	PT Pertamina Hulu Energi NSO	Mobil Exploration Indonesia Inc 100%	PT Pertamina Hulu Energi NSO 100%
17	11367/13/DJM.E/2015	7-Sep-15	West Bangkanai	PT Saka Energi Indonesia	PT Saka Bangkanai Klemantan 99,9%	PT Saka Indonesia Sesulu 0,1%
					PT Saka Indonesia Sesulu 0,1%	PT Saka Energi Indonesia 99,9%
18	11748/13/DJM.E/2015	15-Sep-15	North Madura	AWE (North Madura) NZ Limited	AWE (North Madura) NZ Limited 50%	AWE (North Madura) NZ Limited 50%
					North Madura Energy Limited 25%	Azipac North Madura Limited 50%
					Mitra Energy (Indonesia North Madura) Limited 25%	

Source: DG Oil and Gas, EITI's Data 2015

3.2 Mineral and Coal Mining Sector

3.2.1 Applicable Licenses in Mineral and Coal Mining Sector

Mineral and coal mining license based on Law no. 4/2009 adopts a licensing system called Mining Business License (IUP) which can be classified by mining area permit:

1. Mining Business License (IUP) is a license to conduct mining business activities in Mining Business License Area (WIUP), which is divided into:
 - IUP-Exploration
 - IUP-Production Operation
2. People's Mining License (IPR) is a license to conduct mining activities in People's Mining Area (WPR) with limited area and investment.
3. Special Mining Business License (IUPK) is a license to conduct mining activities in Special Mining Business License Area (WIUPK):

Table 25. Authority to grant IUP - exploration and production based on laws No. 4/2009 and No. 23/2014

Licensor	IUP – Exploration	IUP – Production Operation
	Mining Area	Mining Area and Impacted Area
Minister	Located in more than one province	Located and affecting more than one province Foreign investor
Governor	Located in several regencies/cities within one province	Located and affecting several regencies/cities within one province
	Located in one regency/city	Located and affecting one regency/city

Source: UU No. 4/2009 dan UU No. 23/2014

Meanwhile, the IPR is issued by the Governor and IUPK is issued by the Minister of Energy and Mineral Resources. IUPK is granted irrespective of the geographical location of the associated mining area. Provincial Government has authority to establish Mining Business License Area (WIUP) in the existing mining area in its territory, while cross-provincial mining areas as well as foreign investment become the central authority represented by the Ministry of EMR.

With the existence of the licensing system as described above, KK and PKP2B, which are the contract products of the previous Mineral and Coal Law, are still valid until the contracts / agreements expire. Similarly, KK and PKP2B signed before the enactment of GR No. 23/2010 (as the implementing regulation of Law No. 4/2009) are declared to remain in effect until the terms expire.

KK and PKP2B which have not obtained the first and/or second renewal can be extended to IUP without tender process (Article 112 GR No. 23/2010).

3.2.2 Allocating Mining Business Area

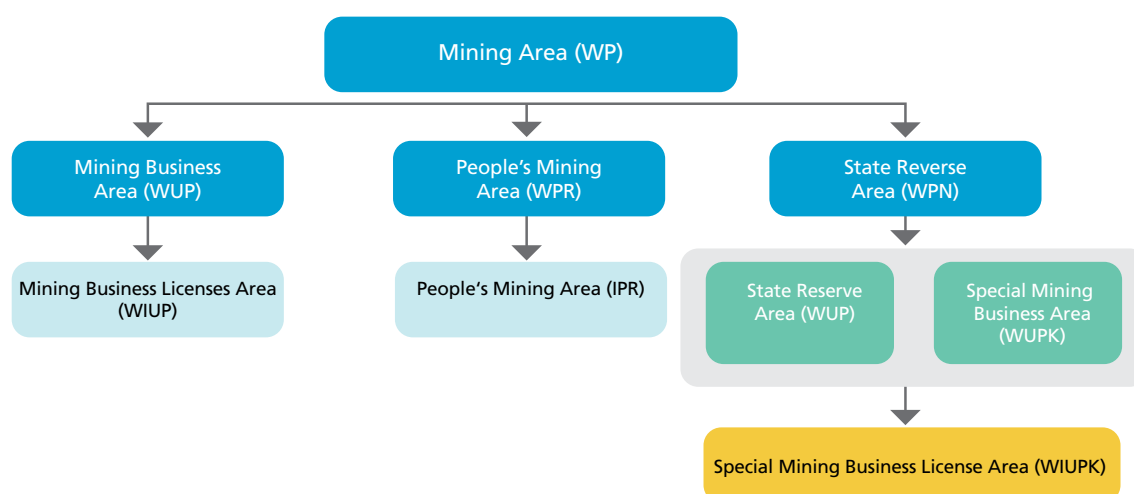
Establishing Mining Area

A mining area (WP) is an area with mineral and/or coal potential that is not bound by government's administrative boundaries and is part of national spatial planning. An area can be allocated as a WP given the following criteria:

- There is indication of mineral or coal deposits; or
- It has potential of other mining commodity resources

WP is further categorized as Mining Business Area (WUP), People's Mining Area (WPR), and State Reserve Area (WPN). WUP is part of WP that has data, potential identification, and/or geological information. WPR is part of WP whereby mining activities are carried out by local communities, while WPN is WP reserved for national strategic interest.

Figure 20. Types of mining areas



Source: Warta Minerba, XV Edition April 2013

To establish a WP, the central government (assisted by the local government) conducts mining investigation and research activities. In conducting such activities, the government may assign assignments to state research institutions or local research institutions. Under certain conditions, the government may cooperate with foreign research institutions after obtaining approval from the Minister of EMR.

The WP plan is established by the Minister of EMR to be a WP after the coordination between the government and the local government, based on data held by both parties, and reported in written form to the DPR. Some of the central government's authority in establishing WP allocations can also be delegated to the provincial government. The establishment of WP allocation is regulated in GR No. 22/2010.

3.2.3 The Establishment of Mining Area and IUP in 2015

The consequence of various issues in the mining sector, include the process of revamping the IUP - phase III, the reconciliation process as the impact of the issuance of Law No. 23/2014 on local government, area expansion and area boundary issues, is no establishment of mining areas and IUP in 2015.

In early 2012, the Directorate General of Mineral and Coal issued a circular on the moratorium of IUP granted by the local government and no IUP issued by the central and local governments in 2015.

3.2.4 The Establishment of Mining Business License Area (WIUP)

Local government determines WIUP for metal minerals and coal within one WP and Minister of EMR ratifies this decision. Prior to deciding WIUPs, the target areas must be announced to the public by the local government. If the metal mineral and coal WIUP is situated in forest area, the local government needs to coordinate with the Ministry of Forestry.

A number of criteria apply in WIUP establishment:

- Geographical location;
- Conservation principles;
- Carrying capacity of the environment;
- Optimization of mineral and/or coal resources; and
- Population density.

Minister of EMR decides tender base price based on data compensation price and/ or recovery of investment costs given the availability of:

- a. Distribution of metal mineral and coal formation;
- b. Indication of metal mineral and coal deposits;
- c. Data on metal mineral and coal potential;
- d. Metal mineral and coal reserve data; and
- e. Supporting infrastructure.

This compensation is recorded as non-tax state revenue.

In terms of permit grant for WIUPK to interested state and local owned enterprises, the compensation payment must be made at least 30 days since the parties are established as WIUPK holders. Five days after establishment, state or local owned enterprises must submit IUPK - Exploration request.

3.2.5 Tender Process of Mining Business License Area

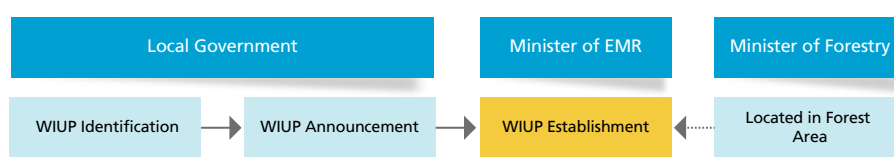
Regulation of the Minister of EMR No. 28/2013 regulates WIUP tendering procedure. Bidding plan must be announced at least 3 months prior to bidding date. Announcement of WIUPK is made by Minister of EMR, while WIUP can be made by either the Minister or Head of local government, depending on certain conditions:

- Minister of EMR - for WIUPs that cross provincial boundaries or sea territory over 12 miles from coastline. Head of local government needs to endorse the WIUP within five days after receiving request of endorsement. If the endorsement is not made within the time frame, they are automatically deemed as approving the WIUP.
- Head of Local Government - for WIUPs within a province or sea territory 4 to 12 miles from the coastline.

To prepare bidding round, Minister of EMR or head of local government forms Bidding Committee, comprising of personnel with competence in mining engineering, mining legal system, and mining financial system, with at least 3 years of experience working in the Ministry of EMR.

The legal status of bidding participants will determine the scope of WIUP that they can bid for.

Figure 21. Flow of mining business license area establishment



Source : GR No. 22/2010

Figure 22. Flow of WIUP Tender Process



Table 26. Legal status of participants eligible to bid by scope of WIUP

Legal Status	WIUP Area (Hectare)		
	<=1000	1000-5000	>=5000
SOE	-	✓	✓
LOE	✓	✓	✓
National private company	✓	✓	✓
Cooperative	✓	✓	-
Individual (person, limited partnership/CV, limited liability partnership/firma)	✓	-	-
Foreign Investment	-	-	✓

Source : Regulation of the Minister of EMR No. 28/2013

In order to participate in the bidding round of WIUP, bidders must meet the following requirements:

- Administrative requirements, among others:
 - Completed tender document;
 - Entity's profile and incorporation deed;
 - Taxpayer Identification Number (NPWP).
- Technical requirements, among others:
 - Minimum 3 years business experience in mineral or coal mining; new companies need to have endorsement from holding company, business partner, or affiliated company in mining sector;
 - Employs at least 1 mining expert and/ or geological expert with minimum 3 years of professional experience;
 - Work and budget plan for 4 years of exploration activities.
- Financial requirements, among others:
 - Last year financial statements audited by Public Accountant's Firm;

- b. Bid bond in cash deposited to government bank in the amount of 10% (ten percent) of compensation value of data and/or investment recovery of WIUP tendering;
- c. Statement of willingness to pay for WIUP tender value at least within five working days after winner announcement

3.2.6 WIUP Tender and the Issuance of IUP in 2015

Ministry of Energy and Mineral Resources issued Circular Letter (SE) No 08.E/30/DJB/2012 about moratorium on issuance of IUP by Local Government until the establishment of new Mining Area. There is no issuance of new IUP in 2015 because the government will establish new Mining Area in 2017.

3.2.7 The Rule of One IUP One Company

One private company may have only one IUP and only listed companies (in the stock exchange) and companies that obtain WIUP for non-metal and / or rocks that may own more than one IUP.

3.3 Challenge and Current Issue Regarding Licensing Process in the Extractive Industry

3.3.1 Transition Period of Oil and Gas Blocks

The certainty of contract extension is important for contractors to be able to calculate the return value of investment in developing a working area. Application for extension of cooperation contract, according to GR No. 35/2004, may be submitted at the earliest 10 years and no later than 2 years before the contract expires. The contractor may apply for a faster contract extension in connection with the gas sale and purchase agreement. However, on many previous occasions, the Government was late in extending the contract of cooperation and often waited until the last minute⁵⁸, such as the contract of Pase block that is extended two years after the contract expired. This uncertainty could result in delayed oil and gas projects and threaten national oil and gas production⁵⁹.

Here is the list of contracts expired by 2024 and have not extended:

Table 27. List of PSCs expired in 2024

No.	Working Area	Expiration Date	Operator
1	Tuban	2018	JOB Pertamina-Petrochina East Java
2	Ogan Komering	2018	JOB Pertamina-Talisman (Ogan Komering)
3	Sanga-Sanga	2018	Virginia Indonesia Co, LLC
4	Southeast Sumatra	2018	CNOOC SES Ltd
5	Blok B, onshore	2018	Exxonmobil Oil Indonesia Inc.
6	North Sumatra Offshore (NSO)/ NSO Ext	2018	Exxonmobil Oil Indonesia Inc.
7	Tengah	2018	Total E&P Indonesie
8	East Kalimantan	2019	Chevron Indonesia Company
9	Pendopo - Raja	2019	Pertamina-Golden Spike
10	Bula	2019	Kalrez Petroleum (Seram) Limited
11	Jambi Merang	2019	JOB Pertamina-Talisman (Jambi Merang)
12	Seram Non Bula	2019	CITIC Seram Energy Ltd
13	Malacca Strait, offshore	2020	EMP Malacca Strait S.A.
14	South Jambi "B"	2020	ConocoPhillips (South Jambi) Ltd
15	Makassar Strait, offshore	2020	Chevron Makasar Ltd.
16	Salawati Kepala Burung	2020	JOB Pertamina-Petrochina Salawati
17	Sengkang	2020	Energy Equity Epic (Sengkang) PTY, LTD.
18	Bentu Segat	2021	EMP Bentu Limited
19	Muriah	2021	PC Muriah Ltd.

⁵⁸ Rambu Energy.com, Indonesia Energy Ministry Says 17 Oil-Gas Contracts Will Expire by 2019, <http://www.rambuenergy.com/2015/01/indonesia-energy-ministry-says-17-oil-gas-contracts-will-expire-by-2019/>, accessed in 24 July 2015.

⁵⁹ IPA, Uncertainty Over Contract Extension Hampers Production, <http://www.ipa.or.id/news/detail/205>, accessed in 11 October 2015

No.	Working Area	Expiration Date	Operator
20	Rokan	2021	PT Chevron Pacific Indonesia
21	Selat Panjang	2021	Petroselat Ltd.
22	Coastal Plain Pekanbaru	2022	BOB Bumi Siak Pusaka
23	Sengkang	2022	Energi Equity
24	Tarakan	2022	Medco
25	Tungkal	2022	Montd'or Oil
26	Rimau	2023	Medco
27	Koridor	2023	Conoco
28	Jabung	2023	Petro China

In 2024, no WK is out of contract

Source: <http://industri.bisnis.com/read/20141215/44/382712/blok-migas-daftar-lengkap-32-kontrak-yang-habis-2015-2024>

There are 28 Working Areas expired in 2015 to 2024. These working areas contribute about 72.5% of national production.

In order to provide certainty for contractors, according to the Regulation of the Minister of EMR No. 15/2015 on the management of expired working area, the Minister of EMR must give approval or rejection no later than one year before the contract period ends. However, the extension of the contract is still experiencing delays that could hamper efforts to increase oil and gas production.

04

CONTRIBUTION OF EXTRACTIVE INDUSTRY IN INDONESIA

THE MINING SECTOR HAS AN IMPORTANT ROLE
IN THE REGION'S ECONOMY, ESPECIALLY IN MINE
PRODUCING AREAS.



This section provides the overviews of Indonesia's extractive industry and its resources distribution and reserves, as well as production/lifting including significant exploration activities. It also discusses the extractive industry's contribution to Indonesia's economy including

to GDP, state revenue, export and employment. The final part of this section discusses the contribution of extractive industry in some regional examples.

4.1 Position of Production and Reserves in a Global Context

OIL AND GAS



Reserves

Oil, ranked 27th in the world

Gas, ranked 14th in the world

Production

Oil, ranked 23rd in the world

Gas, ranked 10th in the world

The 5th largest LNG exporter⁶⁰

Oil

Indonesia has 3.6 billion barrels in proven reserves, ranked 27th for oil reserve contributors, and 23rd for oil producers in the world, contributing around 1% of the global oil production according to data from 2015 BP Statistics.

Gas

Indonesia is ranked 14th in the world for proven gas reserves based on 2015 BP Statistics. Indonesia is also ranked 10th in the world for gas production, accounting for 2% of the global gas production.

COAL

Ranked 10th in the world

Ranked 5th in the world



Indonesia is the fifth largest coal producer – accounting for 5.8% of the global production – after Australia, and the tenth top coal reserves contributor in the world.

OTHER MINERALS

Reserves

Gold, ranked 5th in the world

Tin, ranked 2nd in the world

Production

Tin, ranked 2nd in the world



Indonesia plays a significant role in the world's mineral mining. According to a statistic report by the U.S Geological Survey in 2015, Indonesia is ranked 5th and 2nd in the world for its gold and tin reserves, respectively. Indonesia is also the second largest tin producer in the world.

4.2 Trend of Changes in World Commodity Prices

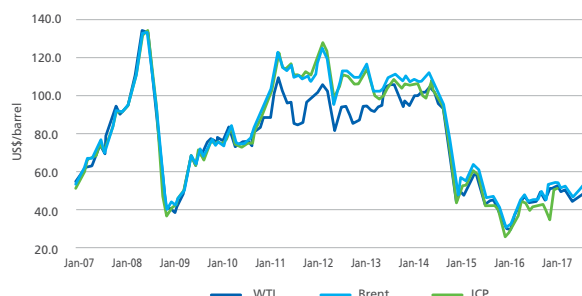
This section discusses the world commodity price trends in oil and gas sector and mineral and coal sector. By 2015 all commodity prices have decreased due to over supply

and slow down the world economy. The decrease also greatly affected the contribution of extractive industry to the Indonesian economy, such as state revenue, GDP and export.

⁶⁰ International Gas Union (IGU). 2015. "IGU World LNG Report", p. 14 http://www.igu.org/sites/default/files/node-page-field_file/IGU-World%20LNG%20Report-2015%20Edition.pdf accessed in 27 November 2017

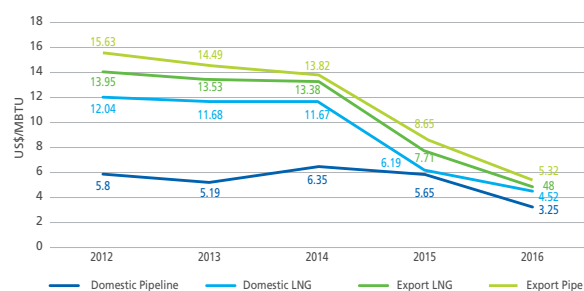
Oil and Gas Sector

Chart 3. World oil price in 2007 - 2017



Source: World Bank, DG Oil and Gas

Chart 4. Gas price by distribution channel in 2012-2016



Source: <http://databoks.katadata.co.id/datapublish/2017/08/30/berapa-harga-gas-indonesia>

The price of oil in Indonesia refers to the reference oil price in the international market, so that changes in international prices will directly affect the price of Indonesian crude oil. Chart 3 illustrates the movement of world oil prices over the past 10 years in which there are two peak oil price periods. The first peak in the final period of 2008 broke the price above US\$ 120 / barrel, but only for a short period and then dropped dramatically to approximately US\$ 40 / barrel due to the global financial crisis pioneered by the financial crisis of US financial companies. The second peak in 2011 lasted quite stable until the third quarter of 2014. The price of oil at that time ranged at US\$ 100 / barrel to above US\$ 120 / barrel. After four years, oil price started to decline by the end of 2014, in which the average price of Indonesia Crude Price (ICP) in 2015 is US\$ 50 / barrel and continues to decline until it reaches the bottom with the ICP of US \$ 27 / barrel in early 2016.

The decline in oil prices is due to several factors, especially the world's abundant oil supply caused by a combination of shale oil revolutions in the United States that led to high oil production and OPEC countries that do not try to balance the market but continue to boost production. With the global economic slowdown, the oil price in 2016 and the next year will be difficult to experience a significant increase.

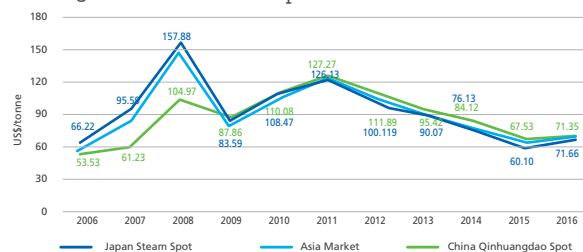
The decline in oil prices has led to the significant decline in Indonesia's gas prices by 2015, particularly the export-channel gas and both domestic and export LNG as seen in Chart 4. LNG prices are most affected by the decline in oil prices since LNG prices typically include the benchmark factor of oil prices in the LNG pricing variable. The domestic LNG price drops to 47%, from US\$ 11.67 / MMBTU in 2014 to US\$ 6.19 / MMBTU in 2015, then the export LNG price drops by 42%, from US\$ 13.38 / MMBTU in 2014 to US\$ 7.71 / MMBTU in 2015.

Meanwhile, domestic-channel gas prices decrease more moderately since, in general, domestic-channel gas prices have a fixed price with or without escalation stipulated in long-term contracts. Domestic-channel gas price in 2015 fell by 11% from US\$ 6.35 / MMBTU in 2014 to US\$ 5.65 / MMBTU in 2015.

Mineral and Coal Sector

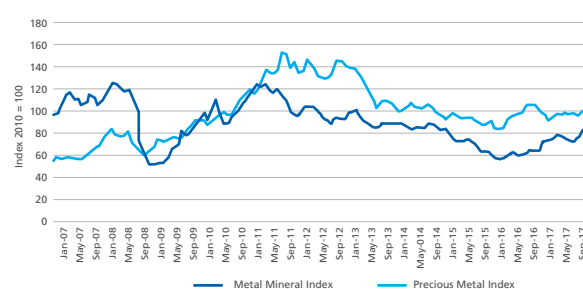
Chart 5 illustrates the world's gradual falling coal prices averaging 15% per annum since 2012 and reaching its base in 2015 in the range of US\$ 60-70 / ton. The decline is due to stagnant world coal demand in line with the slowing of global industrialization growth, especially in China and the change of policy of various countries toward the increase of renewable energy.

Chart 5. International coal price in 2006-2016



Source: BP Statistical Review 2016

Chart 6. Metals and precious metals price indexes in 2007 -2017



Source: World Bank

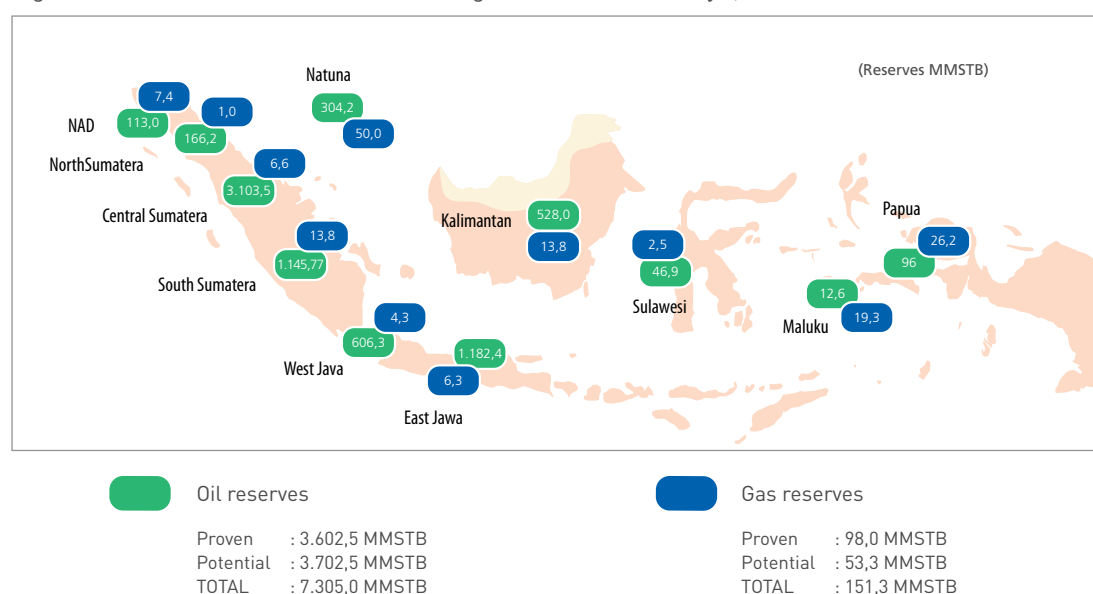
Similar to the world's metal and mineral prices, the slowing down of China's economy and industrialization has also resulted in declining global metal prices gradually from 2012 to 2015. Moreover, China is the center of the world's demand for metals, for example, half of the demand for iron, aluminum and nickel of the world comes from China⁶¹. Chart 6 shows a 20% drop in the price index of metals and minerals by 2015 compared to 2014 and a decline in the precious metals price index by 10% over the same period.

4.3 Distribution and Potency of Extractive Industry in Indonesia

4.3.1 Oil and Gas Sector

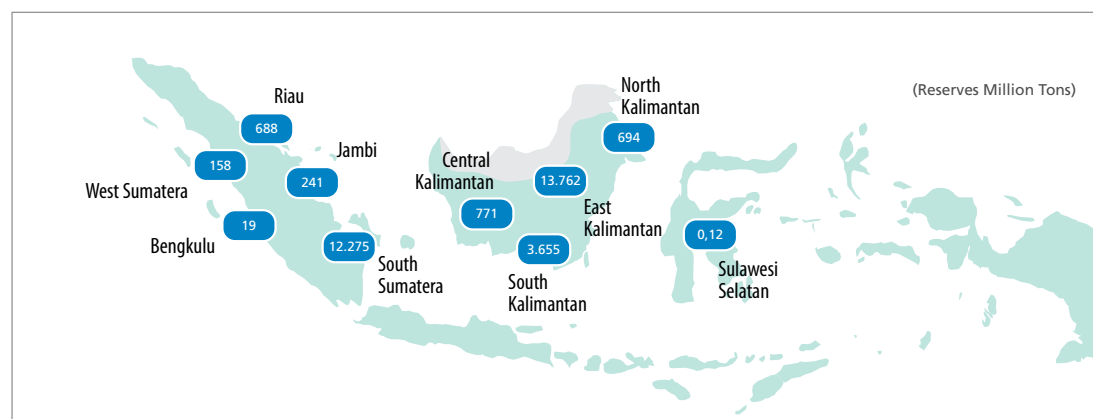
The prospect of Indonesia's oil and gas resources is still quite large and the largest distribution is in Sumatra, Kalimantan, Papua and Java. The prospect of Indonesia's oil resources is concentrated on the island of Sumatra by 62%, followed by Java by 24% of

Figure 23. Distribution of Indonesia's oil and gas reserves on January 1, 2015



Source : Oil and Gas Statistics, DG Oil and Gas 2015, Ministry of EMR

Figure 24. Distribution of coal reserves in Indonesia



Source: Performance Report of the Ministry of EMR 2015, modified

61 IMF, October 2015, "Commodity Special Feature", <https://www.imf.org/external/npr/res/commod/pdf/WEOSpecialOCT15.pdf> accessed in 1 November 2017

national oil reserves. While the largest gas reserves are in Natuna by 33% and the rest are spread in eastern Indonesia such as Papua by 17%, followed by Maluku by 13% of the total prospects of gas resources in Indonesia.

4.3.2 Coal Mining Sector

Indonesia's coal reserves at the end of 2015 reached 32.3 billion tons. The distribution of coal reserves is concentrated in three regions, East Kalimantan (43%), South Sumatra (38%) and South Kalimantan (11%).

4.3.3 Mineral Mining Sector

Papua has primary gold, copper and silver reserves amounted to almost 80% of total national reserves. Almost all tin reserves are located in Bangka Belitung. The island of Kalimantan holds many iron and bauxite reserves in West Kalimantan.⁶²

Map of resources and reserves distribution by region and commodity can be accessed at <http://webmap.psdg.bgl.esdm.go.id/geosain/neraca-mineral-strategis.php?mode=administrasi>

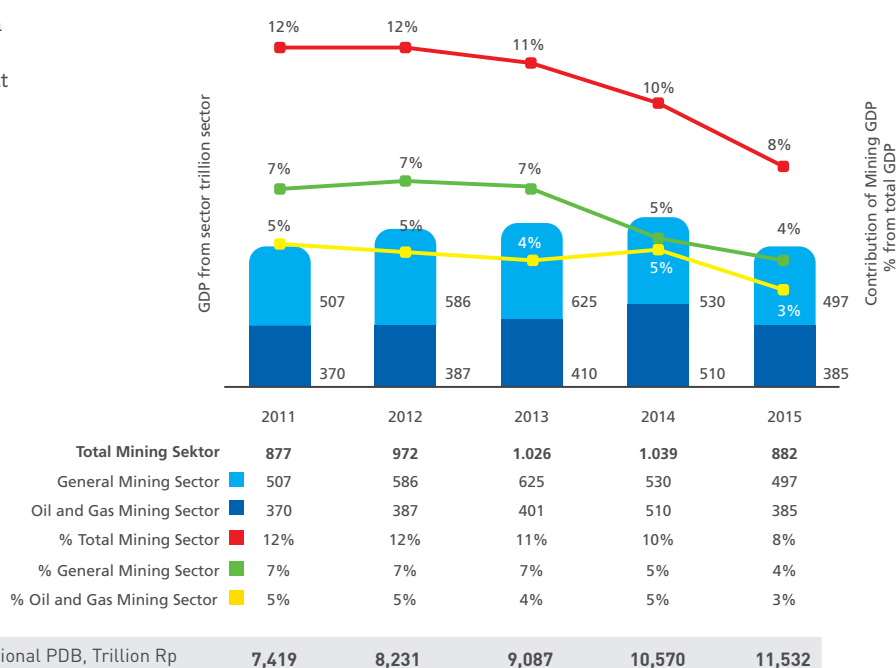
Table 28. Total mineral resources and reserves in Indonesia.

No	Commodity	Total Resources (ton)		Total Reserves (Ton)	
		Ore	Metal	Ore	Metal
1	Primary gold	8,703,669,136	6,613	2,832,377,068	2,537
2	Bauxite	3,617,770,882	1,740,461,414	1,257,169,367	571,254,869
3	Nickel	5,756,362,683	79,172,702	3,197,178,940	50,872,304
4	Copper	29,753,119,232	149,678,344	5,485,960,754	51,213,125
5	Iron	1,397,068,930	418,888,703	279,354,825	97,555,769
6	Iron sand	4,459,586,351	1,683,084,164	808,938,227	397,334,700
7	Manganese	60,893,820	27,977,709	87,236,536	43,134,791
8	Zinc	670,658,336	7,487,776	19,864,091	2,274,983
9	Tin	3,924,474,108	2,464,171	1,592,208,743	572,349
10	Xenotim	6,466,257,914	20,734	-	-
11	Silver	14,469,988,181	838,765	3,056,379,162	1,691,957

Source: Geological Board, KESDM, Data and Mineral Resources Balance "http://psdg.bgl.esdm.go.id/Neraca/2015/executive%20summary%20neraca%20mineral%202015.pdf"

4.4 Contribution of Oil and Gas GDP and Mining GDP to Indonesia's Total GDP

Chart 7. Contribution of mining GDP to total national GDP (at current prices)



Source: BPS (GDP is based on business field – oil and gas mining and mining without oil and gas sector)

⁶² Based on Geology's data in the following website <http://webmap.psdg.bgl.esdm.go.id/geosain/neraca-mineral-strategis.php?mode=administrasi>

Chart 7 outlines the contribution of the Indonesian mining sector to the national GDP at current prices. In nominal terms, the GDP of the mining sector in the period 2011-2014 continues to grow. However, the growth is not in line with the contribution of the mining sector to the national GDP from year to year. It shows the shift of mining industry dominance in the national economy. Although the GDP generated from the mining sector is less significant nationally, that is less than 15% and less than 10% by 2015, the contribution of the mining sector in the GDP of the producing provinces such as Riau, Papua and East Kalimantan is significant with contribution of more than 20% (see Sub-Section 4.9 Contribution of Extractive Industry in the Region (Several Regions Examples)).

In 2015, GDP from the oil and gas mining sector declined by 24% from the previous year to Rp 385 trillion or 3% of the total national GDP. The decline in GDP of other mining sectors is not as much as the decline in the oil and gas sector, which decreased by 6% in 2015 compared to the previous year to 497 trillion rupiah or 4% of the total national GDP. The significant decline in oil and coal prices in 2015 is one of the causes of the decline. The ban on exports starting in 2014 also affected the decline in mining GDP by 2015.

GDP at current prices based on business field can be found on the National Statistics Agency website: http://www.bps.go.id/linkTableStatis/view/id/1199_for_2010_-2014_and_https://www.bps.go.id/linkTableDinamis/view/id/826_for_2014_-2017.

4.5 State Revenue from Oil and Gas Sector and Mineral and Coal Sector

Chart 8 illustrates the significance of the extractive industry's contribution to state revenue in the period of 2012-2014. The contribution of extractive industry, which is quite high, about 30% of the total state revenues in 2012 - 2014 makes this sector a strategic one. However, due to declining oil prices, which is about US\$ 100 / barrel to only US\$ 50 / barrel, state revenue from oil and gas fall by 50% in 2015.

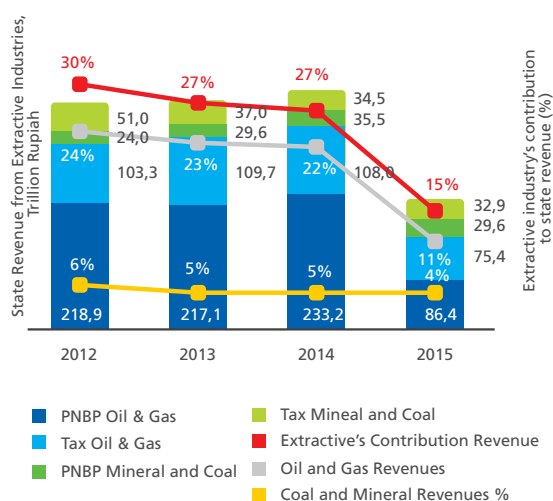
Meanwhile, state revenue from the mineral and coal sector is fluctuating, but the contribution to total state revenues continues to decline from 6% in 2012 to 4% in 2015 due to falling commodity prices.

4.6 Production and Lifting in Oil and Gas Sector and Production in Mineral and Coal Sector

4.6.1 Oil and Gas Sector

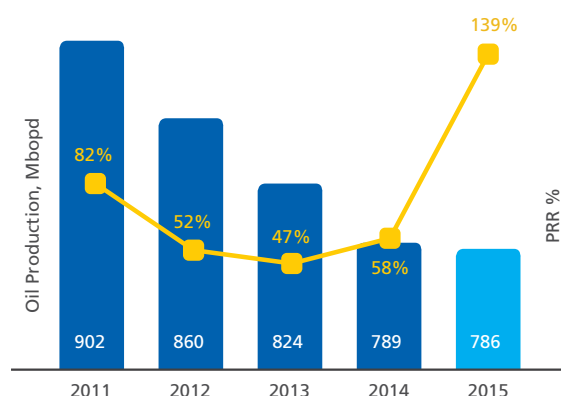
Chart 9 and 10 illustrate the declining production and lifting of Indonesia's oil over the past five years. Oil production in 2015 amounted to 786 Mbopd, while oil lifting amounted to 776 Mbopd. The average decrease in oil production is 4% during 2011-2014 and stagnate by 2015. By 2015, the decrease of oil production can be suppressed by additional production from Banyu Urip Field, Bukit Tua Field, Pematang Lantih Field and Field GG⁶³.

Chart 8. State revenue from the extractive industry



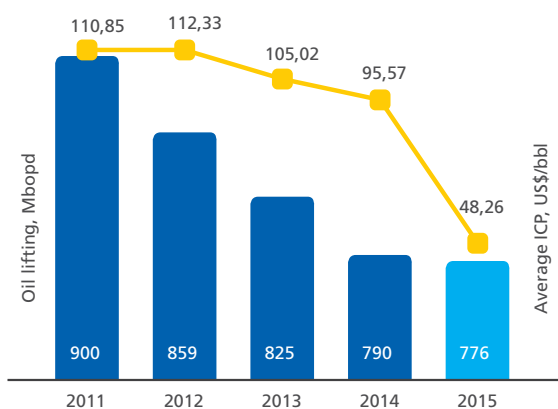
Source: LKPP, DG Tax Annual Report

Chart 9. Oil production in 2011-2015



Source : SKK Migas Annual Report of 2011 - 2015

Chart 10. Oil lifting in 2011 - 2015



Sumber : SKK Migas Annual Report of 2011 - 2015

In addition, there is a significant increase in the Reserve Replacement Ratio (RRR)⁶⁴ of oil to 139% in 2015, which means that the discovery of new reserves can replace 139% of oil that has been produced. The discovery of new reserves in 2015 is the discovery of commercial oil reserves to be developed from 53 fields which contributed to the addition of oil reserves of 398 MMBO (Chart 9). RRR amounted to 139% means the addition of proven reserves can replace the reserves produced in the relevant year as much as 139%.

Chart 10 illustrates a sharp decline in average crude oil prices in 2015, that is 49.5% from the previous year.

Production Volume, Lifting Volume, and Lifting Value of Oil by Main Working Areas

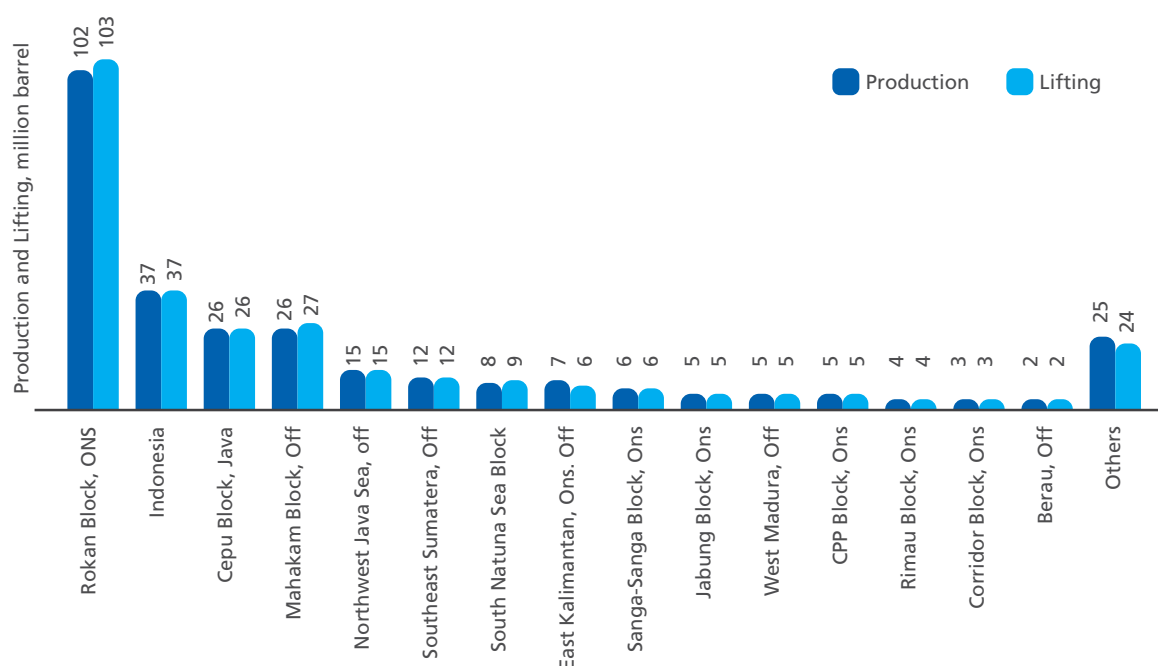
Chart 11 illustrates the 15 main working areas that account for about 90% of national oil production and lifting. In 2015, the Rokan Block, Sumatra managed by PT Chevron Pacific Indonesia is the largest contributor to oil production and lifting in Indonesia with production and lifting of 102 million barrels and 103 million barrels respectively by 2015 representing 36% of total oil production and lifting in 2015. Followed by the production and lifting of Indonesian Block managed by PT Pertamina EP amounting to 37 million barrels each in 2015 or representing 13% of total national production and lifting in 2015. Cepu Block managed by Mobil Cepu Ltd. accounted for 9% of national oil production and lifting in 2015.

Chart 12 illustrates 15 main working areas based on the value of oil lifting in 2015. The Rokan Block is ranked first with the value of oil lifting of 5 billion USD or 36% of the total oil lifting value. Next, the Indonesia and Mahakam Blocks occupy the second and third position with lifting value of 1.8 and 1.3 billion USD respectively or 13% and 10% of the total value of oil lifting in 2015.

4.6.2 Gas Sector

Chart 13 and 14 show that during the last 4 years (2012-2015) there is no significant spike in national gas production. However, the decline of the Reserve Replacement Ratio (RRR) of gas is very alarming, falling from 90% in 2013 to 17% in 2015 in which the discovery of commercial gas reserves to be

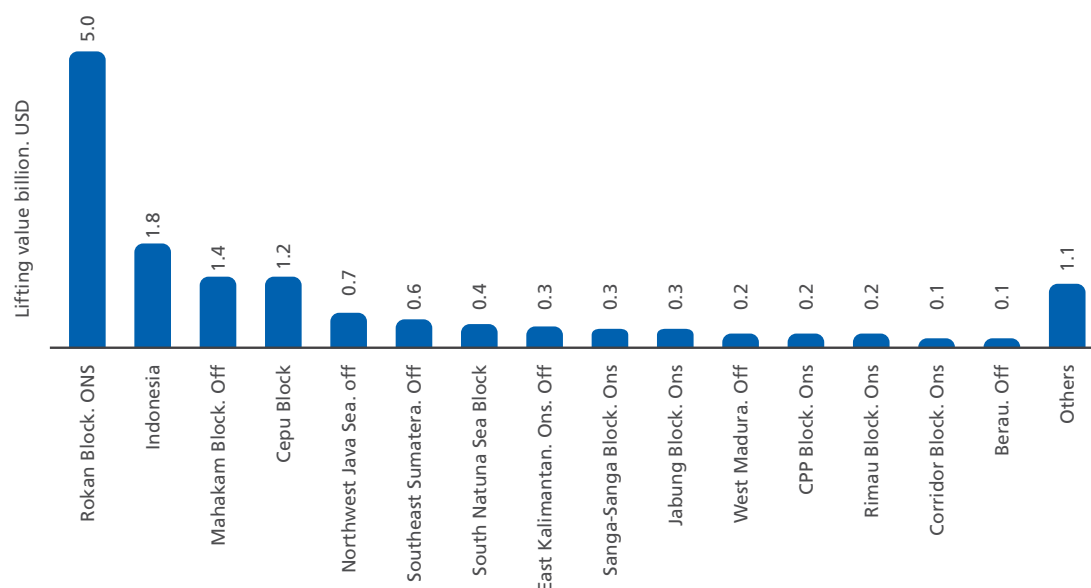
Chart 11. Oil production and lifting of 15 main working areas



Source: Reconciliation Data of SKK Migas 2015

⁶⁴ Look up the definition on List of Abbreviation

Chart 12. Oil lifting value of 15 main working areas



Source: Reconciliation Data of SKK Migas 2015

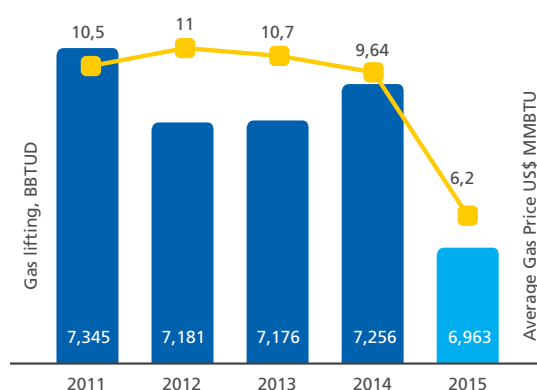
developed from 18 fields contributing to the addition of gas reserves of 492 bscf cannot replace the gas reserves that have been produced amounted to 2,948 bscf (Chart 13). The government is expected to pay attention to intensify gas exploration activities.

Similarly, the lifting of gas is relatively stable during the last five years. However, in 2015, the decrease in gas lifting is quite striking that is decreased 4% compared to gas lifting in 2014, from 7,256 to 6,963 BBTUD.

Production Volume, Lifting Volume, and Lifting Value of Gas by Main Working Areas

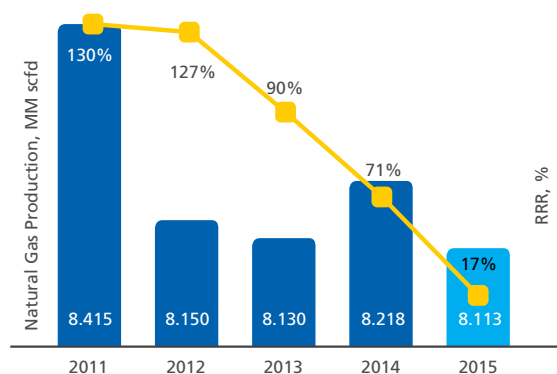
Chart 15 illustrates the main blocks contributing 90% of the total volume of gas production and lifting. The largest contributor to gas production and lifting in

Chart 14. Gas lifting in 2011-2015



Source : SKK Migas Annual Report 2011 - 2015

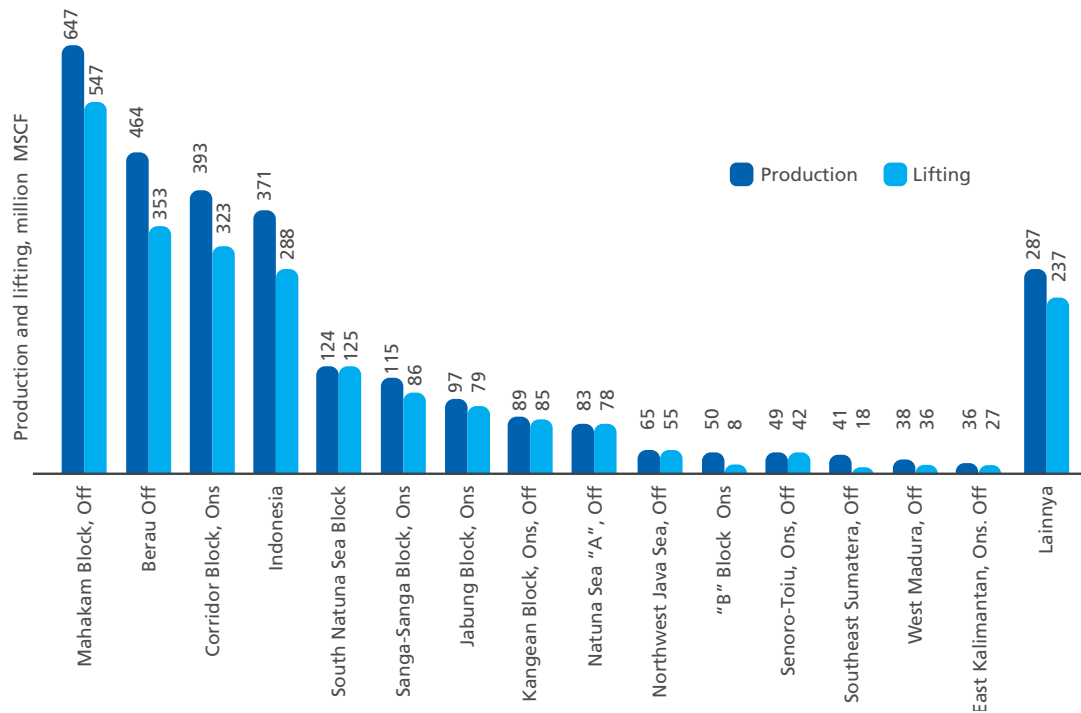
Chart 13. Gas production in 2011-2015



Source : SKK Migas Annual Report 2011 - 2015

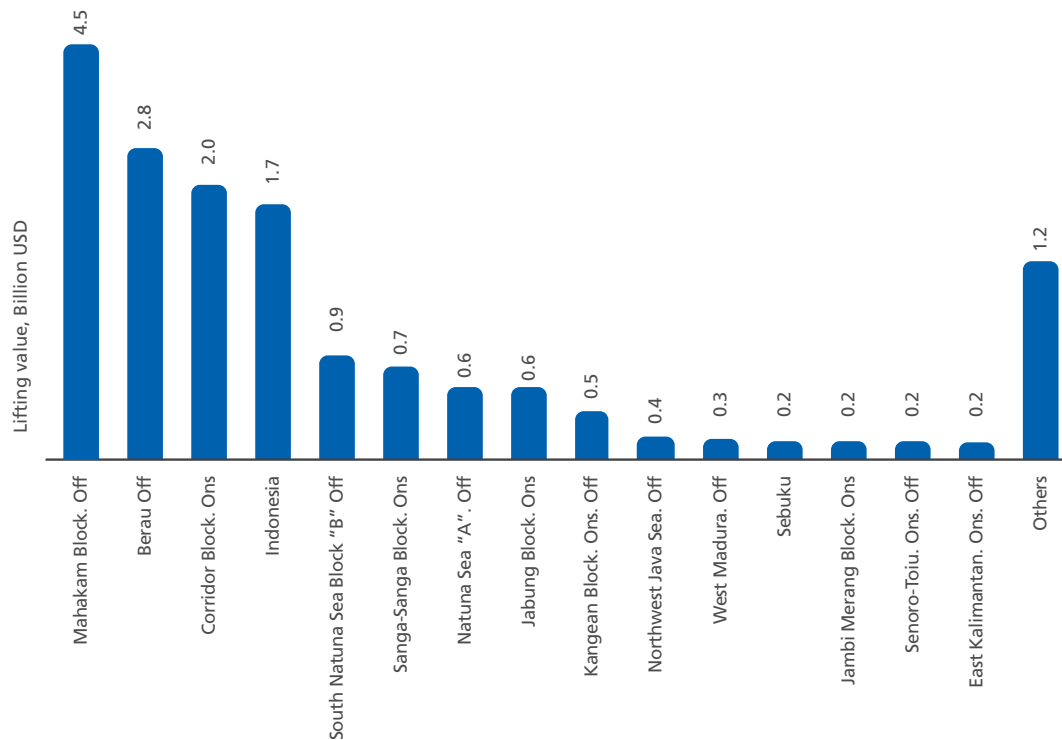
2015 is the Mahakam block managed by Indonesia Petroleum Ltd. and Total E&P Indonesia with total production of 647 million Mscf or 22% of national production and total lifting of 547 million Mscf or 23% of total national lifting. Next, Berau Block managed by BP is the second largest contributor to production and lifting of gas with total production and lifting amounted to 16% and 15% of total national production and lifting, respectively. ConocoPhillips' Corridor Block is in third position with total production and lifting of gas of 393 million Mscf and 323 million Mscf respectively or 13% and 14% of the total volume of gas production and lifting in 2015.

Chart 15. Gas production and lifting of 15 main working areas



Source: Reconciliation Data of SKK Migas 2015

Chart 16. Gas lifting value of 15 main working areas



Source: Reconciliation Data of SKK Migas 2015

Chart 16 illustrates 15 main working areas based on the value of gas lifting in 2015. Mahakam block occupies the first position with a lifting value of gas amounted to 4.5 billion USD or equal to 26% of the total value of national gas lifting. Next, Berau and Corridor blocks are in second and third position with lifting values of 2.8 billion USD and 2 billion USD respectively or 16% and 12% of the total value of national gas lifting in 2015.

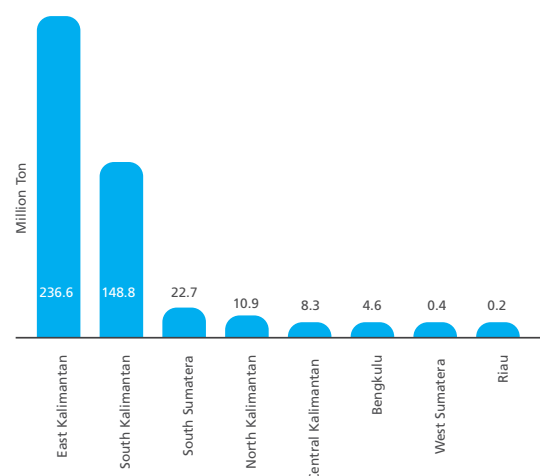
The relevant agencies in the oil and gas sector only provide lifting values and no production value. The reason is the recording of value realization is only conducted at the time of lifting since production is not a realization of sales.

4.6.3 Coal Sector

Chart 17 shows that Indonesia's coal production increases in 2013 and then more stable until 2015. Coal production is unlikely to be affected by the decline in international coal prices due to the increasing domestic demand with government policies and targets for 10,000 MW power plant phase I and II and then 35,000 MW program which is dominated by PLTU.

In 2015 about 90% of coal production activities are concentrated in the island of Kalimantan because coal infrastructure is mostly found on the island of Kalimantan⁶⁵. The largest producers of coal are:

Chart 18. Coal production by producing provinces in 2015



Source: Performance Report 2015 DG Mineral & Coal, BPS

- PT Kaltim Prima Coal, located in East Kalimantan, accounts for 14% of total national production in 2015.
- PT Adaro Indonesia, located in South Kalimantan, accounts for 13% of total national production in 2015.
- PT Kideco Jaya Agung, located in East Kalimantan, accounts for 10% of total national production in 2015.

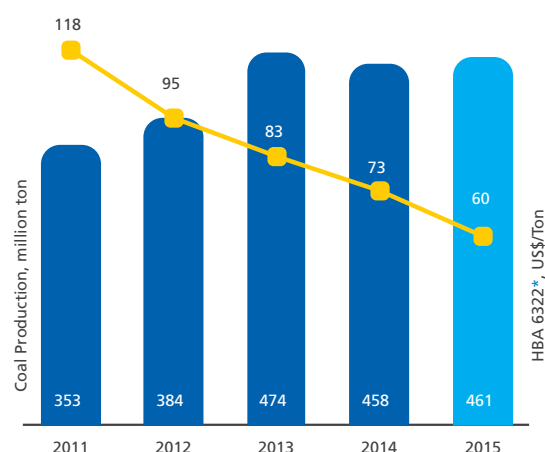
There is a difference in the amount of production stated in Mineral and Coal in the Numbers of the Year of 2011-2016, which is the basis of Chart 17 with Performance Report of DG Mineral and Coal 2015, which is a reference for Chart 18.

Public can see the list of largest coal producers in <http://www.minerba.esdm.go.id/public/38477/produksi-batubara/>. Provision of production value information by relevant institutions is not common.

4.6.4 Main Minerals Production

Table 29 shows the increasing of gold, silver, tin and nickel matte production during the period of 2011-2015. However, that is not the case with copper production, which declined significantly in 2015 caused by the export ban.

Chart 17. Coal production in 2011-2015



Source: Mineral and Coal in amount, 2011-2016, East Kalimantan

Table 29. Volume of main minerals production in 2011-2015

Main minerals	Unit	2011	2012	2013	2014	2015
Copper	Ton	543,942	410,228	521,025	617,840	197,634
Gold	Ton	76	53	57	69	97
Silver	Ton	200	203	208	252	318
Tin	Ton	31,169	130,809	82,954	60,038	70,073
Nickel Matte	Ton	68,000	72,899	78,074	80,341	82,440

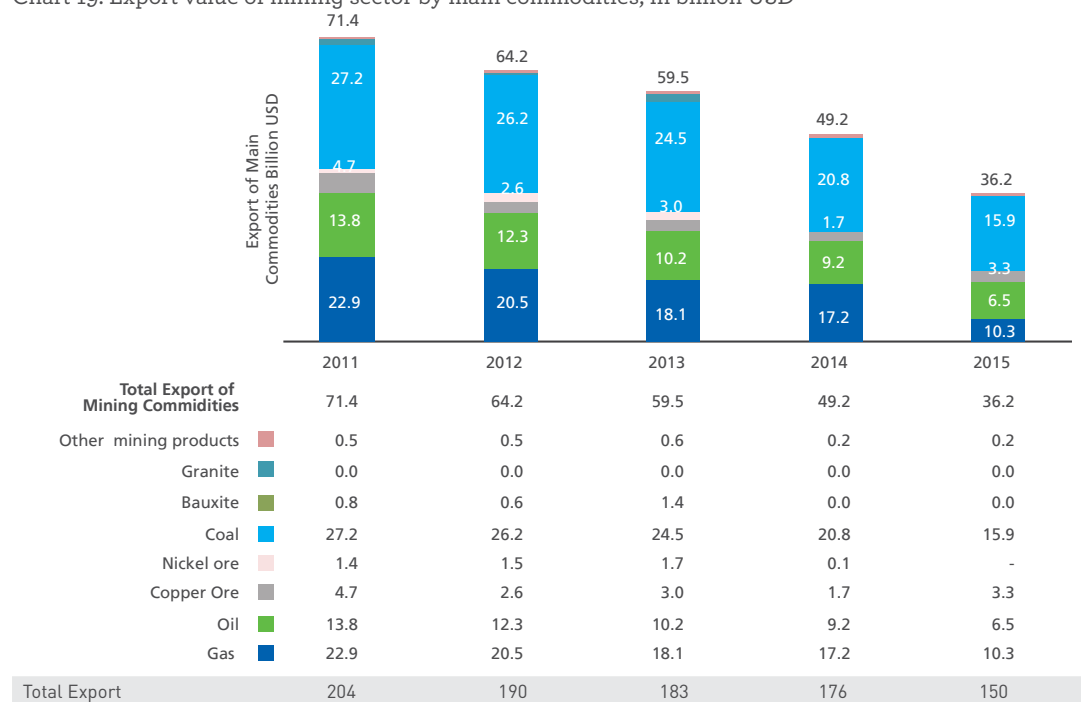
Source : Mineral & Coal in Figures 2011-2016, DG Minerals and Coals

⁶⁵ LAKIN Minerba 2015

4.7 Contribution of Oil and Gas Export and Mineral and Coal Export

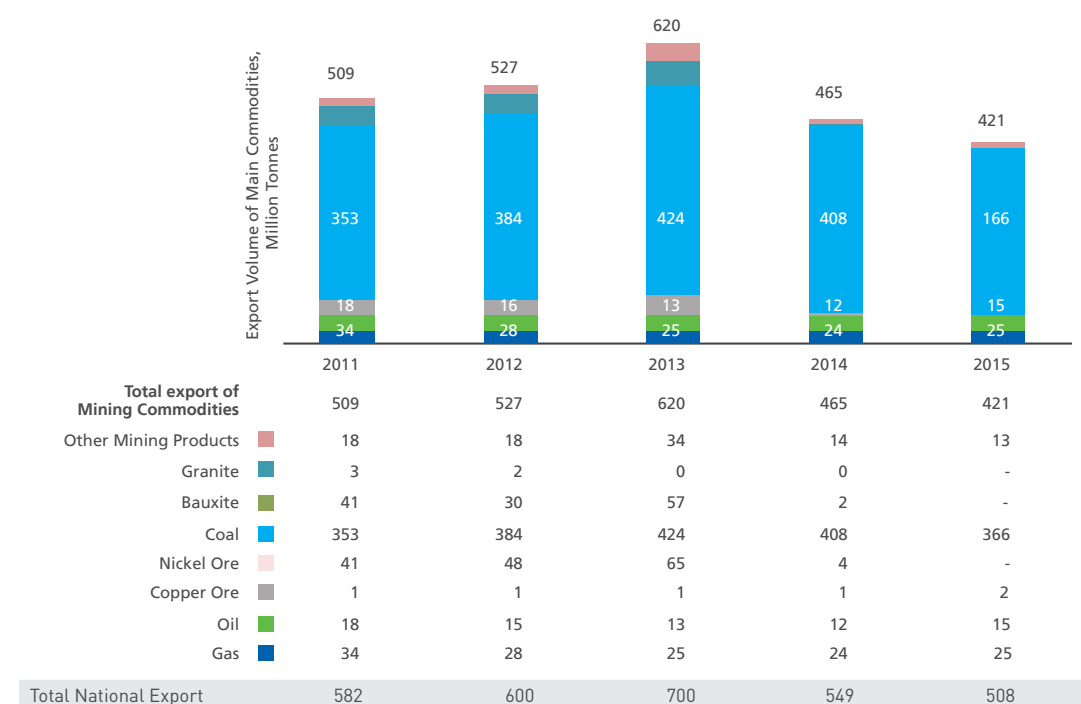
4.7.1 Oil & Gas and Mineral & Coal Sector

Chart 19. Export value of mining sector by main commodities, in billion USD



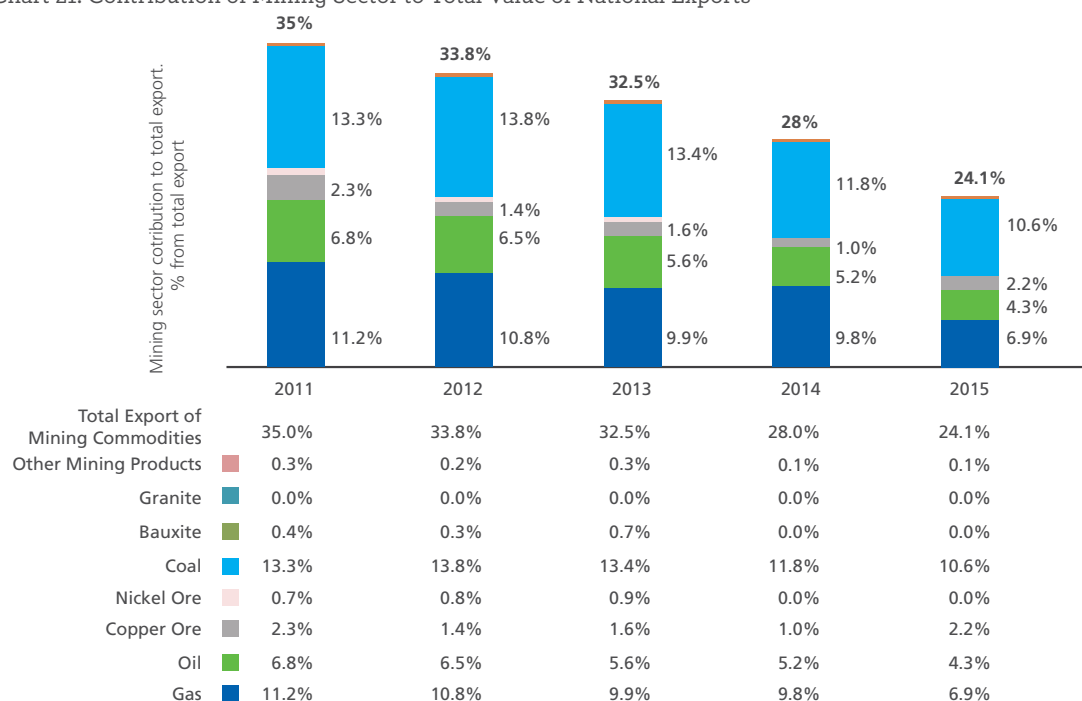
Source: BPS

Chart 20. Export volume of mining sector by main commodities, in million tonnes



Source: BPS

Chart 21. Contribution of Mining Sector to Total Value of National Exports



Source: BPS

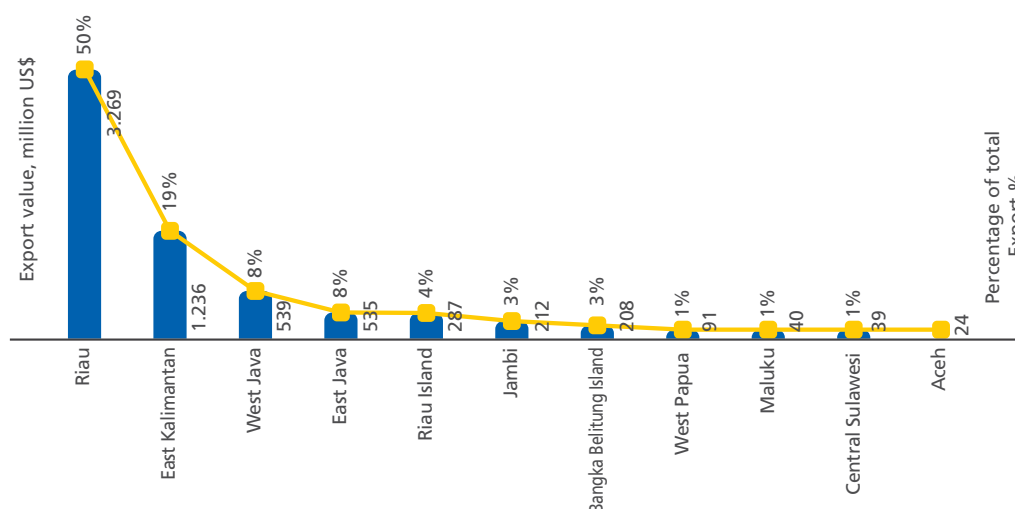
Charts 19-21 illustrate the export of mining commodities and their contribution to national exports for the period of 2011-2015. The contribution of mining export to total national export value is significant, ranging from 24% -35%. The export value is dominated by export value from oil, gas and coal. In 2011-2015, oil and gas exports contribute about 11% -18% of the total value of national export while the value of coal export reaches 10-13% of the total value of national export. The contribution of mining export value in 2011-2015 experiences a downward trend due to international commodity price pressures.

The list of national export by commodities is accessible on the BPS website: <http://www.bps.go.id/Subjek/view/id/8#subjekViewTab3|accordion-daftar-subjek2>

4.7.2 Export of Oil Sector by Main Provinces

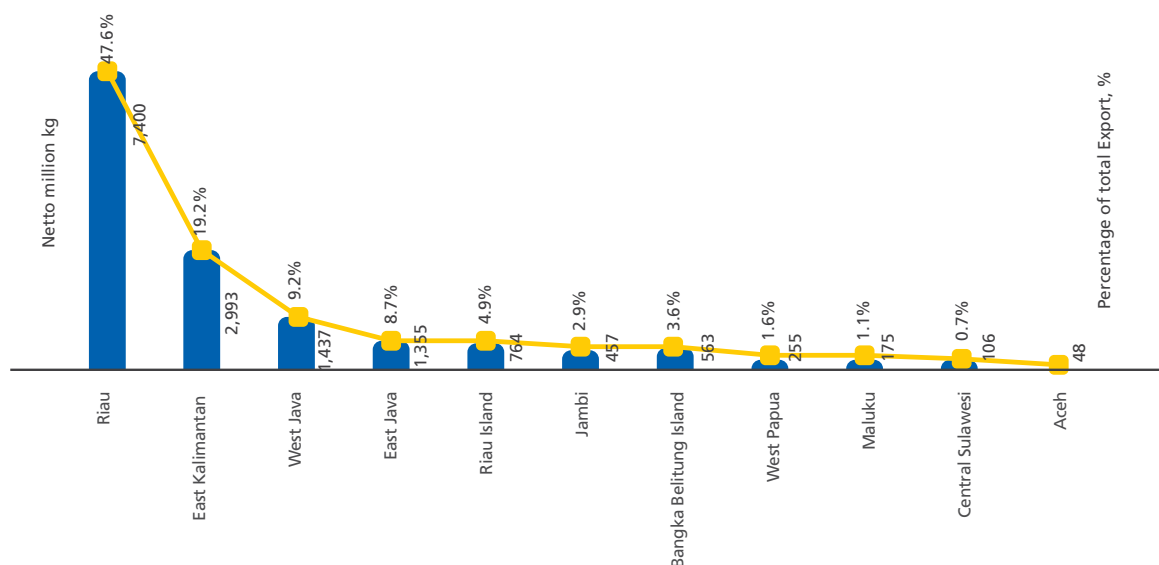
Chart 22 and Chart 23 illustrate the oil export of each province in 2015. Riau Province is the largest contributor of oil export with a net weight of 7,400 million kg and export value amounted to 50% of the total value of national oil export. Followed by East Kalimantan and West Java with export value amounted to 19% and 8% of the total value of national oil export in 2015..

Chart 22. Oil export value by provinces in 2015



Source: Foreign Trade Statistics by SITC Code 2015-2016, BPS

Chart 23. Oil export volume by provinces in 2015



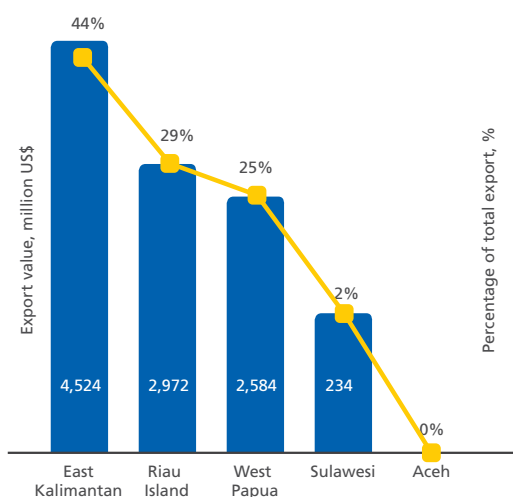
Source: Foreign Trade Statistics according to SITC Code 2015-2016, BPS

4.7.3 Export of Gas Sector by Main Provinces

Chart 24 and 25 illustrate gas export by provinces in 2015. The largest contributor to gas export is the province of East Kalimantan. Total gas export of East Kalimantan Province amounted to 9,415 million kg and accounted for 38% of the total national gas export. Meanwhile, the export value of East Kalimantan Province is 44% of the total value of national gas

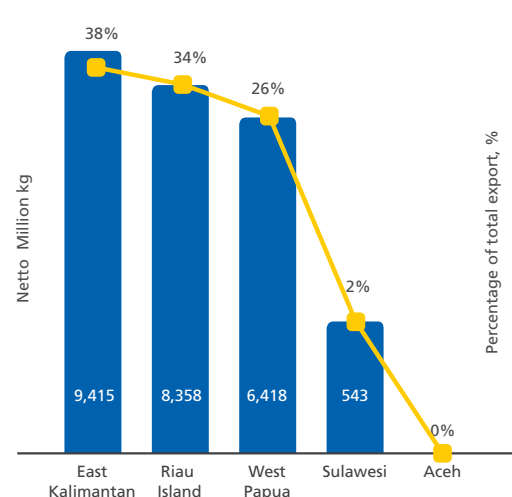
export or US\$ 4,524 million. Next, the second and third largest gas export contributors are Riau Islands Province and West Papua with export value of 2,972 million US\$ and 2,584 million US \$, respectively.

Chart 24. Gas export value by provinces in 2015



Source: Foreign Trade Statistics according to SITC Code 2015-2016, BPS

Chart 25. Gas export volume by provinces in 2015



Source: Foreign Trade Statistics according to SITC Code 2015-2016, BPS

4.7.4 Export of Coal Sector by Main Provinces

Most of the coal produced is exported abroad, which is almost 80% of total coal production in 2015. Chart 26 represents coal export by provinces of company operations. The export of coal (SITC code 321 and 322) originating from Kalimantan Island amounted to 351,000 million kg in 2015 representing 96% of total national coal export in 2015. Export of coal from East Kalimantan amounted to 209,000 million kg (or 57% of the total national coal export) in 2015. Meanwhile, coal export from South Kalimantan amounted to 118,000 million kg (or 32% of total national coal export) in 2015.

Export data by provinces and its commodities in value and volume can be accessed at BPS: <https://www.bps.go.id/publikasi/view/4601>.

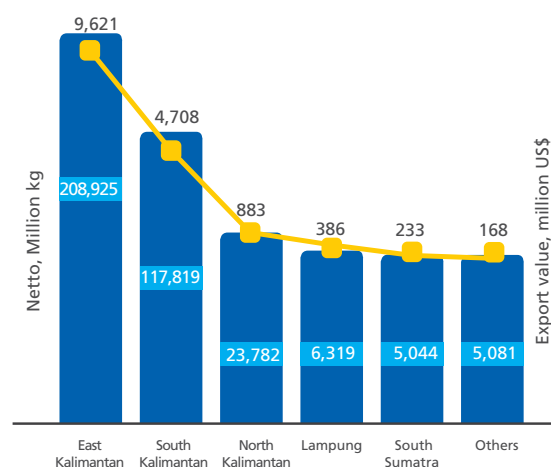
4.8 Significant Exploration Activities

The Implementation Team decides that the definition of a significant exploration project is an exploration project that has proven reserves and will enter the exploitation stage (development).

Oil and Gas Sector

Table 30 represents five significant development projects in terms of the size of the reserves and their scope of work according to SKK Migas annual report 2016. Public can keep up with the latest development of the projects from the most recent official SKK Migas Report, which is Annual Report of SKK Migas at <http://skkmigas.go.id/publications/your-years>.

Chart 26. Coal export by provinces in 2015



Source: Foreign Trade Statistics according to SITC Code 2015-2016, BPS

Mineral and Coal Mining Sector

Exploration mining status data can be accessed in detail based on commodities and provinces on the Geology Agency website, <http://webmap.psdg.bgl.esdm.go.id/geosain/neraca-mineral-strategis.php?mode=administrasi>.

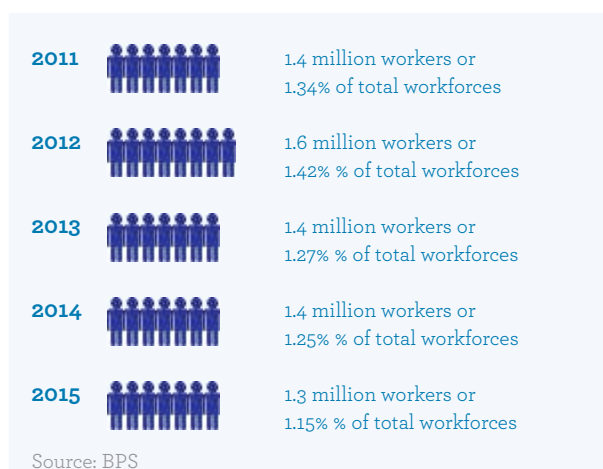
Table 30. Significant oil and gas development projects

Project	Location	First Production	Estimation Production	
IDD project (joint development)	Ganal, Rapak, Makassar Strait and Muara Bakau	2016	Bangka:	110 MMscfd 4000 bopd
		2023	Gehem Hub	420 MMscfd 27000 bopd
		2022	Gendalo Hub	700 MMscfd 20000 bopd
Abadi Inpex Masela	Blok Masela, Arafura Sea, Maluku	2027 *	TBD *	
Tangguh Train - 3	Blok Tangguh, Bintuni, West Papua	2020	700 MMscfd	
			3200 bopd	
Jangkrik field and Jangkrik North East	Blok Muara Bakau, Makassar Strait	2017	450 MMscfd	
			200 bopd	
Madura BD dan MDA-MBH	Blok Madura Strait	2017	Madura BD	110 MMscfd 6600 bopd
		2019	MDA-MBH	175 MMscfd

Source : SKK Migas Annual Report 2016

4.9 Contribution of Extractive Industry to National Employment

Data from Statistics Indonesia (BPS) on this page presents the number of workers in the mining and excavation sectors, which is around 1.3 million people (or 1.15% of the total workforce) in 2015. The small number of workers shows that the extractive industry is a technology-intensive sector. Nevertheless, in some areas the mining sector absorbed quite significant number of workers, see Chart 29.



Working population of 15 years old and above data based on business field can be accessed at <http://www.bps.go.id/linkTableStatis/view/id/970>.

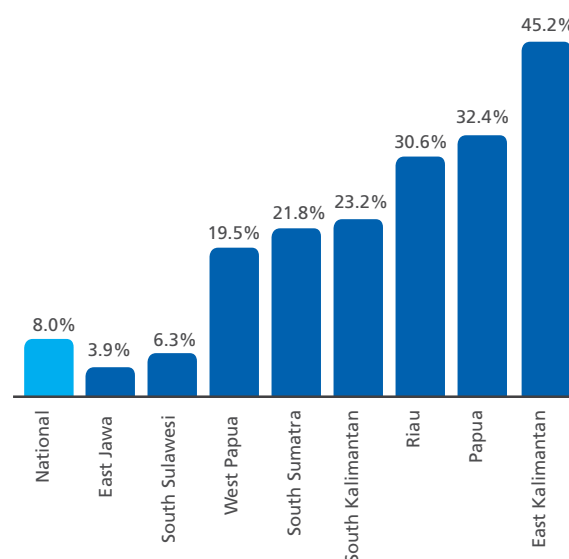
4.10 Contribution of Extractive Industry in the Region (Several Regional Examples)

The mining sector has an important role in the region's economy, especially in mine producing areas. Chart 27 shows that although the mining sector accounts for only about 8% of national GDP, the mining sector can contribute 20-45% of the regional GDP. This role is enhanced by the movements of the followers' sectors (e.g. construction, trade and services) and the emergence of supporting businesses (food and clothing suppliers) in the regional economy. Charts 27 and 28 show that East Kalimantan is the region with the highest natural resources of extractive industry compared to other provinces, indicated by the great contribution of extractive sector and large amount of revenue sharing fund (DBH) received by East Kalimantan Province. Charts 29-30 show the significance of the contribution of the mining sector to producing regions' workforce absorption and regional export.

Local government's direct revenue from the mining sector, such as DBH and retribution can be used for infrastructure development and community welfare improvement. The contribution of extractive industry should not be seen only from the size of the GDP contribution or revenue alone, but also its contribution to sustainable economic development through reducing unemployment, reducing poverty and levelling the income.

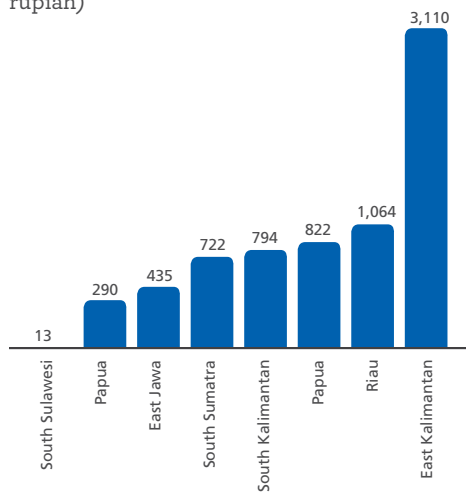
Charts 31-32 show the Gini index and poverty level in the mine-producing areas that vary in relation (either lower or higher) with national ratios. Poverty and inequality rate in some mine-producing areas are still high. However, to draw the conclusion about the relevancy between mining sector contribution and regional welfare, more in-depth study needs to be conducted since there are a lot of factors that need to be considered, among others, inequality of resource ownership, policy in regional development, topology, skill level and other factors.

Chart 27. Contribution of mining and excavation sectors to provincial GDP



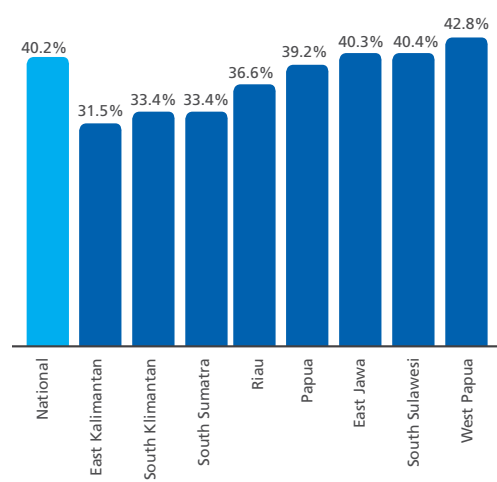
Source: BPS Province, PDRB 2015

Chart 28. Natural resources DBH in 2015 (in billion rupiah)



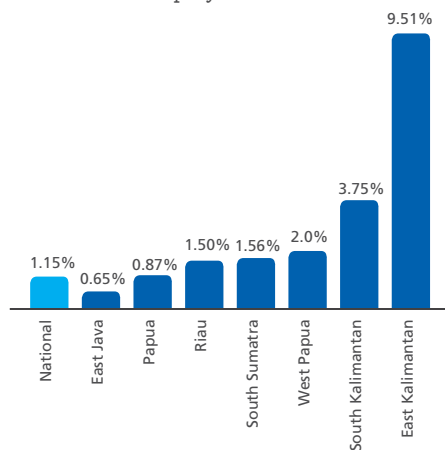
Source: DJPK

Chart 31. Gini index in 2015



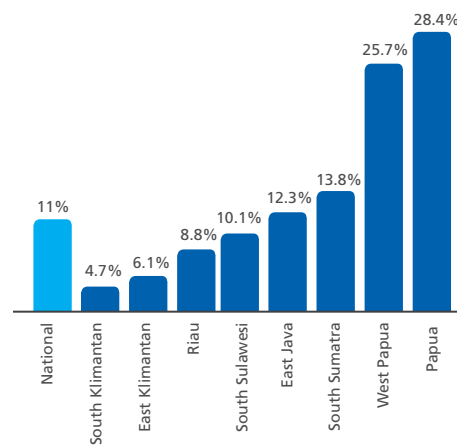
Source: BPS

Chart 29. Contribution of mining and excavation sectors to the employment



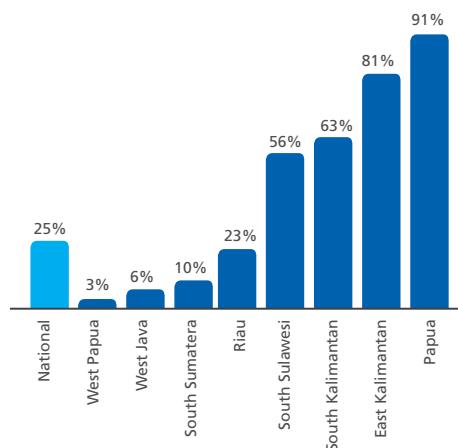
Source: BPS Province

Chart 32. Poverty level in 2015



Source: BPS

Chart 30. Contribution of oil and gas sector and mineral and coal sector to provinces' export



Source: Foreign Trade Statistics, BPS

05 STATE-OWNED ENTERPRISES

THE ROLE OF SOES IS SIGNIFICANT IN THE EXTRACTIVE INDUSTRIES SECTOR IN INDONESIA. PERTAMINA CONTRIBUTES 25% OF THE TOTAL OIL LIFTING AND 18% OF THE TOTAL GAS LIFTING IN 2015. MEANWHILE, MINERAL AND COAL MINING SOES ACCOUNT FOR 6% OF STATE REVENUES FROM MINERAL AND COAL MINING IN 2015.



Based on World Bank research, there are similarities in the motivation of the governments in the world in establishing SOE, among others: providing and improving access to public goods and services, limiting the control of private parties or foreign owners in the domestic economy and promoting development⁶⁶. This is in line with Law no. 19/2003 which stipulates the purpose and objectives of the establishment of SOE in Indonesia, they are:

- to contribute to the national economic growth in general and particularly to state revenue;
- to seek profit;
- to deliver public benefits in the form of the procurement of quality and adequate goods and/or services to fulfil public needs;
- to be the pioneer of business activities that cannot be implemented by the private sector and cooperatives;
- to actively participate in providing guidance and support for small-scale companies, cooperatives and communities.

There are two types of legal entities for SOE, they are Liability Companies (Persero) and Public Companies (Perum). Persero capital is divided into shares in which all or at least 51% of its shares owned by the state for the purpose of making a profit. Perum share capital is owned by the state and is not divided into shares for the purpose of serving the public interest in the form of providing goods and or services. The four SOEs operating in extractive industries are entirely in the form of Persero, namely PT Antam, PT Bukit Asam, PT Timah and PT Pertamina. Three SOEs are listed companies in Indonesia Stock Exchange, namely PT Antam, PT Bukit Asam, PT Timah.

The role of SOEs is significant in the extractive industries sector in Indonesia. Pertamina contributes 25% of the total oil lifting and 18% of the total gas lifting in 2015. Meanwhile, mineral and coal mining SOEs account for 6% of state revenues from mineral and coal mining in 2015.

5.1 Relationship between SOEs and the Government

5.1.1 Authority

An overview of the relationship between SOEs and the central government is presented in Figure 25, illustrating ministerial authority to appoint the directors of a SOE, monitor and formulate technical policies.

- The Minister of SOE serves as a shareholder in a general meeting of shareholders (GMS) held by a liability company and is authorised to handle the SOE's operational/managerial affairs, including appointing directors based on decree of the Minister of SOE.
- The Minister of Finance serves as state asset manager, authorised over public capital as one of SOE funding sources.
- The Minister of Energy and Mineral Resources is authorised to formulate, establish and put in place policies on energy and mineral resources.

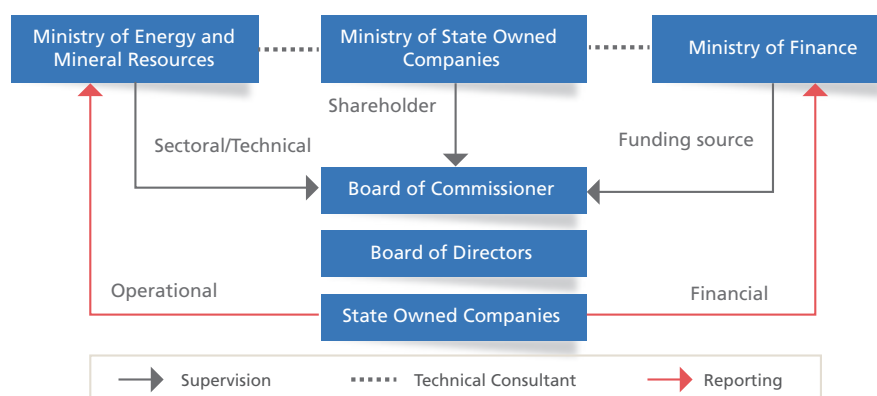
5.1.2 Financial

The Addition of State Equity Participation

The addition and subtraction of state capital participation are proposed by the Minister of Finance to the President based on the initiative of the Minister of Finance, Minister of SOE or Technical Minister. The procedure of state capital participation is regulated in GR No. 44/2005⁶⁷. Each participation and addition to the State Capital Participation with funds derived from APBN must be approved by DPR.

For state equity participation (PMN) in SOEs, the value is presented as a permanent investment in the balance sheet of Central Government Financial Statements. PMNs to state-owned enterprises above 51% are accounted for under the equity method. There is no provision of free equity or carried interest from the addition of state capital participation.

Figure 25. Relationship between state-owned enterprises and government



Sumber: Scoping Study EY

66 PWC. 2015. "State-Owned Enterprises, Catalyst for Public Creation". <https://www.pwc.com/gx/en/psrc/publications/assets/pwc-state-owned-enterprise-psrc.pdf>. Accessed in 15 November 2017

67 Has been partially revised with GR No. 72/2016

The following is the amount of capital participation of the Government of the Republic of Indonesia on Extractive SOEs over the last five years based on the Company's Annual Report:

Table 31. The amount of state equity participation

Item	PT Aneka Tambang (Persero) Tbk	PT Bukit Asam (Persero) Tbk	PT Timah (Persero) Tbk	PT Pertamina (Persero)
	(Million Rp)	(Million Rp)	(Million Rp)	(Million Rp)
Year 2011				
Share value	620,000	749,044	163,574	9,810
% of ownership	65%	65%	65%	100%
Year 2012				
Share value	620,000	749,044	163,574	9,865
The addition of state equity participation				55
% of ownership	65%	65%	65%	100%
Year 2013				
Share value	620,000	749,044	163,574	9,865
% of ownership	65%	65%	65%	100%
Year 2014				
Share value	620,000	749,044	242,053	9,865
% of ownership	65%	65%	65%	100%
Year 2015				
Share value	1,562,000	749,044	242,053	9,865
The addition of state equity participation	3,494,820			
% of ownership	65%	65%	65%	100%

Source: SOEs' Annual Report

Retained Earnings and Payment of Dividends

State-owned companies pay dividends to the government based on the Payout Ratio (POR) – the percentage of net income that state-owned companies pay out as dividends to shareholders. The POR is decided every year in a GMS based on the state-owned company's capability and future projection of capital needs. The POR can also be decided based on proposition from the directors, government policy, proposition from Commission VI of the Indonesian Parliament and a negotiation between the Ministry of SOE and the relevant SOE.

Moreover, Law No. 40/2007 on Limited Liability Companies requires companies to form a general

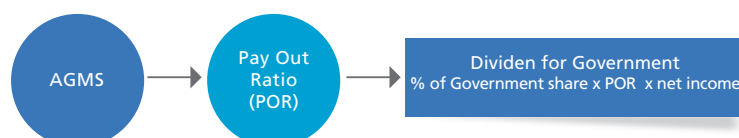
reserve from net income, at least 20% of the amount of issued and fully paid capital.

Dividends must be paid out to the government within one month after they have been decided during the GMS. State-owned companies deposit the dividends into a state account in accordance with the Regulation of the Minister of Finance No. 5/PMK.02.2013.

Government Loan that Forwarded to SOE (Subsidiary Loan Agreement)

For strategic projects, domestic or overseas government borrowings may be lent to SOEs with the criteria and procedures set out in Regulation of the Minister of Finance no. 108 / PMK.05 / 2016.

Figure 26. Mechanism for dividend payout by SOE



Source: DG Budget, Indonesia's State Budget Posture

Audit of SOEs' Financial Reports in 2015 by an Independent Auditor

The four SOEs engaged in the extractive sector have been audited in 2015 by an independent auditor. The public may access the financial reports in the following websites:

Table 32. SOE engaged in the extractive industry

No	Company	Registration Status in the Indonesia Stock Exchange	URL for the audited financial report
1	PT Pertamina (Persero)	Unregistered	http://www.pertamina.com/investor-relations/laporan-presentasi/
2	PT Aneka Tambang (Persero) Tbk	Registered	http://www.antam.com/index.php?option=com_jooget&task=viewcategory&catid=51&Itemid=60
3	PT Bukit Asam (Persero) Tbk	Registered	http://www.ptba.co.id/id/company-report#afr
4	PT Timah (Persero) Tbk	Registered	http://www.timah.com/v3/ina/laporan-laporan-tahunan/

The public can access the financial statements of the SOEs to obtain information on various financial conditions and transactions, such as acquisitions, receivable to government and private parties and short-term and long-term loans from related SOEs.

Corporate Social Responsibility of SOEs Engaged in the Extractive Industry

The Regulation of the Minister of SOE No. PER-09 / MBU / 07/2015 on Partnership and Community Development Programs (PKBL) of SOEs regulates the obligation of state-owned enterprises to implement partnership and community development programs which the source of funds can derive from a maximum allowance of 4% of net profit after tax of the previous year. This ministerial regulation is established to carry out the mandate of Articles 88 and 90 of Law No. 19/2013 concerning SOEs, that is SOEs can set aside some of its net profit for the purposes of small business development and community development around the SOE.

PKBL funds from SOEs are relevant to the EITI standard 2016 requirement 6.1 on social costs.

5.2 PT Pertamina (Persero)

PT Pertamina (Persero) is a merger of two companies: Pertamina and Permina, that was conducted in 1968. In the energy and petrochemicals sectors, the activities of PT Pertamina (Persero) are divided into upstream and downstream activities, and supported by the activities of its subsidiary companies and joint ventures. In 2003, as a result of the release of PT Pertamina (Persero) from its tasks as the regulator of upstream oil and gas industries, based on GR No. 31/2003, PT Pertamina (Persero) became a liability company.

In domestic and international oil and gas business activities, PT Pertamina (Persero) operates alone and in partnership through Operation Cooperation (KSO), a Joint Operation Body (JOB), Technical Assistance Contracts (TAC) and the Indonesia Participating/Pertamina Participating Interest (IP/PPI).

Oil and gas business activities through independent operations are conducted in Pertamina EP's five assets: Asset 1 covering Aceh, North Sumatra and Riau; Asset 2 (South Sumatra); Asset 3 (West Java); Asset 4 (Central and East Java); and Asset 5 (Kalimantan and Papua).

Meanwhile, oil and gas business activities through partnership for working areas in Indonesia in 2015 are conducted with 15 oil and gas partnership projects, 13 Coal Gas Methane (GMB) partnerships, 1 Non-conventional Oil and Gas Partnership (MNK), 7 unitization areas, 22 TAC contracts (7 of which end in 2015), 29 cooperation contracts, 6 IP contracts, 7 JOB-PSC contracts and 2 PPI contracts. Details of PT Pertamina EP's working contracts with partners can be seen in PT Pertamina Annual Report (Persero), see Table 32 for a list of the SOE financial statements websites.

Ownership

PT Pertamina (Persero) is 100% owned by the Government of Indonesia.

Retained Earnings and Dividends

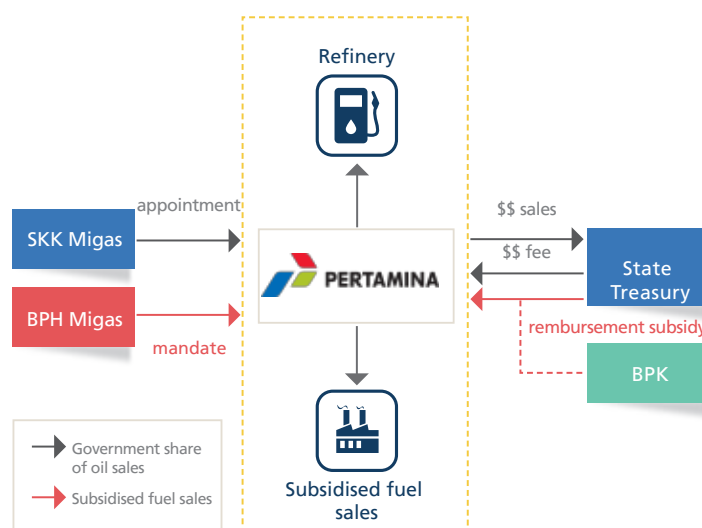
PT Pertamina (Persero) and its subsidiary companies pay out Rp 6.25 trillion in dividends to the government in 2015.

Table 33. Realization of fuel subsidy & LPG 3 kg

Dividend and Retained Earning	2015
Dividends paid out to shareholders	Rp 6,25 triliun
Dividends paid out to the Government	Rp 6,25 triliun
Appropriated retained earnings	USD 3,7 miliar
Unappropriated retained earnings	USD 1,4 miliar

Source: PT Pertamina (Persero) Annual Report 2015

Figure 27. Cash flow of state-owned petroleum sales and fuel subsidies



Mandate of Fuel Subsidy Distribution

The government through the Regulatory Agency for Downstream Oil and Gas (BPH Migas) has mandated Pertamina to distribute subsidised fuel. The mandate has also determined the quota of subsidised fuel that must be distributed based on the state budget or the amendment. Every year, the Supreme Audit Board (BPK) audits the reimbursement of fuel subsidy. Building upon the audit report, the Government pays the reimbursement of the fuel subsidy to Pertamina.

Pertamina's cashflow report 2016 shows that Pertamina received cash from the Government related to subsidies and marketing rewards, in the amount of US\$ 18.4 billion (or Rp 171.9 trillion) in 2014 and US\$ 21.5 billion (or Rp 224.7 trillion) in 2015.

Pertamina's role in Selling the Government Share of Crude Oil/ Condensate

According to BP Migas' guidelines on selling the state's crude oil/condensate share, BP Migas may directly allocate crude oil or condensate to be processed by a domestic refinery. PT Pertamina (Persero) may directly be appointed to sell the state share of crude oil/condensate for domestic refineries' needs based on decree of the Head of BP Migas Number KEP-0131/ BPO0000/2012/S2 dated October 8, 2012.

The government share of lifted oil that matches the specification will be sent to a refinery operated by PT Pertamina (Persero).

Table 34. Realization of fuel subsidy and LPG 3 Kg

No	Product	2015	
		Volume	Billion Rupiah
1	Premium (million kilolitres)	-	-
2	Kerosene (million kilolitres)	0.74	3,053
3	Diesel fuel (million kilolitres)	13.98	13,978
4	3-kg LPG (cubic ton)	5,567,484	30,524
TOTAL			47,555

Source : EITT's Data 2015



Government Loan that Forwarded to PT Pertamina (Persero) and Government Collateral for the Company Loan

Table 35. Loan that forwarded to PT Pertamina (Persero)

Lender	Loan Amount	Loan Purpose	Repayment Period	Interest Rate	Balance as of December 31, 2015
Overseas Economic Cooperation Fund Jepang	¥1.172.872.837	The Development of DPPU Ngurah Rai	May 2007 – November 2024	3,1% per year	¥746.239.253 (US\$6.195)
Japan International Cooperation Agency (“JICA”)	¥26.966.000.000	Lumut Balai Geothermal Power Plant Project	March 2021 – March 2051		¥2.418.323.907 (US\$20.077)
International Bank for Reconstruction and Development (“IBRD”) - World Bank	LA-8082-ID amounted to US\$175.000	Ulubelu and Lahendong Geothermal Clean Energy Investment Project	October 2020 – October 2035		US\$8.580
International Bank for Reconstruction and Development (“IBRD”) - World Bank	LA-TF10417-ID amounted to US\$125.000	Ulubelu and Lahendong Geothermal Clean Energy Investment Project	October 2021 – April 2051		US\$24.906

Source: PT Pertamina (Persero) Annual Report 2015

Revenue from Transportation Services

PT Pertamina (Persero) receives toll fees payments from KKKS, PGN and others for transportation services of oil and gas products through pipes owned by PT Pertamina. In 2015, PT Pertamina (Persero) receives toll fees payments of US\$ 111,755 thousand⁶⁸.

Subsidiary Companies

According to the 2015 financial report, PT Pertamina (Persero) had 25 subsidiary companies, 6 association companies and 6 joint venture entities. Table 36 lists 9 subsidiary companies and 1 joint operation company engaged in the oil and gas exploration and production sectors in Indonesia.

Table 36. The list of subsidiary companies of PT Pertamina (Persero) engaged in the extractive sector

No	Type of Ownership	Company	% of shares (2015)	Sector
1	Direct ownership	PT Pertamina Hulu Energi	100%	Oil and gas exploration and production
2	Direct ownership	PT Pertamina EP	100%	Oil and gas exploration and production
3	Direct ownership	PT Pertamina EP Cepu	100%	Oil and gas exploration and production
4	Direct ownership	Pertamina E&P Libya Limited, British Virgin Island	100%	Oil and gas exploration and production
5	Direct ownership	PT Pertamina East Natuna	100%	Oil and gas exploration and production
6	Direct ownership	PT Pertamina EP Cepu ADK	100%	Oil and gas exploration and production
7	Direct ownership	PT Pertamina Internasional Eksplorasi dan Produksi	100%	Oil and gas exploration and production
8	Direct ownership	Conoco Phillips Algeria Limited, Cayman Island	100%	Oil and gas exploration and production
9	Direct ownership	PT Pertamina Hulu Indonesia	100%	Oil and gas exploration and production
10	Joint operation with indirect ownership	Natuna 2 B.V., Belanda/ Netherlands	50%	Exploration and production

Source: PT Pertamina (Persero) Annual Report 2015

68 EITI's Data 2015

Changes in Ownership of Working Areas in Indonesia During 2015

Table 37 lists acquisition conducted by Pertamina in Indonesia during 2015, the transaction terms are partially available in Pertamina's Annual Report 2015.

Table 37. Changes in ownership of working areas of PT Pertamina (Persero) Tbk

No	Block	Transaction	Participating Interest	Price (in thousand USD)	Remark
1	Blok Mahakam	Acquisition of Participating Interest (PI)	100% and may transfer maximum 30% of PI to Total E & P Indonésie and Inpex Corporation and / or maximum 10% to Local Owned Enterprise to be designated by Local Government	No information	Effective January 1, 2018 with a term of 20 years
2	Blok Offshore North West Java (ONWJ)	Extension of Participating Interest	73.5%	No information	Effective since January 19, 2017 with a term of 20 years
3	Blok Kampar	Acquisition of Participating Interest (PI)	100%	No information	Effective from January 1, 2016 with a term of 20 years
4	Blok NSO	Acquisition of Participating Interest (PI)	100%	No information	Effective since September 30, 2015
5	Blok B	Acquisition of Participating Interest (PI)	100%	No information	Effective since September 30, 2015
6	Blok Nunukan	Addition of Participating Interest (PI)	PI addition of 29.5% to become 64.5%	No information	-
7	Blok Abar	Acquisition of Participating Interest (PI)	100%	No information	Valid for 30 years
8	Blok Anggursi	Acquisition of Participating Interest (PI)	100%	No information	Valid for 30 years
9	Blok MNK Sakakemang	Acquisition of Participating Interest (PI)	50%	No information	Valid for 30 years
10	Blok East Sepinggan	Acquisition of Participating Interest (PI)	15%	USD 10.523	Effective since January 16, 2015

Source: PT Pertamina (Persero) Annual Report 2015

Liquidation of Petral Group

The General Meeting of Shareholders (GMS) of PT Pertamina (Persero) dated July 13, 2015 decided to liquidate the Petral Group and then divert its role related to the procurement of crude oil, fuel and LPG to Integrated Supply Chain (ISC). The liquidation process is still underway at the end of 2015.

Corporate Social Responsibility of PT Pertamina (Persero)

Social responsibility expenses incurred by the company include corporate social responsibility and partnership and community development programmes (PKBL). Table 38 shows the amount of CSR realization of PT Pertamina (Persero) in 2015. More information is available on the official website of PT Pertamina (Persero) (<http://www.pertamina.com/social-responsibility/>).

Table 38. CSR realization of PT Pertamina (Persero)

Activity	2015 (in Billion Rupiah)
Education	52.9
Health	11.5
Environment	14.3
Empowerment	46.2
TOTAL	124.9

Source: PT Pertamina (Persero) Annual Report 2015, p.428

5.3 PT Aneka Tambang (Persero) Tbk

PT Aneka Tambang (Persero) Tbk. was established as a state-owned company in 1968 through a merger of several national mining companies and projects producing one commodity. In 1997, the company publicly offered 35% of its shares in the Indonesia Stock Exchange. In 1999, PT Aneka Tambang (Persero) Tbk. registered its shares in Australia, acquiring the status of a foreign exempt entity which was upgraded to ASX Listing with stricter rules in 2002.



PT Aneka Tambang (Persero) Tbk. is a diversified, vertically-integrated, export-oriented mining company. The company's activities in operation areas rich in minerals throughout Indonesia include nickel ore, ferronickel, gold, silver, bauxite and coal exploration, mining, processing and marketing. Given the vast area of mining concessions and the large numbers of reserves and resources the company has, it has established several joint ventures with international partners to utilise existing reserves through profitable mines.

Ownership

Table 39. The shareholders of PT Aneka Tambang (Persero) Tbk

Shareholder	Share of Ownership (%)
Government of Indonesia	65%
Public	35%

Source: PT ANTAM (persero) Tbk Annual Report 2015

The government had shares in PT Aneka Tambang (Persero) Tbk. in the amount of Rp 1.6 trillion in 2015. The government also had shares called 'dwiwarna' in PT Aneka Tambang (Persero) Tbk, giving the government the power of veto over the appointment and dismissal of directors and commissioners, issuance of new shares, and a merger or liquidation of PT Aneka Tambang (Persero) Tbk.

The Addition of State Equity Participation

In 2015, PT Antam obtains additional state equity participation amounting to Rp3.5 Trillion as stated in Government Regulation No. 73/2015 and additional capital from the public amounting to Rp1.88 Trillion. The addition of capital does not change the composition of share ownership between Government and Public. The additional capital received from the Government will be used by PT Antam to build the Feronikel Haltim Plant covering the construction of processing and refinery facilities as well as supporting infrastructure. Meanwhile, additional capital from the public will be used by the company to finance working capital.

Retained Earnings and Dividends

PT Antam does not pay dividends in 2015 due to financial losses in 2014 as a result of nickel prices.

Table 40. Retained Earnings and Dividends Payout by PT Aneka Tambang (Persero) Tbk.

Dividend and Retained Earning	2015
Dividends paid out to shareholders	-
Dividends paid out to the Government	-
Dividends paid out to other shareholders	-
Appropriated retained earnings	Rp 11,6 trillion
Unappropriated retained earnings	(Rp 2 trillion)

Source: PT ANTAM (Persero) Tbk Annual Report 2015

Guaranteed lendings from the Government and guarantees from PT Aneka Tambang (Persero) for other companies

PT Aneka Tambang (Persero) Tbk. does not have guaranteed lendings from the government, nor does it provide guarantees for other companies.

Subsidiary Companies

According to the annual report 2015 of PT Aneka Tambang (Persero) Tbk, the company has a number of subsidiary companies working in the extractive sector. Those subsidiary companies are:

Table 41. The list of subsidiary companies of PT Aneka Tambang (Persero) Tbk engaged in the extractive sector

No	Type of Ownership	Company	% of shares (2015)	Sector
1	Direct ownership	Indonesia Coal Resources	100%	Coal exploration and mining operator
2	Direct ownership	PT Antam Resourcindo	99,98%	Exploration and mining operator
3	Direct ownership	PT Dwimitra Enggang Khatulistiwa (not yet commercially operated)	99,5%	Exploration and mining operator
4	Direct ownership	PT Cibaliung Sumberdaya	99,15%	Exploration, mining construction and development, mining, production, processing and refining, transportation and sales in the gold industry
5	Indirect ownership	PT GAG Nikel Indonesia (not yet commercially operated)	100%	Exploration and mining operator
6	Indirect ownership	PT Citra Tobindo Sukses Perkasa	100%	Coal exploration and mining operator
7	Indirect ownership	PT Jatim Arindo Persada (not yet commercially operated)	100%	Coal exploration and mining operator
8	Indirect ownership	PT Antam Niterra Haltim (not yet commercially operated)	100%	Coal exploration and mining operator
9	Association	PT Nusa Halmahera Minerals	25%	Gold mining
10	Association	PT Nikel Halmahera Timur	50%	Nickel mining

Source: PT ANTAM (Persero) Tbk Annual Report 2015

Changes in Ownership (Acquisition and Divestment) in 2015

According to the annual report 2015 of PT Aneka Tambang (Persero) Tbk, ANTAM does not conduct any divestment and acquisition in 2015.

Corporate Social Responsibility (CSR) of PT Aneka Tambang (Persero) Tbk.

PT Aneka Tambang (Persero) Tbk. implements partnership and community development program (PKBL) with a view to help the government achieve more equitable development and improve people's welfare.

Partnership and community development program realization of PT Aneka Tambang (Persero) Tbk. in 2015 is as follows:

Table 42. PKBL realization of PT Aneka Tambang (Persero) Tbk

Activity	2015 (in Billion Rupiah)
Community Relation	12
Community Services	0.1
Community Empowerment	22
Infrastructure Development	33
Environmental Management	1.4
TOTAL	68.5

Source: EITI's Data 2015

5.4 PT. Bukit Asam (Persero) Tbk

Historically, coal mining by PT. Bukit Asam (Persero) Tbk in Tanjung Enim began in the Dutch colonial period, in 1919, using an open pit mining method in its first operational area: the Air Laya Mine. From 1923 the company adopted the underground mining method until 1940, and started to produce for commercial purposes in 1938. After the Dutch colonisation, the mine was nationalised. In 1950, the Government of the Republic of Indonesia legalised the establishment of Tambang Arang Bukit Asam State Company (PN TABA).

In 1981, PN TABA became a limited liability company named PT Tambang Batubara Bukit Asam (Persero) Tbk. To improve the development of coal industry in Indonesia, in 1990 the government decided to merge Perum Tambang Batubara with the company. In line with the national energy security development programme, in 1993 the government assigned the company to develop coal briquettes. On 23 December 2002, the company registered itself as a public company in the Indonesia Stock Exchange under the code "PTBA".



Ownership

Table 43. The shareholders of PT. Bukit Asam (Persero) Tbk

Shareholder	Share of Ownership (%)
Government of Indonesia	65,02%
Domestic public	24,35%
Foreign public	10,63%

Source: PT. Bukit Asam (Persero) Tbk Annual Report 2015

As a shareholder, the Government also has a golden share, called a 'dwiwarna' share, giving them the power of veto. The government has approximately Rp 750 billion in shares.

Retained Earnings and Dividends

Table 44. Retained Earning and Dividend Payout by PT. Bukit Asam (Persero) Tbk

Dividend and Retained Earning	2015
Dividends paid out to Shareholders	Rp 705.7 million
Dividends paid out to the Government	Rp 486.2 million
Dividends paid out to other Shareholders	Rp 219.5 million
Appropriated retained earnings	Rp 8.6 trillion
Unappropriated retained Earnings	Rp 1.6 trillion

Source: PT. Bukit Asam (Persero) Tbk Annual Report 2015

Guaranteed Lendings from the Government and Guarantees from PT Bukit Asam (Persero) Tbk. for Other Companies

In 2015, PT. Bukit Asam (Persero) Tbk. did not have guaranteed lendings from the government, nor did it provide guarantees for other companies.

Payment for Transportation Service

PT Bukit Asam (Persero) Tbk makes payments to PT Kereta Api Indonesia (Persero) for coal transportation services. Payment made by PT Bukit Asam (Persero) Tbk for transportation services in 2015 is Rp. 1.7 trillion and USD 72.3 million⁶⁹.

Subsidiary Companies

The annual report 2015 specifies the subsidiary companies of PT. Bukit Asam (Persero) Tbk. engaged in the extractive sector. They are as follows:

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Table 45. Subsidiary companies of PT. Bukit Asam (Persero) Tbk. engaged in the extractive sector

No	Type of Ownership	Company	% of shares (2015)	Sector
1	Direct ownership	PT Batubara Bukit Kendi (Not Operating)	75%	Coal mining
2	Direct ownership	PT International Prima Coal	51%	Coal mining
3	Direct ownership	PT Bukit Asam Banko (Not Operating)	65%	Coal mining
4	Direct ownership	PT Bukit Asam Metana Ombilin (Not Operating)	99,99%	Methane gas mining
5	Direct ownership	PT Bukit Asam Metana Enim (Not Operating)	99,99%	Methane gas mining
6	Direct ownership	PT Bukit Asam Metana Peranap (Not Operating)	99,99%	Methane gas mining
7	Indirect ownership	PT Tabalong Prima Resources (At the Development Stage)	34,17%	Mining

Source: PT. Bukit Asam (Persero) Tbk Annual Report 2015

The complete list of subsidiary and association companies of PT. Bukit Asam (Persero) Tbk. is available in Annual Report 2015 of PT. Bukit Asam (Persero) Tbk.

Changes in Ownership (Acquisition and Divestment) in 2015

According to the Annual Report 2015 of PT Bukit Asam (Persero) Tbk., in May 28, 2015, a subsidiary of PT. Bukit Asam (Persero) Tbk, PT Internasional Prima Coal acquired PT Tabalong Prima Resources that own coal resources of 292 million tons and reserves of 109 million tons.

Corporate Social Responsibility (CSR) of PT. Bukit Asam (Persero) Tbk

The company's CSR programmes include partnership and community development program (PKBL) comprising community development and area development programmes.

The CSR realization of PT. Bukit Asam (Persero) Tbk. integrated into its partnership and community development program (PKBL) in 2015 is as follows:

Table 46. PKBL realization of PT. Bukit Asam (Persero) Tbk

Activity	2015 (in Billion Rupiah)
Community Relation	0.8
Community Services	0.0
Community Empowerment	12
Infrastructure Development	3
Environmental Management	1
TOTAL	16.8

Source: EITI's Data 2015

More information on social responsibility activities implemented by PT Bukit Asam (Persero) Tbk. is accessible at <http://www.ptba.co.id/en/csr>.

5.5 PT Timah (Persero) Tbk

PT Timah (Persero) Tbk. was established in 1976, based in Pangkalpinang, Bangka, and has been a publicly listed company in the Indonesia Stock Exchange (BEI) since 1995. PT Timah (Persero) Tbk. is the largest tin producer in Indonesia, integrated into exploration, mining, processing, smelting and marketing operations. Moreover, PT Timah (Persero) Tbk. is the largest tin exporter in the world that is located in Bangka Belitung Province.

The permissible mining sites of PT Timah (Persero) Tbk. include Bangka Belitung and Riau Islands, with a number of secondary operations taking place in South Kalimantan, Southeast Sulawesi, Banten and Jakarta.

Ownership

Table 47. The shareholders of PT Timah (Persero) Tbk

Shareholders	Share of Ownership (%)
Government of Indonesia	65%
Public	35%

Source: PT Timah (Persero) Tbk Annual Report 2015

The government has a golden share, called 'dwiwarna', allowing the government to have privileges in strategic decision making processes. The shares that the government had is around Rp 242 billion in 2015.

Retained Earnings and Dividends

Table 48. Retained earnings and dividend payout by PT Timah (Persero) Tbk

Dividend and Retained Earning	2015
Dividends paid out to shareholders	Rp 191,4 million
Dividends paid out to the Government	Rp 124,4 million
Dividends paid out to other shareholders	Rp 67 million
Appropriated retained earnings	Rp 4,6 trillion
Unappropriated retained earnings	Rp 536 million

Source: PT Timah (Persero) Tbk Audited Financial Statements 2015

Guaranteed Lendings from the Government and Lending Guarantees for Other Companies

PT Timah (Persero) Tbk. does not have lending collateral from the government, nor has it been a guarantor for other companies, as mentioned in the company's audited financial statements 2015.

Subsidiary Companies

The company's annual report 2015 specifies the company's subsidiary companies engaged in the extractive sector. They are as follows:

Table 49. Subsidiary companies of PT Timah (Persero) Tbk. engaged in the extractive sector

No	Type of Ownership	Company	% of Shares (2015)	Sector
1	Direct ownership	PT Timah Investasi Mineral (TIM)	99,9%	Exploration and mining of non-tin minerals and coal marketing
2	Direct and indirect ownership through PT TIM	PT Tanjung Alam Jaya	PT Timah (Persero) Tbk dan PT TIM masing-masing sebesar 50%	Coal mining
3	Indirect ownership through PT TIM	PT Truba Bara Banyu Enim (TBBE)	99,8%	Coal mining
4	Direct ownership	PT Koba Tin	25%	Tin mining

Source: PT Timah (Persero) Tbk Annual Report 2015



Mining Concessions of PT Timah in Indonesia in 2015

Mining concessions of PT Timah (Persero) Tbk in Indonesia in 2015 can be seen in Annual Report 2015 of PT Timah (Persero) Tbk.

Changes in Ownership (Acquisition and Divestment) in 2015

According to Annual Report 2015 of PT Timah (Persero) Tbk., PT Timah (Persero) does not conduct any acquisition and divestment in 2015.

Corporate Social Responsibility (CSR) of PT Timah (Persero) Tbk.

A manifestation of the company's concern over the environment, through particularly facility and infrastructure, education, training, religion, sport and other social programmes, integrated into partnership and community development program (PKBL) and Corporate Social Responsibility (CSR) program.

The PKBL realization of PT Timah (Persero) Tbk in 2015 is as follows:

Table 50. PKBL realization of PT Timah (Persero) Tbk.

Activity	2015 (in billion rupiah)
Community Relation	4
Community Services	-
Community Empowerment	8
Infrastructure Development	14
Environmental Management	-
TOTAL	26

Source: EITI's Data 2015

5.6 Plan of Oil and Gas SOEs and Mining SOEs Holding

The government plans to establish a holding company for the sake of achieving efficiency and synergy, as well as increase the value of SOE assets that can increase the ability of SOEs for independent funding. Six state-owned holding companies will be established based on the following sectors: oil and gas, mining, toll roads, financial services, housing and food.

The government has issued GR No. 72/2016 regarding the amendment to GR No. 44/2005 on the Procedures of State Capital Participation and Administration in State-Owned Enterprises and Limited Liability Companies as a step of SOE holding establishment. In this regulation, the transfer of SOE shares in the framework of the formation of SOE holding is no longer through the mechanism of APBN because the government's shares in state-owned enterprises are state-separated assets. Further, based on the GR, if the state-owned shares in SOE are transferred into state-owned shares in other state-owned enterprise resulted in most of the shares owned by the other state-owned enterprise, then the SOE becomes a subsidiary of the state-owned enterprise.

Related to the extractive industry, the holding of oil and gas SOEs is a combination between PT Pertamina (Persero) and PT Perusahaan Gas Negara (PGN) with the purposes to i) synergize of capital cost due to the consolidation of infrastructure, ii) avoid the problem of gas allocation conflict which often happened between Pertamina and PGN and iii) realize the price uniformity scheme. The holding of mining SOE consists of PT Inalum (Persero), PT Aneka Tambang (Persero) Tbk, PT Timah (Persero) Tbk and PT Bukit Asam (Persero) Tbk. The objectives of the mining SOEs holding are: i) to take control the mineral reserves and resources by seeking funding to acquire mining companies that already in production stage, ii) to increase product downstream through investment cooperation with global mining companies.

On November 29, 2017, the Ministry of State-Owned Enterprises, together with PT Aneka Tambang Tbk, PT Timah (Persero) Tbk and PT Bukit Asam (Persero) held an Extraordinary General Meeting of Shareholders (EGM) with the agenda of the articles of association amendment since the majority ownership has changed from the Republic of Indonesia to PT Inalum (Persero). As for oil and gas SOE holding offered by the Ministry of SOEs has also been through the finalization stage that begins with the acquisition of Pertagas (a subsidiary of Pertamina) conducted by PGN and then all PGN shares owned by the Government will be transferred to Pertamina through an inbreng scheme. Pertamina will become the holding company while PGN becomes a subsidiary of Pertamina.

SOE holding members are treated equally with SOEs for strategic matters so that the state retains control over the holding company⁷⁰, either directly through dwiwarna shares or indirectly through PT Inalum (Persero) / PT Pertamina (Persero) which is 100 % of its shares are owned by the state.

The establishment of the holding company is not without public debate. Several matters below are still public concerns, among others:

- Harmonization with the revision plan of oil and gas law, because upstream oil and gas institution is planned to be directed through the establishment of oil and gas SOE holding⁷¹;
- The performance of SOE holding cannot meet the expectation of the government to seek funding for expansion because it combines all SOEs even SOE with unhealthy financial performance⁷².



⁷⁰ Kementerian BUMN. 2017. "Siaran Pers: Holding Tambang Sesuai Jadwal". <http://www.bumn.go.id/berita/1-Siaran-Pers-Holding-Tambang->. Accessed in 30 November 2017

⁷¹ Pinsent Masons - Indonesia new Gross Split PSC, Reforminer, Quarterly Energy Notes, April 2017

⁷² Gatra.com. 2017. "Pembentukan Holding BUMN Sektor bisa Memunculkan Masalah Baru". <https://www.gatra.com/ekonomi/makro/291429-pembentukan-holding-bumn-sektoral-bisa-memunculkan-masalah-barurefor>. accessed in 30 November 2017

06

ENVIRONMENTAL AND SOCIAL RESPONSIBILITIES

Companies engaged in the extractive industry have environmental and social responsibilities as regulated in various laws, government regulations and ministerial regulations. Related to those responsibilities, companies working in the extractive industry are required to provide funding for environmental restoration and reclamation.

In the oil and gas sector, such funding is called the Abandonment and Site Restoration (ASR) Fund, while in the mineral and coal sector, it is called the Reclamation Guarantee Fund. Additionally, extractive-sector companies may implement a programme to fulfil the companies' social and environmental responsibilities, known as the Corporate Social Responsibility (CSR).

6.1 Corporate Social Responsibility (CSR)

The government expects mining companies to contribute in improving the welfare of local communities. Obligations in social responsibility and community development are expected to achieve this expectation. CSR programs as mandated by the Law are to increase the economic resilience and community welfare.

The types of CSR programs and the minimum amount of funds required are not regulated in detail in various regulations related to CSR, see subsection 2.4.5 of the Laws and Other Regulations Related to Extractive Industries in the section of CSR regulations. In general, CSR programs consist of social responsibility or the empowerment of local communities around the mining site and environmental responsibility. The following types of CSR programs are generally implemented by mining companies:

Table 51. Type of CSR Programmes

Type	Content
Infrastructure	Road construction, water supply improvement, construction of social buildings, such as: sport hall, government hall, mosque/church, rural electricity facilities.
Economy	Small business assistance, micro capital assistance, seedlings or livestock assistance.
Education	Scholarships, teacher training, teaching aids, cultural programs.
Health	Aid supplies of medicines, surgical aid, campaigns and health education, construction of health centers.
Environment	Environmental education, environmental conservation campaigns, waste management
Donation	Disaster donations, donations of religious activities, provision of revolving funds, corporate loan facilities for community activities.

Source: <https://im4dc.org/wp-content/uploads/2013/09/Mining-and-Development-in-Indonesia.pdf>

Amount of Funds

Companies not performing CSR obligations may be subject to administrative sanctions (e.g. as regulated by Article 110 of GR No. 23/2010). However, the amount of CSR is not regulated by the Government. Therefore, private companies generally have allocation rules of funds for CSR. Meanwhile, allocation of CSR fund for SOEs is clearly regulated, that is maximum 4% of profit of the previous year.

Table 52. Amount of money spent by reporting companies for CSR activities

Activity	Mineral and Coal			Oil and Gas		TOTAL
	Reported in Rupiah	Reported in USD		Reported in USD		
	Rupiah (in million)	USD (in thousand)	Rupiah (in million)	USD (in thousand)	Rupiah (in million)	USD (in thousand)
Community Relation	120,863	33,044	442,525	4,208	56,354	619,742
Community Services	51,549	28,313	379,168	238	3,187	433,904
Community Empowerment	145,784	27,534	368,735	6,380	85,441	599,960
Infrastructure Development	177,974	15,414	206,424	4,586	61,416	445,814
Environmental Management	12,548	304	4,071	1,335	17,878	34,497
TOTAL	508,718	104,609	1,400,924	16,747	224,276	2,133,918

Note: 1 USD = Rp. 13,400

Source: EITI's Data 2015

Table 52 is a summary of the amount of CSR funds reported in the EITI 2015 reporting form. Based on these data, CSR funds generated from oil and gas companies are much smaller than the CSR funds generated from mineral and coal companies, which is understandable since in general the mineral and coal mining area is wider than the oil and gas mining area and involve more surrounding communities in operational activities. The largest contributor of CSR funds in mineral and coal sector is PT Freeport, which contributes 60% of total reported CSR Funds in mineral and coal sector. The second largest contributor is Newmont, which contributes 9% of total reported CSR Funds in mineral and coal sector. Details of each company's CSR amount included in the scope of this report can be seen in the EITI Reconciliation Report in Table 30 / Appendix 5.1 for the oil and gas sector and Table 35 / Appendix 5.3 for mineral and coal sector.

Implementation and Supervision

There is no uniformity in the definition of social responsibility stated in regulations issued by the central and local governments. This matter leads to different types of CSR activities depending on the company's business strategy. CSR activities are mostly carried out by international companies and large Indonesian companies. The concept of CSR is still seen as a form of social⁷³ assistance or donations to pursue short-term goals such as for the community to accept the company's operations. In addition, for the government, especially the local government, conducting supervision is difficult because there is no clear legal and technical regulation of how the local government should oversee the CSR activities.

The Regulation of the Minister of EMR No. 41/2016 is expected to reduce the uncertainty of the CSR programs, especially in the mineral and coal sector. This regulation requires the Governor to create a Community Development and Empowerment blueprint to align company CSR programs with government development policies. CSR activities will be directed to improve the conditions and quality of socio-economic life, including community relations, community services and community empowerment. However, it does not mean that the Company is expected to take on the government's responsibility. The role of the company is to support the government development policies. It is expected that with this regulation, the supervision from the central and local governments will be better and consistent.

6.2 Oil and Gas Mining: Abandonment and Site Restoration Fund (ASR Fund)

Upon the expiration of upstream oil and gas production activities, the remaining production facilities and other supporting facilities and damaged environments can be hazardous for other activities and for the surrounding communities. Therefore, the KKS Contractor is required to perform Abandonment and Site Restoration upon the cessation of production.

The KKS Contractor is required to prepare an ASR fund reserve report of each field within a working area and submit to the Risk Management and Taxation Division. The scope of the report includes, among other things, the ASR activity plan, ASR cost estimation calculations and ASR fund reserves each semester.

Amount of Funds

ASR fund reserves are made by the contractor every semester by depositing funds in USD into a Joint Account. ASR fund reserves can be calculated as follows:

ASR Fund allocated for certain year
$\frac{\text{Estimated ASR Cost} + \text{Adjustment} - \text{ASR Fund Balance}}{\text{Remaining time needed to collect ASR fund}}$

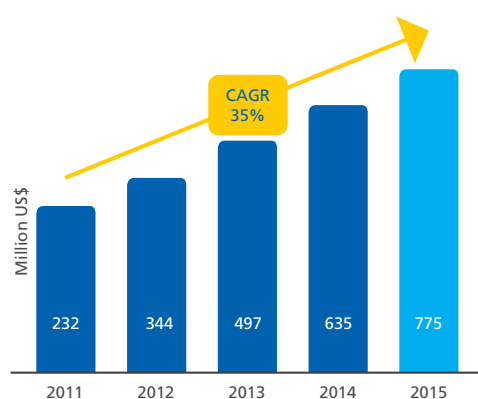
Explanation:

Estimated ASR Cost: Estimated ASR cost based on last evaluation.

Adjustments: Adjustment values resulting from asset changes and estimated ASR cost changes.

The ASR Fund will be placed on a joint account within the managing bank that has been established through an agreement between SKK Migas and KKS Contractor. Every semester, SKK Migas will send ASR fund invoice to KKS Contractor based on cost estimation calculation and ASR fund reserve. The placement of ASR funds shall be done no later than 30 days after the date of the invoice. Until 2015, ASR funds collected in bank accounts amounted to US\$ 775 million with details: i) Bank Negara Indonesia amounting to US\$ 269 million, ii) Bank Rakyat Indonesia amounting to US\$ 254.8 million, iii) Bank Mandiri of US\$ 251 million. SKK Migas has the authority to manage ASR funds and must report to the government in accordance with Oil and Gas Law.

Chart 33. ASR Funds Statistic



Source: SKK Migas Annual Report 2015

⁷³ MVO Netherlands. 2016. "Country Scan CSR Indonesia" <https://mvonederland.nl/sites/default/files/media/Country%20Scan%20Indonesia%2C%20v2.2.pdf>. Accessed in 15 November 2017

Implementation and Supervision

To implement ASR activities, the KKS Contractor shall propose the ASR implementation proposal to the Deputy of Operation Control of SKK Migas no later than 2 years before the execution time. However, ASR implementation for some production installations or other supporting facilities may also be proposed no later than 6 months in advance.

KKS Contractor may apply for the disbursement of ASR funds after the implementation of ASR activities by submitting a Joint Instruction Letter (SIB) along with invoice documents, Official Record of Work Completion signed by the parties concerned and ASR Implementation Agreement.

Based on the Supreme Audit Board (BPK) audit on the SKK Migas Financial Statement 2015, SKK Migas does not recognize any receivable from the ASR bill which has not been paid by 8 KKS Contractors totaling Rp 72,3 billion. SKK Migas requested the 8 PSC Contractors to settle the ASR reserve bill and has been paid Rp 48,3 billion.

6.3 Mineral and Coal Mining: Reclamation and Post-Mining Guarantees

Mineral and coal mining companies are required to provide two types of guarantees: reclamation (exploration and production operations) and post-mining guarantees, pursuant to the Regulation of the Minister of EMR No.7/2014.

1. The provision of the reclamation guarantee in the exploration stage is regulated by the DG Mineral and Coal on behalf of the minister, governor, or regent/mayor in accordance with their respective authority. The guarantee should be provided fully and specified in the work plan and budget (WP&B) for initial exploration. After the WP&B has been approved by the DG Mineral and Coal, the IUP/IUPK-exploration license holder must deposit the guarantee in the form of a time deposit no later than 30 days since the WP&B was approved. The time deposit should be made into a joint account co-opened by the DG Mineral and Coal, the relevant governor or regent/mayor according to their authority, and the relevant exploration license holder in a public sector bank.
2. The reclamation guarantee in the production operation stage for the first five years must be provided fully for five years. However, if the mine's life span is less than five years, this reclamation guarantee should be provided for the life span of the mine. Similar to the reclamation guarantee in the exploration stage, this guarantee is regulated by the DG Mineral and Coal

on behalf of the Minister, the authorised governor or regent/mayor and should be specified in the annual WP&B for production operations. This guarantee may be provided in the form of:

- a. A deposit into a joint account co-opened by the DG Mineral and Coal, the relevant governor or regent/mayor and the relevant IUP/IUPK-production operation license holder in a public sector bank;
 - b. A time deposit into an account co-opened by the DG Mineral and Coal, the relevant governor or regent/mayor and the relevant IUP/IUPK-production operation license holder in a public sector bank;
 - c. A bank guarantee issued by a public sector bank or national private sector bank in Indonesia;
 - d. An accounting reserve if the IUP/IUPK-production operation license holder is listed in the Indonesia Stock Exchange (with traded shares of more than 40%) and has US\$ 50 million in paid-up capital.
3. The Post-Mining Guarantee must be fully collected within two years before going to the post-mining stage. The post-mining guarantee is provided in the form of a time deposit made into an account co-opened by the DG Mineral and Coal, the authorised governor or regent/mayor, and the relevant IUP/IUPK-production operation license holder in a public sector bank. The amount that should be provided is decided by the DG Mineral and Coal on behalf of the Minister and the relevant governor or regent/mayor according to their authority.

The Regulation of the Minister of EMR No. 2/2013 on The Monitoring of Mining Business Management by Provincial and Regency/City Governments stipulates that in order to obtain a people's mining license (IPR), reclamation and post-mining plans should be made based on environmental documents, pursuant to laws and regulations.

Amount of Funds

There is no publicly accessible list on the total amount of reclamation guarantee funding that has been deposited, made available by either the DG Mineral and Coal or local governments.

Table 53 shows the amount of reclamation and post-mining guarantees reported by reporting mineral and coal companies. The detail of amounts reported by each company can be seen in Appendix 3.1 EITI Reconciliation Report 2015.

Table 53. Summary of reclamation guarantee and post-mining fund from EITI reporting companies 2015

Type of Fund	Reported in Rupiah	Reported in USD		TOTAL
	Rupiah (in Million)	USD (in Thousand)	Rupiah (1 USD = Rp. 13.400)	Rupiah (in Million)
Reclamation Guarantee	389,432	61,584	824,733	1,214,165
Post-Mining Fund	49,837	12,710	170,212	220,049
TOTAL	439,269	62,855	994,945	1,434,214

Source: EITI's Data 2015

Implementation and Supervision

In the second semester of 2016, BPK examined the effectiveness of reclamation guarantee and post-mining fund management at East Kalimantan Provincial Government and Kutai Kertanegara Regency. The examination found the following problems: i) not all Mining Business Licenses (IUPs) in Kukar Regency have placed reclamation guarantees in the form of demand deposits, time deposits or bank guarantees; ii) supervision of the implementation of reclamation activities conducted by the Mining and Energy Office of East Kalimantan Province and the Mining Inspector has not been conducted through the reporting and evaluation system and field review. Furthermore, BPK gives recommendation to the Governor of East Kalimantan to: i) establish a placement of guarantee for reclamation in the form of deposit / bank guarantee for the guarantee of reclamation conducted by IUP holders deposited in joint account; ii) order the Head of Mining and Energy Office of East Kalimantan Province to discipline the IUP holders to carry out the reclamation in accordance with the approved reclamation plan.

6.4 People's Mining

There are a lot of communities in mining areas whose economies depend on small-scale mining operations that are carried out by artisanal as well as with the help of machine tools. The definition of Artisanal and Small-Scale Mining (ASM) is largely a mining activity carried out individually, in groups, by families or cooperatives in a traditional and minimal or non-technological manner⁷⁴.

Law No. 4/2009 on Mineral and Coal does not recognize ASM but regulates the People's Mining to accommodate the legality of traditional mining undertaken by the people. People's Mining must be done in the People's Mining Area and get the People's Mining Business License (IPR).

Criteria for determining People's Mining Area (WPR) – Law of Mineral and Coal 2009	<ul style="list-style-type: none"> a. holding secondary mineral deposits found in the river and/or between the side and the riverbank; b. holding primary metal or coal deposits at a maximum depth of 25 (twenty-five) meter; c. terrace sediment, flood plain, and ancient river sediment; d. the maximum area of WPR is 25 (twenty-five) hectares; e. mentioning the type of commodity to be mined ; and/or f. being an area or place of people's mining activities carried out for at least 15 (fifteen) years.
Requirements of People's Mining License (IPR) – Law of Mineral and Coal 2009	<ul style="list-style-type: none"> 1. The area of mining for 1 (one) IPR that can be granted to: <ul style="list-style-type: none"> • An individual shall be a maximum of 1 (one) hectare; • a group of individuals shall be a maximum of 5 (five) hectares; and/or • a cooperative shall be a maximum of 10 (ten) hectares. 2. IPR shall be issued for a maximum period of 5 (five) years and can be extended.

⁷⁴ IIED. 2003. "Artisanal and Small Scale Mining". <http://pubs.iied.org/pdfs/9268IIED.pdf> accessed in 15 November 2017

Procedures of Granting People's Mining License (IPR), Article 48 of GR No. 23/2010	<ol style="list-style-type: none"> 1) Administrative requirements <ol style="list-style-type: none"> a. an individual shall include at least: <ol style="list-style-type: none"> 1. letter of application; 2. a resident identification card; 3. information about mining commodities for which an application is submitted; and 4. a certificate from the local office of urban administrative division/office of rural administrative division. b. a community group shall include at least: <ol style="list-style-type: none"> 1. letter of application; 2. information about mining commodities for which an application is submitted; and 3. a certificate from the local office of urban administrative division/office of rural administrative division. c. a local cooperative shall include at least: <ol style="list-style-type: none"> 1. a letter of application; 2. a taxpayer identification number; 3. a deed of establishment of the cooperative that has been validated by the competent official; 4. information about mining commodities for which an application is submitted; and 5. a certificate from the local office of urban administrative division/office of rural administrative division. 2) Technical requirements shall be a statement that sets forth at least: <ol style="list-style-type: none"> a. shafts for IPR not exceeding 25 (twenty-five) meters in depth; b. use of mechanical pumps, retorting or machinery with total power of not more than 25 (twenty-five) horsepower for 1 (one) IPR; and c. no use of heavy equipment and explosives. 3) Financial requirement shall be the previous year's financial statement and shall be required only for local cooperatives.
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6.4.1 Illegal Mining (PETI)

Illegal mining is generally carried out by people with simple equipment and unlicensed, not environmentally and safety oriented. However, it does not rule out the possibility that large mining companies will undertake illegal mining, such as mining in protected forest areas. This section focuses more on illegal mining discussions conducted by the community. Illegal mining (PETI) has minimal supervision from the government and endanger the environment and health, endanger the safety of miners and prone to landslides. In addition, PETI resulted in reduced state revenues from mineral and coal sector, mineral resources wastage and creating an unfavorable investment climate. There has been

no official release from the government which is the result of an adequate study of how much the state losses from PETI.

PETI is an act that is categorized as criminal and may be punished with imprisonment of 10 (ten) years and a fine of not more than Rp 10,000,000,000. (ten billion rupiah) (Article 158 of Law No. 4/2009 on Mineral and Coal).

To cope with PETI, some researchers and observers of PETI agree if PETI is a complex problem that requires an integrated solution with due consideration to social, economic and legal conditions. Consistency of law enforcement is necessary but supervision and guiding approach is preferred⁷⁵. The government is expected to supervise and improve the capacity of mining communities regarding the implementation of good mining practices. Furthermore, the Government is expected to accommodate illegal miners by cooperation between mining companies and people's mining in certain areas or by involving Local Owned Enterprises that can employ miners⁷⁶.

Figure 28. Character of illegal miners

Aspect of Modality	<ul style="list-style-type: none"> • Low level of human resources and skill • Low level of social - economy • Conservative perception
Aspect of Institutional	<ul style="list-style-type: none"> • No work organization • No economic organization
Aspect of Technology/ Environmet	<ul style="list-style-type: none"> • Excavation techniques are unsafe and unhealthy • Inefficeint processing techniques • Poor waste handling

Source: <http://iesr.or.id/files/Pertambangan%20Ilegal%20di%20Indonesia.pdf>

⁷⁵ Redi, Ahmad. 2016. "Dilema Penegakan Hukum Penambang Mineral dan Batubara Tanpa Izin pada Pertambangan Skala Kecil". <http://rechtsvinding.bphn.go.id/artikel/ART%207%20JRV%205,3%20WATERMARK.pdf>. accessed in 15 November 2017

⁷⁶ Zulkarnain, Iskandar. LIPI. "Pertambangan Ilegal di Indonesia dan Permasalahannya". <http://iesr.or.id/files/Pertambangan%20Ilegal%20di%20Indonesia.pdf>. accessed in 15 November 2017

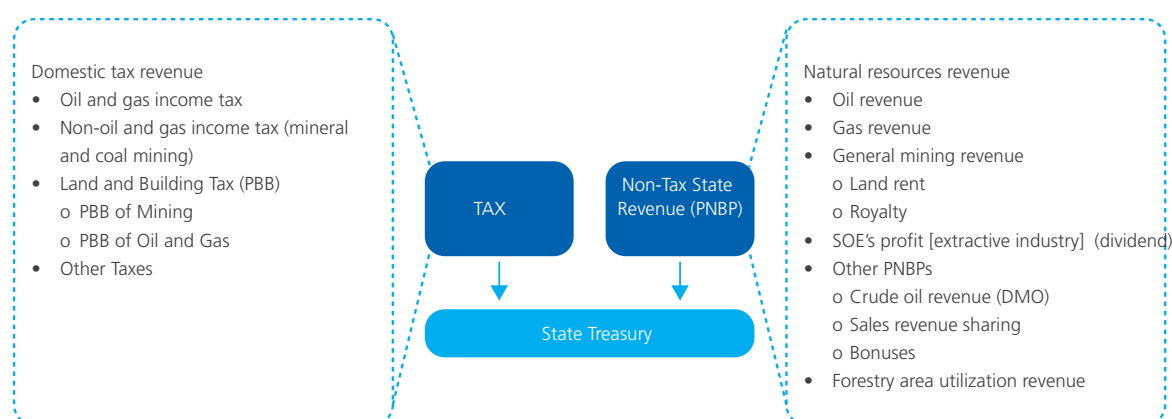
07

MANAGEMENT OF STATE REVENUE GENERATED FROM EXTRACTIVE INDUSTRY

STATE REVENUES FROM TAXES AND NATURAL RESOURCES ARE SHARED WITH LOCAL GOVERNMENT AS BALANCE FUND, AS STIPULATED BY LAW NO.33/2004 AND GR NO. 55/2005 ON FISCAL BALANCE BETWEEN CENTRAL AND LOCAL GOVERNMENT.

Based on the Central Government Financial Report (LKPP), state revenues from extractive industries are largely derived from tax revenues and non-tax state revenues (PNBP) deposited to the state treasury as illustrated in Figure 29. The state treasury is managed by the Directorate General of Treasury and the management is regulated by Law No. 1/2004 on State Treasury and Ministerial Regulations.

Figure 29. Extractive revenue reported in LKPP



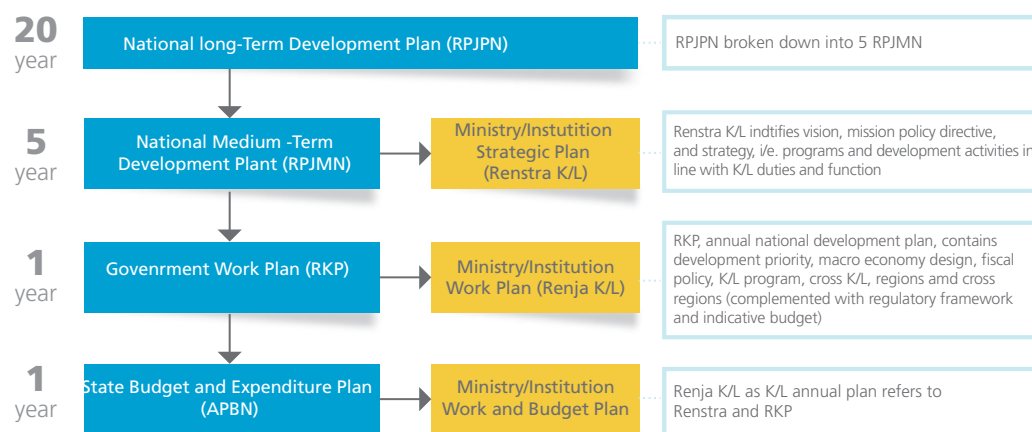
State revenues derived from extractive industries are accounted for in the central government budget and financial report accessible on the Ministry of Finance's website www.kemenkeu.go.id/page/financialsheets-committees. In 2015, Indonesia has no other revenue (other than the revenue mentioned above) from extractive industries that are not recorded in the state budget (APBN) and does not have national sovereign wealth funds and development funds or state investment institutions that manage funds derived from extractive industry companies.

7.1 State Financial Planning, Budgeting and Audit

7.1.1 Budget Planning

Budget planning process in Indonesia starts with the formulation of long-term development plan, which subsequently is broken down into medium and short-term plan. The National Long-Term Development Plan (RPJPN) 2005-2025 is enacted as Law No.17/2007 and is broken down into 4 Medium-Term Development Plan (RPJMN) – each focused on different themes and priorities. RPJMN 2015-2019 is the third RPJMN under Presidential Regulation No 2/2015. RPJMN documents are accessible to the public on website <http://bpkp.go.id/sesma/konten/2254/Buku-I-II-dan-III-RPJMN-2015-2019.bpkp>.

Figure 30. Relationship between development planning and budgeting arrangement



7.1.2 National Budgeting Approach

Indonesia's budgeting system adopts three approaches pursuant to State Finances Law No.17/2003, namely:

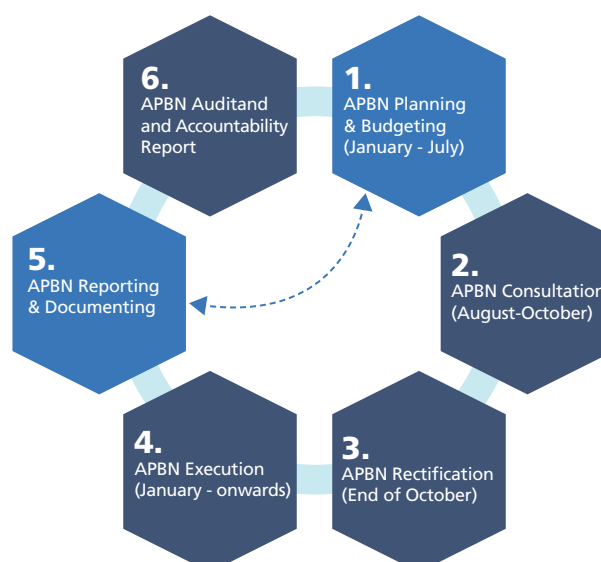
- Unified budget. Unified budgeting is the integration of all planning and budgeting processes across ministries/institutions. Budget is classified by organization, function, program, type of activity, and type of expenditure. The purpose of unified budgeting is to avoid funding duplication.
- Medium-term Expenditure Framework (MTEF). MTEF is policy-based budgeting approach. Ministries/Institutions will be required to translate their RPJMN and Renstra programs into annual Work and Budget plan. MTEF aims to ensure sustainable fiscal discipline, as METF proposed by Ministries/Institutions is the plan that projects to one subsequent year.
- Performance Based Budgeting (PBB). PBB approach takes into account funding and funding output as well as expected outcome, including efficiency in achieving outcome and output. PBB refers to performance indicators, cost standard, and performance evaluation. The purpose of PBB is:
 - To emphasize on performance in the process of achieving output and outcome using budget appropriation (input)
 - To develop budget based on certain objectives targeted in one fiscal year according to Ministries/Institutions' strategic plan and/or responsibilities.

Process of State Budgeting to State Budget (APBN) Audit

There are number of parties involved in the formulation of APBN, namely central government, Indonesia House of Representatives (DPR), and (recommendations from) subnational government. DPR approves APBN proposed by Central Government. The annual APBN cycle is as follows:

1. First phase: APBN planning and budgeting process. In this phase, the government, BPS, and Indonesia Central Bank prepare macro-economic base assumptions that will be used as reference in formulating budget plan (fiscal capacity) of Central Government. Two key elements in this phase are: activity planning and budgeting.
2. Second phase: APBN consultation. Plan of activities proposed by Ministries/ Institutions based on development priority directives from the President is discussed in trilateral meeting. Attending the meeting are Ministries/ Institutions as chief operating officer (COO), Minister of Finance as chief financial officer (CFO), and Minister of National Development Planning (PPN)/ Bappenas. The output of this consultation is APBN Bill and Financial Note - submitted to DPR for further consultation. APBN Financial Note presented before the DPR as well as APBN and Revised APBN are accessible on website <https://www.kemenkeu.go.id/uaapbn>.
3. Third phase: consultation between Central Government and DPR, taking into consideration recommendations from Regional Representative Council (DPD). Once Central Government and DPR reach an agreement, DPR passes APBN Bill and ratifies the APBN.
4. Ministries/Institutions and State Treasury execute APBN, referring to Budget Execution Document (DIPA).
5. Concurrent with the execution of APBN, Ministries/Institutions and State Treasury develops report and documentation as basis of LKPP, which consists of Budget Realization Report (LRA), Balance Sheet, Cash Flow Report (LAK), and Notes to Financial Statements (CALK). Financial statements are made based on Government Accounting Standards (SAP).
6. BPK audits LKPP submitted by Ministries/ Institutions and State Treasury. After audit

Figure 31. State budget (APBN) cycle



Source: APBN and LKPP, available for download on the Ministry of Finance website.

process is completed, the President, at the latest 6 months after the end of a fiscal year, presents APBN accountability report to DPR. This report will be discussed and ratified by DPR. Audit reports on LKPP are accessible on website <http://www.bpk.go.id/lkpp>.

7.1.3 Outlook of Extractive Industry

The public can access outlook on extractive industry from various sources published by relevant government agencies. The following are some documents that can be used as a public reference of targets and strategies along with the assumptions and policy directions used to achieve these goals, such as production estimates and targeted supporting infrastructure development in the 5 year planning period.

Strategic Plan (Renstra) of the Ministry of EMR 2015 – 2019

Renstra of the Ministry of EMR has purposes:

1. To guarantee domestic supply of energy and raw materials;
2. To optimize state revenue generated from the EMR sector;
3. To realize more targeted energy subsidies and competitive pricing;
4. To increase the investment in the EMR sector; and
5. To realize professional management and human resources as well as increase the capacity of science and technology and service of geology sector.

Public can access the detail of Renstra in https://www.esdm.go.id/assets/media/content/Renstra_KESDM.pdf.

Renstra of DG Oil and Gas and DG Mineral and Coal can be accessed in the following websites: <http://www.migas.esdm.go.id/public/images/uploads/posts/renstra-migas-2015-2019.pdf> and <https://www.minerba.esdm.go.id/library/publish/Renstra%20DJMB%202015-2019.pdf>.

Indonesia Energy Outlook by National Energy Council (NEC)

One of NEC's responsibilities is to study Indonesia's energy condition for the period of 2013-2050. NEC observes Indonesia's energy demand compared to energy supply from national production or import. This study will be a source of reference for the government and other parties to forecast

Indonesia's energy condition and can be the basis of policy formulation as well as Indonesia's energy development. This outlook can be accessed in <http://www.den.go.id/index.php/publikasi/index/EnergyOutlook>.

7.1.4 Process of Auditing in the Extractive Industries Sector

Oil and Gas Sector

SKK Migas and government auditors (BPKP, BPK, and Directorate General of Tax) conduct annual audit of KKSs that already in production stage. The scope of the audit includes oil and gas lifting and cost recovery aspects, including compliance with accounting policies and other policies in accordance with contracts, compliance with laws and regulations related to cost recovery and compliance with regulations related to upstream oil and gas operations.

Mineral and Coal Sector

Substantively the management and supervision of state finances from mineral and coal mining activities mainly related to the management and supervision of Non-Tax State Revenues (PNPB) of this sector. Audit on the management of state finances can be done by the Supreme Audit Agency (BPK) based on Law no. 15/2006 on BPK as well as by the Financial and Development Supervisory Agency (BPKP) based on Government Regulation No. 60/2008 on Government Internal Control System and Presidential Regulation No.192 / 2014 on BPKP.

There is a difference between audit standards applied by BPK, BPKP as well as SKK Migas and international audit standards. However, it cannot be said that BPK, BPKP and SKK Migas audit standards are in no way compatible with international audit standards. These audit standards are designed with special needs or interests that are different from those required by an independent auditor. In some cases, they may even be more extensive than international standards, though in other cases the standards may not be as required by international standards. The BPK audit report can be accessed at <http://www.bpk.go.id/ihips>.

7.2 Distribution of Revenue and Payment to Local Government

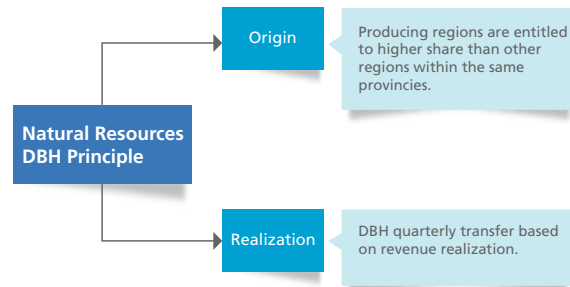
State revenues from taxes and natural resources are shared with local government as balance fund, as stipulated by Law No.33/2004 and GR No. 55/2005 on fiscal balance between central and local government. The fund consists of revenue sharing fund, general allocation fund and specific allocation fund. Based on its sources, revenue sharing fund is categorized into taxes DBH and natural resources DBH (natural resources: forestry, general mining, fishery, oil and gas and geothermal). DBH's source of funding is APBN and its distribution to local government follows percentage stipulated by Law No. 33/2004.

The following section discusses fund allocation of non-tax revenue from extractive industry.

Revenue Sharing Fund (DBH) Principle

The allocation of natural resources DBH is based on origin principle (derivative) and realization principle. Both principles must be satisfied in order for the local government to receive revenue sharing generated by extractive industry. Derivative principle means there must be oil and gas production activities carried out in that province or Regency/City, or within the region's sea territory (12 kilometers from coastline⁷⁷). Producing province or Regency/ City is entitled to a bigger share of the revenue. The other principle, realization principle, means that the revenues are recognized and recorded in State's Treasury.

Figure 32. DBH Principle



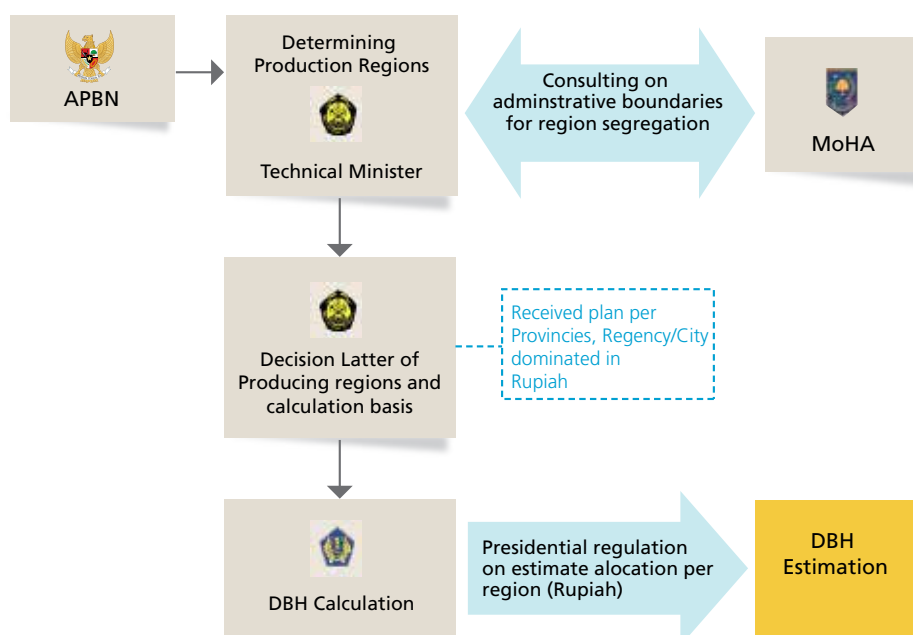
Source: Directorate of Balance Funding, Minister of Finance

Phases Natural Resources DBH Allocation

Phases to allocate natural resources DBH are:

1. Minister of EMR, in consultation with Minister of Home Affairs, identifies producing regions and basis of natural resources DBH calculation at the latest 60 days before the start of a fiscal year. The result is submitted to Minister of Finance.
2. Minister of Home Affairs, with advise from Minister of EMR, decides the producing region for natural resources located in borders or cross more than one territories. This decision must be made at the latest 60 days after line ministry submits its recommendations.

Figure 33. Natural resources DBH allocation estimation mechanism (GR No. 55/2005)



Source: Directorate of Balance Funding, Minister of Finance

⁷⁷ The 4 km limit of the coastline is part of the district, and the limit of 4 – 12 km from the coastline becomes part of the province, ie. The province as a producer.

3. Decision of the Minister of Home Affairs in point 2 above will be the basis of natural resources DBH calculation by Minister of EMR.
4. Minister of Finance establishes estimation of DBH allocation for each region, at the latest 30 days after Minister of EMR submits the decisions.
5. Estimation of Oil and/or Gas DBH for each region is issued at the latest 30 days after Minister of EMR issues the decision (point 1) along with estimation of government's share, and estimation of other deducting components.

7.2.1 Revenue Sharing Fund (DBH) Scheme for Extractive Industry

Oil and Gas DBH Scheme

The scheme of DBH calculation from oil and gas and mining sectors is as follows:

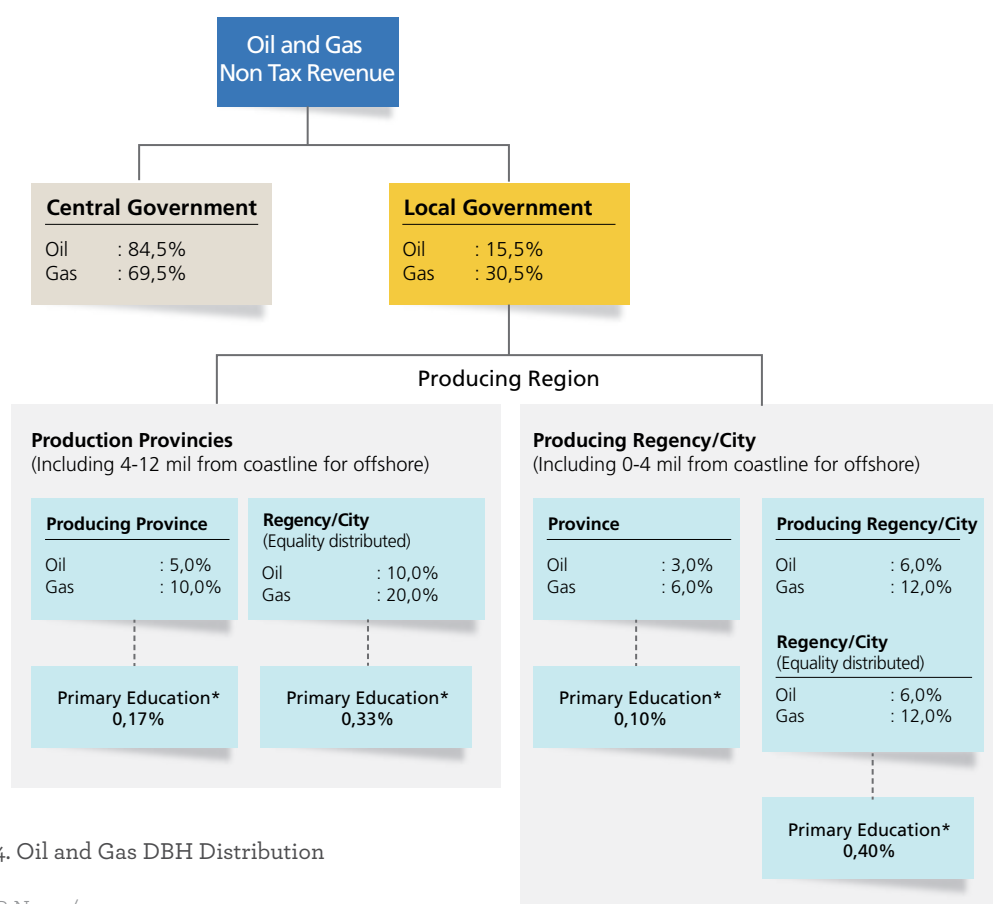


Figure 34. Oil and Gas DBH Distribution

Source: GR No. 55/2005

Oil and gas DBH scheme follows the scheme stipulated by Law No. 33/2004 and GR No. 55/2005. From oil and gas non-tax revenue (PNBP), 15% from oil and 30% from gas are transferred to local government as oil and gas DBH. The PNBP shared to local government is only PNBP from blocks operating within 12 miles from the coastline, while PNBP generated by operations located more than 12 miles from the coastline is entirely allocated to central government. Shared PNBP is further divided to producing regions – province or regency/city– as illustrated by Figure 34.

Oil and Gas DBH for Special Autonomy Region
Pursuant to Special Autonomy Law, there are three provinces granted with status as Special Autonomy Region, namely Aceh, Papua and West Papua⁷⁸. These provinces are entitled to higher percentage of oil and gas share compared to other regions⁷⁹.

⁷⁸ Currently oil and gas natural resources SDA Migas only exist in West Papua in accordance with the statement from the Head of Sub-Directorate General of Fiscal Balance in the EITI Journalist's workshop . Bogor, 7 September 2015.

⁷⁹ Presentation of Head of Sub-Directorate General of Fiscal Balance. "Kebijakan DBH SDA". EITI Journalist's workshop. Bogor, 7 September 2015. Because oil and gas only exist in West Papua.

Table 54. DBH scheme for special autonomy region

Commodity	% for region under special autonomy arrangement	Additional share for special autonomy province 55%	Province as producing region		Regency/City as producing region		
			Province	Regency/City in the Province	Province	Producing Regency/City	Regency/City in the Province
Oil	70%	55%	5%	10%	3%	6%	6%
Gas	70%	40%	10%	20%	6%	12%	12%

Source: Directorate of Balance Funding, Ministry of Finance

The share of oil and gas revenue of those provinces is 30% for central government and 70% for local government in the form of Oil and Gas DBH. Hence, provinces under special autonomy receive additional of 55% from oil revenue and the remaining 15% is distributed according to scheme in above figure. Meanwhile for gas revenue, provinces under special autonomy receive additional of 40% and the remaining 30% distributed in according to scheme in Figure 12. In summary, the distribution of oil and gas DBH portion for Special Autonomy Region is shown in Table 54.

Specific allocation (earmarked) of oil and gas DBH for certain programs in non-special autonomy region

- Additional 0.5% oil and gas DBH is specifically provided for education funding in that region. Specific allocation (earmarked) of oil and gas DBH for certain programs in special autonomy region

- Article 36 of Law No. 21/2001 required Papua and West Papua Provinces to allocate oil and gas DBH minimum of 30% for education and minimum of 15% for health and nutrition improvement.

Meanwhile, Aceh Province is required to allocate minimum of 30% oil and gas DBH for education.

The Minister of Finance shall monitor and evaluate the use of primary education budgets derived from oil and gas DBH, see sub section 7.2.2.

Mining DBH Scheme

Local government share from royalty and land rent is 80%. Table 36 presents the share for producing regions and non-producing regions.

DBH disbursement process is discussed in reconciliation report 2015.

Table 55. General mining DBH scheme

Type of DBH General Mining	% For Local Government	Share (%)		
		Province	Producing Regency/City	Other Regency/City in the Province
Land Rent for Producing Regency/City	80	16	64	-
Land Rent for Producing Province	80	80	-	-
Royalty for Producing Regency/City	80	16	32	32
Royalty for Producing Province	80	26	-	54

Source: Directorate of Balance Funding, Ministry of Finance

7.2.2 DBH Accountability Method and Utilization Efficiency

Monitoring and Evaluation

Article 32 and 34 of GR No.55/2005 stipulate monitoring and evaluation responsibility of the Minister of Finance over DBH earmarked for primary education:

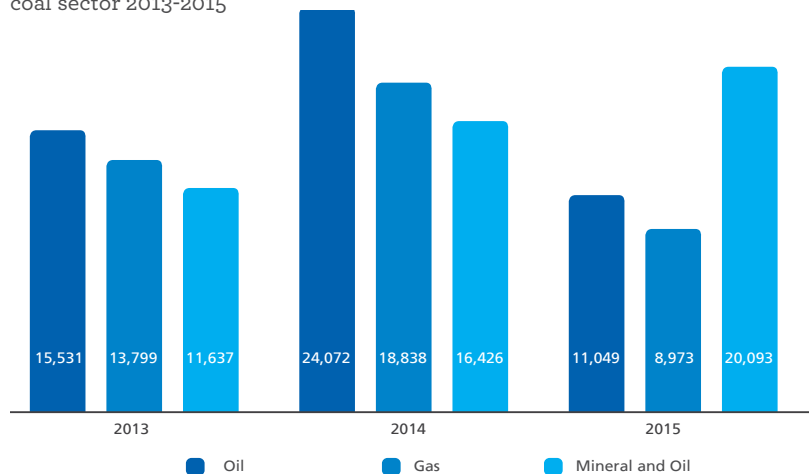
1. Minister of Finance monitors and evaluates budget utilization of oil and gas DBH for primary education.
2. If, based on the monitoring and evaluation, there is any indication of primary education budget misuse, Minister of Finance shall ask functional monitoring officer to conduct audit.
3. Result of audit can be used as basis of consideration for next fiscal year's DBH allocation

For non-earmarked DBH, central government monitors idle DBH in regions. If idle money is identified, central government will replace cash transfer to local government into State Bonds (SUN). The criterion is 3 months idle money in local government account in the amount that exceeds national average⁸⁰.

DBH Realization in 2015

Chart 34 shows the realization of oil and gas sector and mineral and coal sector DBH throughout the year 2013-2015. The realization of both oil and gas DBH in 2015 encounters a significant decrease of more than 50% due to the decrease of oil price in 2015, around US\$ 50 / barrel in 2015 from around US\$ 100 / barrel in 2014.

Chart 34. Actual DBH of oil and gas sector and mineral and coal sector 2013-2015



Notes: Including special autonomy regions and earmarked of 0,5% for oil and gas DBH

Source: EITI's Data 2015

Table 56. Ten (10) largest recipient regions of oil and gas sector and mineral and coal sector DBH
In Million Rp

No	Oil		Gas		Mineral and Coal	
	Region	Total DBH	Region	Total DBH	Region	Total DBH
1	Riau Province	1,048,999	Kutai Kartanegara Regency	1,158,774	East Kalimantan Province	1,790,176
2	Bengkalis Regency	1,040,512	East Kalimantan Regency	1,045,952	East Kutai Regency	1,603,274
3	Bojonegoro Regency	770,182	Musi Banyuasin Regency	580,973	Kutai Kartanegara Regency	1,343,942
4	Siak Regency	563,820	West Papua	574,339	South Kalimantan Province	801,079
5	Rokan Hilir Regency	563,511	South Sumatera Regency	367,740	Berau Regency	778,275
6	Kampar Regency	460,671	Riau Island Province	220,317	Paser Regency	657,185

⁸⁰ Presentation of Head of Sub-Directorate of Fiscal Balance (Q&A Session). "Kebijakan DBH SDA". EITI Journalist's Workshop. Bogor, 7 September 2015.

No	Oil		Gas		Mineral and Coal	
	Region	Total DBH	Region	Total DBH	Region	Total DBH
7	East Java Province	398,399	Aceh Province	215,365	West Kutai Regency	619,716
8	East Kalimantan Province	303,850	North Penajam Paser Province	201,283	Mimika Regency	588,823
9	Kutai Kartanegara Regency	302,138	Bontang City	192,664	Samarinda City	508,681
10	West Papua	246,602	Samarinda City	187,067	Tanah Bumbu Regency	446,311

Note: including earmarked of 0,5% for oil and gas DBH

Source: EITI's Data 2015

Table 37 is a list of the 10 largest DBH receiving areas for oil, gas, mineral and coal sectors. The recipient of the largest oil DBH is Riau province amounting to Rp 1 trillion and four regencies from Riau Province included in top 10 recipients of oil DBH, that is Regency of Bengkalis, Regency of Siak, Regency of Rokan Hilir and Regency of Kampar. Top 10 recipients of gas DBH are dominated by East Kalimantan Province, namely: Regency of Kutai Kertanegara, Regency of Penajam Paser, Bontang City and Samarinda City. Seven (7) areas in East Kalimantan are included in the 10 largest recipients of mineral and coal DBH.

7.3 Payment from Oil and Gas Company and Mineral and Coal Company to Local Government

7.3.1 Based on Local Regulation (Perda)

The Local Government in its authority may impose levies on oil and gas companies and mineral and coal companies. The provision for this arrangement is Law No. 28/2009 on Local Tax and Retribution (PDRD). Law No. 28/2009 replacing Law No. 18/1997 which has been amended and supplemented by Law no. 34/2000. The policy regarding PDRD is regulated by the Local Government in a Local Regulation (Perda).

Law No. 28/2009 regulates the following: (1) the existence of limitation on types of local taxes and / or retributions that may be collected by local government (Close List); (2) the granting of greater authority to local government in the field of taxation in the form of maximum rate increase; (3) the existence of a supervisory system on the collection of PDRD which was originally has a nature of repressive and cancellation became preventive and corrective, that is, the evaluation of Local Regulation draft of PDRD conducted by the Government (Minister of Home Affairs and Minister of Finance) before the regulation is enacted; and (4) the existence of sanctions for the Local Government that stipulates the local regulation without performing the evaluation procedure, the sanctions are in the form of the delay or withholding of General Allocation Fund and / or Revenue Sharing Fund or Restitution Fund⁸¹.

Payments of PDRD to Local Government from mining companies are generally in the form of Motor Vehicle Fuel Tax, Motor Vehicle Tax (PKB) and Tax on Change of Motor Vehicle Ownership (BBNKB), Building Permit (IMB) Retribution, Surface Water Tax and Interference Licenses Retribution (HO).

Table 58 is the amount of GDP reported by oil and gas companies and mineral and coal companies in the EITI reconciliation form 2015.

Table 57. Table of PDRD rates

Type of PDRD	Rates
Motor Vehicle Tax (PKB)	<ul style="list-style-type: none"> Private PKB rate for the first vehicle ownership amounted to 1% and maximum of 2%, second ownership and so on are progressive, amounted to 2% and maximum of 10%. Public and Social PKB rate amounted to minimal 0,5% and maximum 1%. Heavy and Large Equipment PKB rate amounted to 0,1% and maximum 0,2%
Tax on Change of Motor Vehicle Ownership (BBNKB)	<ul style="list-style-type: none"> BBNKB rate for the first handover amounted to 20%, second handover and so on amounted to 1%. Heavy and Large Equipment BBNKB rate for the first handover amounted to 0,75%, second handover and so on amounted to 0,075%
Motor Vehicle Fuel Tax (PBBKB)	<ul style="list-style-type: none"> Private PBBKB rate amounted to a maximum 10%. Public and Social PBBKB rate amounted to minimal 50% of Private PBBKB rate
Surface Water Tax	Maximum 10%

Source : Law No. 28/2009 on PDRD

⁸¹ National Legal Development Board Ministry of Law and Human Rights. 2013. "Analisis dan Evaluasi tentang Pajak dan Retribusi Daerah", Kadar Pamuji. "Kebijakan Pengelolaan Pajak Daerah dalam Kerangka Penyelenggaraan Otonomi Daerah". Jurnal Dinamika Hukum Vol.14 No.3. September 2014.

Table 58. PDRD reported by companies in 2015

Sector	Reported in Rupiah	Reported in USD		Total
	Rupiah (in Million)	USD (in Thousand)	Rupiah (in Million)	Rupiah (in Million)
Oil and gas	52,078	-	-	52,078
Mineral and Coal	405,899	38,921	521,541	927,440
TOTAL	457,977	38,921	521,541	979,518

Source: EITI Data 2015

Since 2012 several associations, including the Indonesia Mining Association (IMA) and the Indonesian Mining Services Association (Aspindo) have been concerned about the imposition of PKB and BBNKB for heavy equipment used by mining companies. The objection was submitted by the associations by proposing a judicial review of Law No. 28/2009 and Law No. 22/2009 on Road Traffic and Transportation (LLAJ) to the Constitutional Court (MK). Companies and entrepreneurs of heavy equipment consider heavy equipment as a means of production instead of transportation as regulated in Law No. 22/2009. Therefore, it cannot be imposed PKB and BBNKB.

There are three Constitutional Court Decisions related to the Material Testing of the Law No. 28/2009, namely: (1) 1 / PUU-X / 2012 (a verdict related to the Law No. 28/2009); (2) Number 3 / PUU-XIII / 2015 (a verdict related to the Law No. 22/2009); and (3) 15 / PUU- XV / 2017 (a verdict related to the Law No. 28/2009). The conclusions of these three Constitutional Court Decisions are: heavy equipment is not transportation; and heavy equipment can still be taxed, but the legal basis for the taxation of the heavy equipment is not because the vehicle is a motor vehicle. The implication of these Constitutional Court Decision is heavy equipment used in mining activities cannot be imposed PKB and BBNKB by the Local Government because it is not a motor vehicle.

7.3.2 Commitment between Company and Local Government (Pemda)

In addition to the PDRD, the company can pay directly to Pemda based on the commitment of the mineral and coal company's management with the local government. This payment is a form of participation of mineral and coal companies in sustainable development and contribution of mineral and coal companies in local development. The amount of direct payments to local governments based on commitments / agreements of both parties based on the reporting company can be seen in Table 16 of EITI Reconciliation Report 2015.

7.4 Current Issue of Extractive Revenue Management

7.4.1 The Role of Local Government in the Reconciliation Process of DBH Calculation

Local governments have a vested interest in the Revenue Sharing Fund as one of the most significant sources of budgetary funding, especially for producing regions that are accustomed to obtaining high DBH. Article 28 of the Government Regulation No. 55/2005 regulates a mechanism for data reconciliation between the Central Government and the Local Government on a quarterly basis. However, local governments are often unable to project the amount of revenue sharing funds (especially for oil and gas) themselves because the jurisdiction of revenue sharing calculation is the authority of the Central Government. While at the regional level, the Local Governments also face difficulties related to access of oil lifting data from KKS Contractors and detailed cost recovery calculation from SKK Migas.

Reconciliation between local government and Ministry of Energy and Mineral Resources is conducted quarterly for the lifting numbers that lasted until now. However, reconciliation between the local government and the Ministry of Finance (DG Fiscal Balance and DG Budget) has not been done since 2015 due to the reorganization of the Ministry of Finance and the absence of a technical regulation (Regulation of the Ministry of Finance) governing this reconciliation procedure.

Therefore, it is necessary to have a technical procedure of DBH reconciliation process which clearly describes the procedures of Local Government to access cost recovery calculation from SKK Migas and calculation of deduction factor from DG Budget. This is to provide confidence to the Local Government regarding the amount of the Balancing Fund to be allocated to a region.

7.4.2 PNBP Receivables

According to Central Government Financial Report (LKPP) 2015, Total PNBP receivables owned by the Government of Indonesia amounted to Rp 159.6 trillion. Approximately 17% of the total amount or Rp 26 trillion, mostly derived from royalty and land rent receivables of KK / IUP and PKP2B. The main cause of the PNBP arrears from mining business players is the unresolved restitution / refund of the Government⁸². This restitution practice is conducted by mining companies referring to a contract stating that taxes arising out of contract will be borne by the government. Then the tax return will be made with a set off mechanism of the mining company's obligations⁸³. The unfinished process of restitution lead to the reluctance of paying royalties to the Government. Based on LKPP 2016, part of PNBP receivables in 2015 has been completed, which has been settled amounting to Rp 19 trillion.

The Government has made various efforts to collect PNBP receivables, such as by requesting assistance from the provincial government to collect PNBP from mining companies in their respective regions. In addition, the Government also plans to limit the granting of licenses for companies that still have payment obligations to the Government⁸⁴.

7.4.3 Petroleum Fund

Petroleum Fund is the Sovereign Wealth Fund which is set aside. The funding is derived from oil and gas activity revenues and the utilization of the fund is regulated by Government Regulation⁸⁵. Various countries rich in oil and gas resources have practiced this petroleum fund collection. The allocation and mechanism for the collection of the petroleum fund vary across countries, for example Canada which established the Alberta. Fund beginning with setting aside CAD1.5 million, then collecting 15% (originally 30%) of royalty revenues and Norway established the Government Pension Fund-Global in which part of funding derived from all taxes on oil and gas activities and dividends from Statoil (Norwegian Oil and Gas SOE)⁸⁶.

The utilization of petroleum funds also varies greatly depending on the specific needs and objectives of government development and may change according to the latest circumstances⁸⁷. In general, petroleum funds are used to stabilize fluctuating commodity prices, saving for future generations when natural resources are depleted, and financing strategic development goals.⁸⁸

Initiative of Petroleum Fund in Indonesia

Indonesia does not yet have petroleum fund both at the national and regional levels, but several initiatives have emerged. At the central level, the initiative is still in the early stage, for example derived from the revision draft of the Oil and Gas Law prepared by DPR. While at the level of Local Government, this initiative already exists in the Regency of Bojonegoro and the Regency of Musi Banyuasin⁸⁹. Both regencies are rich in oil and gas potential, Cepu Block operates in Bojonegoro and Ramba / Rimau Block operates in Musi Banyuasin.

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- CHAPTER VIIA PETROLEUM FUND, Article

37A: "(1) The Management Unit shall undertake and manage the Petroleum Fund in a transparent and accountable manner. (2) The Petroleum Fund as referred to in paragraph (1) is intended for activities related to the replacement of Oil and Gas reserves, renewable energy development, and for the benefit of future generations. (3) The Petroleum Fund as referred to in paragraph (1) shall originate from a certain amount of total commercial production which is set aside exclusively outside the Central Government's and contractor's shares."

The Regency of Bojonegoro has already initiated to establish the Petroleum Fund first. Meanwhile, the Regency of Musi Banyuasin is still undertaking a joint study with UNDP. The draft of Local Regulation (Raperda) of the Bojonegoro Petroleum Fund has been prepared and has been consulted to the Ministry of Home Affairs, Bappenas and Ministry of Finance⁹⁰ and awaits discussion at the DPRD level⁹¹. The funding source is planned to be derived from 40% of revenue of oil and gas DBH and mining sector land and building tax DBH and all Participating Interest received by the region. Revenues from the placement of the petroleum fund portfolio can only be used to improve human resources in education, health and socio-culture.

82 Gustidha Budiartie, dkk. "Macet Royalti Akibat Restitusi". Tempo. Juni 2016. hal. 86 - 88. <http://www.apbi-icma.org> accessed in 1 November 2017

83 Anggita Rezki Amelia. "Kementerian Energi Tagih Piutang Royalti 5 Perusahaan Batubara". <http://katadata.co.id/berita/2016/11/01/pemerintah-tagih-piutang-pnbp-sektor-tambang> accessed in 1 November 2017

84 Ibid.

85 Migasreview.com. 2015. "Mengenal petreleoum fund". <http://www.migasreview.com/post/1425436202/mengenal-petreleoum-fund.html> accessed in 1 November 2017

86 Poelzer, Greg. 2015. "Global Lesson from Norway Energy Based Economy.

87 IMF. 2013. "Soveriegn Wealth Fund: Aspect of Governance Structure and Investment management". <https://www.imf.org/external/pubs/ft/wp/2013/wp13231.pdf> accessed in 1 November 2017

88 Op.cit

89 Musi Banyuasin Regency is not specific to Oil and Gas alone but is more common in other natural resources including Rubber.

90 Bojonegor Institute. 2016. "Rumusan Dana Abadi Migas Kabupaten Bojonegoro". <http://bi.or.id/rumusan-dana-abadi-migas-kabupaten-bojonegoro/> accessed in 15 November 2017

91 Kumparan.com. 2017. "Pimpinan Dewan: Perda Dana Abadi Belum Memiliki Landasan Hukum". <https://kumparan.com/beritabojonegoro/pimpinan-dewan-perda-dana-abadi-belum-memiliki-landasan-hukum> accessed in 15 November 2017

Success Factors

The establishment of Petroleum Fund requires careful consideration as implementation may be counterproductive e.g raising inflation, misuse of funds and unsuccessful investments caused by unwise investment decisions. Some of the factors below according to the UNDP and IMF study are essential to the success of the Petroleum Fund:

- **Institution and Manager of Petroleum Fund**
Regardless of whether the institution of the Petroleum Fund is established through an existing institution or with the establishment of an independent institution, the operations of the petroleum fund must be independent and having its own account. In addition, the role of senior government officials should be minimal. This independence is to ensure the Petroleum Fund to operate focus on its founding objectives and reduce political influence. Government Pension Fund-Global from Norway is operated by the Central Bank based on the mandate granted by the Ministry of Finance. Bojonegoro Petroleum Fund is planned to be managed by the Regional Public Service Agency (BLUD) and has its own account.
- **Reporting and Transparency**
Reporting and Transparency are important to increase public trust, improve discipline from Petroleum Fund operators, and reduce the risk of

corruption and mismanagement. The Norwegian Central Bank as manager of Petroleum Fund issues quarterly and annual reports, including performance reports of investment returns, all reports published. The Raperda of Petroleum Fund has mandated the disclosure of public information. In addition, the Trustee of Bojonegoro Petroleum Fund will deliver reports on the results of supervision to the public through DPRD.

- **Investment Strategy**
The investment strategy is highly dependent on the type of petroleum fund and mandate given. Generally in the early stages of formation, petroleum fund is usually invested in liquid and low risk investment products. Norway's Government Pension Fund-Global (GPFG) focuses on diversified investments and is invested overseas. Currently, the GPFG's investment policy is 60% equity (GPFG owns shares in 7000 companies with maximum allowable ownership of 5%) and 40% fixed income, while the Bojonegoro Petroleum Fund will be invested in deposits and Bank Indonesia Certificates (SBI).

There are many other factors that need to be considered by the Government in the establishment of the Petroleum Fund apart from the above three factors.

08

RECOMMENDATION



The Implementation Team expects the EITI Report to include recommendations to improve transparency and governance levels in the extractive industry. The following recommendations are agreed along with findings during the preparation of EITI Contextual Report 2015.

1. **Adequate technical procedures that clearly illustrate how local governments can access data to be able to project the amount of revenue sharing funds for oil and gas.**

Background

Local governments have a vested interest in the Revenue Sharing Funds (DBH) as one of the most significant sources of budgetary funding. Article 28 of the Government Regulation No. 55/2005 on the Proportionality Fund regulates data reconciliation mechanism between the Central Government and the producing regions on a quarterly basis for DBH of natural resources. For DBH of oil and gas, reconciliation between local government and the Ministry of Energy and Mineral Resources is conducted quarterly for the lifting numbers that lasted until now. However, the reconciliation between the local government and the Ministry of Finance (Directorate General of Fiscal Balance and Directorate General of Budget) has not been done since 2015 due to the reorganization of the Ministry of Finance and the absence of a technical regulation (Regulation of the Ministry of Finance) governing this reconciliation procedure. Furthermore, the mechanism of reconciliation between the Ministry of Finance and local government is not clearly regulated in GR No 55/2005.

Meanwhile, local government is often unable to project the amount of revenue sharing funds due to difficulties related to the access of data calculation of cost recovery from SKK Migas and deduction factors from Directorate General of Budget. Although actually both agencies are open to provide data if there is a written request from the local government.

Article 28 of Government Regulation No. 55/2005: "(1) The calculation of DBH realization of natural resources shall be conducted quarterly through data reconciliation mechanism between the central government and the producing regions except for DBH Fishery resources. (2) In the event that the realization of natural resource DBH is derived from oil and / or natural gas revenues, the calculation is based on the realization of oil and / or natural gas lifting from the technical department."

Recommendation

Hence, it is necessary to agree on adequate technical procedures that clearly illustrate how local governments can access cost recovery calculations from SKK Migas and Directorate General of Budget deduction factor calculations.

2. **EITI Secretariat to send a letter to the PPID ESDM to open PKP2B and KK contracts in the upstream mineral and coal sector**

Background

EITI Standard 2016 Requirement 2.4 requires disclosure of contractual content related to exploration and exploitation of the extractive industry. In 2011, the Central Information Commission (KIP) on its decision letter No.197 / VI / KIP-PS-M-A / 2011 ruled that the copy of the mineral and coal contracts sought by the plaintiff is an open information. Based on the information from PPID ESDM (<http://eiti.ekon.go.id/rapat-coordinasi-keterbukaan-informasi-kontrak-pertambangan/> and interview with PPID ESDM), the public can make a request letter for the opening of a copy of the contract for the contractor of the upstream mineral and coal. This is conducted to comply with the above KIP decision.

Recommendation

The Implementation Team recommends the EITI Secretariat to send a request letter to the PPID ESDM requesting the copy of the PKP2B and KK contracts of the upstream mineral and coal sector to be opened to the public.

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WORD

Barrel is measurement unit for liquid volume that generally use in petroleum industry; 1 barrel is averagely 159 liter.

Barrel Oil per Day - BOPD is total oil per day produced by well, eld, or an oil company.

Beneficial Ownership is the owner who actually receives benefits from the ownership of the assets and not the owner of the assets that are registered by law.

Business Entity (BE) is every legal entity that operates and is incorporated based on the Indonesian law and domiciled within the territory of the unitary state of the Republic of Indonesia.

Cadastre system is a spatial information system of property ownership or a comprehensive land that is usually managed by the government. Regarding EITI Standard 2016 requirements 2.3, implementing countries are required to publish cadastral information systems. Required information is: i) the owner of the license, ii) coordinates, iii) the date of application, the date of issuance of the license, and the duration of the license; iv) commodities produced for licenses already in production.

Condensate is 1) gas hydrocarbon in reservoir pressure and temperature but 2) Liquid at normal pressure and temperature 3) a liquid product consisting of mix of light hydrocarbon produced from gas recycle process with expansion and cooling.

Conservation Forest is forest area with typical characteristics, with main function to conserve biodiversity and ecosystem thereof.

Concession is any grant of right, permit for land from government to company, person or other entities.

Crude Oil (Oil) is unrefined petroleum product composed of hydrocarbon deposits and other organic minerals that maintain liquid after processing.

Earmarking in public financial management is allocation of state revenue for public program or other public services.

EITI's Data 2015 is data collected by the Independent Administrator of the reporting enterprise for the reconciliation process in accordance with the scope set by the Implementing Team.

Exploitation is a series of activities aimed at producing petroleum and natural gas from the working area stipulated, consisting of drilling and completion of wells, the building of transport, storage and processing facilities to separate and purify petroleum and natural gas in the eld as well as other activities supporting the exploitation.

Exploration is activities aimed at obtaining information on geological condition to find and obtain the estimated reserves of petroleum and natural gas in the working area stipulated.

Extractive Industry is any processes that involve the extraction of raw materials from the earth that includes minerals, coal, oil and gas.

Firm commitment is contractor work plan and budget pursuant to PSC in first 3 year exploration period.

Free carry or carried interest is the profit proportion received by the partner regardless of whether the partner contributes to the funding or not.

Golden share - Saham Dwiwarna is a special share (a golden share) that has privileges comparing to other ordinary shares. Privilege rights primary in directors appointment. In Indonesia capital market, this share owned by GoI for 1 (one) share.

Information Committee is an independent institute that functions to implement Law No.14/2008 and its implementing regulation(s), to provide the standard technical directives for Public Information service and to settle Public Information disputes through mediation and/or non-litigation adjudication.

Joint Study is activities performed by BE or PE and DG Oil and Gas in order to direct offer of working area by collecting, analyzing and evaluating data to find out oil and gas potential.

Lifting is volume of oil/gas sold at delivery point (custody transfer point).

LNG (Liquid Natural Gas) is natural gas (predominantly methane, CH₄) that has been liquefied in low temperature and maintain liquid for ease of storage or transport.

Mineral Resource is a concentration or occurrence of material of intrinsic economic interest in or on the earth's crust in such form, quality and quantity that there are reasonable prospects for eventual economic extraction. Mineral resource with certain geological condence could change to reserves after mining feasibility study and meet mining criteria.

National Legislation Program - Program Legislasi Nasional (Prolegnas) is program outlining list of bills which the DPR and GoI intend to produce.

Natural Gas (Gas) is a produce of the natural process in form of hydrocarbon in a pressure condition and at an atmosphere temperature that in the form of gas, which is obtained from a petroleum and natural gas mining process.

New Energy is energy from new energy source.

Open Area is a certain region within the Indonesian mining jurisdiction that has not yet allocated as working area.

Permanent Business Entity (BUT) is a business entity established and incorporated outside Indonesia which is conducting activities in the territory of Indonesia.

Planned on Development (POD) is field development in working area that must be approved by Minister of EMR based on SKK Migas's consideration and regional government consultation.

Potential Reserves is petroleum estimated in reservoir.

Primary Energy is an energy form found in nature that has not been subjected to any conversion or transformation process.

Probable Reserves are those unproved reserves which analysis of geological and engineering data suggests are more likely than not to be recoverable.

Production Forest is forest area with main function to yield forest produces.

Protected Forest is forest area with main function to protect life buffer system to arrange water management, prevent flood, erosion, prevent brine water intrusion, and maintain land fertility.

Proved Reserves are those quantities of petroleum which, by analysis of geological and engineering data, can be estimated with reasonable certainty to be commercially recoverable, from a given date forward, from known reservoirs and under current economic conditions, operating methods, and government regulations.

Public Information is information that is produced, stored, managed, sent and/or received by a Public Agency relating to the organizer and the organizing of the state and/or the organizer and the organizing of other Public Agencies pursuant to this law and other information pertaining to the interest of the public.

Quasi fiscal expenditures is any activities undertaken by state-owned banks and enterprises, and sometimes by private sector companies at the direction of the government, where the prices charged are less than usual or less than the "market rate."

Renewable Energy is energy from a source that is not depleted when used.

Reserves are quantities of petroleum/minerals which are anticipated to be commercially recovered from known accumulations from a given date forward.

Reserves replacement ratio (RRR) is ratio between additional reserves and gas or oil production in the same year.

Scoping study EY is EITI 2012-2013 scoping study prepared by Ernst & Young as a preliminary study to de ne scope for EITI 2012 -2013 report.

State Reserve Area - Wilayah Pertambangan Negara (WPN) shall be part of a mining area that is reserved for national strategic purposes.

Working Area is a certain region within the Indonesian mining jurisdiction used for the exploration and exploitation.

APPENDIX

APPENDIX 1: General Provisions in Existing Extractive Industries' Contracts

Oil and Gas Sharing Contracts

Could be seen in EITI Indonesia's Secretariat webpage (<http://eiti.ekon.go.id/draft-kontrak-psc/>)

Contract of work and PKP2B for mineral and coal mining

No	General Provisions	Notes
1	Definition	Set about limits/understandings of terms in the contract.
2	Appointment and responsibility of the Company	Explaining that the Government as the owner of the Natural Resources and the Company only as a designated party. Companies must report the detailed work plans and be responsible of RKAB to the Government.
3	Mode of operation	Organizing the form of company, place of residence and other activities, including subcontract mining activities to other Company as long as it is not violating the articles.
4	Area of the contract of work	Organizing the Company's mining area, including the decision which may dispose of some of its land to other Companies.
5	General period of inquiry	Organizing the general investigation stage of the approved mining area.
6	Exploration period	Organizing the stages of exploration work and the Company's obligation at this stage.
7	Reports and deposit guarantee	Organizing the Company's obligations to the Government (reporting on activities and depositing guarantees).
8	Fairness study period	Organizing the stages of the fairness study and the Company's obligation at this stage.
9	Construction period	Organizing about when the Construction started by the Company.
10	Operation period	Organizing about the matters relating to the period of operation and obligation to process mining products in the country (if already have a smelter).
11	Marketing	Regulates the rights of the Company to market the mining products directly, domestically and exported, at a reasonable price. If the price is not fair, the Government is entitled to evaluate.
12	Import and re-export facilities	Organizing the clause on import permits of mining equipment as long as it is not domestically produced and import duty tariffs and imported VAT.
13	Taxes and other financial liabilities of the Company	Organizing about the taxes and not taxes that are incurred by the Company including the tariffs, calculation methods, and the provisions of which laws apply to the contract.
14	Reporting, inspection, and work plan	Organizing the Company's obligation to provide reports (financial), documentation obligations, and the right of the Government to conduct inspection of such reports.
15	Exchange of payment instruments	Organizing about the allowed payment tools and mechanisms.

No	General Provisions	Notes
16	Special rights of the Government	Organizing the rights of the Government over mining areas.
17	Employment opportunities and training for Indonesian citizens	Organizing the terms of use of Indonesian workers, foreign workers, and knowledge transfer.
18	Promotion of national interest	Organizing the obligation to prioritize the domestic interest in the resulting mine.
19	Regional cooperation in the provision of additional infrastructure	Organizing about coordination with local government for development in region.
20	Environmental management and protection	Organizing the obligation to maintain the environment in the mining area and on safety.
	Ketentuan-ketentuan kemudahan	Mengatur hak yang diberikan kepada Perusahaan untuk memudahkan kegiatan konstruksi
21	Development of local business activities	Organizing the Company's obligations to develop its business activities and the local Company.
22	Terms of convenience	Organizing the rights granted to the Company to facilitate construction activities.
23	Circumstances force	Explain what constitutes a state of coercion and its implications for the agreement.
24	Negligence	Explain what is meant by its negligence and its implications for the agreement.
25	Dispute resolution	Organizing the settlement process in case of a dispute.
26	Termination	Setting the rights and obligations of each party at each stage in the event of termination of agreement.
27	Cooperation of the parties	Organizing the good cooperation between the Government and the Company.
28	The terms of the parties	Organizing the good cooperation between the Government and the Company.
29	Transfer of rights	The transfer of rights with the transfer of shares of the Company must be with the approval of the Minister.
30	Financing	Arranging sufficient financing for mining business by Financial Companies.
31	Time period	Organizing the effective date of the contract validity including the extension.
32	Choice of law	Contracts are subject to the laws in force in Indonesia.

General Provisions in Mining Business License (IUP)

IUP of Exploration shall contain the provisions at least about:

- Company's name;
- Location and area;
- General spatial plan;
- Assurance of sincerity;
- Investment capital;
- Extension of activity stage;

- g. Rights and obligations of IUP's holders;
- h. Duration of activity stage;
- i. Type of business provided;
- j. Development plans and community empowerment around the mining area;
- k. Taxation;
- l. Dispute resolution
- m. Fixed fees and exploration contributions; and
- n. amdal.

IUP of Production Operation shall contain at least shall at least the following terms:

- a. Company's name;
- b. Location and area;
- c. Mining location;
- d. Location of processing and purification;
- e. Transportation and sales;
- f. Investment capital;
- g. The period of validity of IUP;
- h. Period of activity stage;
- i. Settlement of land issues;
- j. The environment including reclamation and post-mining activities over time;
- k. Reclamation and post-mining assurance funds
- l. IUP's renewal;
- m. Rights and obligations of IUP's holders;
- n. Development plans and community empowerment around the mining area;
- o. taxation;
- p. non-tax state revenues consisting of fixed fees and production fees;
- q. dispute resolution;
- r. occupational Health and Safety;
- s. mineral or coal conservation;
- t. utilization of domestic goods, services and technology;
- u. the application of good economic and engineering principles of mining;
- v. development of Indonesian workforce;
- w. management of mineral or coal data; and
- x. mastery, development, and application or mineral or coal mining technology.

Source: Law No. 4/2009 on Mineral and Coal Mining

APPENDIX 2: Matrix Contextual Report and EITI Standard 2016

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EITI INDONESIA REPORT 2015 **CONTEXTUAL REPORT**

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