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2014 NEGATIVE INVESTMENT LIST – IMPLICATIONS FOR MINING, OIL & GAS AND POWER PLANT SECTORS¹²³⁴⁵

INTRODUCTION

In late April, the President issued a regulation setting out the details of those sectors of the Indonesian economy which are now (i) closed for foreign investment, (ii) open for foreign investment and (iii) partially closed/partially open for foreign investment (“**2014 Negative Investment List**”).

The mining sector has been relatively unaffected by the 2014 Negative Investment List subject to the potentially important exceptions of (i) mining equipment and spare parts distribution and (ii) geological services. The upstream oil & gas services sector has, however, been significantly affected in any number of areas by the 2014 Negative Investment List. The 2014 Negative Investment List also makes some changes which are relevant to the power plant or electricity generation sector.

Although the Negative Investment List covers all or most sectors of the Indonesian economy, this article is confined to reviewing those changes reflected in the 2014 Negative Investment List which are directly relevant to the mining, oil & gas services and power plant sectors only. Readers should be aware, however, that the 2014 Negative Investment List also makes significant changes to various sectors of the Indonesian economy outside the mining, oil & gas services and power plant sectors, which changes to other sectors are not covered in this article.

BACKGROUND

The Negative Investment List had not been the subject of a comprehensive review and reissuance since 2010.

The Negative Investment List is primarily intended to set out the Government’s position on new foreign investment in those sectors of the Indonesian economy where foreigners may only invest through the medium of an Indonesia incorporated, limited liability, foreign investment company

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⁵ This article appeared in the June - July 2014 issue of Coal Asia Magazine.

(“PMA Company”).

It is important to understand, though, that the Negative Investment List is not the only source of restrictions on foreign investment in various sectors of the Indonesian economy, which restrictions are also to be found in ministerial regulations and decrees. This is particularly the case for the mining sector where foreign investment has been seriously affected by numerous regulations issued by the Ministry of Energy & Mineral Resources over the past few years.

Notwithstanding the foregoing, the 2014 Negative Investment List may be seen as evidencing, at least in part, how the Government’s attitude, towards foreign investment in various sectors of the Indonesian economy, has changed over the past 5 years.

COMMENTARY

1. Overview of Major Changes

The major changes, which the 2014 Negative Investment List has made to permitted levels of foreign investment/ownership in the mining, oil & gas services and power plant sectors only, are summarized in the table below.

MAJOR CHANGES RELEVANT TO MINING, OIL & GAS SERVICES AND POWER PLANTS ONLY

No	Business Activity	KBLI	Specific Activities Covered	Old NIL (Maximum foreign investment/ ownership)	New NIL (Maximum foreign investment/ ownership)
1. Distribution					
	Distribution	00000	Wholesale, Export, Import	Not specifically regulated in the Old NIL – therefore notionally open for 100% foreign investment/ownership	33%
2. Surveying Services					
	(i) Oil & Gas	71100	Oil & gas surveying	Not regulated in the Old NIL – therefore notionally open for 100% foreign investment/ownership	49%
	(ii) Geological and Geophysical Surveying in the fields of energy and mineral resources	71100	Geological and geophysical surveying	Not specifically regulated in the Old NIL - therefore notionally open for 100% foreign investment/ ownership	49%

No	Business Activity	KBLI	Specific Activities Covered	Old NIL (Maximum foreign investment/ ownership)	New NIL (Maximum foreign investment/ ownership)
	(iii) Geothermal Surveying	71100	Geothermal surveying	Not specifically regulated in the Old NIL – therefore notionally open for 100% foreign investment/ownership	95%
3. Architecture, Civil Engineering & Other Technical Consultation Services					
	(i) Engineering Procurement Construction	71100	Provision of engineering, procurement and construction services	95%	Not specifically regulated in the New NIL – therefore notionally open for 100% foreign investment/ownership
	(ii) Electricity Installation Consultation	71100	Technical design and consultation activities re expansion and project realization of electrical engineering work	95%	95%
	(iii) Field Testing and Measurement Work	71100	Provision of field testing and measurement services	<p>(i) For construction services using simple technology and/or low risk and/or with a work value of less than Rp.1,000,000,000: closed for foreign investment</p> <p>(ii) For construction services using advanced technology and/or high risk and/or with a work value of more than Rp.1,000,000,000: open for foreign investment/ownership up to a maximum of 67%</p>	<p>(i) For construction services using simple technology and/or low risk and/or with a work value of less than Rp.1,000,000,000: closed for foreign investment</p> <p>(ii) For construction services using advanced technology and/or high risk and/or with a work value of more than Rp.1,000,000,000: open for foreign investment/ownership up to a maximum of 67%</p>

No	Business Activity	KBLI	Specific Activities Covered	Old NIL (Maximum foreign investment/ ownership)	New NIL (Maximum foreign investment/ ownership)
4.	Power Plants				
	(i) Power Plants	35101	Generating electricity and operating power plant facilities	<p>(i) For power plants with a capacity of less than 1 MW: reserved for micro, small and medium sized enterprises and cooperatives (“UMKM”) and, therefore, closed for foreign investment/ownership</p> <p>(ii) For power plants with capacity between 1 – 10 MW: 100% open for foreign investment/ownership but subject to “partnership” with UMKM</p> <p>(iii) For power plants with a capacity of more than 10 MW: open for foreign investment/ownership up to a maximum of 95%</p>	<p>(i) For power plants with a capacity of less than 1 MW: 100% domestic investment and, therefore, closed for foreign investment/ownership.</p> <p>(ii) For power plants with capacity between 1 – 10 MW: open for foreign investment/ ownership up to a maximum of 49%</p> <p>(iii) For power plants with a capacity of more than 10 MW: (A) during initial “concession period”, open for 100% foreign investment/ownership, subject to obligation of “partnership” with Government in carrying out electrical power generating activities</p> <p>(B) after initial “concession period” expires, open for foreign investment/ownership up to a maximum of 95%</p>
5.	Oil & Gas Construction Services				
	(i) Platforms	09100	Platform construction	Not specifically regulated in the Old NIL. However, several business activities, classified as part of KBLI 09100, were open for foreign investment/ ownership up to a maximum of 95%	75%
	(ii) Spherical Tanks	09100	Spherical tank construction	Same as 5(i) above	49%
	(iii) Oil & Gas Upstream Production Installations	09100	Installation of drilling equipment and well drains construction	Same as 5(i) above	Closed for foreign investment/ownership
	(iv) Onshore Pipeline	42219	Installation of onshore pipelines	Not specifically regulated in the Old NIL. However,	Closed for foreign investment/ownership

No	Business Activity	KBLI	Specific Activities Covered	Old NIL (Maximum foreign investment/ ownership)	New NIL (Maximum foreign investment/ ownership)
	Installations		for oil & gas business	several business activities, classified as part of KBLI 42219 and including construction of water transmission pipelines, telecommunications and electricity networks, were regulated as follows: (i) for construction with a work value of more than Rp.1,000,000,000: open for foreign investment/ownership up to a maximum of 67% (ii) for construction with work value of less than Rp.1,000,000,000: closed for foreign investment/ownership	
	(v) Offshore Pipeline Installation	42219	Installation of offshore pipelines for oil & gas business	Same as 5(iv) above	49%
	(vi) Horizontal and Vertical Tank Construction	42914	Construction of horizontal and vertical tank facilities	Not specifically regulated in the Old NIL – therefore notionally open for 100% foreign investment/ownership	Closed for foreign investment/ownership
	(vii) Storage Installation and Onshore Marketing of Oil & Gas	42914	Construction, maintenance and repair of oil & gas storage facilities	Not specifically regulated in the Old NIL – therefore notionally open for 100% foreign investment/ownership	Closed for foreign investment/ownership
6.	Drilling Services				
	(i) Onshore Oil & Gas Drilling	09100	Onshore drilling process, including installation of drilling equipment	95%	Closed for foreign investment/ownership
	(ii) Offshore Oil & Gas Drilling	09100	Offshore drilling process, including installation of drilling equipment	95%	75%

No	Business Activity	KBLI	Specific Activities Covered	Old NIL (Maximum foreign investment/ ownership)	New NIL (Maximum foreign investment/ ownership)
	(iii) Geothermal Drilling	09900	Geological observation, pumping and channeling of mining commodities and mining experiment services, etc	100%	95%
7. Oil & Gas Supporting Services					
	(i) Well Operation & Maintenance Services	09100	Pumping, blocking and closing of production wells maintenance, repair and dismantling of cementing oil & gas wells	95%	Closed for foreign investment/ownership
	(ii) Design and Engineering Services	71100	Architect consultancy services, such as building design and drafting, architecture services, including building inspection services, technical planning and consultancy, such as machinery, factory and industry processes, projects involving civil, hydraulic and traffic engineering, project expansion and realization related to construction, project expansion using air conditioning, cooler, hygiene and pollution control techniques, acoustic techniques etc	Not specifically regulated in the Old NIL – therefore notionally open for 100% foreign investment/ownership	Closed for foreign investment/ownership

No	Business Activity	KBLI	Specific Activities Covered	Old NIL (Maximum foreign investment/ ownership)	New NIL (Maximum foreign investment/ ownership)
	(iii) Technical Inspection Services	71203	inspection activities in relation to product design, products, services and processes including inspection, pressing equipment, pre-shipment, production process, installation, maintenance, periodical inspection of the safety of motorized vehicles but does not include building inspection services	55%	Closed for foreign investment/ownership

2. Some of the Major Changes in Detail

2.1 Mining

2.1.1 **General:** Although the 2014 Negative Investment List does not make any specific changes to the permitted levels of foreign investment/ownership for (i) mineral exploration or production or (ii) mining services, a number of changes to the permitted levels of foreign investment/ownership in more general areas of economic activity, such as distribution and surveying, are potentially very relevant to companies that support mineral exploration and production or mining services provision in various ways.

2.1.2 **Distribution of Mining Equipment & Spare Parts:** The 2014 Negative Investment List has introduced a potentially important change for the mining sector by, for the first time, including “Distribution” as a discrete sector of the Indonesian economy. Previously, “Distribution” was not included in the Negative Investment List and, therefore, it was widely accepted that a PMA Company carrying on “Distribution” could be 100% foreign owned.

The 2014 Negative Investment List now limits foreign ownership of PMA Companies carrying on “Distribution” to a maximum of 33%.

It is important to understand that “Distribution” includes the activities of importation and wholesaling.

The potential significance, for the mining sector, of the new restriction on foreign ownership of PMA Companies carry on “Distribution” is that, in recent years, many foreign mining equipment and spare parts providers, supplying to mineral explorers and producers, as well as to mining services providers, operating in Indonesia, have set up their own 100% foreign owned PMA Companies to import into Indonesia and distribute, at the wholesale level, mining equipment and spare parts. This was done so as to enable Indonesian mining companies and mining services providers to continue to buy foreign produced mining equipment and spare parts notwithstanding the obligation, in the 2009 Mining Law and attached to all mining licenses/mining services in the form of IUPs and IUJPs, that Indonesian mining companies and mining services providers source their required goods and services locally. As long as the foreign produced mining equipment and spare parts were imported into Indonesia and sold, at the wholesale level, by an Indonesian legal entity in the form of a PMA Company, this was generally regarded as technical compliance, by mineral explorers, producers and services providers, with the obligation to source goods locally.

While so long as the Investment Co-ordination Board (“**BKPM**”) continues to interpret “Distribution” in an expansive manner, it seems that foreign mining equipment and spare parts suppliers, wanting to set up PMA Companies for the purpose of handling importation and wholesaling, will be confined to a maximum of only 33% ownership of the resulting PMA Companies.

Although it is not apparent from reading the 2014 Negative Investment List itself, BKPM currently takes the view that already established, 100% foreign owned, PMA Companies, carrying on importation and wholesaling of mining equipment and spare parts, are not obliged to immediately reduce their foreign shareholding to 33%. BKPM’s position, at the moment, is that such existing PMA Companies may continue to be 100% foreign owned until such time as they need to go back to BKPM for an amendment of their existing BKPM approvals to add an additional business line, to increase the amount of their investment funds etc. BKPM has, however, also indicated that existing PMA Companies, carrying on importation and wholesaling of mining equipment and spare parts, which are currently more than 33% foreign owned but less than 100% foreign owned will not be allowed to increase their foreign shareholdings.

The position of BKPM, as outlined in the previous paragraph, effectively gives an element of “grandfather protection” for existing PMA Companies which do not meet the new foreign ownership restrictions reflected in the 2014 Negative Investment List (“**Limited BKPM GP**”). Limited BKPM GP, though, merely reflects the current unwritten policy of BKPM and, therefore, is subject to change without notice. Existing PMA Companies certainly have no legal right to insist upon the Limited BKPM GP.

- 2.1.3 **Geological Services:** The other potentially important change for the mining sector, introduced by the 2014 Negative Investment List, is the reduction in the maximum level of foreign ownership of PMA Companies, providing geological and geophysical surveying services in the fields of energy and mineral resources, from 100% to 49%.

A wide range of consultancy service providers, to the mining sector, have traditionally used PMA Companies, with the approved business line of geological services, as their legal entities for operating in Indonesia. Now that such PMA Companies may no longer be wholly or even majority foreign owned, this may represent a significant impediment to new consultancy services providers, to the mining sector, entering the Indonesian market.

Existing wholly foreign owned PMA Companies, providing geological and geophysical surveying services in the fields of energy and mineral resources, should be able to rely on the same Limited BKPM GP available to PMA Companies carrying on distribution of mining equipment and spare parts as explained in 2.1.2 above.

2.2 Oil & Gas

2.2.1 Oil & Gas Construction Services: The maximum permitted foreign ownership for PMA Companies, carrying on activities in any of the major areas of oil and gas construction services, has been significantly reduced by the 2014 Negative Investment List. Most significantly, construction services in the areas of (i) oil and gas upstream production installation, (ii) horizontal and vertical tank installation and (iii) storage installation for onshore marketing of oil and gas which, previously, were notionally open for 100% foreign ownership, are now closed entirely for foreign investment.

While existing, wholly foreign owned, PMA Companies operating in the oil and gas construction services sector should be able to take advantage of the Limited BKPM GP, it is not presently clear whether or not SKK Migas will adopt a similar position to that taken by BKPM. The particular problem which oil and gas services providers face in this regard is the need to obtain and renew, on a regular basis, a business or operating license/permit from SKK Migas, something which requires a supporting recommendation from BKPM. The writer understands that, since the issuance of the 2014 Negative Investment List, BKPM has started refusing requests, for this recommendation letter, from PMA Company oil & gas services providers which are not compliant with the new foreign investment/ownership restrictions in the 2014 Negative Investment List. This need to go back to BKPM, on a regular basis, for a supporting recommendation seems to substantially undercut the benefit which might otherwise be available from the Limited BKPM GP.

2.2.2 Oil & Gas Supporting Services: Oil and gas supporting services have been most seriously affected by the 2014 Negative Investment List with (i) well operation & maintenance services, (ii) design and engineering services and (iii) technical inspection services now wholly closed to foreign investment/ownership despite having previously been notionally open to maximum foreign investment/ownership of 95%, 100% and 55% respectively.

The same uncertainty exists as to whether or not SKK Migas will allow existing, wholly foreign owned, PMA Companies operating in the oil and gas supporting services sector to take advantage of the Limited BKPM GP presently accepted by BKPM. As, however is the case with oil & gas construction services providers, the need to go back to BKPM, on a regular basis, for a supporting recommendation (as part of the SKK Migas business or operating license/permit renewal process) seems to substantially undercut the benefit which might

otherwise be available, to oil & gas supporting services providers, from the Limited BKPM GP.

2.3 **Power Plants:** Foreign promoters of and potential foreign investors in large (**i.e.**, more than 10 MW) power plant projects will understandably be concerned by the new requirement, under the 2014 Negative Investment List, that they “partner” with the Government during an initial “concession period”. This is despite the fact that foreign parties may notionally have 100% investment/ownership during the initial concession period. There are 2 sources of concern. First, the length of the initial “concession period” is unspecified and, therefore, open-ended. Second, just what role the Government will play in the day to day operations of the project, during the concession period” and as part of the “partnership” arrangement remains very unclear.

3. **Trying to Understand the Rationale for the Changes in the 2014 Negative Investment List**

3.1 **Mining:** The downturn in mining industry profitability, as a result of the extended period of low mineral commodity prices, has undoubtedly created a difficult operating environment for all (i) suppliers, whether foreign or local, of mining equipment and spare parts and (ii) geological services. As a result of this difficult operating environment, competition has become particularly intense, driving prices of equipment and services ever lower and posing a real threat to the continued existence of some suppliers. The new restrictions on foreign investment in/ownership of PMA Companies operating in these sectors may, therefore, be seen as part of an endeavor to create greater opportunities for struggling domestic players by reducing the ability of new foreign players to operate independently of domestic players in the Indonesian market.

3.2 **Oil & Gas Services:** Compared to the mining sector, the increased restrictions on foreign investment in/ownership of PMA Companies operating in the oil & gas services sector are much more difficult to understand. This is because these new restrictions come at a time when Indonesia is facing declining oil production and when reversing that trend is supposedly a matter of the highest national priority. The casual observer could be forgiven for thinking that it would actually be much more logical for the Government to reduce the restrictions on foreign investment in/ownership of PMA Companies operating in the oil and gas services sector as part of an endeavor to ensure that oil and gas producers in Indonesia have access to the best available international expertise and technology as 1 of the drivers for increasing or at least reducing the decline in the country’s oil production.

Certainly, the increased restrictions on foreign investment in and ownership of PMA Companies operating in the oil & gas services sector do not sit very well with Indonesia’s National Energy Policy for the period 2014 to 2050 as set out in the early 2014 Government Regulation re National Energy Policy (“**GR 2014/NEP**”). Article 5 of GR 2014/NEP makes the realization of “energy independence” and “energy security” the primary aims and objectives of the National Energy Policy for the period 2014 to 2050, with (i) “energy independence” being defined as ensuring the availability of energy utilizing the maximum potential of domestic resources (Article 1.26) and (ii) “energy security” being defined as ensuring the availability of energy and people’s access to energy at affordable prices in the long term and with proper

regard for environmental protection (Article 1.25).

It is very clear from GR 2014/NEP that coal is intended to be the major source of energy in Indonesia during the period covered by the National Energy Policy and that, in this regard, coal and its various derivatives will increasingly replace oil for domestic energy purposes. Nevertheless, coal is never going to entirely replace oil for domestic energy purposes and, therefore, maximizing cost efficient and effective oil and gas production is an inherent part of the National Energy Policy. Indeed, this is made quite explicit in Article 10(1)(a) of GR 2014/NEP which provides that the availability of sufficient energy is dependent upon, among other things, (i) improved resource exploration, (ii) increased energy production from domestic energy resources and (iii) improved reliability of production systems, transport and distribution of energy supply. Increasing maximum permitted, foreign investment/ownership in the oil & gas services sector is surely more likely to increase the availability of sufficient energy, from domestic oil and gas sources, than is reducing maximum permitted, foreign investment/ownership in the oil and gas services sector.

A closer reading of GR 2014/NEP, however, indicates that energy independence and energy security are not the only goals of the National Energy Policy. More particularly, Article 24(2) of GR 2014/NEP makes clear that, as part of developing the local energy industry, the Government wants to (i) increase local content in the national energy industry, (ii) provide greater opportunities for national companies in the management of oil and gas and (iii) build the domestic energy industry through the “purchases” of “licenses”. This last point indicates to the writer that, as part of the National Energy Policy, the Government is hoping to reduce and replace direct foreign investment/ownership in the oil & gas services sector with licenses of technology and know-how from foreign suppliers of oil & gas services to domestically owned companies which will then provide the relevant services using the technology and know-how they have obtained, through licenses, from now-excluded foreign suppliers of oil & gas services.

It remains to be seen whether or not foreign providers of oil & gas services, in the nature of (i) oil & gas construction services, (ii) drilling services, (iii) surveying services and (iv) oil & gas supporting services, will be willing to license their valuable technology and know-how to domestically owned companies. This seems especially problematic given the relatively poor protection currently available for intellectual property rights in Indonesia.

SUMMARY & CONCLUSIONS

The 2014 Negative Investment List further restricts foreign investment/ownership in various areas which are very relevant to the mining, oil & gas and power plant sectors although mineral and oil & gas explorers and producers are not themselves directly impacted by the changes which the 2014 Negative Investment List makes. The potential implications of these further restrictions for foreign sellers of mining equipment and spare parts, as well as for foreign providers of oil & gas services, are particularly concerning.

While the rationale for the reductions in the maximum permitted foreign investment in /ownership of PMA Companies carrying on the activities of distribution of mining equipment & spare parts and provision of geological services may be clear enough in the current difficult economic environment facing the mining industry, the same is not the case for the reductions in the maximum permitted foreign investment in /ownership of PMA Companies carrying on the activities of provision of oil & gas services. Given Indonesia's declining oil production, it would seem more logical to allow greater foreign investment in the oil and gas services sector as 1 way to help counter this worrying trend. However, a careful reading of Indonesia's new National Energy Policy reveals that the goals of energy independence and energy security may be as much, if not more, about increasing domestic ownership of services providers as they are about increasing or, at least, reducing the rate of decline in Indonesia's oil production. The supposed national priority of increasing the country's oil production seems less compelling in these circumstances.

The undeniable fact that the 2014 Negative Investment List has also reduced the restrictions on foreign investment in other sectors of the Indonesian economy unrelated to mining, oil & gas and power plants will be of little consolation to foreign investors in the mining, oil & gas services and power plant sectors.

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