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MEASURES TO STOP ILLEGAL MINERAL & COAL EXPORTS – A PROBABLE TRIUMPH OF FORM OVER SUBSTANCE¹²³⁴⁵

INTRODUCTION

The Government is becoming increasingly worried about the scale of Indonesia's illegal mineral & coal exports and the loss of Government revenue these illegal mineral & coal exports represent.

Illegal coal exports have, for many years, been a particularly serious problem for Indonesia.

The enforcement of the long proposed, January 2014 ban on the export of unprocessed metal minerals, as a way of forcing metal mineral producers to carry out domestic processing and refining, is only likely to have materially increased the size of the problem.

In an endeavor to reduce the quantity of illegal mineral & coal exports and the associated loss of Government revenue, the Government has introduced various administrative and regulatory changes, over the past 12 months, with regard to the sale and transportation of minerals & coal. Further changes are foreshadowed, in the coming months, with regard to the export of coal.

Notwithstanding the actual and proposed administrative and regulatory changes, however, it must be seriously questioned whether these initiatives stand much chance of success. In this regard, it has to be asked whether it is reasonable to expect that those mineral & coal producers and traders, which have previously flouted, with relative impunity, the laws on illegal mining and illegal export, will now voluntarily comply with the new administrative procedures and the new regulatory regime when there is clearly so much to be gained, financially, from business as usual? Indeed, the real reason for the scale of Indonesia's illegal mineral & coal exports seems to have very little at all to do with inadequate existing administration procedures for exports or with insufficient existing regulations on the sale, transportation and export of minerals & coal and everything to do with the poor enforcement of those existing administrative procedures and regulations at the national, provincial and regional levels. As such, the slew of new and proposed administrative and regulatory initiatives may be, in large measure, just a wasted effort and, in every sense, a triumph of form over substance unless these initiatives are complemented by rigorous enforcement efforts at the national, provincial and regional levels.

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In this article, the writer will briefly review the nature and scale of Indonesia's illegal mineral & coal export problem before looking, in some detail, at the new and proposed administrative and regulatory initiatives for combating the problem as well as at their likely chance of success.

BACKGROUND

It has been widely reported in the popular press that the trade data of Indonesia's trading partners show vastly greater imports of coal and metal minerals (particularly, bauxite and nickel) from Indonesia than the trade data of Indonesia indicates is exported. To date, most of the attention has focused on coal which accounts for roughly 84%, by value, of Indonesia's total mineral exports. An article in the 3 October 2013 edition of the Singapore Business Times suggested that the discrepancy amounted to as much as 12-15% of Indonesia's total coal production of some 420 million tons or 50 to 60 million tons of illegal coal exports annually. At the time and on the basis of the average 2012 benchmark price for coal, the Singapore Business Times estimated that the associated loss of tax revenue to the Government amounted to about US\$460 million annually. Although coal prices have fallen significantly in the last 2 years, the magnitude of the lost tax revenue remains huge by any measure. This is all the more so when one realizes the Singapore Business Times was really only referring to unpaid non-tax state revenues or "royalties". Recognizing that illegal exporters of minerals & coal surely do not declare and pay income tax on the net profits of their illegal activities, the total losses to the Government, from all sources, are undoubtedly much greater.

At the June 2014 Coaltrans Conference in Bali, the current Director General of Minerals & Coal, Dr. Sukhyar, acknowledged the huge problem posed by illegal coal exports and seemed to accept the general correctness of the widely reported figure of 50 to 60 million tons in illegal coal exports annually.

Although a much smaller problem, traditionally, in terms of lost tax revenue, it must be assumed that illegal exports of metal minerals are becoming a growing problem for Indonesia and one that is likely to have increased exponentially post January 2014 when it became no longer possible to export nickel, bauxite and other so-called "Category 2 Metal Minerals" in anything other than fully processed and refined form. The assumed exponential increase in illegal exports of Category 2 Metal Minerals, post January 2014, will have not been driven, primarily, by a desire to avoid paying the royalties due on the first sale of these Category 2 Metal Minerals (as is the case for illegal coal exports) but, rather, by the complete inability of producers of these Category 2 Metal Mineral producers to legally export their unprocessed minerals even if they are prepared to pay the applicable royalties. In the absence of any or sufficient domestic demand for unprocessed Category 2 Metal Minerals, the relevant producers are left with only 3 alternatives – (i) carry out full domestic processing and refining even if it is uneconomic or impractical due to infrastructure constraints, (ii) cease operating and go out of business altogether or (iii) find a way to keep exporting their unprocessed Category 2 Metal Minerals illegally. It would, perhaps, not be surprising if some small and medium sized Category 2 Metal Mineral producers decided to follow the example, which has, apparently, been long set by some of Indonesia's small and medium sized coal producers, and opt for the third alternative. That this is, indeed, the case is strongly suggested by a 13 January 2014 article in The Jakarta Post which quoted the commander of Naval Base Region IV, which covers the bauxite abundant Riau Islands, as saying that "his force was intensifying patrols to prevent [unprocessed metal] mineral ore from being shipped overseas", What is

surprising, however, is following a couple of early reports of the Indonesian navy having intercepted 2 illegal cargoes of bauxite immediately after the January 2014 enforcement of the export ban, there have been no follow up reports in the popular media on any continuing successes of the Indonesian navy in intercepting illegal shipments of unprocessed Category 2 Metal Minerals. It would seem then that either small and medium sized Category 2 Metal Mineral producers are, in fact, very law abiding and have decided to simply shut down and go out of business altogether or the Indonesian navy has been remarkably ineffectual despite clearly understanding the seriousness of the potential problem. If the latter is, in fact, the case, one can only speculate as to what might be the real cause of these ineffectual efforts.

In the previously referenced 3 October 2013 Singapore Business Times article, Thamrin Sihite from the Ministry of Energy & Mineral Resources (“**MoEMR**”), suggested that it was the existence of a large number of so-called “mouse ports”, in the coal producing regions of Indonesia, which enabled coal producers, without mining licenses (“**IUPs**”), to load coal onto ocean going barges, from small and remotely located jetties, for transfer and illegal export. While this may well partially explain Indonesia’s illegal coal exports, it seems inherently implausible to the writer that very small scale coal producers, without IUPs or adequate capital equipment, could really be exclusively responsible for 50 to 60 million tons of illegal coal exports per year. Putting this in context and as pointed out in the 3 October 2013 Singapore Business Times article, 50 to 60 million tons of illegal coal exports per year is equivalent to the entire annual coal imports of Taiwan which is the world’s 5th largest coal importer. The writer has also calculated that the shipment of 50 to 60 million tons of illegal coal exports per year requires between 770 and 925 fully loaded Panamax bulk carriers, of 65,000 DWT capacity each, to transport the same. It is extraordinary then that the writer does not recall ever seeing many reports in the popular media of the Indonesian police preventing the loading of illegal coal cargoes on to ocean going barges or of the Indonesian navy intercepting illegal shipments of coal at sea. Perhaps those Panamax carriers are simply hard to spot – curious really given that a Panamax carrier is 294.13 metres long (nearly 3 times the length of an international standard football field) and 32.31 metres wide.

COMMENTARY

1. **Preliminary Remarks:** The Government’s actual and proposed measures to stop illegal exports of minerals & coal and thereby increase Government revenues from mining include (i) administrative changes designed to ensure the more timely collection of royalties payable at the time of first sale of minerals & coal, (ii) regulations restricting the set of producers from which mineral & coal traders can source minerals & coal and proposals to limit the export of coal to 14 (or, possibly, 15) specified ports only and (iii) the cancellation of the IUPs of non-compliant mineral & coal producers and traders.

2. **More Rigorous Collection of Non-Tax State Revenue**
 - 2.1 **Overview:** In July 2013, DGoMC issued 2 circulars directed at ensuring the timely payment of taxes by mining companies – DGoMC Circular No. 4 re Optimization of Non Tax State Revenue (“**DGoMC Circular 4/2013**”) and DGoMC Circular No. 5 re Supervision & Inspection of Marketing & Finance for IUP Holders (“**DGoMC Circular 5/2013**”).

2.2 **DGoMC Circular 4/2013:** Addressed to all IUP holders, DGoMC Circular 4/2013 seeks to ensure the timely payment of taxes by mining companies through imposing new deadlines and procedures for the payment of:

- (a) deadrent not later than 1 month after the issuance of the relevant IUP in the case of 1st year obligations and, thereafter, not later than 1 month in advance of the expiry of each year of the IUP validity period, with payment to be made by direct deposit to the State Treasury; and
- (b) royalties before the relevant minerals or coal are hipped or transported, with payment to be made by direct deposit to the State Treasury.

IUP holders, with outstanding deadrent or royalty payment obligations as of the date of DGoMC Circular 4/2013, and which have already been warned about their outstanding obligations, were given 1 month, from 4 July 2013, to pay all outstanding amounts of deadrent and royalties.

IUP holders, which failed to satisfy their outstanding deadrent and royalty payment obligations by 4 August, are prohibited from shipping, transporting or selling their minerals or coal.

Where the IUP holder is shown to have been negligent in (i) reporting its deadrent or royalty payment obligations or (ii) in making the applicable deadrent or royalty payments and this results in a loss of State revenue (something which, presumably, will always be the case), penalties of imprisonment for up to 1 year and/or a fine of up to 2 times the outstanding deadrent or royalty amount are to be imposed on the IUP holder.

Where the IUP holder is shown to have intentionally (i) not reported or discharged its deadrent or royalty payment obligations or (ii) maintained or submitted false, forged or incomplete documents, records or reports in respect of its deadrent or royalty payment obligations, the applicable penalties become imprisonment for up to 6 years and/or a fine of up to 4 times the outstanding deadrent or royalty amount.

Repeating any of the intentional offences, as outlined in the previous paragraph and within 1 year, results in a doubling of the applicable penalties.

DGoMC Circular 5/2013: Addressed to all Governors, Regents and Mayors in mining areas, DGoMC Circular 5/2013 sets out how the Government intends to enforce the new deadlines and procedures for payment of deadrent and royalties as set out in DGoMC Circular 4/2013.

More particularly, DGoMC Circular 5/2013 requests the relevant Governors, Regents and Mayors to carry out inspections of the marketing and finance activities of IUP holders before minerals & coal are shipped or transported for the purpose of ensuring that all applicable deadrent and royalties have been paid by the IUP holders.

Governors, Regents and Mayors are directed to prohibit the sale, shipment or transportation of the minerals & coal of IUP holders, with outstanding deadrent or royalty payment obligations as of the date of DGoMC Circular 5/2013 and which, having already been warned about their outstanding obligations, fail to pay all outstanding amounts of deadrent and royalties within 1 month from 4 July 2013.

- 2.3 **Assessment:** Prohibiting the sale, shipment and transportation of minerals & coal, where the relevant IUP holder has not discharged its deadrent and royalty payment obligations, certainly **should be** a big incentive for IUP holders to keep their deadrent and royalty payment obligations up to date, even ignoring the penal sanctions of imprisonment and large fines. Whether or not, however, DGoMC Circular 4/2013 and DGoMC Circular 5/2013 will, in fact, prove to be the necessary incentive depends, to a very large degree, on the Government's practical ability to enforce DGoMC Circular 4/2013 and DGoMC Circular 5/2013. In this regard and as DGoMC Circular 5/2013 makes all too clear, the Government is relying heavily on support from Governors, Regents and Mayors, in mining areas, to enforce the new payment obligations through timely inspections and preventing the sale, shipment and transportation of minerals & coal, where the relevant IUP holder is found, as a result of these inspections, to have not discharged its deadrent and royalty payment obligations. Theoretically, as the Provinces and Regencies receive a share of the non-tax State revenue collected by the Government, Governors, Regents and Mayors in mining areas have good reason to cooperate with the Government in carrying out the inspections requested and preventing the sale, shipment and transportation of minerals & coal in appropriate cases. However, it seems questionable whether or not most Provinces and Regencies, in mining areas, have the necessary human and technical resources to carry out the requested inspections of IUP holder marketing and finance activities on a regular basis. Further, with regional autonomy, it is doubtful that the Government has the legal authority to compel the Provincial Governments and Regional Governments to act as its collection and enforcement agents for deadrent and royalty payment obligations if the Provincial Governments and Regional Governments are not otherwise willing to do so voluntarily. Finally and most importantly, the supposed incentive Governors, Regents and Mayors, in mining areas, have to cooperate with the Government in carrying out the requested inspections and preventing the sale, shipment and transportation of minerals in appropriate cases, must be regarded as being highly questionable if, in fact, officials at the Provincial Government and Regional Government level are actually complicit in the illegal sale and export of minerals & coal and derive a substantial direct and personal financial benefit from such complicity. Should such complicity exist, it is likely to provide a much more effective and tangible incentive **not** to cooperate in preventing the sale, shipment and transportation of minerals & coal in appropriate cases.

Perhaps the best evidence of the ineffectiveness, for whatever reason, of DGoMC Circular 4/2013 and DGoMC Circular 5/2013 is the complete absence of any reports from DGoMC on the imposition of any penalties as a result of non-compliance with DGoMC Circular 4/2013 and DGoMC Circular 5/2013.

3. **Stricter Licensing of Mineral & Coal Traders**

- 3.1 **Overview:** Recognizing that (i) there would be no illegal sales/exports of Indonesia's minerals & coal without willing foreign buyers as well as willing domestic sellers and (ii) the key role played by mineral & coal traders in intermediating between such willing foreign buyers and willing domestic sellers of Indonesia's minerals & coal, the Government has increasingly tried to combat the problem of illegal mineral & coal exports by more closely regulating the activities of mineral & coal traders. This has included both (i) imposing new restrictions on the set of mineral & coal producers from which traders can source minerals & coal and (ii) making it more difficult to obtain a Special Operation Production IUP for Transportation & Sales, being the business license required by all mineral & coal traders operating in Indonesia and which do not have their own production activities ("**Special IUP for Transportation & Sales**"). In November 2013, MoEMR issued Regulation No. 32 of 2013 re Procedures for the Granting of Special Permits in respect of Minerals and Coal Mining Activities ("**MoEMRR 32/2013**"). More recently, in May 2014, DGoMC issued Instruction No. 2 of 2014 re Postponement of Issuance of Special IUPs for Transportation & Sales ("**DGoMCI 2/2014**").
- 3.2 **MoEMRR 32/2013:** MoEMRR 32/2013 sets out, for the first time, the detailed administrative, technical, environmental and financial requirements which must be met by applicants for Special IUPs for Transportation & Sales.

The applicable administrative requirements include the requirement to provide copies of (i) the memoranda of understanding re transportation and sales of minerals & coal which the applicant has entered into with producers of minerals & coal, (ii) the IUPs/IUPKs of the relevant producers of minerals, (iii) the certificate issued by DGoMC, upon request and payment, in respect of the inclusion of the IUP/IUPK of each of the relevant producers of minerals & coal in the Clean & Clear List maintained by DGoMC ("**C&C List**") and (iv) the memoranda of understanding re sale and purchase of minerals & coal which the applicant has entered into with domestic and foreign buyers of minerals & coal (Article 16(1) of MoEMRR 32/2013).

The applicable technical requirements include, in respect of each IUP/IUPK holder from which the applicant intends to source minerals & coal, (i) copies of the production plan, work plan and budget and (ii) proof of payment of 5 years' deadrent and royalties (Article 17(2) of MoEMRR 32/2013).

MoEMRR 32 /2013 goes on to provide that, if and when approved and issued, Special IUPs for Transportation & Sales will set out the details of each producer from which the relevant holder of the Special IUP for Transportation & Sales intends to source minerals & coal (Article 20(5)(g) of MoEMRR 32/2013). By implication and as interpreted and applied by MoEMR, if the holder of a Special IUP for Transportation & Sales subsequently wants to source minerals & coal from a new producer, it is necessary for the holder of the Special IUP for Transportation & Sales to amend its Special IUP for Transportation & Sales so as to include the details of the new producer before actually sourcing any minerals & coal from that new producer. This involves submitting a new application including the same prescribed information in respect of the new producer as was the case with the existing producers covered by the relevant Special IUP for Transportation & Sales.

Just in case there was any doubt as to the objective of the above described requirements, MoEMR 32 /2013 expressly prohibits holders of Special IUPs for Transportation & Sales from sourcing minerals & coal from producers which do not have IUPs/IUPKs that are included in the C&C List (Article 28 of MoEMRR 32/2013).

Failure to observe the above prohibitions may result in the imposition of progressive and increasingly severe administrative sanctions on holders of Special IUPs for Transportation & Sales. These sanctions are in the form of (i) written warnings, (ii) suspension of activities and (iii) revocation of Special IUPs for Transportation & Sales.

- 3.3 **DGoMCI 2/2014:** In a surprising development, given the comprehensive nature of MoEMRR 32 /2013, DGoMCI 2/2014 postpones, for 12 months, the issuance of any further Special IUPs for Transportation & Sales which are in respect of inter-province or cross border (i.e., foreign) sales of coal only and on the basis of applications submitted after 16 May 2014. Already submitted applications for Special IUPs for Transportation & Sales and applications to extend/renew existing Special IUPs for Transportation & Sales are not affected by the 12 month moratorium.

It should be carefully noted that DGoMCI 2/2014 does not impose any moratorium on the issuance of new Special IUPs for Transportation & Sales in respect of metal minerals, non-metal minerals or rocks.

- 3.4 **Assessment:** The stricter licensing requirements for mineral & coal traders, reflected in MoEMRR 32 /2013, are clearly intended to make it much more difficult for (i) Indonesian mineral & coal producers to sell and export their minerals & coal without paying the applicable royalties and (ii) mineral & coal traders to facilitate or at least be complicit in the sale and export of minerals & coal without the applicable royalties having been paid. If nothing else, it should make more transparent the source of all minerals & coal handled by holders of Special IUPs for Transportation & Sales.

The inherent weakness of MoEMRR 32 /2013, however, is that it assumes mineral & coal traders will comply with MoEMRR 32 /2013 and not source minerals & coal from producers which do not have IUPs/IUPKs that are included in the C&C List. This assumption may not be warranted for at least 2 reasons. First, it has always been illegal to sell and/or export minerals & coal in respect of which the applicable royalties have not been paid because minerals & coal belong to the State until such time as all taxes due to the State in respect of such minerals & coal have been fully paid. Yet, this has not prevented some mineral & coal traders from facilitating such illegal sales/exports over a long period of time. Why then is it likely that these “renegade” mineral & coal traders will now start complying with the law when they did not do so previously? Clearly, the benefits from non-compliance exceed the benefits from compliance. Second, the Government has not been previously able to effectively police all sales and exports of minerals & coal because it lacks the large number of competent and honest employees/officials required to do so. There is nothing in MoEMRR 32 /2013 which changes this unfortunate fact. The reality seems to be that MoEMRR 32 /2013 will simply make life much more difficult for the large number of law abiding mineral & coal traders, in terms of the

applicable requirements for obtaining and amending/extending/renewing their Special IUPs for Transportation & Sales without, however, doing anything at all to combat the activities of the small minority of “renegade” mineral & coal traders.

The rationale for DGoMCI 2/2014 is unclear although it has obvious parallels with the existing moratorium on the issue on new Exploration IUPs which is intended to give MoEMR an opportunity to resolve the various problems associated with a large number of the existing IUPs/IUPKs. It may be MoEMR/DGoMC has belatedly realized that a more thorough reform of coal trading is required than that presently provided for by MoEMRR 32 /2013. Alternatively, MoEMR/DGoMC may have simply come to the conclusion that, in the current highly depressed market for coal, interest in Indonesian coal is much reduced and, consequently, there are already more than enough coal traders to intermediate between domestic producers and foreign buyers of Indonesian coal.

4. **Proposed Restrictions on Coal Exports**

- 4.1 **Overview:** Recognizing that coal is, by far, the largest component of Indonesia’s illegal mineral & coal exports, the Government recently indicated that it is considering restrictions specifically targeted at coal exports. The proposed new restrictions on coal exports include (i) requiring all exporters of coal to register themselves with the Ministry of Trade (“**MoT**”) and (ii) limiting coal exports to 14 (or, possibly, 15) specified ports only.
- 4.2 **Registration of Coal Exporters:** Although the details of the coal exporter registration proposal have yet to be spelled out by the Government, it seems reasonable to assume that the coal exporter registration proposal would be implemented (if at all) by extending the ambit of (i) MoT Regulation No. 29 of 2012 re Export Requirements for Mining Products (“**MoTR 29/2012**”) and (ii) DGoMC Regulation No. 574 of 2012 re Procedures for Obtaining Registered Exporter Status (“**DGoMCR 574/2012**”) to include coal. At the moment, MoTR 29/2012 and DGoMCR 574/2012 only cover those metal minerals which may still be exported in semi-concentrate form and subject to the payment of an export tax.

Extending MoTR 29/2012 and DGoMCR 574/2012 to include coal would require that:

- (a) would-be exporters of coal have the status of “Registered Exporters of Mining Products” (“**Registered Exporter**”);
- (b) in order to become a Registered Exporter, application for Registered Exporter status be made to MoT’s Director General of Foreign Trade (“**DGoFT**”) (“**RE Application**”);
- (c) the RE Application be accompanied by various supporting documents including, most importantly, a recommendation from DGoMC (“**RE Recommendation**”) which would only (i) be granted after satisfying various conditions including that (A) in the case of producers, the relevant Operation Production IUP is on the C&C List and (B) in the case of traders, the relevant trader holds a Special IUP for Transportation & Sales and is in full compliance with all its obligations under the Special IUP for Transportation &

Sales; and (ii) the RE Recommendation would have to be renewed every months;

- (d) each export transaction be the subject of a separate export approval from DGoFT on behalf of MoT (“**Export Approval**”);
- (e) the application for Export Approval be accompanied by a recommendation from DGoMC (“**EA Recommendation**”), which EA Recommendation is separate and distinct from the RE Recommendation the exporter obtained from DGoMC in order to apply for its Registered Exporter status;
- (f) a so-called “verification or technical search” be carried out in respect of each export transaction which the Registered Exporter wishes to undertake in reliance upon its Export Approval (“**Verification**”);
- (g) the Verification be carried out by a surveyor approved by DGoFT on behalf of MoT (“**Surveyor**”) and appointed by the Registered Exporter; and
- (h) the Registered Exporter submit monthly reports, on its coal export activities, to the Director of Industrial Products Export & Mining with copies to DGoMC.

4.3 **Limiting Coal Exports to 14 Ports Only:** Enquiries made with DGoMC re the proposal to limit coal exports to 14 (or, possibly, 15) ports only indicate that the 14 (or, possibly, 15) ports are all located in Kalimantan and Sumatera as follows:

- (a) **East Kalimantan:**
 - (i) Balikpapan Bay;
 - (ii) Adang Bay;
 - (iii) Berau; and
 - (iv) Maliy;
- (b) **South Kalimantan:**
 - (i) Tobaneo;
 - (ii) [Pulau Laut];
 - (iii) Sungai Danau; and
 - (iv) Batu Licin;
- (c) **Sumatera:**
 - (i) Aceh;
 - (ii) Padang Bay;
 - (iii) Riau Bay;
 - (iv) Jambi Bay;
 - (v) Bengkulu Port;
 - (vi) Tanjung Api-Api; and

(vii) Tarahan.

All the specified 14 (or, possibly, 15) ports are sea ports not river ports. Accordingly, the proposed limitation on the use of 14 (or, possibly, 15) ports should not place any restrictions on the use of river ports for the intermediate transportation of coal from the mine site to 1 of the 14 (or, possibly, 15) specified sea ports for export.

4.4 **Assessment:** As is the case with the stricter licensing requirements for mineral traders, it seems likely the proposed restrictions on coal exports will make life significantly more difficult, in terms of administration and compliance, for the great majority of law abiding coal exporters. Just as metal mineral producers and traders have found obtaining and maintaining (i) their status as Registered Exporters and (ii) the Export Approvals frustrating, inefficient, time consuming and expensive, it is inevitable coal exporters, whether they be coal producers or coal traders, will have a similar experience.

At the same time, it is not clear to the writer that the proposed restrictions on coal exports will do much to address the real causes of illegal coal exports. More particularly, it is hard to imagine why the small number of producers and traders, currently engaged in the illegal export of coal, would feel compelled to comply with the proposed restrictions on coal exports when the current system works just fine for them and compliance would necessarily bring to an end the much more lucrative illegal coal export trade.

Once again, the inherent weakness in the proposed restrictions on coal exports will surely be enforcement. It is not presently legal to export coal without paying the applicable royalties and port authorities are meant to satisfy themselves that the applicable royalties have been paid before allowing the loading of coal for export. This, however, is clearly not happening in many cases either because of the complicity of some port officials or because the coal is being exported through so-called “mouse ports” in remote locations where there are no officials on duty. How is MoEMR/MoT going to prevent (i) the complicity of officials at the 14 (or, possibly, 15) specified ports and/or (ii) the continued use of “mouse ports” where there are no officials on duty if and when the proposed restrictions on coal exports become a reality? In the case of “mouse ports”, although there may not be any officials on duty at these remote locations, it would be quite naïve to imagine that some local government officials and police, in the Regencies where these “mouse ports” exist, are not fully aware of and otherwise, to a greater or lesser degree, complicit in the use of such “mouse ports” for the export of coal without paying the applicable royalty. It is by no means clear to the writer that, even assuming MoEMR/MoT has the necessary commitment and will to deal with these matters, it has the legal authority and the human resources required to do so.

5. **Cancellation of IUPs**

5.1 **Overview:** As a supposedly tangible sign of its seriousness in stopping illegal mineral & coal exports, MoEMR has been reported as having (i) revoked a total of 85 Operation Production IUPs for nickel in Morwali Regency, Central Sulawesi (Business Indonesia 3 June 2014) and (ii) temporarily suspended 62 Special IUPs for Transportation & Sales (The Jakarta Post 9 June

2014).

5.2 **Assessment:** Although the cancellation of a small number of IUPs and Special IUPs, as described in 5.1 above, is a step in the right direction and DGoMC has foreshadowed more cancellations to come, with Jambi supposedly being the next target area (Business Indonesia 3 June 2014), it must be questioned whether or not these cancellations will make any significant difference to the overall level of illegal mineral & coal exports. This is for a number of reasons.

First, merely because non-compliant IUPs are cancelled, does not mean that the former holders of those cancelled IUPs will simply cease production and look for another source of livelihood. As a practical matter, what is to stop the former holders of those cancelled IUPs simply resuming production once MoEMR/DGoMC turns its attention to another geographic area?

Second, there is the widely acknowledged problem of rampant illegal mining in Indonesia by parties which have never had IUPs at all, whether compliant or non-compliant. Self-evidently, the cancellation of non-compliant IUPs is no threat to the activities of illegal miners without any IUPs in the first place.

Third, DGoMC acknowledges there are (i) 4,880 IUPs not on the C&C List and (ii) of these 4,880 non-compliant IUPs, the holders of 1,978 IUPs for metal minerals, non-metal minerals and rocks and 400 IUPs for coal have already commenced production without it being clear as to what has happened to the resulting minerals & coal (Business Indonesia 3 June 2014). Why have all these non-compliant but producing IUPs not been cancelled already?

Fourth, while so long as mineral & coal traders can identify (i) overseas buyers willing to purchase the minerals & coal of illegal miners in Indonesia, (ii) illegal miners willing to supply the required minerals & coal and (iii) ports (whether “mouse ports” or otherwise) from which the required minerals & coal can be exported with the complicity of some local government officials, port officials, police and/or navy personnel and without payment of the applicable royalties, is it really going to seriously impede the operations of these rogue mineral & coal traders if their Special IUPs for Transportation & Sales have been temporarily suspended or even cancelled?

The common themes in each of the above reasons are (i) the practical inability of MoEMR/DGoMC to actually control what happens “on the ground” in the mineral rich areas of Indonesia in terms of mineral & coal exports and (ii) the practical ability of illegal miners and rogue traders to continue exporting minerals & coal from Indonesia, indefinitely and without payment of the applicable royalties so long as they can continue to count on the willing complicity of some local government officials, port officials, police and/or navy personnel.

SUMMARY & CONCLUSIONS

The Government is right to be concerned about the problem of illegal mineral & coal exports from Indonesia and the consequent loss of Government revenue from non-payment of the applicable royalties and income tax.

It is inevitable that the January 2014 export ban on unprocessed metal mineral exports has only exacerbated the problem of illegal exports of metal minerals while illegal exports of coal continue unabated.

The Government has taken and is continuing to take a variety of administrative and regulatory actions in an endeavor to control and, hopefully, reduce the problem of illegal mineral & coal exports. While the writer is pleased to assume the good intentions of the Government in pursuing these actions, the likely success of these actions seems highly questionable. This is because the magnitude of Indonesia's illegal mineral & coal exports has very little, if anything, to do with inadequate existing administrative procedures or inadequate existing regulations and everything to do with the inadequate enforcement of existing administrative procedures and regulations at the provincial and regional levels.

Even after all the new and proposed administrative procedures and regulations are in place, the common themes are likely to continue to be (i) the practical inability of MoEMR/DGoMC to actually control what happens "on the ground" in the mineral rich area of Indonesia in terms of mineral & coal exports and (ii) the practical ability of illegal miners and rogue traders to continue exporting minerals & coal from Indonesia, indefinitely and without payment of the applicable royalties so long as they can continue to count on the complicity of some local government officials, port officials, police and/or navy personnel. Unless and until this unfortunate reality materially changes, it is hard to see the problem of Indonesia's illegal mineral & coal exports becoming any less severe.

The Government also needs to face the fact that the undeniable existence of both large numbers of small time, illegal miners and so-called "mouse ports" cannot really explain the magnitude of Indonesia's illegal mineral & coal exports.

Once again, in addressing the fundamental issues facing the Indonesian mining industry, the Government seems to be in danger of allowing form to triumph over substance when it comes to controlling illegal mineral & coal exports and the consequent loss of Government revenue from the non-payment of the associated royalties and income tax.

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