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### CoW/CCoW RENEGOTIATIONS AND INTERNATIONAL ARBITRATION – A TALE OF 2 (VERY DIFFERENT) CITIES<sup>12345</sup>

#### INTRODUCTION

The long running renegotiation of Indonesia’s Contracts of Work (“**CoWs**”) and Coal Contracts of Work (“**CCoWs**”) (“**CoW/CCoW Renegotiations**”) have headed in very different directions for 2 of the largest CoW/CCoW holders being PT Freeport Indonesia (“**Freeport**”) and PT Newmont Indonesia (“**Newmont**”).

Freeport recently finalized its CoW/CCoW Renegotiations with the Government of Indonesia (“**GoI**”), over the so-called “6 Strategic Issues” in respect of which GoI has been seeking major changes to the CoWs/CCoWs and which are at the very heart of the CoW/CCoW Renegotiations (“**6 Strategic Issues**”). Freeport has also now signed a Memorandum of Understanding (“**MoU**”) with GoI regarding the in-principle agreement reached between them on the 6 Strategic Issues (“**Freeport MoU**”). Newmont, on the other hand, has commenced international arbitration against GoI over Newmont’s continuing inability to obtain an export license that it needs in order to be able to recommence exporting semi-processed copper concentrate (“**Export License**”) (“**Newmont Arbitration**”). If recent reports in the popular press are to be believed, Newmont’s renegotiation of its CoW with GoI (“**Newmont CoW**”) is effectively “on hold” pending resolution or withdrawal of the Newmont Arbitration.

Much is being made of what are seen to be the very different approaches taken by Freeport and Newmont to the CoW/CCoW Renegotiations, with Freeport adopting what might be regarded by some as a “carrot” approach and Newmont adopting what might be regarded by others as a “stick” approach. Strong views are being expressed, in various circles, as to which approach makes more sense in terms of the likelihood of delivering a good, long term outcome for the CoW holder concerned and having regard to cultural sensitivities in Indonesia.

In reality, however, the respective situations of Freeport and Newmont are so very different that simplistic comparisons of their respective approaches to the CoW/CCoW Renegotiations, as well as the associated value judgments of which is the better approach, may well be quite misconceived. To misquote the title of a famous book by Charles Dickens, this is very much “A Tale of 2 (Very Different) Cities” in which both approaches may yet prove to be right or, conceivably, both approaches may yet prove to be wrong.

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<sup>5</sup> This article appeared in the August-September 2014 issue of Coal Asia Magazine.

Of perhaps greater interest, than the different approaches themselves of Freeport and Newmont to the CoW/CCoW Renegotiations, are the likely implications of these respective approaches for the numerous other CoW/CCoW holders that are still in the midst of their own CoW/CCoW Renegotiations.

In this article, the writer will review the different approaches of Freeport and Newmont, as well as some only of the interesting legal and strategic issues raised by these different approaches, before focusing on what the different approaches of Freeport and Newmont may mean for the future of the CoW/CCoW Renegotiations still facing all the other CoW/CCoW holders.

## BACKGROUND

1. **Overview:** The long and tortuous history of the CoW/CCoW Renegotiations is set out in a number of previous articles by the writer. Interested readers may refer to (i) *“Amendments to Contracts of Work – Apparent Progress but at What Cost?”*, Coal Asia Magazine, May 2012, Petromindo; (ii) *“CoW/CCoW Renegotiations – The Current Position and the Likely End Game”*, Coal Asia Magazine, July 2013, Petromindo; and (iii) *“Trying to Understand the CCoW/CoW Renegotiations – A Conundrum Wrapped in an Enigma”*, Coal Asia Magazine, March 2014, Petromindo.

Much attention has, inevitably, focused on the 3 largest, foreign owned and controlled holders of metal mineral CoWs being Freeport, Newmont and PT Vale Indonesia (“**Vale**”). GoI has unquestionably placed a very high priority on concluding the CoW/CCoW Renegotiations with at least 1 of Freeport, Newmont and Vale as a way of “breaking the logjam” of the CoW/CCoW Renegotiations and otherwise making it more difficult for the large number of medium sized and smaller CoW/CCoW holders (particularly, medium sized and smaller foreign owned and controlled CoW/CCoW holders) to continue refusing to conclude the CoW/CCoW Renegotiations on terms acceptable to GoI.

2. **Export Licenses:** The exports of both Freeport and Newmont have been in abeyance since January this year when GoI made it clear that, despite allowing “in-principle” the continued interim export of semi-processed Category 1 Minerals for a further 3 years, the actual realization of such exports would be dependent upon obtaining an Export License. The obtaining of Export Licenses has proved very elusive for both Freeport and Newmont, with Newmont being forced to halt production altogether as its storage facilities became full and Freeport reducing its production as the process of obtaining Export Licenses dragged on interminably for both companies. GoI’s continuing refusal to issue Export Licenses to Freeport and Newmont effectively became its major point of leverage in the ongoing CoW/CCoW Renegotiations with Freeport and Newmont as the inability to export their production, in semi-processed or concentrate form, substantially curtailed the cash flows of both companies. It quickly became apparent that the “grand compromise”, which GoI announced in January, would be of little benefit to CoW producers of Category 1 Minerals unless and until they could conclude their CoW/CCoW Renegotiations on terms acceptable to GoI.

3. **Conclusion of Freeport CoW/CCoW Renegotiations:** Multiple 2013 reports in the popular media indicated that Vale was likely to be the first of the “Big 3” to conclude the CoW/CCoW Renegotiations. In fact, however, Freeport has become the first to conclude the CoW/CCoW Renegotiations to the extent, at least, of reaching “in principle” agreement on the 6 Strategic Issues and signing the, most probably not legally binding, Freeport MoU.

Trying to make sense of the confused and confusing (if not outright conflicting) reports in the popular press, it seems that (i) at a limited cabinet meeting on 24 July, the President approved the conclusion of the Freeport CoW/CCoW Renegotiations, (ii) for unknown reasons, the Freeport MoU was signed later that day or early on 25 July although the Coordinating Minister of the Economy (“**CMoE**”) had only just indicated this would not happen until sometime in August after the Idul Fitri (Islamic New Year) holidays, (iii) at about the same time as the signing of the Freeport MoU, Freeport was issued with the Export License and (iv) Freeport will recommence its export of semi-processed copper concentrate within a matter of days.

Just what is in the Freeport MoU remains unclear but, most probably, Freeport and GoI have agreed, in principle only, that (a) Freeport will (i) provide a bond of US\$115 million as evidence of its commitment to build a local smelter in conjunction with other parties, (ii) pay increased royalties on its copper and gold sales of 4% and 3.75% respectively, (iii) pay an export tax, on its copper concentrate exports, over the next 3 years, at declining rates linked to the progress of the smelter construction, (iv) accept a 30% divestiture obligation and (v) reduce its contract area to 10,000 HA for exploitation and 112,000 HA for supporting activities while (b) GoI will issue a special mining license (“**IUPK**”) to Freeport, sometime between 2019 and 2021, which will enable Freeport to continue operating in Papua after 2021 and until at least 2035.

The handling of the 2021 expiry date of the Freeport CoW previously seemed to be a major stumbling block to the conclusion of the Freeport CoW/CCoW Renegotiations, with Freeport insisting that it needed certainty now as to the legal status of its operations, in the 2021 to 2035 period, before undertaking a contemplated major expansion of its underground mining operations and GoI being equally insistent that this could not be settled until 2019 or 2 years before the expiry date of the Freeport CoW and as contemplated by the Freeport CoW itself. Freeport and GoI have, however, apparently managed to overcome this stumbling block in a way that meets both parties’ minimum needs.

It remains unclear, at least to the writer, just how the 30% divestiture obligation will be handled and, more particularly, what divestiture price mechanism Freeport has accepted. It may be that this is something that remains to be worked out.

4. **Commencement of Newmont Arbitration:** Again, trying to make sense of the confused and confusing (if not outright conflicting) reports in the popular press, it seems that (i) Newmont’s continuing inability to obtain an Export License caused it to declare force majeure, on 5 June, in respect of various long term supply contracts, (ii) after much “toing and froing” over whether or not it would also declare a dispute under its CoW and proceed to international arbitration, Newmont announced on 1 July that both it and its majority shareholder (a Dutch investment company, Nusa Tenggara Partnership BV (“**NTPBV**”)) had finally commenced international arbitration against GoI,

(iii) notwithstanding (ii), Newmont has now written to CMOE indicating that it wishes to resume negotiations over the Export License and, presumably, continue the Newmont CoW/CCoW Renegotiations while still proceeding with the Newmont Arbitration and (iv) CMOE has publicly rebuffed Newmont's expressed wish, saying it is impossible for GoI to resume any Export License negotiations/CoW/CCoW Renegotiations with Newmont unless and until the Newmont Arbitration is discontinued.

The Newmont Arbitration has been brought pursuant to the terms of the Newmont CoW as well as pursuant to the bi-lateral investment treaty between Holland and Indonesia ("**H-I BIT**"). Both the Newmont CoW and the H-I BIT provide for the ultimate resolution of disputes by international arbitration. Although the matter in issue, in the Newmont Arbitration, is notionally the refusal of GoI to issue Newmont an Export License, as Newmont says it is entitled to under the Newmont CoW, no one should doubt that the Newmont Arbitration really concerns GoI's continuing insistence upon concluding the CoW/CCoW Renegotiations, as they relate to the Newmont CoW, on terms unacceptable to Newmont in respect of 1 or more of the 6 Strategic Issues.

## COMMENTARY

### 1. **Contrasting and Understanding the Different Approaches of Freeport and Newmont**

The different approaches of Freeport and Newmont to the CoW/CCoW Renegotiations can surely be explained by the very different commercial realities facing Freeport and Newmont in Indonesia.

1.1 **Freeport:** Freeport currently operates the world's second largest, open pit copper mine at Grasberg in Papua which employs some 30,000 workers. Freeport's CoW contract area is also said to include land sitting atop 1 of the world's largest gold ore reserves. The Papua copper and gold resource remains only partially exploited at this stage and Freeport is proposing a major expansion of its underground mining operations, at Big Gossan in Papua's Mimika Regency, to more fully exploit this copper and gold resource which is expected to last well beyond the expiry of its existing CoW in 2021. Further, the Papua copper and gold mining operations is said to contribute some 19% of the worldwide copper earnings of Freeport's parent company, Freeport McMoRan Gold & Copper Inc. ("**Freeport USA**").<sup>6</sup> As such, Freeport's Papua copper and gold mining operations are a hugely valuable, critically important, long term strategic asset of Freeport USA that is expected to continue generating major financial returns for many decades to come. It is entirely understandable, therefore, that Freeport and Freeport USA were, in the final analysis, willing to make almost any and all concessions, requested by GoI in the course of the CoW/CCoW Renegotiations, so long as this allows Freeport to continue to carry on and, indeed, expand its Papua copper and gold mining operations.

As long as (i) Freeport can be reasonably satisfied as to the security of its long term tenure over the Papua copper and gold mining operations and (ii) its projected marginal return from continuing to operate in Papua exceeds its projected marginal cost of these continuing operations, it is entirely rational, from an economic perspective, for Freeport to have substantially accepted GoI's position with regard to the 6 Strategic Issues and thereby conclude the CoW/CCoW Renegotiations as quickly

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<sup>6</sup> Michael Taylor and Allison Martel of Reuters, 9 July 2014 edition of The Jakarta Post.

as possible so that normal operations can resume and it can proceed with the planned expansion of its underground mining activities on a timely basis. That this was always likely to be the ultimate outcome of Freeport's CoW/CCoW Renegotiations cannot be seriously questioned given the economic imperatives facing Freeport. Accordingly, the fact that Freeport's CoW/CCoW Renegotiations went on as long as they did is to be seen more in the context of Freeport simply trying to secure the best possible deal with regard to each of the 6 Strategic Issues rather than in the context of Freeport ever having seriously contemplated abandoning its Papua copper and gold mining operations so long only as its minimum preconditions (as described above) were met.

The real issue for Freeport, in terms of concluding the CoW/CCoW Renegotiations, was likely to have been one of timing. More particularly, was it better to conclude the Freeport CoW/CCoW Renegotiations during the term of the current GoI or to delay the conclusion of the Freeport CoW/CCoW Renegotiations until the new GoI takes office in October 2014 and in the hope that a better deal, on the 6 Strategic Issues, might be possible under the new GoI? No doubt, Freeport made its own careful calculations of the likely outcome of the 9 July Presidential Elections and of the probable implications of the same for the future of its CoW/CCoW Renegotiations. The very close run nature of the 8 July Presidential Elections and the real possibility that Prabowo Subianto, with his stridently anti-foreign policy positions on mining and resources, might have been Indonesia's next President could only have encouraged Freeport to seek to conclude its CoW/CCoW Renegotiations with the current GoI. On the other hand, the somewhat more measured statements of Jokowi Widodo ("**Jokowi**"), as the other Presidential candidate and the ultimate winner, with regard to mining and resources might have encouraged Freeport to consider postponing the conclusion of its CoW/CCoW Renegotiations until after October 2014. In this regard, Jokowi's statement in the second of the 3 Presidential Candidate Debates that, in what was understood to be a reference to the CoW/CCoW Renegotiations:

*"A contract is a contract and therefore contracts which have already been signed need to be respected."*

would surely have been minutely analyzed by Freeport and its advisers for leads on how a new GoI, under Jokowi, was likely to approach any CoW/CCoW Renegotiations that still remained outstanding as of October 2014. The fact that, notwithstanding these seemingly encouraging words from Jokowi, Freeport still chose to conclude its CoW/CCoW Renegotiations and sign the Freeport MoU with the current GoI, rather than take its chances with the new GoI, may well have reflected the conclusion that, in the final analysis, it is "better to deal with the devil you know than with the devil you don't". Freeport may also have decided that, even though Jokowi was the winner of the 9 July Presidential Elections, his practical ability to make substantial concessions to those CoW/CCoW holders, which had still not concluded their CoW/CCoW Renegotiations before the end of the term of the current GoI, was severely limited by the fact that Indonesia's resource nationalist attitudes were driven largely by systemic and long term factors that were likely to be just as much a constraint for the new GoI as they have been for the current GoI - Interested readers may refer to the writer's recent article on these systemic and long term factors "*Mining Law, Policy & Regulation In Indonesia After 2014 – What Can We Realistically Expect?*", Coal Asia Magazine, May 2014, Petromindo. Further, the relatively weak ruling coalition, of diverse political parties, Jokowi will now head, could not have encouraged much hope, on the part of Freeport, that it was likely to get a significantly better deal from the new GoI than it was already close to finalizing with the current GoI.

It is important to note, however, that Freeport has “hedged its bets” considerably in concluding its CoW/CCoW Renegotiations during the term of the current GoI. This is because, although the Freeport MoU is now in place, this is really just the “end of the beginning” rather than the “beginning of the end” of the process of actually affecting the necessary amendments to the Freeport CoW. In this regard, it is critical to understand that the Freeport MoU is, most probably, not legally binding on either party but, rather, merely a statement of present intention only and simply sets out, in very “broad brush” terms, the “in principle” agreement reached by Freeport and the current GoI on the 6 Strategic Issues. Now that the Freeport MoU has been signed, the potentially much bigger task remains of negotiating the detailed, article by article, drafting amendments required to the Freeport CoW in order to implement the Freeport MoU and which detailed drafting amendments will be set out in a legally binding CoW amendment agreement between GoI and Freeport (“**Freeport CoW Amendment Agreement**”). Based on the draft CoW/CCoW Amendment Agreements presented by DGoMC to all CoW/CCoW holders in 2013, the Freeport CoW Amendment Agreement will be a highly detailed and lengthy document. Accordingly, much work remains to be done before the CoW/CCoW Renegotiations between Freeport and GoI can really be said to be finished, something which will actually only be the case when the Freeport CoW Amendment Agreement is signed.

It is entirely possible that the Freeport CoW Amendment Agreement will still be a “work in progress” once the new GoI takes office in October 2014 and, accordingly, it may well be the new GoI, rather than the current GoI, which has the greatest input on the negotiations surrounding the precise wording of the Freeport CoW Amendment Agreement as ultimately signed. That this is likely to be the case was acknowledged by the Director General of Minerals & Coal (“**DGoMC**”) when he was quoted in the 26 July edition of The Jakarta Post as saying that:

*“The [Freeport] MoU has been signed [and] the amendment of the [Freeport] CoW should be made six months after the signing of the [Freeport] MoU.”*

In this regard and even attributing absolute good faith to both parties and notwithstanding the signing of the Freeport MoU, there can be no certainty that Freeport and GoI will find it easy to conclude the Freeport CoW Amendment Agreement. As always, the “devil will be in the detail” and the parties may genuinely disagree on what drafting changes are necessary to the Freeport CoW in order to properly implement the Freeport MoU. As such and to the extent the Freeport MoU includes a “guarantee” of Freeport’s right to continue its Papua copper and gold mining operations after 2021, albeit with an IUPK rather than with a CoW, Freeport may have cleverly “locked in a deal” on this critical issue, under the current GoI, while still leaving itself lots of room to maneuver, in terms of negotiating the “fine print” of its overall acceptance of the 6 Strategic Issues, with the new GoI – in every sense, the best possible outcome as far as Freeport is concerned. As long as the Freeport CoW Amendment Agreement is eventually signed, the actual detail of what has been included and, more importantly, what has not been included in the Freeport CoW Amendment Agreement will surely be lost on most people including, first and foremost, the Indonesian public.

It may also well be the case that the current GoI will be more than pleased to leave it up to the new GoI to handle the inevitably difficult negotiations over the detailed drafting changes required to the individual articles of the Freeport CoW. The current GoI will still be able to take all the credit for the signing of the Freeport MoU which most people including, first and foremost, the Indonesian public

will simply assume is the end point, rather than an interim point at best, of the Freeport CoW/CCoW Renegotiations. This is already evident in the current GoI's characterization of the signing of the Freeport MoA as being the "end of the Freeport CoW/CCoW Renegotiations" when, in fact, this is really far from the case. Jokowi's negative reaction to the early signing of the Freeport MoU, as reported in the 26 July edition of The Jakarta Post, may be seen as an expression of concern on the part of Jokowi that the current GoI is unfairly and inappropriately taking credit for bringing about the "end of the Freeport CoW Renegotiations" while leaving, for the new GoI to handle, the potentially much more difficult (and thankless) task of negotiating and finalizing the Freeport CoW Amendment Agreement. Jokowi's concern can only have been heightened by the fact that the new GoI's future negotiating position, re the necessary amendments to the Freeport CoW, has effectively been already substantially constrained by what is set out in the Freeport MoU as agreed to by the current GoI but not the new GoI.

- 1.2 **Newmont:** Newmont's Batu Hijau mine is undeniably a significant copper and gold resource but only employs some 8,000 workers and, more importantly, is said to contribute only about 3% of the revenues of Newmont's parent company Newmont Corporation ("**Newmont USA**")<sup>7</sup> which has vast copper and gold resources outside of Indonesia. The long term potential of the Batu Hijau mine is also considered not to warrant any need to extend the Newmont CoW beyond its current 2030 expiry date. Accordingly, Newmont USA does not have any big expansion plans for the Batu Hijau mine that would result in it becoming a more valuable and strategic asset over time.

It should be immediately apparent that, although Newmont USA would, of course, like Newmont to continue operating the Batu Hijau mine until the expiry of the Newmont CoW in 2013 and clearly derives significant financial benefit from its Indonesian mining operations, the Batu Hijau mine does not have anything like the same long term, strategic and financial importance to Newmont USA as do the Grasberg and Gosan mines for Freeport. Further, while Newmont has reluctantly expressed a willingness to participate in a joint smelter development, with Freeport and Amtam, the smaller scale of Newmont's operations probably makes the economics of such joint smelter development markedly worse for Newmont than for Freeport.

This absence of any serious dependence of the long term financial health of Newmont USA on the continuation of the Newmont CoW, even up to 2030, and the relatively greater economic burden for Newmont of carrying out domestic processing and refining, make it less necessary for Newmont to accept GoI's position on the 6 Strategic Issues and otherwise conclude its CoW/CCoW Renegotiations on a timely basis. As such, Newmont may be seen to have more commercial flexibility, than does Freeport, in terms of its approach to the CoW/CCoW Renegotiations. While Newmont will surely not relish the unspecified "harsh consequences" CMOE has threatened Newmont with if it persists in continuing the Newmont Arbitration, these unspecified "harsh consequences" are not likely to "strike fear in the hearts" of Newmont USA's senior management in Denver Colorado. Simply put, GoI has much less leverage, in respect of the CoW/CCoW Renegotiations, over Newmont and Newmont USA than it does over Freeport and Freeport USA.

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<sup>7</sup> Michael Taylor and Allison Martel of Reuters, 9 July 2014 edition of The Jakarta Post.

Notwithstanding the foregoing and at first sight, the commencement of international arbitration against the current GoI may seem to be a dangerous strategy for Newmont/NTPBV to pursue. This is because it is, most probably, unrealistic to expect that the Newmont Arbitration will cause GoI to rethink its approach to the immediate issue of Newmont's Export License or the greater issue of the concessions it is seeking from Newmont in respect of the 6 Strategic Issues and otherwise adopt a more conciliatory stance on either or both these matters. As amply evidenced by the current GoI's previous reaction to the commencement of international arbitration, in 2013, by Churchill Mining Plc, the current GoI does not see the commencement of international arbitration against it as a mere normal exercise of legal rights by a foreign investor which has formed the view its long running negotiations with the current GoI are not likely to lead anywhere in the foreseeable future. Instead, the current GoI sees the commencement of international arbitration against it as an attack on Indonesia's sovereignty and an attempt to "bully" Indonesia into doing something it does not want to do. Although hardly rational, having regard to the well established and documented right, under both the Newmont CoW and the H-I BIT, to finally resolve disputes by international arbitration, Newmont/NTPBV surely must have anticipated the current GoI's reaction when they decided to commence the Newmont Arbitration. Certainly, GoI has reacted to the Newmont Arbitration just as any well-informed observer would have predicted. Having initially suggested, quite mildly on 4 July, that the Newmont Arbitration was likely to be discontinued once the Freeport CoW/CCoW Renegotiations were concluded<sup>8</sup>, CMoE quickly adopted a much more hostile (and inevitable) stance, being subsequently quoted in the 8 July edition of The Jakarta Post as saying that Newmont would be told to "*revoke its arbitration*" and faced "*bitter consequences*" if it did not do so, with GoI threatening to "*take measures that would definitely be detrimental to Newmont itself*" should Newmont/NTPBV persist with the Newmont Arbitration. In the same article, the Minister of Industry was quoted as saying that the "*closure of its mining site could be a possibility*". A subsequent 17 July article in The Jakarta Globe quoted DGoMC as saying that GoI would soon be sending Newmont a notice of default under the Newmont CoW in respect of Newmont's cessation of production at its Batu Hijau mine and, if Newmont did not cure its default, the Newmont CoW would likely be terminated and the Batu Hijau mine taken over by state-owned enterprise PT Aneka Tambang. DGoMC's justification for the proposed issuing of a notice of default was said to be that:

*"The default is due to the stopping of production, so we [GoI] can say they [Newmont] are negligent."*

Although DGoMC did not link either the proposed issuing of a notice of default or the threatened consequent termination of the Newmont CoW to the commencement of the Newmont Arbitration, it would clearly be naïve in the extreme to imagine that the threatened termination is really about anything other than the Newmont Arbitration.

Since the announcement of the Newmont Arbitration, virulent nationalistic and anti-Newmont sentiment has, predictably, "raised its ugly head", with a researcher at the Centre for Indonesian Law & Politics, Mr. Giri Ahmad Taufik, publishing an article entitled "*Newmont's Lawsuit and Sovereignty*" ("**CILP Article**")<sup>9</sup> in which it is said, amongst other less controversial things, that:

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<sup>8</sup> Thomas R. Sembiring and Maryati Dimursi, "*Hopes High for Withdrawal of Newmont Lawsuit*", Coal Asia Magazine, July August 2013, Petromindo at 130 – 131.

<sup>9</sup> 11 July 2014 edition of Kompas.

*“Newmont’s lawsuit must be considered a threat to [the] government’s sovereignty in running the country. Hence the Government should not tolerate the legal acrobatics Newmont is pursuing.”*

*“This is of significance in order to give clear signals to other multinationals that the additional value policy for the mineral and coal industry is a constitutional mandate which has no room for bargaining. All objections, resistance and considerations raised should be finalized during the course of current negotiations [CoW/CCoW Renegotiations].”*

*“Any action taken outside the context of renegotiation [CoW/CCoW Renegotiations] constitutes a resistance against the sovereignty of the nation and should be responded [to] harshly and [in a] well measured [manner].”*

Strong stuff indeed!! If nothing else, however, and assuming the author of the same is really just a proxy for the current GoI, the CILP Article leaves no doubt as to the direct linkage (at least in the mind of the current GoI) between the commencement of the Newmont Arbitration, Newmont’s perceived insufficient commitment to domestic processing and refining and the consequent need (as the current GoI sees it) to take strong action against Newmont in the form of terminating the Newmont CoW and giving PT Aneka Tambang control of the Batu Hijau mine if necessary. Essentially, the CILP Article says what CMoE and DGoMC were too well advised or perhaps just too politic to say.

The President himself has now also made his position clear on the Newmont Arbitration, being quoted by CMoE, in a 24 July news item from Thomson Reuters; as having said:

*“The government will take stern action against Newmont.”*; and that

*“[Newmont] does not value working on Indonesian soil, the birthplace of Indonesia’s ancestors.”*

Given GoI’s negative reaction was entirely predictable, the question inevitably arises as to why Newmont/NTPBV decided to, nevertheless, commence the Newmont Arbitration. The writer would surmise that Newmont came to the conclusion there was no prospect of the Export License being issued to it anytime soon because of its unwillingness to conclude the CoW/CCoW Renegotiations on terms which involved Newmont substantially accepting GoI’s position on each of the 6 Strategic Issues. Accordingly, unless some dramatic step was taken, Newmont would not receive its Export License and the Newmont CoW/CCoW Renegotiations would drag on fruitlessly until 2015 at least. With Newmont having substantially shut down its operations and consequently very little cash flow, continuation of the current impasse for up to another 12 months was simply intolerable from the commercial perspective of Newmont. At the same time, if GoI terminated the Newmont CoW, as a result of the commencement of the Newmont Arbitration, this would not be a major financial setback for Newmont USA.

To the extent Newmont USA sees its exit from Indonesia, by not later than 2030 and possibly much sooner, as inevitable given the resource limitations of the Batu Hijau mine, the Newmont Arbitration may, in fact, make good commercial sense. If Newmont/NTPBV are able to (i) obtain, from the

Newmont Arbitration, a sufficiently large award in their favor and (ii) enforce that award against GoI, this may substantially compensate Newmont USA for the premature loss of its Indonesian operations while, at the same time, enabling it to quickly exit a very difficult working environment in Indonesia which has surely consumed vast amounts of Newmont USA senior management time with only a limited financial return. Accordingly, while many people (including the writer) would normally see commencing international arbitration against the current GoI as effectively being an exit strategy for an imprudent foreign investor, if the particular foreign investor would not be particularly sorry to exit Indonesia as long as the effective exit price (i.e., the arbitration award) is sufficiently attractive, arbitration may, in fact, be a perfectly rational strategy for that investor to pursue.

Whether or not Newmont ultimately succeeds in the Newmont Arbitration and obtains a suitably generous arbitration award against GoI remains, of course, to be seen and there is little to be had in the way of absolute certainty when it comes to international arbitration. Nevertheless, DGoMC's attempt to justify issuing a default notice to Newmont, under the Newmont CoW, on the basis of Newmont's alleged "negligence" in ceasing production surely does not stand up to very close scrutiny as a credible legal argument. Negligence really has no role to play in breach of contract disputes and to link Newmont's alleged "negligence" to non-performance of its contractual obligations under the Newmont CoW is actually to hopelessly confuse 2 quite separate and distinct avenues of legal redress. GoI will certainly have to do a whole lot better in terms of legal argument, than "negligence in ceasing production", as justifying the issuing of a default notice under the Newmont CoW, if GoI is to be able to convince the arbitrators of the correctness of the GoI's position. This is all the more so when Newmont's undeniable cessation of production is actually due to the current GoI's refusal to issue Newmont with an Export License, something which most lawyers would have little difficulty in recognizing as a classic example of the occurrence of a force majeure event which suspends Newmont's relevant performance obligations under the Newmont CoW for the duration of the force majeure event. Likewise and most unfortunately for GoI, the fact that Newmont may, indeed, not sufficiently "value working on Indonesian soil, the birthplace of Indonesia's ancestors" [to accept the current GoI's position on the 6 Strategic Issues and without regard to the economic impact on Newmont], this is hardly a potential legal justification for termination of the Newmont CoW which is likely to commend itself to the arbitrators even if it may well resonate with certain segments of the Indonesian public.

Newmont, however, is not relying just on the Newmont Arbitration to deliver its desired outcome. Rather, Newmont's recently expressed willingness to resume negotiations with the current GoI over the issuance of an Export License while, at the same time, continuing the Newmont Arbitration process indicates a much more nuanced and sophisticated strategy than the simple "stick approach" that some commentators have characterized the commencement of the Newmont Arbitration as being. Given the issuance of the Export License seems to be firmly tied to the conclusion of Newmont's CoW/CCoW Renegotiations, Newmont may be also assumed to have signaled to the current GoI its willingness to resume the Newmont CoW/CCoW Renegotiations. Essentially, Newmont is showing the current GoI that Newmont is still willing to settle all outstanding matters amicably while making sure the current GoI understands that "time is ticking by" and there is now, for the first time, an effective deadline for concluding negotiations/re negotiations over the Export License and the Newmont CoW, which deadline is getting ever closer. Although CMOE has been quoted as firmly rejecting any possibility of resuming negotiations/re negotiations over the Export License and the Newmont CoW while so long as the Newmont Arbitration continues, it may well be that this official

“tough talk” is just for the consumption of the Indonesian public while, behind the scenes, CMOE and the current GoI will be willing to see if a “face saving formula” can be found that involves Newmont more or less simultaneously (i) discontinuing the Newmont Arbitration, (ii) resuming and concluding the Newmont CoW/CCoW Renegotiations, (iii) signing its own MoU with GoI and (iv) and receiving the long denied Export License.

## 2. Possible Implications for Future of CoW/CCoW Renegotiations

2.1 **Overview:** The very different approaches which Freeport and Newmont have taken to their respective CoW Renegotiations may have a variety of different implications for the remaining CoW/CCoW holders which have yet to complete their own CoW/CCoW Renegotiations. It is possible to identify and analyze these different implications under 2 broad scenarios which might be respectively referred to as the “good news scenario” and the “bad news scenario”.

2.2 **The Good News Scenario:** Freeport’s conclusion of its CoW/CCoW Renegotiations and the signing of the Freeport MoU, will enable the current GoI to take a more relaxed and conciliatory attitude to the remaining CoW/CCoW Renegotiations. In this regard, many people believe that Freeport and the Freeport CoW have always been the primary and real focus of the current GoI’s efforts, in the course of the CoW/CCoW Renegotiations, to get CoW/CCoW holders to accept its position on the 6 Strategic Issues. Under this scenario, now that the current GoI is able to claim victory in the Freeport CoW/CCoW Renegotiations, the need to have all the other CoW/CCoW holders and, more particularly, the other foreign CoW/CCoW holders accept substantially the same terms as Freeport may disappear. This scenario would suggest that all the other CoW/CCoW holders and, more particularly, the other foreign CoW/CCoW holders could see a softening of the current GoI’s position in the remaining CoW/CCoW Renegotiations, something which makes early conclusion of the remaining CoW/CCoW Renegotiations likely as the current GoI allows greater flexibility in terms of acceptance of GoI’s position on each of the 6 Strategic Issues.

It is also possible to see the Newmont Arbitration in positive terms vis-à-vis the remaining CoW/CCoW Renegotiations. Under this scenario, the current GoI will realize that it was a mistake to have pushed Newmont/NTPBV to the point of commencing international arbitration by being too inflexible in the Newmont CoW/CCoW Renegotiations and insisting Newmont could only obtain its Export License once the Newmont CoW/CCoW Renegotiations were concluded on terms which involved Newmont substantially accepting GoI’s position on each of the 6 Strategic Issues. In order to avoid the commencement of other international arbitrations against GoI by disgruntled CoW/CCoW holders, the current GoI will show a new found willingness to understand the CoW/CCoW holders’ positions and to accept more pushback from the CoW/CCoW holders on some or all of the 6 Strategic Issues.

2.3 **The Bad News Scenario:** Freeport’s conclusion of its CoW/CCoW Renegotiations and the signing of the the Freeport MoU, will enable and encourage the current GoI to bring almost irresistible pressure to bear on the other CoW/CCoW holders. The other CoW/CCoW holders will be told that it makes no sense for them to hold out on agreeing to the current GoI’s position on any of the 6 Strategic Issues now that the biggest CoW holder has, to a greater or lesser degree, accepted the current GoI’s position on all the 6 Strategic Issues. International interest in and concern over the CoW/CCoW

Renegotiations will substantially disappear once Freeport is no longer part of the CoW/CCoW Renegotiations and the other CoW/CCoW holders will be increasingly depicted as being obstructionist and unrealistic in refusing to accept the same deal as and otherwise wanting a better deal than Freeport got from the current GoI.

The Newmont Arbitration will make it much more difficult, both politically and psychologically, for the current GoI to agree to any compromises proposed by the CoW/CCoW holders in respect of the 6 Strategic Issues. This is because of the current GoI's concern that its acceptance of any such compromises will be viewed, by the Indonesian public, as the current GoI backing down in the face of the Newmont Arbitration and being anxious to avoid a flood of "copycat" Newmont Arbitrations by quickly concluding the remaining CoW/CCoW Renegotiations on terms acceptable to the remaining CoW/CCoW Holders. As a consequence, the current GoI will decide to take a particularly tough line with Newmont in order to show the other CoW/CCoW holders (i) that the current GoI is not intimidated by the Newmont Arbitration and (ii) what the other CoW/CCoW holders can expect if they are foolish enough to follow in Newmont's footsteps and start international arbitration against GoI. Under this scenario and given the virulent resource nationalism present in Indonesia today, even the new GoI may feel constrained to not compromise on any of the 6 Strategic Issues out of concern its nationalist credentials will be questioned by many Indonesians if it does so and bearing in mind that the leading party in the new GoI coalition, PDI-P, was heavily criticized for being too accommodating to foreign investment when it was last in government from 2004 to 2006.

2.4 **Assessment:** Regrettably, the writer believes the "bad news scenario" is more likely to prove to be substantially correct than is the "good news scenario". This is for 2 reasons.

First, in the last couple of years the current GoI has increasingly pursued a "top down" strategy in connection with the CoW/CCoW Renegotiations, concentrating its efforts on trying to conclude the CoW/CCoW Renegotiations with 1 of the "Big 3" foreign CoW holders (i.e., Freeport, Newmont and Vale) in the belief that a successful and concluded CoW/CCoW Renegotiation with 1 of the largest foreign CoW holders would create an almost unstoppable momentum for the numerous medium sized and smaller CoW/CCoW holders to "fall into line" and accept the same terms in respect of the 6 Strategic Issues which the current GoI has just negotiated with 1 of the largest foreign CoW holders. Now that the current GoI seems to have finally achieved the first objective of its "top down strategy" (i.e., concluding the Freeport CoW/CCoW Renegotiations), it would be understandable if the current GoI experiences renewed resolve to see the Top Down Strategy through to the end and concentrate all its efforts on achieving the second and ultimate objective of getting all the remaining CoW/CCoW holders to accept substantially the same terms on each of the 6 Strategic Issues as recently agreed with Freeport.

Second, there is little to suggest that the current GoI is going to respond differently to the Newmont Arbitration compared to its earlier responses to the Churchill Mining arbitration or the even earlier GoI response to the Karaha Bodas arbitration in the late 1990's. Indeed, the threats of punitive action against Newmont, made by CMoE, DGoMC and the President, strongly suggest that the current GoI's response to the Newmont Arbitration will focus on punishing Newmont for exercising its legal rights in a way that the current GoI finds disagreeable rather than on addressing the legal issues raised by the Newmont Arbitration in a calm, rational and considered manner. Sadly, it seems that the current GoI has not learnt anything from past GoI mistakes in handling the Churchill Mining

arbitration and the Karaha Bodas arbitration, which mistakes are discussed at length in the writer's article "*Churchill Mining International Arbitration – The GoI Reaction*", Coal Asia Magazine, September 2012, Petromindo. This decidedly hostile attitude to Newmont/NTPBV and the refusal to recognize Newmont/NTPBV's legal right to commence the Newmont Arbitration is likely to be reflected in a similar "take no prisoners and leave no wounded" approach to dealing with the other CoW/CCoW holders. The current GoI will probably conclude, quite erroneously, that the best approach for it to take in dealing with the other CoW/CCoW holders is to show no willingness to negotiate on any of the 6 Strategic Issues while, at the same time, making it clear to the other CoW/CCoW holders that they can expect similar treatment to Newmont if they pursue international arbitration against the current GoI in an endeavor to win concessions from the current GoI on any of the 6 Strategic Issues.

It is, of course, tempting to think that the timing of the announcement of the conclusion of the Freeport CoW/CCoW Renegotiations, following so soon after the announcement of the commencement of the Newmont Arbitration, was anything but coincidental and actually reflected a new sense of urgency on the part of the current GoI to conclude the Freeport CoW/CCoW Renegotiations out of concern that Freeport and the other CoW/CCoW holders might go down the same path as Newmont. On closer examination, however, this seems inherently unlikely for several reasons. First, Newmont had been threatening international arbitration for a long time. Second, it had become increasingly apparent, over recent months, that Freeport and the current GoI were getting ever closer to concluding the Freeport CoW/CCoW Renegotiations and that it was Freeport, rather than Vale, which was most likely to be the first major foreign CoW holder to conclude the CoW/CCoW Renegotiations. Third, the current GoI already had maximum incentive to conclude the Freeport CoW/CCoW Renegotiations as early as possible given that Freeport represents, to many Indonesians at least, the "unacceptable face" of foreign investment in the local mining industry. It actually seems more plausible to the writer that Newmont/NTPBV may have been influenced in their decision to, at last, commence the Newmont Arbitration by the increasingly apparent, imminent end to the Freeport CoW/CCoW Renegotiations and the consequent realization that Freeport would definitely not be taking a united stand with Newmont in pushing for greater concessions from the current GoI on each of the 6 Strategic Issues, thereby reducing the perceived downside for Newmont/NTPBV in finally proceeding with the long threatened Newmont Arbitration.

## **SUMMARY AND CONCLUSIONS**

Although Freeport and Newmont are clearly now pursuing quite different strategies in trying to resolve the long running CoW/CCoW Renegotiations, it does not necessarily follow that 1 strategy must be right and the other strategy must be wrong. For Freeport USA, given the huge long term, strategic and financial importance of its investment in Indonesia as well as the substantial untapped potential of the remaining copper and gold resource which Freeport presently controls, remaining in Indonesia and in control of that copper and gold resource probably justifies the early conclusion of the Freeport CoW/CCoW Renegotiations and on terms which involve Freeport accepting, to a greater or lesser degree, GoI's position on each of the 6 Strategic Issues. At the same time and somewhat counter-intuitively, for Newmont USA, given the much more limited strategic and financial importance of its investment in Indonesia as well as the fact that there is not any substantial untapped potential of the remaining copper and gold resource which Newmont presently controls, remaining in Indonesia and in control of that copper and gold resource probably does not justify the

early conclusion of the Newmont CoW/CCoW Renegotiations and on terms which involve Newmont accepting, to a greater or lesser degree, GoI's position on each of the 6 Strategic Issues. Rather, in the case of Newmont USA but not in the case of Freeport USA, an early exit from Indonesia, at a suitably high exit price in the form of a favorable and enforceable arbitration award, may make good commercial sense

Having regard to the foregoing, both Freeport and Newmont may well be pursuing commercially sensible strategies having regard to their very different commercial positions. To assume that, if Freeport's strategy is correct, Newmont's strategy must therefore be wrong or vice versa is wholly misconceived. Although the current GoI will, inevitably, say that the Freeport strategy is the only prudent approach for a foreign investor in Indonesia's mining sector to pursue and Newmont's strategy shows a lack of understanding of how things are and should be done in Indonesia, this is also incorrect. The respective situations of Freeport and Newmont are not readily comparable. As such, this is in every sense "A Tale of 2 (Very Different) Cities" where both strategies may be right or, conceivably, both strategies may be wrong. Only time will tell.

The implications, for those remaining CoW/CCoW holders which have yet to complete their CoW/CCoW Renegotiations, of the different approaches taken by Freeport and Newmont are as yet unclear. While it is possible to articulate and develop a good news scenario as well as a bad news scenario, the bad news scenario seems more credible at this stage. The remaining CoW/CCoW holders will, most likely, face an increasingly confident and emboldened current GoI determined to see its Top Down strategy through to the very end and not willing to make any compromises in respect of the 6 Strategic Issues out of concern this will be perceived as weakness in the face of the Newmont Arbitration. The new GoI's "hands" may also be substantially "tied" by the mistakes of the current GoI in handling the CoW/CCoW Renegotiations with Newmont. Not a "pretty picture" indeed for those CoW/CCoW holders that have yet to conclude their CoW/CCoW Renegotiations!!

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