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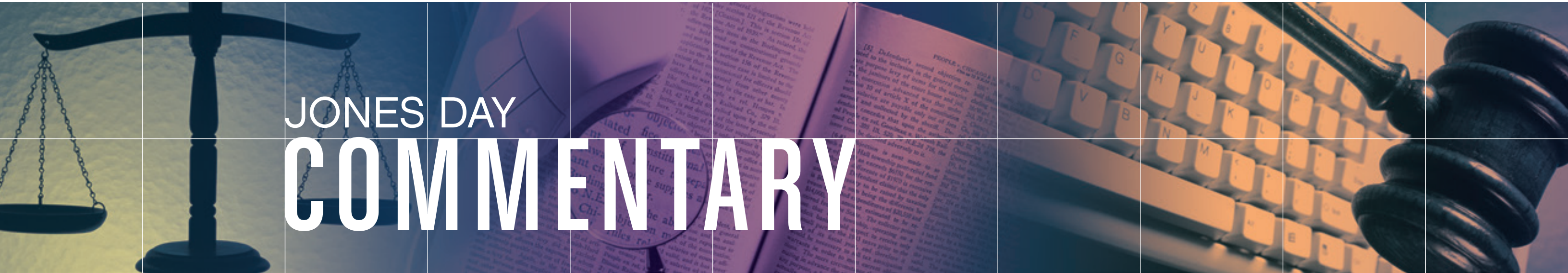

EARLY EFFECTS OF INDONESIA'S ORE EXPORT BAN

The unpredictable regulatory environment in the Indonesian mining sector is again surfacing as a major issue for domestic and international mining companies operating in Indonesia. Senior figures in Indonesia's minerals and energy ministry have recently indicated that metal ore and concentrate exports have ground to a halt since the imposition of the ban on ore shipments on January 12.

While initially tabled as a blanket ban designed to bolster the long-term domestic profitability of Indonesia's mining industry, last-minute regulatory changes diluted the ban to allow some industries to continue exporting unprocessed mineral ore.

The reprieve was extended to copper, manganese, iron ore, lead, and zinc concentrates, and it lowered the minimum processing requirements prior to export. According to Energy and Mines Minister Jero Wacik, 66 companies are allowed to continue to export because they have satisfied government officials that investment in local smelters is imminent.

However, considerable uncertainty remains regarding the future operations of the country's hundreds of bauxite and nickel miners, all of which require refinement prior to export.

REGULATORY BACKGROUND

The history of this regulation can be traced back to 2009. Previously, contracts of works ("CoWs") between the Indonesian government and a particular mining company lasted for a period of 30 years. In 2009, CoWs were replaced by mining business licenses (or *Izin Usaha Pertambangan* ("IUP")) that cover exploration and production. While CoWs entered into prior to 2009 are to be honored, albeit with some renegotiation of terms, new licenses or renewals of CoWs are to be as IUPs. In contrast to CoWs, IUPs are subject to changes in fiscal policy and to reforms of the mining regulatory code.

In February 2012, the government announced further regulatory changes. First, majority or wholly foreign-owned companies must surrender 51 percent of their shares to an "Indonesian participant" after 10 years. The Indonesian government was to have the right of first refusal, followed by state governments and the

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Indonesian private sector. Many investors voiced concerns that 10 years was insufficient time to recoup the costs, let alone make an adequate return because of the capital-intensive nature of mining projects. Some argued that the regulatory change amounted to a mandatory divestment of equity.

The second announcement in February 2012 concerned the ban on the export of raw materials, with no certainty provided as to when it would be implemented.

POSSIBLE CONSEQUENCES

The immediate effects of the ban saw a rise in the price of nickel and the Indonesian rupiah. Further potential flow-on effects include disruptions to supply agreements, shipping charters, and trade agreements around the world, leading to instances of "force majeure" notifications and subsequent disputes. For example, Indonesia accounts for 15 percent of global nickel supplies, with China one of its major customers for high-grade laterite nickel, which is used in the production of stainless steel. The flow-on effects of an increase in nickel prices and an interruption to Chinese steel production could be significant for the global construction and manufacturing sectors. The ban may also give rise to claims by investors against Indonesia pursuant to investment treaties.

Indonesia is a party to 63 bilateral investment treaties ("BITs") with countries all over the world, including Australia, China, India, Korea, Malaysia, The Netherlands, Singapore, and the UK. It is also a party to the ASEAN Comprehensive Investment Agreement signed by Indonesia at the 14th ASEAN Summit in February 2009. The number of investment treaties to which Indonesia is a party suggests that there may be significant scope for international investors to seek redress for any losses caused by the export ban under the various dispute resolution provisions of these treaties.

For example, pursuant to the BIT between Indonesia and China, investors are protected from expropriation and "measures having effect equivalent to nationalization" under Article VI. Article IX relates to investor–state dispute resolution that allows for ad hoc arbitration under the rules of the International Center for Settlement of Investment Disputes. However, whether a claim is available or not will depend, in part, on whether the export ban can be construed as a measure having a nationalizing effect. A potential claimant will need to review the provisions of the relevant BIT and also the timing of the relevant investments in Indonesia's mining industry and the laws and regulations affecting the investment at the time.

CONCLUSION

It is important to note that despite the historical uncertainty affecting the mining industry in Indonesia and exacerbated by this recent ban, there has only ever been one mining investment-related ICSID arbitration. It is too soon yet to determine whether the numerous foreign investors affected by this ban feel that their ongoing business interests are better served by finding alternatives to investor–state arbitration.

In the meantime, the Indonesian Mineral Entrepreneurs Association is planning challenges to the ban in the Supreme and Constitutional Courts in Indonesia, while miners, laid off by the ban, have already taken to the streets to protest the regulations. It is very likely that the mining ban will become a significant feature of the political discussions leading up to the elections later this year, especially given its significant and immediate impact on government revenue.

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