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IDX LISTINGS FOR PMA MINING COMPANIES – STILL NOT A "SURE FIRE" SOLUTION TO THE DIVESTITURE OBLIGATION[1][2][3][4][5]

INTRODUCTION

One of the more interesting aspects of the April 2016 draft of Indonesia's proposed new minerals and coal mining law ("**April Draft Mining Law**") is the suggestion that the divestiture obligation, applicable to all PMA Companies holding IUPs/IUPKs (**i.e.**, mining business licenses) ("**Divestiture Obligation**"), may be satisfied, in certain instances, by way of an initial public offering and Indonesian Stock Exchange listing ("**IDX Listing**") ("**ADML Article 79(4)**").

ADML Article 79(4) will, inevitably, re-invigorate the long running debate and discussion over, to what extent if any, an IDX Listing can be used to either avoid altogether the need to comply with the Divestiture Obligation or, at least, to satisfy the Divestiture Obligation in a way that provides a viable alternative to offering divestiture shares to Indonesian government and private interests at "bargain basement" prices.

Indonesia's recently revised and updated Negative Investment List, as set out in Presidential Regulation No. 44 of 2016 re List of Business Activities that are Closed for Investment and List of Business Activities that are Open for Investment with Certain Conditions ("**PR 44/2016**"), is also very relevant to any assessment of whether or not IDX Listings may be used to avoid or satisfy the Divestiture Obligation.

In this article, the writer will look at the potential implications of both ADML Article 79(4) and PR 44/2016 for IDX Listings by PMA Companies holding IUPs/IUPKs.

BACKGROUND

There has been much confusion, in the past, as to the implications, for the Divestiture Obligation, of PMA Companies, holding IUPs/IUPKs, undertaking an IDX Listing. This confusion was largely due to the lack of consensus, among the various interested regulatory authorities, as to whether or not undertaking an IDX Listing meant either (i) that a PMA Company, holding an IUP/IUPK, thereby became a "local party" (**i.e.**, a **Non**-PMA Company) and, so, was not subject to the Divestiture Obligation at all or (ii) remained a PMA Company but otherwise automatically fulfilled the Divestiture Obligation by virtue of the IDX Listing.

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[1] Bill Sullivan, Licensed Foreign Advocate with Christian Teo & Partners (in association with Stephenson Harwood LLP).
[2] Bill Sullivan is the author of "*Mining Law & Regulatory Practice in Indonesia – A Primary Reference Source*" (Wiley, New York & Singapore 2013), the first internationally published, comprehensive book on Indonesia's 2009 Mining Law and its implementing regulations.
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IDX Listings by PMA Companies and the Divestiture Obligation involve three very different Government agencies being (i) BKPM as the primary regulator of PMA Companies, (ii) OJK as the capital markets regulator and (iii) ESDM as the administrator of the Divestiture Obligation. Accordingly, merely because BKPM takes a particular position on the foreign investment status implications, for a PMA Company, of an IDX Listing, this does not necessarily mean that ESDM takes the same position with regard to the Divestiture Obligation implications, for a PMA Company holding an IUP/IUPK, of an IDX Listing. As a minimum, therefore, it is essential to consider the separate positions of BKPM and DGoMC.

The Divestiture obligation is, nevertheless, administered by ESDM and not by BKPM or OJK. Accordingly, in the final analysis it is ESDM, rather than BKPM or OJK, which must be satisfied that a particular PMA Company IUP/IUPK holder is either not subject to the Divestiture Obligation at all or is subject to the Divestiture Obligation but has fulfilled the same as a result of its IDX Listing.

Prior to 2010, it was generally accepted that, once a company carried out an IDX Listing, it was to be regarded as a "local company" (**i.e.**, a Non-PMA Company) provided that:

(a) it was initially established as a Non-PMA Company, with only Indonesian nationals or Indonesian companies wholly owned by Indonesian nationals as its shareholders; or

(b) if it was initially established as a PMA Company, (i) its foreign shareholders disposed of their shares to the public or to Indonesian nationals or Indonesian companies and (ii) the IDX Listed company had BKPM formally revoke its status as a PMA Company.

Between 2010 and 2013, however, (i) the issuance of a number of draft and final regulations, by MoEMR and BKPM, purporting to deal with the implications of IDX Listings by PMA Companies in the context of the Divestiture Obligation or otherwise and (ii) the subsequent amendment of these regulations left the position very confused and confusing.

Government Regulation 77 of 2014 re Third Amendment of Government Regulation No. 23 of 2010 re Implementation of Mineral & Coal Mining Enterprise Activities ("**GR 77/2014**") sought to address some of the confusion by providing that, if PMA Company IUP/IUPK holders are IDX Listed, then a "**maximum**" of 20% of the "**total amount of shares**" may be counted towards satisfaction of the Divestiture Obligation ("**GR 77/2014 Article 97(2a)**").

Unfortunately, it is unclear whether GR 77/2014 Article 97(2a) allows a "**maximum**" of 20% of (i) all the issued shares of the IDX Listed company or (ii) only 20% of all the issued shares of the IDX Listed company not held by founders and/or insiders (**i.e.**, 20% of the "public" shares only) to be counted towards satisfaction of the Divestiture Obligation. Enquires made with ESDM, at the time of the issuance of GR 77/2014, indicated that the "20%" mentioned in GR 77/2014 Article 97(2a) was actually intended to mean 20% of all the issued shares of the IDX Listed company regardless of whether those shares were held by the public or by founders/insiders. **For example**, if a PMA company Production Operation IUP/IUPK holder carried out an IDX Listing and offered 40% of its shares to the public, then the PMA company IUP/IUPK holder would only be considered to have divested a "**maximum**" of 20% of all of its issued shares to Indonesian parties as a result of the IDX Listing. Accordingly, if the PMA company Production Operation IUP/IUPK holder did not carry out either underground mining or own processing and refining activities, then the now IDX Listed

Production Operation IUP/IUPK holder was required to divest a further 31% of its shares to Indonesian parties in order to satisfy the Divestiture Obligation as opposed to a further 11% of its shares only if it had been able to count the full 40% of its shares sold to the public as part of the IDX Listing.

The 20% restriction was, presumably, imposed by GR 77/2014 Article 97(2a) in recognition of the difficulty of tracking who really owns the shares of an IDX Listed company once the IDX Listing has taken place and the shares are able to be freely traded on market.

To the extent the 20% restriction acts as (i) a negative inducement for PMA Company IUP/IUPK holders to undertake IDX Listings and (ii) consequentially, a positive inducement to, instead, sell shares privately to substantial Indonesian business groups so as to satisfy the Divestiture Obligation, the 20% restriction may be seen as inconsistent with encouraging greater, broad based (**i.e.**, retail) Indonesian ownership of mining companies.

It remains uncertain just what factors will be considered in determining the **actual** percentage of shares considered to have been divested by an IDX Listed, PMA Company IUP/IUPK holder given GR 77/2014 Article 97(2a) refers to a "**maximum**" of 20% being counted towards satisfaction of the Divestiture Obligation. ESDM was said to be in the process of revising MoEMR Regulation No. 27 of 2013 re Procedures and Price Determination of Divestiture Shares, and Change of Investment in Minerals and Coal Mining ("**MoEMRR 27/2013**") so as to include further details of the procedures for satisfying the Divestiture Obligation in the case of IDX Listed, PMA Companies holding IUPs/IUPKs. It was suggested that the proposed revisions to MoEMRR 27/2013 would include the procedures for determining the actual percentage of shares deemed to have been divested by an IDX Listed, PMA Company IUP/IUPK holder in various situations. To date, however, the proposed revisions to MoEMRR 27/2013 have never eventuated.

Given the convoluted history of IDX Listings and the Divestiture Obligation, it would be hardly surprising if many PMA Company IUP/IUPK holders and their professional advisers hope that, if and when it becomes law, ADML Article 79(4) will finally make it clear that, at long last, IDX Listings are now accepted as a legitimate way for PMA Company IUP/IUPK holders to fully satisfy their Divestiture Obligations. Sadly, PMA Company IUP/IUPK holders and their professional advisers are almost certainly going to be very disappointed in this regard.

Readers interested in knowing more about the April Draft Mining Law and its current status are referred to the writer's earlier article, "*ESDM Draft New Mining Law - A Very Mixed Bag*", which appeared in the May – June 2016 edition of Coal Asia Magazine.

COMMENTARY

1. April Draft Mining Law

1.1 **Outline of Proposed Divestiture Obligation**: Article 79 of the April Draft Mining Law ("**ADML Article 79**") sets out the Divestiture Obligation in terms which may be broadly translated as follows:

(a) After five years of production, PMA Company IUP/IUPK holders must divest an unspecified percentage of shares ("**Divestiture Shares**") to Indonesian parties.

(b) The offer mechanism for the Divestiture Shares must give priority to Indonesian parties.

(c) The Divestiture Shares are to be offered "gradually" to:

   (i) the Central Government, the Provincial Governments and the Regional/City Governments;

   (ii) State Owned Enterprises ("**BUMNs**") and/or Regional Government Owned Enterprises ("**BUMDs**"); and

   (iii) national private business entities (**i.e.**, Non-PMA Companies).

(d) **If the divestment, as referred to in (b) above, is not "achieved", the Divestiture Share offering shall be carried out by way of the "stock exchange"**.

(e) In the event that the Divestiture Share offering, as contemplated by (c) and (d) above, does not achieve the intended outcome (**i.e.**, satisfaction of the Divestiture Obligation), the Divestiture Obligation will be carried forward, on a cumulative basis, to following years and the specified Divestiture Share offering mechanism repeated.

(f) The amount, classification, time and procedures for Divestiture Share offerings shall be set out in a subsequently issued Government Regulation.

Those parts of the April Draft Mining Law envisaged Divestiture Obligation, as set out in (a), (b), (c), (e) and (f) above, appear to be substantially the same as presently set out in the 2009 Mining Law and its implementing regulations. The possible/probable point of departure, however, from the 2009 Mining Law and its implementing regulations is to be found in (d) above; namely, "**If the divestment, as referred to in (b) above is not achieved, the Divestiture Share offering shall be carried out by way of the stock exchange"** (**i.e.**, ADML Article 79(4)).

Although open to various interpretations, ADML Article 79(4) **may** reflect the present intention of ESDM to allow the Divestiture Obligation to be satisfied, in whole or in part, by way of an IDX Listing in the event that none of the Central Government, the Provincial Governments, the Regional/City Governments, BUMNs, BUMDs or Non-PMA Companies are willing and able to acquire the Divestiture Shares on offer.

1.2 **Assessment of Proposed IDX Listing Alternative**: It is important **not** to overstate the significance of the proposed IDX Listing alternative as apparently provided for in ADML Article 79(4).

First, ADML Article 79(4) is **not** a total departure from the existing position. As explained in the Background section, GR 77/2014 already allows PMA Company IUP/IUPK holders, which are IDX Listed, to count some of their issued shares as being effectively Indonesian owned for the purposes of satisfying the Divestiture Obligation.

Second, even on the most expansive reading of ADML Article 79(4), the proposed IDX Listing alternative will only be available if **none** of the Central Government, the Provincial Governments, the Regional/City Governments, BUMNs, BUMDs or Non-PMA Companies are willing and able to acquire the Divestiture Shares on offer. In other words, the IDX Listing alternative will **not** be automatically available to PMA Company IUP/IUPK holders in terms of satisfying the Divestiture Obligation; rather, it is only intended to be a "fallback" alternative/alternative of "last resort" if none of the priority Indonesian party offerees are willing and able to acquire the Divestiture Shares on offer. As such, PMA Company IUP/IUPK holders and their professional advisers **cannot** expect to be able to simply elect, in the first instance, to satisfy the Divestiture Obligation by proceeding with an IDX Listing. Indeed, it would seem there is to be **no** election or discretion at all. Once the Divestiture Shares are not taken up by any of the priority Indonesian party offerees, ADML Article 79(4) appears to say that an IDX Listing (preceded by an initial public offering) will be the **mandatory** fallback alternative/alternative of last resort albeit subject, presumably, to there being sufficient available market interest and support for the IDX Listing. In the absence of sufficient market support, the divestiture process will just be carried forward to the following year and repeated.

Third, it remains to be seen whether, if none of the priority Indonesian party offerees are willing and able to acquire the Divestiture Shares on offer, the relevant PMA Company IUP/IUPK holder can satisfy 100% of its Divestiture Obligation by way of the IDX Listing alternative or, instead, the to be issued implementing regulation (as clearly contemplated by ADML Article 79) will impose some upper percentage restriction on the extent to which the Divestiture Obligation can be satisfied by way of a IDX Listing. In this regard, it is important to note that, as previously highlighted in the Background section, existing GR 77/2014 Article 97(2a) refers to a "**maximum**" of 20% of an IDX Listed company's issued shares being counted towards satisfaction of the Divestiture Obligation.

Fourth, as currently worded, ADML Article 79(4) arguably makes more restrictive, not less restrictive, the opportunities for PMA Company IUP/IUPK holders to undertake IDX Listings as a way to at least partially satisfy the Divestiture Obligation. This is because ADML Article 79(4) only seems to allow the use of IDX Listings to satisfy the Divestiture Obligation in a particular year once it is clear that **no** priority Indonesian party offeree is willing and able to acquire the Divestiture Shares on offer that year. This is to be compared with the present situation whereby GR 77/2014 allows PMA Company IUP/IUPK holders, which are IDX Listed, to count some of their issued shares as being effectively Indonesian owned for the purposes of satisfying the Divestiture Obligation. GR 77/2014 does **not** place any limitations on when PMA Company IUP/IUPK holders may undertake IDX Listings in order to partially satisfy their Divestiture Obligations.

Fifth, and perhaps most importantly, it must be questioned how likely or otherwise it is that, in the case of an already producing IUP/IUPK holder, there will be **no** priority Indonesian party offeree willing and able to acquire the Divestiture Shares on offer as this is the only situation in which ADML Article 79(4) becomes relevant. In the final analysis, the willingness or otherwise of priority Indonesian party offerees to acquire the Divestiture Shares on offer will always be a question of the applicable divestiture price. ADML Article 79 is silent on the critical question of the divestiture price which, presumably, is to be dealt with by way of subsequent regulation. If the Government continues to insist upon a divestiture price

substantially equivalent to cost recovery only, then there is likely to be little opportunity for ADML Article 79(4) to operate as there will surely almost always be some party, from among the Central Government, the Provincial Governments, the Regional Governments, BUMNs, BUMDs and Non-PMA Companies, willing and able to acquire Divestiture Shares in an already producing mining company at the "bargain basement" price equal to a proportion of accrued capital and operating costs to date less certain liabilities.

1.3 **Possible Rationale for ADML Article 79(4)**: If, as suggested in 1.2 above, ADML Article79(4) does not really represent a huge advance on the current position and, indeed, could be more restrictive than the current position, is there another possible rationale for ADML Article 79(4) which explains its inclusion in the April Draft Mining Law?

Once such possible explanation is that the actual purpose behind ADML Article 79(4) is, in fact, **not** to make it easier to satisfy the Divestiture Obligation in the case of **all** PMA Company IUP/IUPK holders but, rather, to simply provide the Government with a "face saving" solution to the problem posed by the Divestiture Obligation in the case of **just one** soon to be PMA IUPK holder; namely, PT Freeport Indonesia ("**Freeport Indonesia**").

Freeport Indonesia is presently owned as to 90.64% by its US parent and as to 9.36% by the Government. Pursuant to Freeport Indonesia's Contract of Works ("**CoW**"), it is obliged to divest up to 30% of its issued shares to Indonesian parties prior to 2021. In 2016, Freeport Indonesia's Divestiture Obligation is 10.46% of its issued shares ("**2016 FI Divestiture Shares**"). As part of its ongoing CoW renegotiations, which will eventually see Freeport Indonesia become an IUPK holder, Freeport Indonesia and the Government having been trying, without success, to agree the purchase price for the 2016 FI Divestiture Shares. Freeport Indonesia has valued the 2016 FI Divestiture Shares at US$1.7 billion. This figure has, however, been rejected by the Government. The Director General of Minerals & Coal, Bambang Gatot Ariyono, was quoted in the 12 April 2016 edition of The Jakarta Post as having said the "*price was too high and the Government was currently considering **alternative** options*."

One alternative option would certainly be to have a BUMN, such as PT Bukit Asam, PT Aneka Tambang or Inalum (either individually or in combination) acquire the 2016 FI Divestiture Shares. This alternative has been widely discussed and various BUMNs have publicly expressed interest in acquiring the 2016 FI Divestiture Shares. However, as reported in the 15 January 2016 edition of The Jakarta Post, the Ministry of State Owned Enterprises appears to have in mind a valuation for the 2016 FI Divestiture Shares of US$500 million to US$1 billion only, far less than the price sought by Freeport Indonesia.

Given the Government is not legally able to compel Freeport Indonesia to sell, whether to a BUMN or to itself, the 2016 FI Divestiture Shares at a price deemed to be too low by Freeport, the question arises how this "standoff", over the value of the 2016 FI Divestiture Shares, is going to be resolved without causing the Government undue embarrassment at a time when everything to do with Freeport Indonesia and the renegotiation of its CoW is a hugely sensitive political issue. Another alternative option would be to allow Freeport Indonesia to satisfy its Divestiture Obligation, in respect of the 2016 FI Divestiture Shares, through an IDX Listing.

Looked at from the perspective of what to do about the 2016 FI Divestiture Shares, ADML Article 79(4) may take on a new significance because this is one instance where it is most unlikely that any of the priority Indonesian party offerees will be willing and able to acquire the 2016 FI Divestiture Shares for the Freeport Indonesia asking price of US$1.7 billion. Assuming Freeport Indonesia cannot be prevailed upon to reduce its asking price to US$500 million to US$1 billion, ADML Article 79(4) could provide a convenient "way out" of a difficult situation for all parties concerned. The Government and BUMNs avoid a large financial commitment at a time of severe and growing budgetary constraints for the public sector. At the same time, the Government ensures that Freeport Indonesia does not manage to avoid complying with its Divestiture Obligation, in respect of the 2016 FI Divestiture Shares, by valuing the 2016 FI Divestiture Shares at a price no priority Indonesian party offeree is willing and able to pay. The Indonesian public is given the chance to acquire some or all of the 2016 FI Divestiture Shares as part of a Freeport Indonesia IDX Listing, thereby enabling the Government to say it has realized the supposed objective underlying the Divestiture Obligation; namely, greater Indonesian ownership of Freeport Indonesia. Freeport Indonesia is not forced to sell the 2016 FI Divestiture Shares at what it says would be a gross undervalue but, rather, is allowed to "take its chances" with the market. Arguably, a good outcome for everyone. It has also been suggested to the writer that the Government may see another, less obvious, benefit to Freeport Indonesia resolving the issue of what to do about the 2016 FI Divestiture Shares by way of an IDX Listing. This additional benefit is said to be making it impossible or, at least, much more difficult for certain opportunistic Indonesian business groups and local entrepreneurs to indirectly gain control of the 2016 FI Divestiture Shares, at a "fire sale" price, by having a co-operative BUMD "front" the acquisition of the 2016 FI Divestiture Shares in reliance upon a back to back arrangement with an Indonesian business group or local entrepreneur that effectively enables that party to extract most of the benefit from the subsequent ownership of the 2016 FI Divestiture Shares.

If, in fact, ADML Article 79(4) is really an initiative to deal with the issue of what to do about the 2016 FI Divestiture Shares only, ESDM needs to be very careful that, in trying to find a clever solution to this Freeport Indonesia specific issue, it does not inadvertently make it more difficult for PMA Company IUP/IUPK holders, in general, to use IDX Listings as a means of partially satisfying their Divesture Obligations. As pointed out in 1.2 above, ADML Article 79(4) is, arguably, inconsistent with the more broadly worded GR 77/2014. In the event that ADML Article 79(4) becomes law, GR 77/2014 would have to be revised so as to eliminate the identified inconsistency, thereby removing the general right of PMA Company IUP/IUPK holders to, whenever they so choose, undertake IDX Listings as a way of having a maximum of 20% of their issued shares counted towards satisfaction of the Divestiture Obligation.

2. **PR 44/2016**

PMA Company IUP/IUPK holders and their professional advisers could be forgiven for overlooking a most obliquely worded provision of Indonesia's new Negative Investment List as set out in PR 44/2016.

Article 8.1 of PR 44/2016 ("**PR 44/2016 Article 8**") specifies that:

> "*In those cases where implementation of investment, in business fields that are open with certain conditions as provided for in Article 2.1(c), is carried out indirectly or by way of portfolio, including investments carried out by way of the domestic capital markets, then the business fields that are closed with certain conditions, as provided for in Article 2.1(c), shall become the business fields that are open*."

Believe it or not and although certainly not apparent from a superficial reading (or even from an in-depth reading for that matter!!), PR 44/2016 Article 8 has quite a lot to say about the legal implications for PMA Companies generally, including PMA Company IUP/IUPK holders, of undertaking IDX Listings.

Based on enquiries made by the writer's staff with BKPM, PR 44/2016 Article 8 is actually meant to be interpreted such that:

(a) any investment made by a foreign party in an IDX Listed company, by way of acquiring shares that are part of the "public float", shall be regarded as domestic investment; and

(b) any investment made by a foreign party in an IDX Listed company, by way of acquiring shares that are **not** part of the "public" float, shall be regarded as foreign investment.

BKPM's position is, in effect, that PR 44/2016 Article 8 means an IDX Listing does **not** automatically result in a company being regarded as an Indonesian party for the purposes of the foreign investment regime. Rather, the legal status of an IDX Listed company, for foreign investment purposes, really depends on whether or not there is any foreign party holding shares that are not part of the "public float".

As interpreted by BKPM, PR 44/2016 Article 8 is, in effect, a re-confirmation and restatement of the pre-2010 position described in the Background section.

If foreign parties only hold shares that are part of the "public float", in the case of a particular IDX Listed company, then that IDX Listed company will be regarded as a local Indonesian company (**i.e.**, a Non-PMA Company). If, however, there is a foreign party holding any shares that are not part of the "public float", in the case of a particular IDX Listed company, then that IDX listed company will be (i) regarded as a foreign party and (ii) be deemed to have the legal status of a PMA Company.

In other words, PR 44/2016 Article 8 makes clear that PMA Company IUP/IUPK holders cannot simply avoid the Divestiture Obligation altogether by undertaking an IDX Listing and thereby automatically change their legal status from PMA Company to Non-PMA Company. It is only in those instances where the foreign investors, in a PMA Company IUP/IUPK holder, exclusively have shares being part of the "public float" at the time of the IDX Listing that the IUP/IUPK holder will be regarded as a Non-PMA Company and, therefore, probably not be subject to the Divestiture Obligation.

Even in the very restrictive situation identified in the previous paragraph, it is still a matter for ESDM, rather than BKPM, to determine whether or not the Divestiture Obligation applies to the newly IDX

Listed IUP/IUPK holder. This is because, as has been pointed out in the Background section, the applicability or otherwise of the Divestiture Obligation, in the case of a particular IUP/IUPK holder, is actually a matter for determination by ESDM, **not** BKPM.

SUMMARY AND CONCLUSIONS

Much as PMA Company IUP/IUPK holders and their professional advisers might want to read into ADML Article 79(4) a new opportunity to satisfy the Divestiture Obligation through IDX Listings, such a reading of ADML Article 79(4) is, almost certainly, unwarranted.

It seems more likely that ADML Article 79(4) may just be intended to be a "one off" solution to and clever "workaround" for dealing with the Government's pressing need to resolve what to do with the Divestiture Obligation in the case of Freeport Indonesia and the 2016 FI Divestiture Shares.

Unless handled very carefully, ADML Article 79(4) could, if it was to become law, actually make the opportunity for PMA Company IUP/IUPK holders, in general, to use IDX Listings to at least partially satisfy their Divestiture Obligations more restrictive, **not** less restrictive.

At the same time, the newly issued Negative Investment List re-confirms and restates the highly restrictive pre-2010 position regarding the legal status implications of a PMA Company IUP/IUPK holder undertaking an IDX Listing.

It seems then that, for the foreseeable future, IDX Listings for PMA Company IUP/IUPK holders will still not offer a "sure fire" solution to dealing with their Divestiture Obligations.

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[This article has been contributed by Bill Sullivan, Senior Foreign Counsel with Christian Teo & Partners. Christian Teo & Partners is a Jakarta based, Indonesian law firm and a leader in Indonesian mining law and regulatory practice. Christian Teo & Partners operates in association with international law firm Stephenson Harwood LLP which has nine offices across Asia, Europe and the Middle East: Beijing, Dubai, Hong Kong, London, Paris, Piraeus, Seoul, Shanghai and Singapore. Readers may contact the author at email: *bsullivan@cteolaw.com*; office: 62 21 5150280; mobile: 62 815 85060978]