

## CONCESSIONAL COAL PRICE – NOT FOR METAL MINERAL PROCESSING & REFINING INDUSTRY<sup>12345</sup>

### INTRODUCTION

The Ministry of Energy & Mineral Resources has recently extended the availability of Indonesia's hugely concessional coal price to a much wider group of domestic coal users than was previously the case.

Domestic coal users in the metal mineral processing & refining industry have, however, been expressly excluded from the right to benefit from the concessional coal price. This is a potentially significant development as many owners and operators of metal mineral processing and refining facilities are obliged to build their own coal fired power plants to ensure an adequate supply of electricity for their processing and refining facilities. Low-cost electricity is also a critical pre-condition to economic metal mineral processing and refining activities in the case of certain metal minerals given the large amounts of electricity required for metal mineral processing and refining activities.

The reasons given by the Ministry of Energy & Mineral Resources, for denying the metal mineral processing & refining industry the right to benefit from the concessional coal price, are not consistent with long standing Government practice re subsidies or with the numerous policy announcements that the Government has made, over many years, about the importance of requiring full domestic processing and refining of all metal minerals.

In this article, the writer will review the decree extending the availability of the concessional coal price before examining, in some detail, the official reasons for denying only the metal mineral processing & refining industry the right to benefit from the concessional coal price.

### BACKGROUND

Indonesia has, for some years now, required coal producers to prioritize the supply of coal to the domestic market ("**DM Obligation**") by imposing (i) annual DM Obligation quotas on certain coal producers and (ii) a ceiling price of US\$70 per tonne on the sale of coal, with certain quality specifications, to the State electricity company ("**PLN**") and so-called independent power producers ("**IPPs**") generating electricity for public purposes ("**PLN & IPP Concessional Coal Price**").

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The DM Obligation applies to (i) holders of Coal Contracts of Work (“CCoWs”), coal production operation special mining business licenses being continuations of former CCoWs, coal production operation special mining business licenses (“**Continuation Coal IUPKs**”) and coal production operation mining business licenses (together, “**Relevant Coal Producers**”) and (ii) in certain instances, holders of coal transportation and sales permits (“**Coal T&S Permit Holders**”).

The DM Obligation and the PLN & IPP Concessional Coal Price have their legal basis in the (i) 2009 Mining Law as amended by the 2020 Job Creation Law and (ii) the implementing regulations issued pursuant to the 2020 Job Creation Law including, most importantly, Government Regulation 96 of 2021 re Implementation of Mineral & Coal Mining Business Activities (“**GR 96/2021**”).

Articles 157 and 160 of GR 96/2021 make clear that:

- (a) Relevant Coal Producers must prioritize the “integrity” (**i.e.**, the availability of sufficient supplies) of coal for domestic purposes;
- (b) MoEMR is empowered to determine how much coal is required for domestic purposes; and
- (c) in order to ensure the fulfilment of the need for coal for the “national interest” (**i.e.**, domestic purposes), MoEMR may also determine the domestic selling price of coal.

The Government’s expansive interpretation of what constitutes the “national interest” is the guiding principle of the DM Obligation.

The DM Obligation was subsequently extended to Coal S&T Permit Holders, in the event of unfulfilled/unsatisfied domestic coal needs, by MoEMR Decree No. 139 of 2021 re Fulfilment of Domestic Coal Needs (“**MoEMR Decree 139/2021**”).

In 2021, the DM Obligation was further extended to require Relevant Coal Producers and (in some instances) Coal S&T Permit Holders to supply coal to domestic coal users, other than PLN and IPPs, in certain specified industries being the cement and fertilizer industries only, at a concessional price of US\$90 per tonne for coal with certain quality specifications (“**IU Concessional Coal Price**”) (MoEMR Decree No. 206 of 2021 re Coal Selling Price to Fulfil National Need for Raw Materials/Fuel in Cement & Fertilizer Industries (“**MoEMR Decree 206/2021**”).

Non-compliance with the DM Obligation, including failure to supply coal to domestic users at the PLN & IPP Concessional Coal Price or the IU Concessional Coal Price (as the case may be), makes Relevant Coal Producers and, in some instances, Coal S&T Permit Holders liable to various sanctions set out in Decree No. 13 of 2022 re Guidelines for the Imposition of Administrative Sanctions, Prohibition of Overseas Coal Sales and Imposition of Fines as well as Compensation Funds Requirement for Non-fulfilment of Domestic Coal Requirements (“**MoEMR Decree 13/2022**”).

MoEMR has now, once again, extended the DM Obligation with the issuance of Decree No. 58 of 2022 re Coal Selling Price to Fulfil National Needs for Industrial Raw Materials/Fuel (“**MoEMR Decree 58/2022**”).

A virtual “socialization” of MoEMR Decree 58/2022 was held on 30 March 2022 (“**30 March Socialization**”).

## **ANALYSIS AND DISCUSSION**

### **1. MoEMR Decree 58/2022**

- 1.1 **Restated IU Concessional Coal Price:** Coal supplied to domestic industrial users must be sold at a price, FOB vessel, of US\$90 per tonne for coal with the quality specifications of (i) calorific value – 6,322 kcal/kg, (ii) total moisture - 8%, (iii) total sulphur – 0.8% and (iv) ash – 15%, with the selling price to be adjusted (in accordance with the various formulae in the appendix to MoEMR Decree 58/2022) in the event of different quality specifications (“**Restated IU Concessional Coal Price**”) (“**First Stipulation**”) (“**CCP Adjustment Formulae**”).

The CCP Adjustment Formulae remain unchanged from those formulae that were originally attached to MoEMR Decree 206/2021 when only domestic coal users, in the cement and fertilizer industries, were entitled to the IU Concessional Coal Price.

The First Stipulation significantly extends, for the first time, the availability of a concessional coal price to many industrial users of coal in addition to coal users carrying on business in the cement and fertilizer industries.

A literal reading of the First Stipulation might suggest that (i) there is no longer a separate PLN & IPP Concessional Coal Price of US\$70 per tonne for coal with certain quality specifications and (ii) all industrial users of coal, regardless of industry, are entitled to the benefit of the Restated IU Concessional Coal Price. **Neither** of these propositions, however, is correct.

Although not apparent from MoEMR Decree 58/2022 itself, it is tolerably clear that the PLN & IPP Concessional Coal Price of US\$70 per tonne for coal, with certain quality specifications, supplied to PLN and IPPs continues to apply independently of MoEMR Decree 58/2022.

As explained in 1.2 below, there is also an important exception to the availability of the Restated IU Concessional Coal Price in the case of one particular category of industrial users of coal.

- 1.2 **Exception for Metal Mineral Processing & Refining Industry:** Domestic users of coal in the metal mineral processing and refining industry (“**MMP&R Industry**”) are **not** entitled to the benefit of the Restated IU Concessional Coal Price (“**MMP&R IU Exception**”) (“**Second Stipulation**”).

Reading the First Stipulation and the Second Stipulation together, the Restated IU Concessional Coal Price is available to all domestic users of coal in any industry **except for** domestic users of coal in the MMP&R Industry.

No reason or explanation is provided, in MoEMR Decree 58/2022 itself, for the MMP&R IU Exception. This, though, is something that is discussed, at length, in Part 2 below.

- 1.3 **Coal S&T Holders:** The Restated IU Concessional Coal Price must be offered by Coal S&T Permit Holders to domestic users of coal in any industry (**except for** domestic users of coal in the MMP&R Industry) if and when Coal S&T Permit Holders are appointed by the Director General of Minerals & Coal (“**DGoMC**”) to meet unfulfilled/unsatisfied domestic coal needs (“**Third Stipulation**”).

Reading the First Stipulation and the Third Stipulation together, it will usually be Relevant Coal Producers which are obliged to offer the Restated Concessional Coal Price to relevant domestic users of coal. However, in certain circumstances, offering the Restated IU Concessional Coal Price also becomes an obligation of Coal S&T Permit Holders. This is consistent with MoEMR Decree 139/2021’s extension of the DM Obligation to Coal S&T Permit Holders in the case of unfulfilled/unsatisfied domestic coal needs.

- 1.4 **Applicable Sanctions for Non-Compliance:** Relevant Coal Producers and Coal S&T Holders, which do not carry out their obligations pursuant to MoEMR Decree 58/2022, are liable to the various sanctions set out in MoEMR Decree 13/2022 which start with a 60-day suspension of business activities, as well as fines and compensation payments, before ultimately progressing to cancellation of business licenses in the event of continuing non-compliance.

- 1.5 **Adjustment of Existing Contract Prices:** Relevant Coal Producers and Coal S&T Permit Holders, which have existing coal supply contracts with industrial users and whose contracts provide for a coal selling price that is either lower or higher than the Restated IU Concessional Coal Price, are obliged to adjust/amend their existing coal supply contracts so that the coal selling price becomes the Restated IU Concessional Coal Price (“**Fifth Stipulation**”).

Notwithstanding the Fifth Stipulation contemplates the possibility of there being existing coal supply contracts that provide for a coal selling price which is lower than the Restated IU Concessional Coal Price, for coal with certain quality specifications, it is hard to imagine any commercial situation in which this would actually be the case. This is because (i) the Restated IU Concessional Coal Price is extremely low given the current market price of coal (with the relevant quality specifications) and (ii) long term coal supply contracts are meant to be revised annually so as to ensure that the selling price is not less than the latest benchmark price published by DGoMC, usually on a monthly basis.

The Fifth Stipulation also fails to make clear that, in the case of Coal S&T Permit Holders with existing coal supply contracts providing for a coal selling price that is either lower or higher than the Restated IU Concessional Coal Price, the price adjustment obligation should, logically, only apply if and when a particular Coal S&T Permit Holder is appointed by DGoMC to meet unfulfilled/unsatisfied domestic coal needs. It will be interesting to see how DGoMC interprets and applies the Fifth Stipulation in practice.

- 1.6 **Revocation of MoEMR Decree 206/2021:** MoEMR Decree 206/2021, which made the IU Concessional Coal Price available to coal users in the cement and fertilizer industries only, is revoked (“**Sixth Stipulation**”).

The Sixth Stipulation makes clear that, going forward, the availability of a concessional coal price for domestic users of coal, other than PLN and IPPs, is governed exclusively by MoEMR Decree 58/2022 and the higher order laws and regulations in respect of which it purports to provide administrative guidance.

## 2. **Stated Policy Reasons for MMP&R IU Exception**

- 2.1 **Preliminary Remarks:** During the 30 March Socialization, DGoMC and the Director of Coal Development Exploitation (“**DoCDE**”) gave three reasons for the MMP&R IU Exception, as reported in the 31 March 2022 edition of on-line news portal Bisnis.com (“**Stated Policy Reasons**”). The Stated Policy Reasons are that domestic coal users in the MMP&R Industry should not be entitled to the Restated IU Concessional Coal Price because:

- (a) the MMP&R Industry is “***not** directly related to the livelihood of many people*” (“**First SP Reason**”);
- (b) *the Government does “**not** provide industrial subsidies that are **not** in line with the spirit of the free market*” (“**Second SP Reason**”); and
- (c) all of the MMP&R Industry’s products will be exported and [are] **not** for domestic needs (“**Third SP Reason**”).

Assuming Bisnis.com has correctly quoted what DGoMC and DoCDE actually said during the 30 March Socialization, the Stated Policy Reasons are certainly worthy of close attention and otherwise make very interesting reading. The writer will now evaluate each of the Stated Policy Reasons in turn.

- 2.2 **First SP Reason:** At the risk of serious understatement, the First SP Reason is hard to reconcile with 10++ years of Government policy that has insisted upon domestic processing and refining of all metal minerals on the basis that this is the only way to ensure that Indonesia and all Indonesians obtain an appropriate level of benefit from the exploitation of Indonesia’s metal mineral resources.

The whole rationale of making the domestic processing and refining of all metal minerals an obligation of every metal mineral producer is that this will deliver extraordinary benefits to Indonesia and all Indonesians in the form of higher value export sales, increased Government tax revenue and new employment opportunities for Indonesian workers. If, in fact, these claimed benefits are illusory, why have metal mineral producers been forced to invest vast sums of scarce capital in the construction of metal mineral processing and refining facilities?

The “livelihood” of Indonesians and improvements in that livelihood are also surely to be measured by more than job opportunities alone. The long-claimed huge increases in Government tax revenue, that will supposedly result from insisting upon

domestic processing and refining of all metal minerals, should enable the Government to greatly increase its expenditure on education, health care, infrastructure and numerous other initiatives that are meant to, at least in theory, deliver a huge improvement, in the livelihood of the average Indonesian, as measured by a variety of metrics.

DGoMC's advancement of the First SP Reason, as part of the justification for the MMP&R IU Exception, comes at an interesting time given the long-claimed benefits of domestic processing and refining of all metal minerals are being increasingly challenged by at least some academics and researchers based on the available empirical evidence of the positive economic consequences of Indonesia's domestic processing and refining policy or, rather, the relative lack of any such empirical evidence. In this regard, reference may be usefully made to a very recent article by researcher, Krisna Gupta, that was published in *The Jakarta Post*, in early April, with the title "*Indonesia's Claim that Banning Nickel Exports Spurs Downstreaming is Questionable*". As Gupta points out, the Government has failed to disclose any data which unequivocally establishes that banning the export of unprocessed and unrefined Nickel ore has delivered or will, inevitably, deliver the benefits that are meant to flow from compulsory downstream processing and refining of all metal minerals including Nickel ore. Gupta highlights that the Government's focus on the resulting increase in added value metal mineral exports may be seriously misleading as it overlooks the fact that (i) the Government may actually experience revenue loss, from reduced corporate tax and export duty collections, as a result of the numerous tax holidays and other incentives offered to investors in smelter projects, (ii) there has simply been a transfer of added value from mining companies to domestic smelting companies as mining companies are forced to sell their mineral ore to domestic smelting companies at a far lower price than is available for mineral ore on the international market and (iii) any increase in employment opportunities in the MMP&R Industry may be offset by declining employment opportunities in the mineral ore mining industry. Of course, many knowledgeable industry observers have, since the initial introduction of the domestic processing and refining obligation as part of the 2009 Mining Law, seriously questioned the economics of insisting upon domestic processing and refining of all metal minerals.

To the extent the First SP Reason is a, no doubt, wholly unintentional acknowledgment by DGoMC that the long-claimed benefits of insisting upon domestic processing and refining of all metal minerals may actual be far less, in reality and in terms of the resulting impact on people's livelihood, it raises very challenging questions for the Government about the integrity of its industrial policy.

- 2.3 **Second SP Reason:** It will, no doubt, be a surprising revelation for many people that the Government does "*not provide industrial subsidies that are not in line with the spirit of the free market*". Finding any empirical evidence to support this proposition, prior to the announcement of the MMP&R IU Exception, would likely be a herculean task indeed. It is also, probably, rather "too late in the day" for DGoMC to be unduly concerned about the danger of interfering with "*the spirit of the free market*" if the benefit of the Restated IU Concessional Coal Price had been extended to domestic coal users in the MMP&R Industry. Notwithstanding the lofty ideals implied by the Second SP Reason, the reality in Indonesia is rather different from that suggested by the Second SP Reason.

Like many other countries, particularly in the developing and newly developed/industrialized world, Indonesia has long provided extensive subsidies to Indonesian households and businesses in pursuit of a wide range of economic, social and political objectives including, most importantly, encouraging economic development, poverty relief and promoting electoral support for the ruling Government party or coalition. Indonesia's energy subsidies are particularly extensive and have resulted in the country having relatively low electricity prices compared to many other countries in South East Asia and elsewhere. In June 2021, Indonesian electricity prices were (i) Rp1,444.70 (US\$0.101) per kWh for households and (ii) Rp1,114.74 (US\$0.078) per kWh for businesses. This is to be compared with household electricity prices in (i) Singapore of US\$0.178 per kWh, (ii) the Philippines of US\$0.165 per kWh and (iii) Thailand of US\$0.114 per kWh.

The DM Obligation and the PLN & IPP Concessional Coal Price actually represent a huge subsidy for PLN and are otherwise completely inconsistent with "*the spirit of the free market*". While it may be technically true that this subsidy is not being provided by the Government to PLN, this is merely because the Government has transferred, on a wholly non-voluntary basis, responsibility for subsidizing PLN's loss-making operations to coal producers which are primarily (although not exclusively) private sector parties. While IPPs also benefit from the PLN & IPP Concessional Coal Price, this simply means that PLN does not have to pay a price for electricity, generated by IPPs and supplied to the grid for public consumption purposes, that reflects the market price of the coal used to generate that electricity.

The Government has also just extended the "subsidy" inherent in the IU Concessional Coal Price by means of the announcement of the Restated IU Concessional Coal Price that now enables not just domestic coal users in the cement and fertilizer industries to buy coal at far below market value but all other domestic coal users as well, save for domestic coal users in the MMP&R Industry, to buy coal at far below market value.

Given the various points made above, there must be a certain irony in DGoMC socializing the issuance of MoEMR Decree 58/2022 and the extension of the subsidy represented by the Restated IU Concessional Coal Price while, at the very same time, claiming that the Government does "*not provide industrial subsidies that are not in line with the spirit of the free market*".

- 2.4 **Third SP Reason:** The Third SP Reason, while more or less currently correct, completely overlooks the fact that the MMP&R Industry is (i) the direct and intended result of the Government's policy of insisting upon domestic processing and refining of all metal minerals and (ii) left with no choice but to export most of its production because there is no domestic market for that production. In other words, the Government has mandated the creation of an industry, the production of which is, to a large extent, not needed domestically at this time.

The Government would, of course, like to see the development of domestic industries which need the production of the MMP&R Industry. This is particularly evident in the case of that part of the MMP&R Industry which produces processed and refined products utilizing Nickel ore. The Government's enthusiasm for and overt encouragement of the development of an electric battery industry in Indonesia is a

particularly good example of the Government seeking to create domestic need for at least some of the by-products of downstream processing and refining of Nickel ore. Likewise, the Government has, on several occasions, urged European and Japanese stainless steel manufacturers to relocate their manufacturing plants to Indonesia rather than continue to pursue their long running World Trade Organization claims against Indonesia in respect of its ban on the export of Nickel ore. If either of these initiatives is ultimately successful, there will be a domestic need for at least some of the production of the MMP&R Industry. These are, however, matters over which domestic users of coal in the MMP&R Industry have absolutely no control or influence whatsoever.

As metal mineral producers are being compelled to invest in the MMP&R Industry, it hardly seems reasonable to deny the MMP&R Industry the same incentives that are being offered to all other domestic users of coal for industrial purposes and merely because the production of the MMP&R Industry is not intended for the fulfilment of domestic needs. Increasing the value of Indonesia's metal mineral exports, **not** producing goods in order to meet domestic needs that previously had to be fulfilled with imports, was always and continues to be the primary objective of making full downstream processing and refining of all metal minerals an obligation of every metal mineral producer.

2.5 **Possible Real Reason:** Given that none of the Stated Policy Reasons stand up to serious scrutiny, we need to look elsewhere for the real reason for the MMP&R IU Exception.

The real reason for the MMP&R IU Exception may simply be “pushback” from still politically well-connected coal producers which have almost certainly grown very concerned and frustrated about the extent to which they seem to be increasingly expected to assume responsibility for funding the Government's policy initiatives (over which they have no control) through disguised subsidies, to PLN, IPPs and other domestic users of coal, in the form of accepting way below market prices for a significant part of their coal production. While Indonesia's coal producers have undeniably been treated very generously by the Government in terms of (i) being granted Continuation Coal IUPKs, (ii) keeping most of their former contract areas and (iii) being protected from the recognition of the priority right to former contract areas long claimed by State-owned enterprises, they are certainly being required to pay a high price for this generous treatment.

Given the forthcoming 2024 presidential elections, coal producers probably accept (albeit reluctantly) there is no realistic prospect of them being able to convince the Government of the need to increase public purpose electricity prices so as to reflect the international market price of the coal used to produce much of that electricity. However, also making the Restated IU Concessional Coal Price available to the MMP&R Industry may just be a “bridge too far” for many coal producers and not something that the Government feels is a sufficiently politically sensitive issue to warrant imposing a further financial burden on coal producers. It is certainly hard not to feel at least a little empathy for coal producers in this regard. Some possible indication of this being the real reason for the MMP&R IU Exception may be found in the following reported comment of DGoMC during the 30 March Socialization:

*“There is indeed an exception for the smelter industry. We don’t mean it bad but, rather **to maintain balance** and also the honor of our nation internationally.”*

The need to “*maintain balance*”, that DGoMC referred to during the 30 March Socialization, may well be the balance between ensuring Indonesia’s coal producers continue to be willing implements of Government policy (as part of the quid pro quo for their generous treatment in numerous matters) on the one hand and recognizing there need to be some limits on the extent to which major coal producers are expected to subsidize the Government’s political largesse on the other hand. The writer would not, however, want to even hazard a wild guess at what the MMP&R IU Exception may have to do with maintaining “*the honor of our nation internationally*”!!! Readers will have to use their own imagination in trying to determine the intended meaning of this intriguing phrase.

## **SUMMARY & CONCLUSIONS**

The list of domestic coal users, entitled to the benefit of concessional coal prices, has been gradually extended way beyond PLN and IPPs.

With the issuance of MoEMR Decree 58/2022, all domestic users of coal for industrial purposes, other than domestic coal users in the MMP&R Industry, are now entitled to the benefit of the Restated IU Concessional Coal Price.

The various Stated Policy Reasons, for the MMP&R IU Exception, cannot be reconciled with many years of Government insistence upon full downstream processing and refining of all metal minerals as the only way to ensure that Indonesia and all Indonesians obtain an appropriate level of benefit from the exploitation of the country’s metal mineral resources. Likewise, the Government’s long-standing commitment to providing subsidies and general disregard for “the spirit of free enterprise” mean that the real reason for the MMP&R IU Exception must be found elsewhere.

Coal producers may simply be close to reaching the limit of their willingness to be made responsible for the funding of Government policies over which they have no say.

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