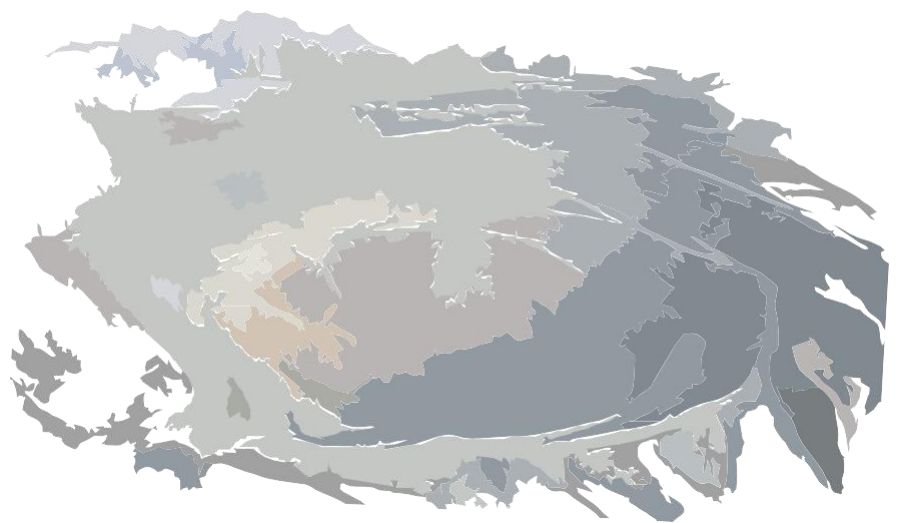


REPORT

MONITORING TOWARDS THE DISPUTE BETWEEN INDONESIA GOVERNMENT AND FREEPORT IN 2017



INDONESIA FOR GLOBAL JUSTICE



Written by : Budi Afandi
Edited by : Rachmi Hertanti
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Indonesia Vs. Freeport :

“Negotiations in the Shadow of the Arbitration Tribunal”

Why is IGJ do monitoring?

Freeport McMoran Inc. emphasized its rejection of the Work of Contract (WOC/KK) into a Special Mining Permit (IUPK) of Production Operations offered by the Indonesian Government since 10 February 2017. Freeport believes that the change is against the agreement in the WOC, then it constitutes the delinquency of the Government of Indonesia against KK. Therefore the Freeport "intimidate" would leading the Indonesian Government to the International Arbitration if they are not solve the problem. Freeport confirmed the refusal through press conference in Jakarta (20/2/2017) and gave 120 days since 18 February 2017 to the Government to find a win – win solution between them.

WOC between Freeport and the Government is stated firmly the mechanism of dispute settlement through the international arbitration (UNCITRAL)¹. Nevertheless, it has become the interesting discourse on the global level that Investor-State Dispute Settlement (ISDS) considered as take a side to the investor's interest and frequently is considered as an obstacle for the State in constitute its sovereignty², particularly the developing countries.

Generally, the foreign investors are suing the State in term of making or implementing some certain regulation that may interfere their business. In Indonesia, as much as 70% of the ISDS's claims is occurred in the mining sector³ as Churchill Mining, a British Mining Company which demanded the Indonesian government to pay a loss of USD 1 Billion due to the revoked of the Mining Area Permit by the East Kutai Regent, either as Newmont in ICSID. It has clearly impact, the ISDS is the mechanism that used by the foreign investor to detainee, restrain, the State ability to enforce the norm (law) instead of make the state to issue some certain regulations for the investor's benefit.

Relation of ISDS with the power of state and sovereignty is need an attention, specially when Indonesia is continuously inviting the foreign investment. The relation raising the question of how the position of the Indonesian government's efforts to enforce the rule of law in the interest rotation to "facilitate" investment and the threat of international arbitration claims?

Monitoring by the Indonesia for Global Justice (IGJ) is one of several activities conducted in the framework of of advocacy and monitoring of disputes between the Government and PT Freeport Indonesia (Freeport McMoran Inc). This monitoring is based on media reports that can be accessed by the public and conducted within of 120 days (following the term which Freeport delivered). Materials considered as relevant to the disputes of both parties are published in a separate channel called "**FOCUS FREEPORT**". The publication is done periodically in two weeks. The materials has been published without analysis and then a description of occasion that occurring within the period monitoring in 120 days. The expected outcome of this process is the public could mapping the important events during the negotiations process as well as the document analysis regarding some events in the dispute.

From the monitoring, the IGJ concluded that the mechanism of ISDS directly affects the state's ability to enforce norms (regulations) and reduce the role of the state as a public institution into a private institution. On the other hand, ISDS has indirectly opened space for negotiations on the substance of legislation in Indonesia, which should be the authority of the state.

Summary of Disputes

Law of the Republic of Indonesia Number 4 of 2009 concerning Mineral and Coal Mining (Minerba Law) order the transition of the Minerba supervision to the licensing regime. Moreover, the Minerba Law order to do purification and cultivation of the mining products before being exported. Formerly, those two order have not been implemented optimally.

On 12th January 2017, the Government of Indonesia determined a restriction on export of concentrates after published three regulations related to the mineral mining activities in previous day⁴. In those regulations, the Government requires mining company to changes the status of contract into permit in order to export.

Then, on 10th February the Government issued a Special Mining Permit (IUPK) for Freeport and AMMAN which simultaneously changed the Work of Contract (KK) of both companies into IUPK⁵. AMMAN was mentioned to accept the government's actions, but neither PTFI which immediately reacted and mentioned the Indonesian Government has violated the agreement in the KK. Consequently, on 17th February, Freeport sent a letter of notification to the Minister of EMR regarding the act of default and KK violation by the Government of Indonesia. The action followed by the Press Conference (on 20th February) to confirm its rejection of changing the KK into IUPK and gave the Government of Indonesia of 120 days to find win-win solutions (starting since the Government received a written letter from Freeport). In case both of the parties do not reach any consent, PTFI will sue the Government into the International Arbitration.

After the "threat" of the international arbitration, both parties (the Government of Indonesia and Freeport) agreed the negotiation process until October 2017. Lately, precisely in April 2017, it was reported that Freeport has approved the change of KK status to IUPK. Hence, the next phase will be focused on the issue of stock divestment, smelter and assurance of investment certainty. However, the Government have to change the technical regulations which regulates the basic transition of KK into IUPK, namely the Ministerial Regulation of ESDM Number 5 of 2017 into the Ministerial Regulation of ESDM Number 28 of 2017. The Government claimed that there is no longer opportunity to the International Arbitration since Freeport has approved the change to IUPK. In the last period of 120 days, Freeport said that they are agreed to build a smelter and requested the issuance of the Government Regulation (PP) to guarantee the investment, particularly the change of KK into IUPK.

Threat of ISDS : Barrier implementation of the Law Order

The Minerba Law has clearly mandated the efforts to increase the added value of mineral and coal mining products by "refining and processing" domestically before being exported⁶. In addition, the Minerba Law also clearly mandates the termination of the contract-based into licensing⁷. Unfortunately these two things are very difficult to implement, especially in relation to the foreign mining company in Indonesia. One of the barrier is the possibility of investors suing the state known as Investor-State Dispute Seating (ISDS). At the International level, ISDS is controversial because it is considered more favorable to investors and has reduced the sovereignty of the state⁸. Therefore, some countries trying to release the regulation of ISDS from their existing agreements⁹.

In the presence, Indonesia was once sued by the Newmont Nusa Tenggara (NNT) for imposed the restriction of exporting the raw materials. The lawsuit then revoked and both parties agreed some conditions through a Memorandum of Understanding (MoU) which granted an exception related to the restriction of the raw material exports¹⁰.

Instead of NNT which had registered its lawsuit to the International Arbitration Tribunal, Freeport preferred to submitted an objection notification to the Government of Indonesia as regulated in the KK. Freeport has been expressing its desire to bring the issue to the International Arbitration in case the Government does not find a win-win solutions. The absence of formal ISDS process does not mean that mechanism has not affected the Government of Indonesia yet. In the form of "threat", it has been able to suppress the power of the Government authority.

An investigative review titled "The Billion Dollar Ultimatum"¹¹ demonstrates how ISDS is used as a "weapon" by investors to pressure the country (especially Indonesia) which is one of the causes due to the lack of transparency in the process. It is seems to be seen in the course of negotiations between the Government of Indonesia and PTFI in the period of 120 days. The IGJ notes that the direct impact of the ability of investors to sue the state is the loss of the state's ability to enforce its legislation, in this context is the Minerba Law, at least there are two main issues namely the adjustment of KK to IUPK and the construction of smelter and processing facilities. The adjustment of KK to IUPK should be done at least one year since the Minerba Law is enacted in 2009 (in 2010)¹². While the construction of refining and processing facilities should be done at least 5 years after the Minerba Law is enacted (in 2014)¹³.

The Government has been published two regulation at once in the beginning of 2017¹⁴ as an effort to enforce the will of Minerba Law which unfortunately conducted in circumstances that violates and undermines the Minerba Law itself. The requirement to adjust KK to IUP along the smelter development should be entering the law enforcement phase considering the limitation time which regulated by the Law. In the context of the adjustment of the KK (renegotiation), both parties have held a series of meetings since 2012 which producing to the Memorandum of Understanding (MoU)¹⁵, referring to Article 169 (b) and Elucidation of Article 169 (b) of the Minerba Law. As stated in the MoU, both of the parties compromising the continuation of mining operations in the form of Special Mining Permit (IUPK), processing and refining will be carried out domestically by realizing an additional copper refining facility in Indonesia by prioritizing the use of domestic labor, goods and services.

Therefore, the change of KK into IUPK or smelter development is not only the will of the Minerba Law but also the agreement of both parties. So as, it is rather of "odd" when Freeport refuses to change the form of KK to IUPK which is rumored to have been agreed through the MoU. It's getting odd, when it is used as an excuse to consider the Government of Indonesia has defaulted so deserve to be brought to the International Arbitration. Apart from these peculiarities, this condition shows how investors are able to intersect capability of the state (Indonesia) which in fact has sided with the spirit to simplify the investment. The impact of these intercepts is showed from the changes which made by the Government to the Ministerial Regulation No. 5 of 2017 on Enhancement of Added Value through Mineral Processing and Purification Activities in Motherland.

As the Government perspective, this regulations is a technical rules which generally born to implement the mandate of the Law. Through the Ministerial Regulation No. 5 of 2017, the Government intends to terminate the form of KK by pressuring investors to fulfill the obligation to build smelters. Article 19 of the Ministerial Regulation of ESDM No. 5 / 2017 states:

"Revision in the forms of mining business as referred in the Article 17 point 2 shall be made by claiming for the revision of the form of its mining business to IUPK of Production Operation as well as termination of the Contract of Work to the Minister before the expires of period"

However, it's about 40 days after Freeport issued a threat to the International Arbitration, the Government immediately changed the provision into :

"Revision in the forms of mining business as referred in the Article 17 point 2 shall be made by claiming for the revision of its mining business to IUPK of Production Operation to the Minister."

There is no longer regulation regarding to the "termination of KK" which is the core of the spirit of improving the management of Minerba. In point of fact, appears of new clauses that recognize the KK existing¹⁶ and allow the management opportunity to remain in the form of KK if there is no settlement in conforming the implementation of the IUPK Production Operations¹⁷. In the context of the Indonesian Government disputes with Freeport, the phrase of "conformation to the implementation of the IUPK Production Operation" may refer to a negotiated process goes on the next October. The revision clause of the Ministerial Regulation of ESDM No. 5 of 2017 is clearly a form of defeat the power of the Government in enforcing the mandate of the Law in the presence of investors. Since it's basically the new regulatory model is not in favor of the interests of Indonesia. If negotiations is abolishing and management re-using the KK model, then Freeport has benefited from obtaining an export license until October 2017¹⁸. Therefore, the remaining stakes is on the extension of the KK (which can also be interpreted as a matter of guarantee of investment certainty).

At the end of 120 days period of the IGJ monitoring period, Freeport asked the Government of Indonesia to issuing the Government Regulation (PP) related the guarantee of investment certainty. This request of course is seemed amusing, particularly if the PP will be applied to every investments in the Minerba sector. The PP referring to the Law No. 12 of 2011 on the Formulation Procedure for Legislation is "The Government Regulation is the Laws and Regulations set by the President to implement the Law as appropriate". Even though there is an opportunity to make PP for certain needs¹⁹ beyond the Government one-years scheming, then it should involve the decision of the Supreme Court. If the Government fulfills the request it is indicating that the government's effort to support the investment is meaningless. On the other hand, it shows that ISDS has significantly reduced the power of the state over itself.

Recommendation

The issue of the Government in the International Arbitration has been existing before, and it is not merely that the Government has been defeated in the process. In spite of it, permitting the investor to suing the State is contradict of the public and private interest on the one line, in this circumstances the public interest is often defeated.

Therefore, considering those things, the IGJ recommends the Government of Indonesia to:

- 1) To be consistent in implementing the mandate of the Minerba Law, particularly in relation to the adjustment of KK;
- 2) refuses the investment stability guarantee agreement because it is against the Law, moreover it will be reloading the dispute mechanism to the International Arbitration, that mechanism which should be through the PTUN below the IUPK regime.
- 3) Unfold the negotiation process to the public, particularly the people of Papua.

South Jakarta, 25th June 2017

Endnotes :

¹ Article 21 of KK

² <https://corporateeurope.org/international-trade/2014/04/still-not-loving-isds-10-reasons-oppose-investors-super-rights-eu-trade>

³ *Lembar Fakta Ancaman Perjanjian TPP*, Indonesia for Global Justice, 2013

⁴ the PP 1 of 2017, the Ministerial Regulation of ESDM No. 5 of 2017 and No. 6 of 2017

⁵ <https://igj.or.id/fokus-freeport/>

⁶ Art. 170 of the Minerba Law

⁷ Read the Art. 35 of the Minerba Law which describes the management of Minerba solely in the form of: IUP, IPR and IUPK. There is no more management takes the form of contracts, hence, the extension of Freeport's operations and other KK holders must be in the form of a permit, however, still, the Minerba Law recognizes the existence of appearance contracts until the end period of the contract.

⁸ ISDS and Sovereignty, NZIER, in September 2015,

⁹ <https://lop.parl.ca/Content/LOP/ResearchPublications/2015-115-e.html?cat=economics>

¹⁰ Hilde van der Pas & Riza Damanik, Netherlands – Indonesia Bilateral Investment Treaty rolls back implementation of new Indonesian mining law: The case of Newmont Mining vs Indonesia; IGJ, TNI, EU-ASEAN FTA Network, in November 2014

¹¹ https://www.buzzfeed.com/chrishamby/the-billion-dollar-ultimatum?utm_term=.ss25A3i0Lp#.ug8yl651Qz,

¹² Read the Art. 169 para. 2 of the Minerba Law

¹³ Read the Art. 170 of the Minerba Law

¹⁴ The Civil Society Coalition believes that the issuance of these both of the legislation is considered against to the Minerba Law, therefore the Coalition of Civil Society Guards of the Natural Resources Constitution has formally filed a lawsuit against the PP No. 1 of 2017 on the Fourth Amendment of PP 23 of 2010 concerning the Implementation of Minerba Mining Business Activities into Supreme Court on Thursday (30/3).

¹⁵ <http://www.rappler.com/indonesia/109077-kronologi-negosiasi-perpanjangan-kontrak-freeport-indonesia>

¹⁶ Article 19 para. 3

¹⁷ Article 19 para. 7

¹⁸ IUPK temporary PTFI be in force till 10th October 2017

¹⁹ Read the Art. 25 and Art. 28 of the Law No. 12 of 2011