MINISTRY OF FINANCE OF REPUBLIC OF INDONESIA

Fiscal Regimes for EI: Issues and Challenges in Indonesia

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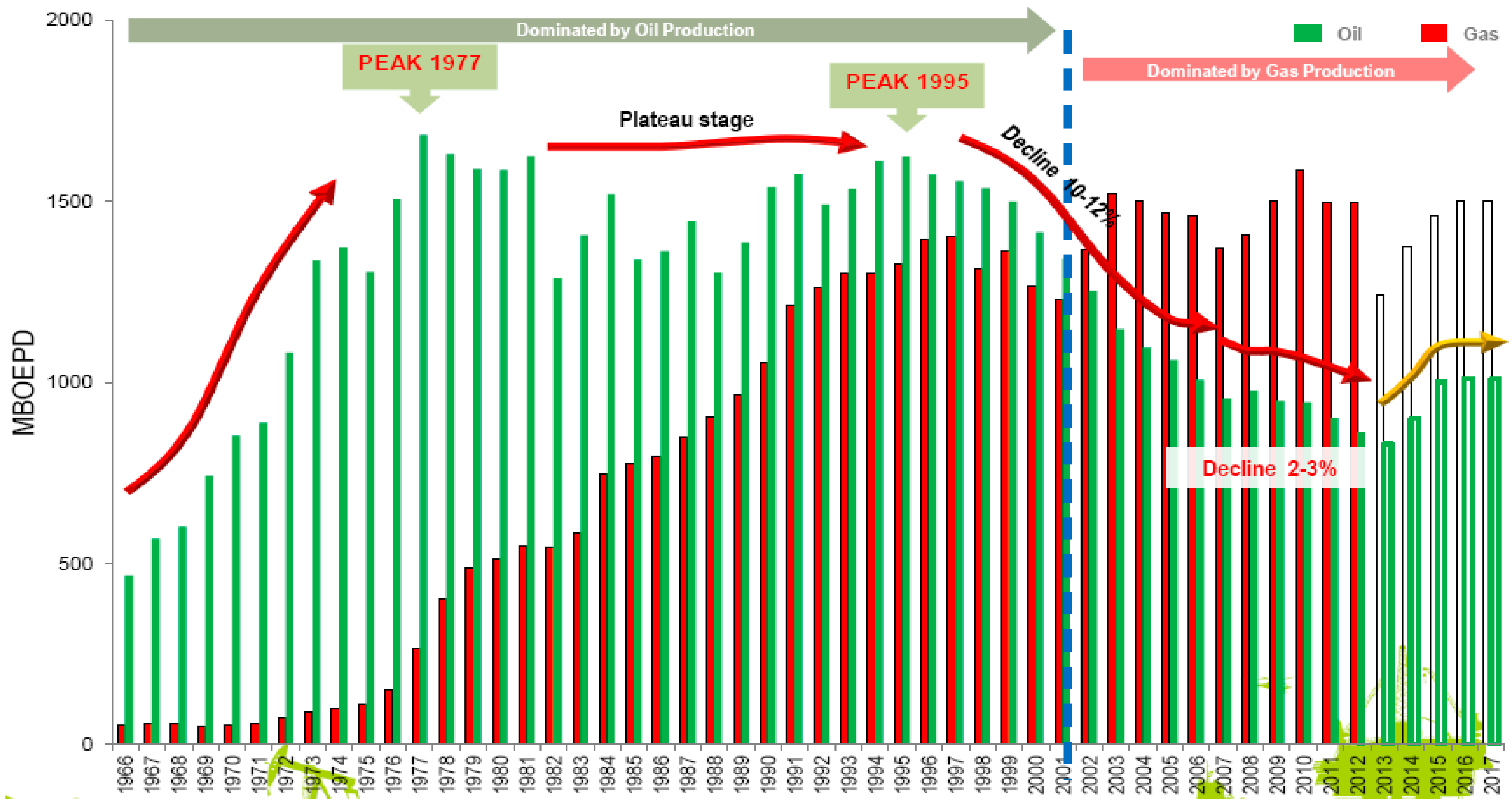
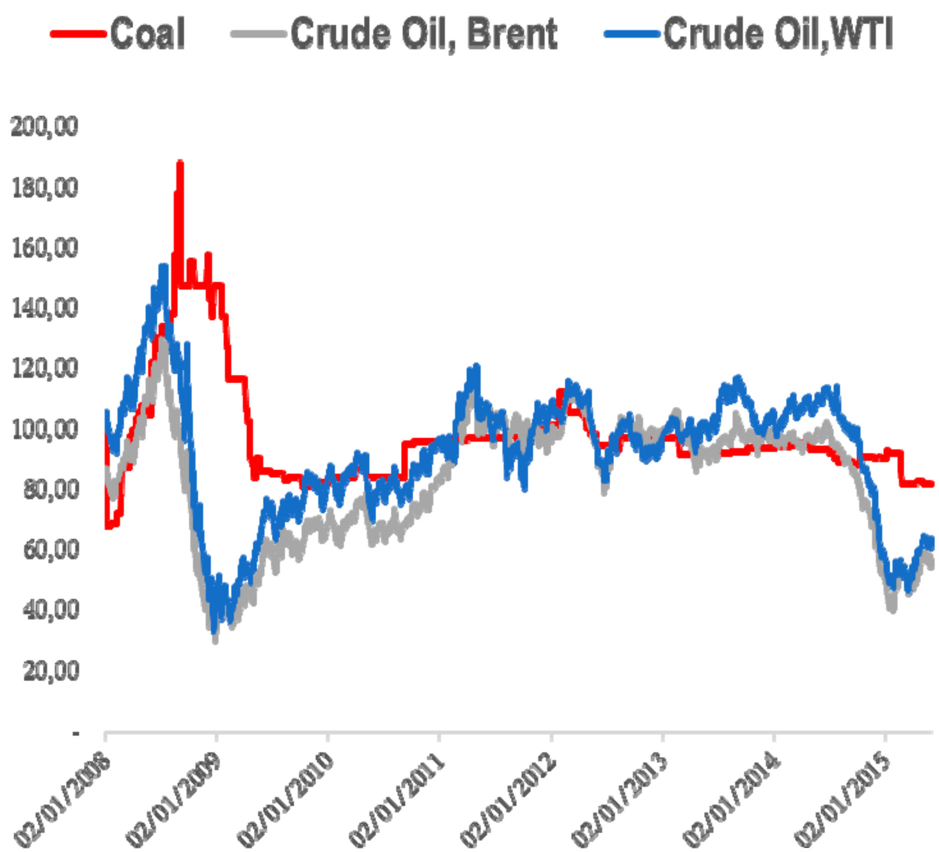
Introduction: Indonesia's Oil and Gas Production



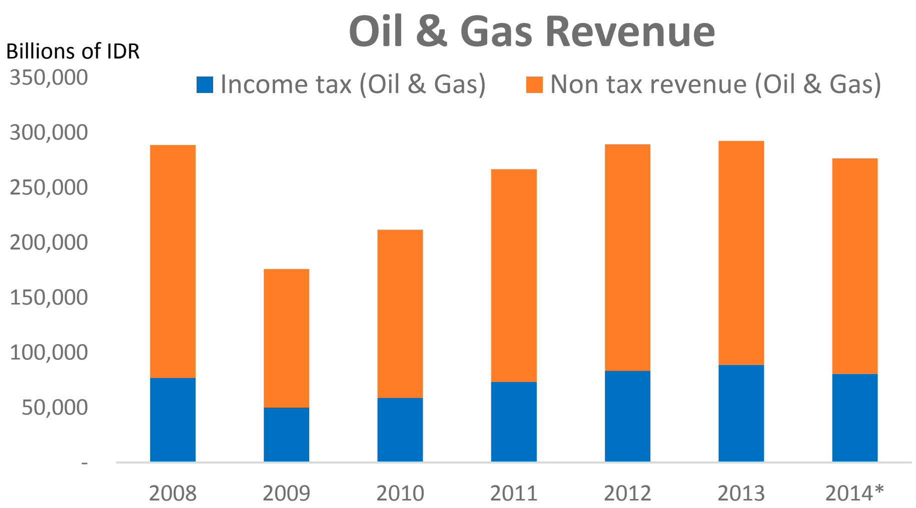
- Indonesia oil and gas production tends to decrease in future years because of small investment activities on exploration of the new wells.
- On the other hand, domestic need for oil and gas is increasing significantly due to industries and transportation.

Recent Trend Of Major Commodity Prices



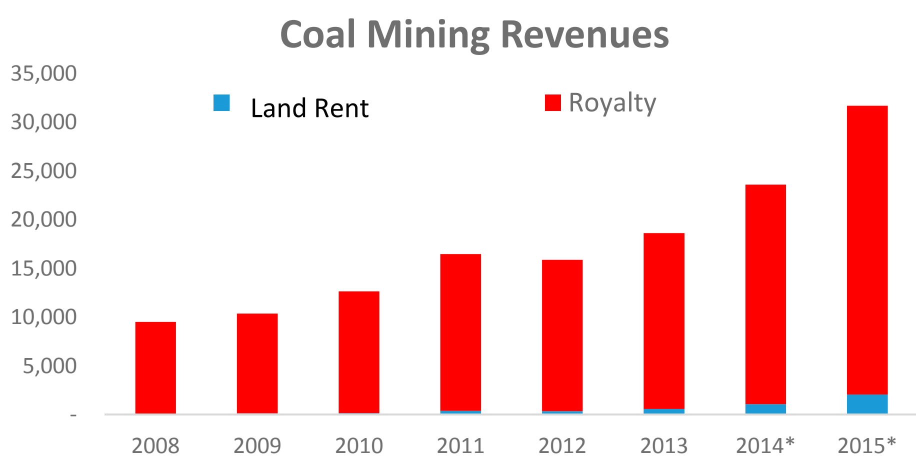
- After suddenly plummeted in 2009, both coal and crude oil price were began to recover gradually until 2011.
- From 2011 to 2014, crude oil prices have fluctuated, whereas coal price remained steady.
- Following this, crude oil prices considerably dropped in early 2015 and are estimated to rebound again.

Introduction: Natural Resources Revenues



Source: State Budget Realization
* State Budget-Revised

- **Oil and gas tax revenue has increased since 2009 and remained stable during the period of year from 2011 to 2014.**
- **Income tax revenue target from oil and gas for 2015 decreases due to decreasing of Indonesian Crude-oil Price (ICP) and crude oil lifting capacity.**



- **Over the last 5 years, total amount of non-tax revenue from extractive industries (non-oil & gas) gradually increases following the increase of production and taxpayers compliance.**

Mining : Fiscal & Non Fiscal Policy

General:

- Mining activity approval is based on Lisence, not Contract;
- Mining business entity should be in the form of limited enterprise in accordance with Indonesia law;
- One business entity holds one license;
- Companies are banned to export mineral ore. In order to export mineral products, companies, either alone or together, has the obligation to build the smelter

State exercises the contract until the term of contract is expired. However, the provisions of the contract must be adjusted, e.g.:
-Mining area,
-contract extention form,
-state revenue,
-smelter establishment obligation,
-divestment obligation, and
-local content

Mineral and Coal Law
(Law no 4/2009)

RENEGOTIATION

Company obligation in accordance with State Revenue:

- Royalty based on sales
- Corporate Income Tax → tariff 25%
- Value Added Tax and Luxury Sales Tax → 10% sales
- Land and Builidng Tax
- Import and Export Duty
- Local Tax → for local revenue

Mining : Existing Mining Taxation

Type of Taxation	License Based (Minerba Law 4/2009)	Contract Based (before Minerba Law 4/2009)
Coal Royalty	Prevailing Law; royalty tariff on low: medium: high rank = 3%:5%:7% from sales	Nailed down; Royalty Tariff 13,5% (it is called Government Share)
Mineral Royalty	Prevailing Law; royalty tariffs are varied from 1,5% to 6% which depends on Mineral commodities. The highest tariff, 6%, is levied on diamond, e.g. Royalty tariff on gold 3,75%, silver 3,25%, copper, 4%.	Nailed down; royalty tariffs are varied based on commodities, e.g. Royalty tariff on gold 1,5%, silver 1%, copper, US$ 0,25/ton
Corp Tax	Prevailing Law, Corp Income Tax 25%	Nailed down, varied from 30% to 45%
Witholding Tax	Prevailing Law, Income Tax Act 36/2008	Prevailing Law, Income Tax Act 36/2008
VAT	Prevailing Law, VAT Tariff 10%	Nailed down, VAT tarif varied between 5% (sales tax) and 10% (VAT).
Duty Import	Prevailing Law, Exempted	Nailed down, exempted
Duty Export	Prevailing Law, Duty Export on certain mineral concentrates	Company does not have obligation to pay duty export
Local Tax	Prevailing Law	Nailed Down

Renegotiation

Note:

- Indonesia has 2 types of contract, which are Contract of Work for mineral and Coal Contract of Work.
- Recently, more than 100 contracts are still valid. The renegotiation started in 2011 and is still progressing.

Mining : Royalty

- In mining, Indonesia applies consession system where company has to pay royalty to central government. The method of royalty is changed from spesific tariff to ad valorum tariff.
- Mineral royalty tariff in Indonesia varies and depends on the type of mineral products. There are 66 mineral commodities which tarriffs are imposed. For example:

No	Mineral Product	Tariff	No	Mineral Product	Tariff
1	Alumina	3% from sales	6	Nickel ore	5% from sales
2	Alumunium	3% from sales	7	Nickel Matte	4% from sales
3	Bauxite	3,75% from sales	8	Ferronickel	4% from sales
4	Iron ore	3% from sales	9	Copper	4% from sales
5	Gold	3,75% from sales	10	Tin	3% from sales

- For coal, tariff depends on the quality rank of coal and the mining method.

No	Quality coal rank	Open Pit Tariff	Underground Tariff
1	Low (≤ 5100 Kcal)	3% from sales	2% from sales
2	Medium (> 5100 – 6100 KCal)	5% from sales	4% from sales
3	High (≥ 6100 Kcal)	7% from sales	6% from sales

Mining : Existing Fiscal Incentives & Protection

Fiscal Incentives & Protection

Fiscal Incentives

- **Investment Allowance** (Govt Regulation 18/2015) → for building smelter of iron ore, iron sand, uranium, thorium, tin ore, black tin ore, bauxite, copper, nickel ore, manganese, zinc, and zircon → for downstream mineral mining. The facilities are:
  - Reduced net income tax for 30% of total investment (5% a year for 6 years).
  - Accelerated depreciation.
  - 10% or lower income tax rate based on tax treaty, on dividend paid to non-resident tax payer.
  - Extention of Compensation for losses from 5 to 10 years.
- **Exemption of Value Added Tax for import** of machinery and equipment, excluding spare part (Government Regulation No 31/2007) for both upstream and downstream mining activity
- **Exemption of Import Duty** for machinery, goods, and materials for construction and development. (Ministry of Finance Regulation No 176/PMK.011/2009)

Fiscal Protection

Export duty on concentrate of copper, iron, manganese, zinc, titanium, and lead (Ministry of Finance Regulation No 153/PMK.011/2014).

This policy is correlated to the construction stage of those mineral smelter. For those exporters who do not build smelter, export duty tariff are varied between 25% -60%. On the contrary, for exporters who build smelters, the export duty tariff are varied between 0% - 7,5%.

Mining: Fiscal Administration

- Fiscal administration for royalty revenue, central revenue, and local revenue is different.
- Royalty revenue is administered by central government through Directorate General of Mineral and Coal MEMR and the revenue will be distributed to province and local government in every 3 months.
- Central revenues, which are income tax, value added tax and land and building tax on mining production, are administered by central government through Directorate General of Taxes MoF. The revenues from land and building tax on mining production are distributed to province and local government.
- Central revenues, which are import and export duty are administered by central government through Directorate General of Customs and Excises MoF
- Local revenues, which are land and building tax and groundwater tax, are administered local government.

Mining: Issues and Challenges

- Tough and Hard Renegotiation

  Indonesia government is renegotiating all contracts (more than 110 contracts) with company to amend 5 strategic issues, including state revenue. As mandated in Coal and Mineral Law, the output of state revenue is the increasing of state revenue. Up until now, government has already amended 11 contracts to conform with Coal and Mineral Law.

- Low Price Mining Commodities

  Government plans to revise mineral and coal tariff to increase state revenue. However, with low price of commodities, especially coal, Indonesia holds revising mineral and coal tariff.

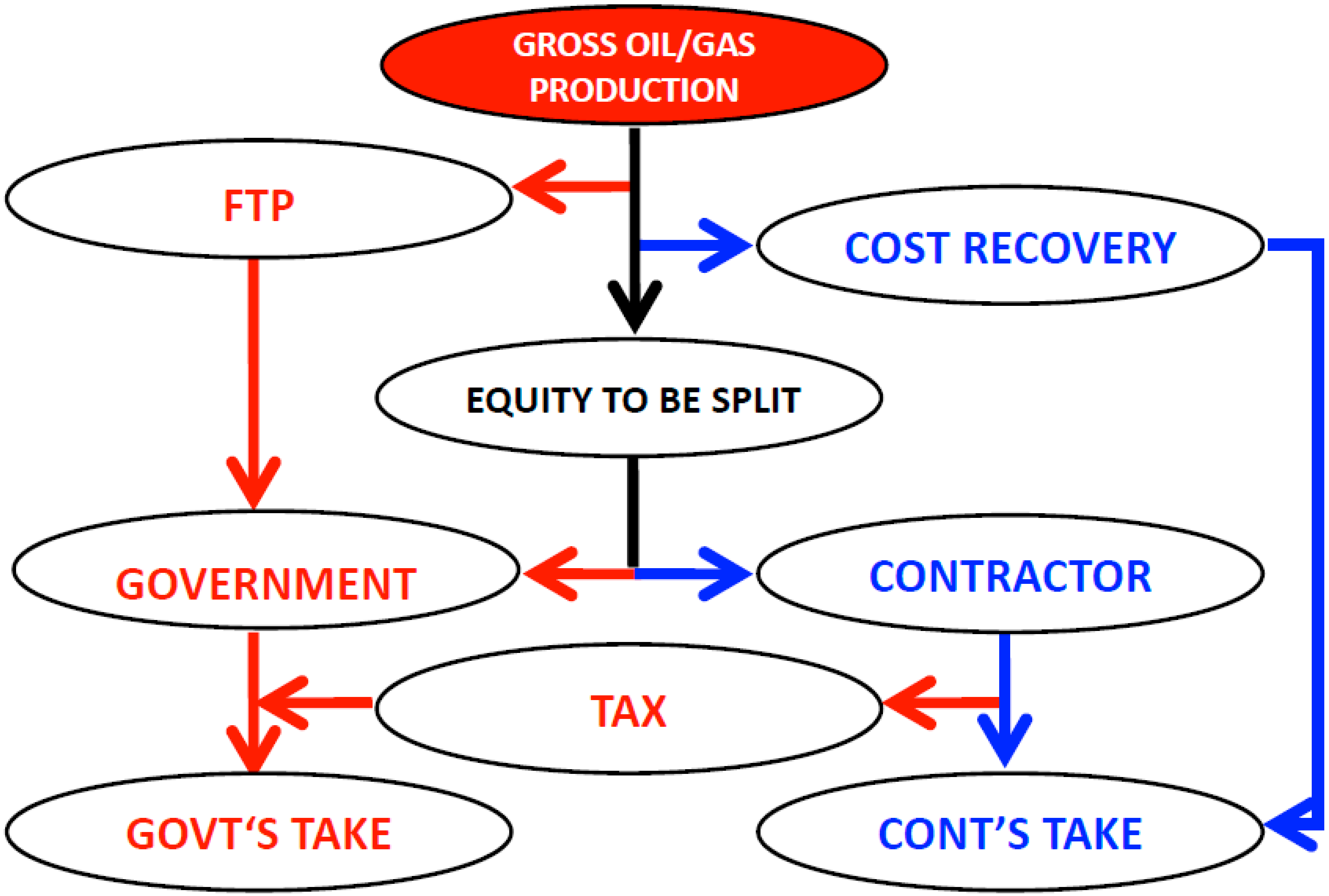
- Royalty Administration and Policy Governance

  Government is developing system to make mining royalty administration governance and transparant.

Petroleum: Fiscal Policy

- Taxation obligation for E&P oil and gas taxpayers are based on Production Sharing Contract (PSC) and tax legislation (Govt Regulation No 79/2010 and the derivatives)
- In principle, all the cost/investment incurred in Exploratioin & Production activities are recoverable by government (cost recovery).
- Based on PSC, production after cost recovery is splitted (equity to be split) between Government and Contractor based on particular percentage.
- In general, The government has the rule of thumb of equity to be split for oil and gas policy. However, the policy of equity to be split for oil and gas (after tax) is different between contractors depends on the economic value of the project itself.
- Contractor cannot reduced by any losses or other tax reliefs from other business activities (Ring Fencing Policy)

Petroleum: Production Sharing Contract Concept



Petroleum: Fiscal Incentives

Tax Income Incentives

- ❑ Relief of witholding income tax article 22 on import goods in relation to oil and gas upstream activities.
  Ref: Minister of Finance Regulation No 107/PMK.011/2015

Value Added Tax and Import Duty Incentives

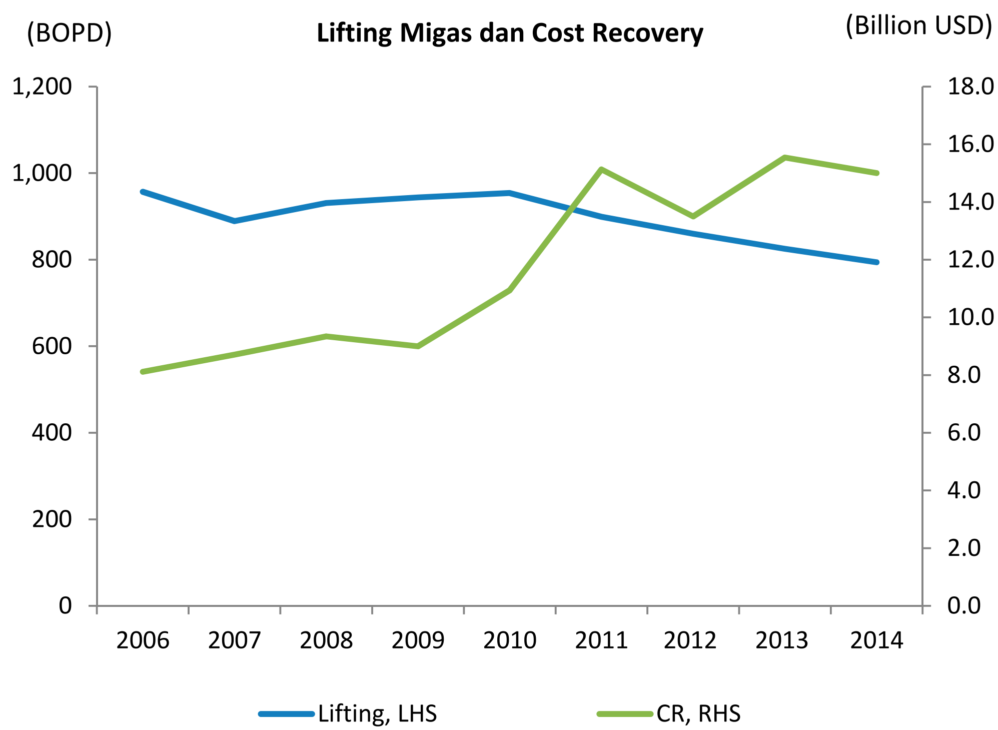
- ❑ Relief of Value Added Tax and Import Duty on import goods in relation to oil & gas upstream activities with some certain requirements.

  Ref: Minister of Finance Regulation No 70/PMK.011/2013 & 177/PMK.011/2007 and 176/2012

Land and Building Tax Incentives

- ❑ Contractor is exempted on Land and Building Tax just only on On exploration stage.

Recent Trend Of Cost Recovery and Oil Lifting



- Since 2006 to 2014, there is an increasing trend of cost recovery. In 2006, the realization of cost recovery is US$ 8,1 billion and increasing to US$ 15 billion in 2014.

- Conversely, there is a decreasing trend of oil lifting. In 2006, oil lifting is 957 barrel oil per day (bopd) and decreasing to 794 bopd.

Petroleum: Issues and Challenges

- The annual increase of recovery cost is inversely proportional with the decrease of oil and gas production

  Nowadays, public question the annual increase of recovery cost, but on the contrary, oil and gas production is declining. Public suspect that there were some mark up on the recovery cost. The Ministry of Finance is assessing any other alternatif to increase the production other than the recovery cost method.

Thank you