Workshop "Sharing on Transparency"
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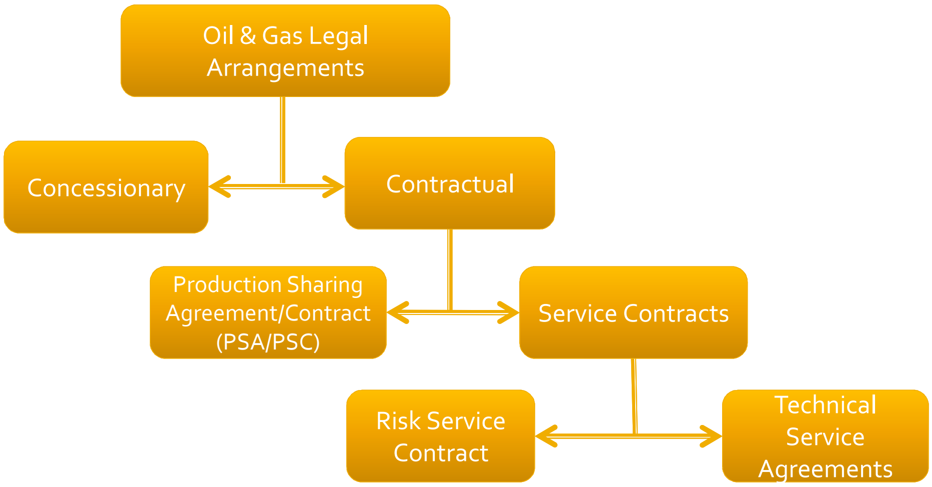
Hydrocarbon & Governance Challenges in Indonesia

FABBY TUMIWA
INSTITUTE FOR ESSENTIAL SERVICES REFORM
www.iesr.or.id

HYDROCARBON FISCAL REGIME IN INDONESIA

Hydrocarbon Legal Arrangements



Main Differences Concessionary & PSCs

Features	Concessionary	PSCs
Ownership of resources	Held by sovereign state	Held by sovereign state
Title transfer point	At the well head	At the export point
Company entitlement	Gross production less royalty	Cost oil & gas + profit oil & gas
Entitlement percentage	Typically 90%	Typically 50-60%
Ownership facilities	Held by the company	Held by the state
Management & control	Typically less government control	More direct government control and participation
Government participation	Less likely	More likely
Ring fencing	Less likely	More likely

PSC Characteristic

- Started in the 60s, in Indonesia
- Work commitment
- Bonus payment
- Royalties
- Recovery of production cost
- Profit oil split between company (contractor) and host country
- Overall share of host country depends on the bargaining
- Most of developing countries now prefer PSC

PSC Advantage & Disadvantage for Host Countries

ADVANTAGE

- All financial and operational risk rests with the company;
- Government shares potential profit without making a direct investment;
- PSA can be enacted into law to provide legal security.

DISADVANTAGE

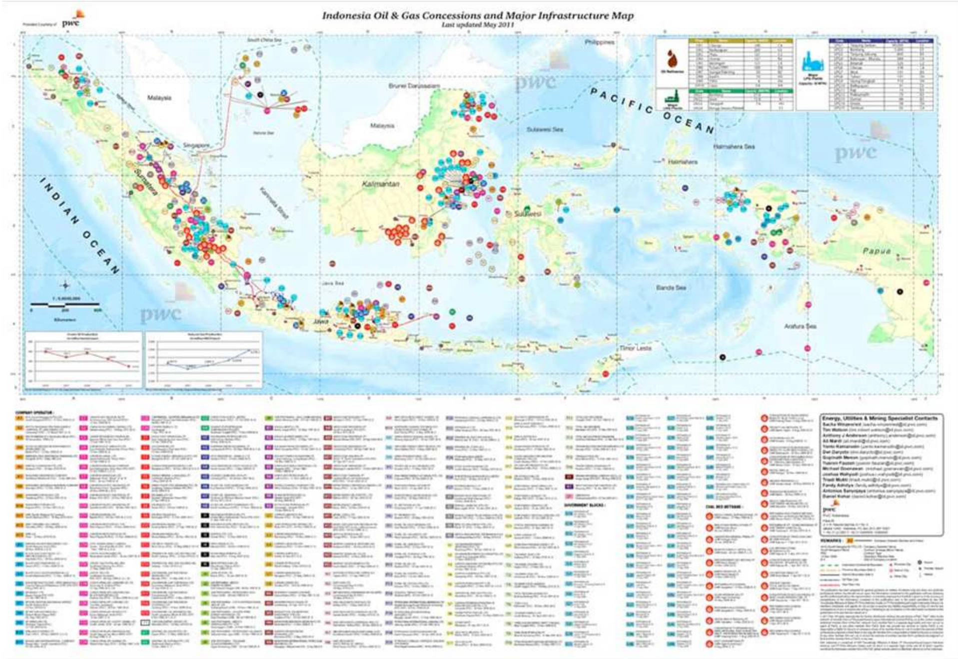
- Requires highly negotiation skills;
- Requires excellent data & information of the oil & gas reserves in the particular field;
- Requires high degree of supervision on cost of exploration, development and operation;
- Requires excellent regulatory management;
- Difficulty to enforce of social & environment standard, beyond the contract terms.

Indonesia Hydrocarbon Fiscal Regime

- Indonesia oil & gas applies Production Sharing Contract (PSC) regime:
  - Contractor is working on specific Working Area (or Block).
  - Contractor is responsible to all risk.
  - Exploration, development and operation costs are held by the contractor and will be recovered by the government from the commercial production.
  - Production minus cost recovery will be split between government and contractor based on certain percentage.

Indonesia Hydrocarbon Fiscal Regime

- Working Area or block given to the contractor is ring fence.
- Contractor must pays taxes (e.g. Income tax).
- All equipments of the contractor are owned by government.
- Contract period is 30 years, including 6 to 10 years for exploration, and can be extended.
- Contractor must supply petroleum & gas for Domestic Market Obligation (25% of contractor's share).



Indonesia PSC Fiscal Terms

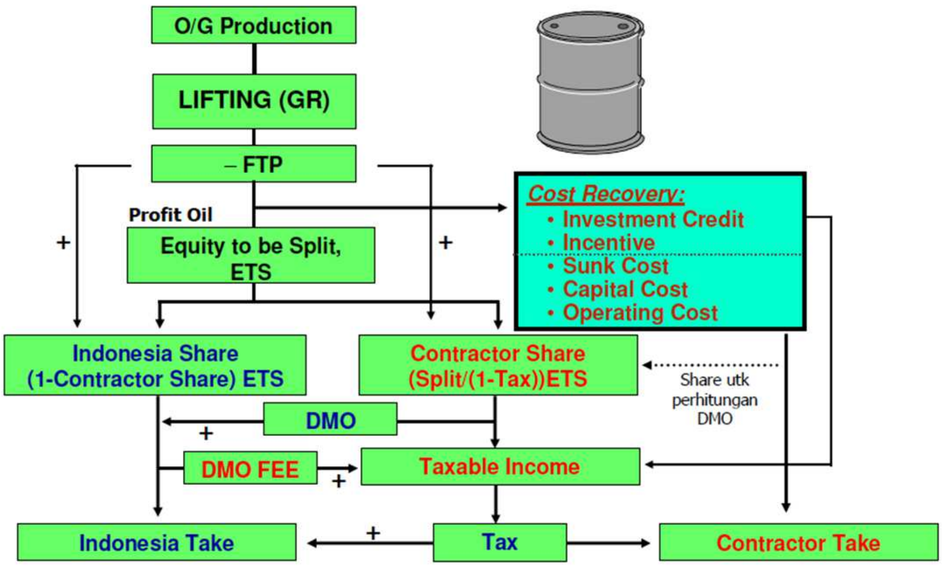
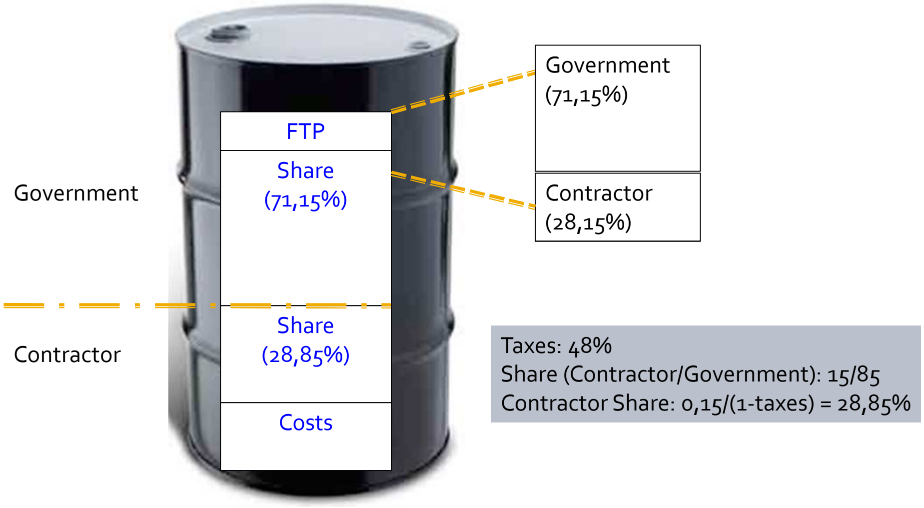


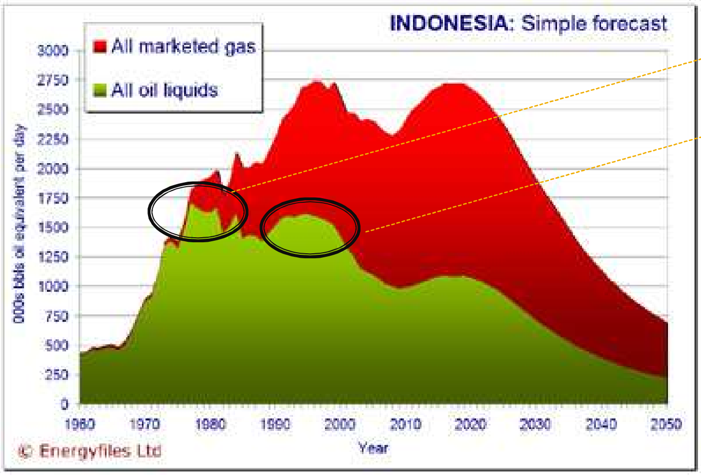
Illustration of Sharing under PSC



Oil & Gas Revenue Sharing in Indonesia

- Total revenues from O&G is about $ 30 bn annually
- Revenue sharing of Central Government and Local Government where oil and gas produced:
  - Typical: 15.5% for petroleum and 30,5% for natural gas
  - Special Region of Aceh Province: 70% for Aceh, and 30% for Central Government

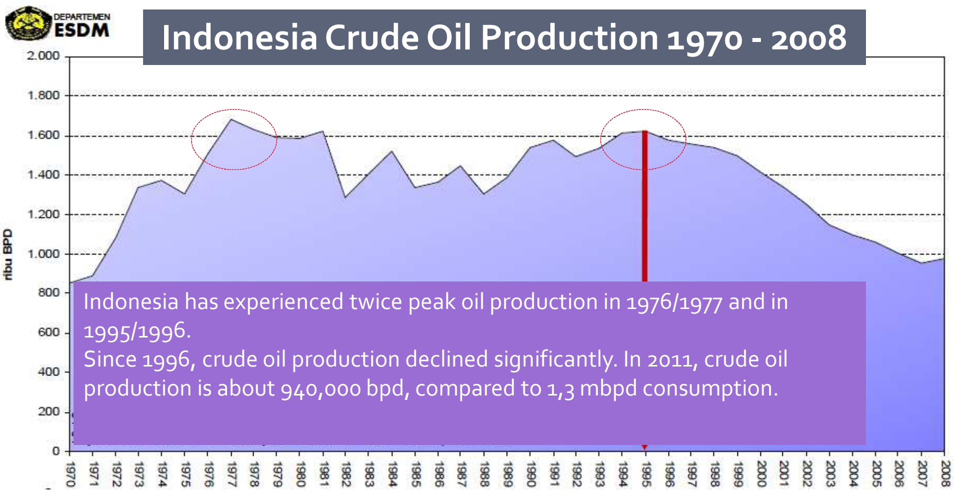
Realization and Prediction of Production of Indonesia Oil & Gas 1960 – 2050 (2008)



Peak oil production 1

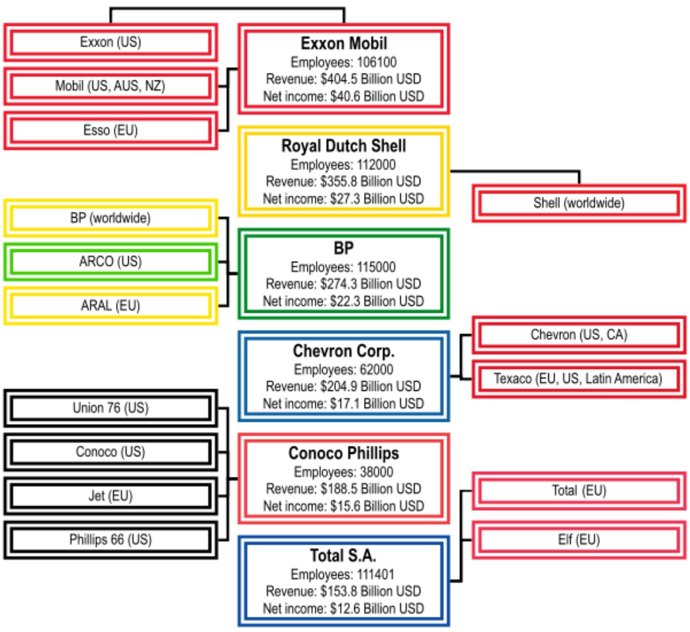
Peak oil production 2

Indonesia Crude Oil Production 1970 - 2008



Indonesia has experienced twice peak oil production in 1976/1977 and in 1995/1996.
Since 1996, crude oil production declined significantly. In 2011, crude oil production is about 940,000 bpd, compared to 1,3 mbpd consumption.

EITI


Exxon (US)
Mobil (US, AUS, NZ)
Esso (EU)
Exxon Mobil
Employees: 106100
Revenue: $404.5 Billion USD
Net income: $40.6 Billion USD
Royal Dutch Shell
Employees: 112000
Revenue: $355.8 Billion USD
Net income: $27.3 Billion USD
Shell (worldwide)
BP (worldwide)
ARCO (US)
ARAL (EU)
BP
Employees: 115000
Revenue: $274.3 Billion USD
Net income: $22.3 Billion USD
Chevron (US, CA)
Texaco (EU, US, Latin America)
Chevron Corp.
Employees: 62000
Revenue: $204.9 Billion USD
Net income: $17.1 Billion USD
Union 76 (US)
Conoco (US)
Jet (EU)
Phillips 66 (US)
Conoco Phillips
Employees: 38000
Revenue: $188.5 Billion USD
Net income: $15.6 Billion USD
Total (EU)
Elf (EU)
Total S.A.
Employees: 111401
Revenue: $153.8 Billion USD
Net income: $12.6 Billion USD

List of ASEAN countries GDP (nominal), CIA World Factbook 2008 estimates

Rank	Country	GDP (millions of USD)
—	***World***	**78,360,000**
—	*European Union*	18,930,000
—	*United States*	14,330,000
—	*ASEAN*	1,486,467
1	Indonesia	496,800
2	Thailand	272,100
3	Malaysia	214,700
4	Singapore	192,800
5	Philippines	186,000
6	Vietnam	90,880
7	Brunei	17,180
8	Myanmar	13,700
9	Cambodia	10,820
10	Laos	5,187

The Big Six: Revenues vs GDP (2008)

OIL AND GAS COMPANIES:

- Exxon: $404,5 billion
- RD Shell: $355,8 Billion
- BP: 274,3 Billion
- Chevron: $204,9 billion
- Conoco Phillips: $188,5 billion
- Total SA: $153,8 billion

ASEAN COUNTRIES:

- Indonesia: $496,8 Million
- Thailand: $272,1 million
- Malaysia: $214,7 million
- Singapore: $ 192,8 million
- Philippine: $186 million
- Vietnam: $90,880 million
- Brunei: $17,180 million
- Myanmar: $13,700 million
- Cambodia: $10,820 million
- Laos: $5,187 million

Global Norms and Standards of EI

- Required companies to report payment to host government:
  - USA's Dodd – Frank Act (Cardin – Lugar provision)
  - EU transparency legislation
- Guidelines for Companies
  - OECD Guidelines for Multinational Enterprises
  - UN Global Compact
- Human Rights Standard
  - Voluntary Principle on Security and Human Rights
  - UN's Guiding Principles on Business and Human Rights
- Environmental & Social Standard:
  - IFC's Policy and Performance Standard on Social and Environmental Sustainability
- Financial Transparency
  - Equator Principles
- Revenue Collection:
  - Extractive Industries Transparency Initiative (EITI)
- Public Revenue & Expenditure Transparency
  - IMF's Code of Good Practice on Fiscal Transparency
  - World Bank's Public Expenditure and Financial Accountability (PEFA)

Extractive Industries Transparency Initiative (EITI)

- Established in 2003;
- The EITI is a global standard, a voluntary, multi-stakeholder initiative intended to promote accountability and good governance in resource-rich states through the generation and publication of credible data on payments made by EI sector companies to host state governments;
- By 2012: 14 compliant countries, 22 candidate countries, 123 reports.

Extractive Industries Transparency Initiative

EITI Criteria in Brief

- Prudent use of natural resource wealth as an engine for sustainable economic growth
- Effective management of resource wealth by sovereign governments;
- Regular, easily accessible publication of payments made and revenues received;
- Recognition of the fluctuation of benefits of resource revenue streams due to price volatility and the need to governments to manage such;
- Transparency of government and corporate financial management and accounting of EI revenues, including credible audit of payments and revenues;
- Accountability of the government to all citizens for resource revenue management;
- Disclosure of all EI payments to a host country; Greater transparency in the context of both contracts and laws;
- Engagement of civil society and all stakeholders in seeking solutions to problems stemming from EI sector projects;
- For a complete principle and criteria go to: http://eiti.org/eiti/principles

Implementation of EITI looks like this

- Host country publicly signs up to EITI.
- National Multi-stakeholder Implementation Group (MSWG) is formed.
- Time-bound work plan is drawn up by MSWG.
- MSWG determines sector & boundaries for EITI reporting and templates developed based on that.
- Reporting-reconciliation process is executed.
- Results made public, supported by a communications program.
- Process begins again.
- Implementing country undergoes validation every two years.

Extractive firms in Indonesia that support EITI

Oil and gas: BP, ChevronTexaco, ConocoPhilips, Eni, ExxonMobil, Hess, Marathon, Santos, Shell, StatoilHydro, Talisman, Total, Woodside.

Minerals and coal: BHP Billiton, Eramet, Freeport, INCO, Newmont, OZ Minerals, Rio Tinto, Sumitomo

However, **all** firms within an implementing country, not just those which support EITI as a matter of corporate policy, must report.

Indonesia AND EITI (1)

- EITI process firstly initiated in 2006, but preparation started in 2008, formal interest in EITI submitted in 2009
- First in the South East Asia
- Why did Indonesia decided to implement EITI?
  - The raise of decentralization in Indonesia context
  - Local governments demand central government to be transparent on revenue sharing mechanism
  - The need to increase investment in oil and gas sector
  - Improving overall investment climate
- Indonesia kicked of the process to implement EITI in 2010

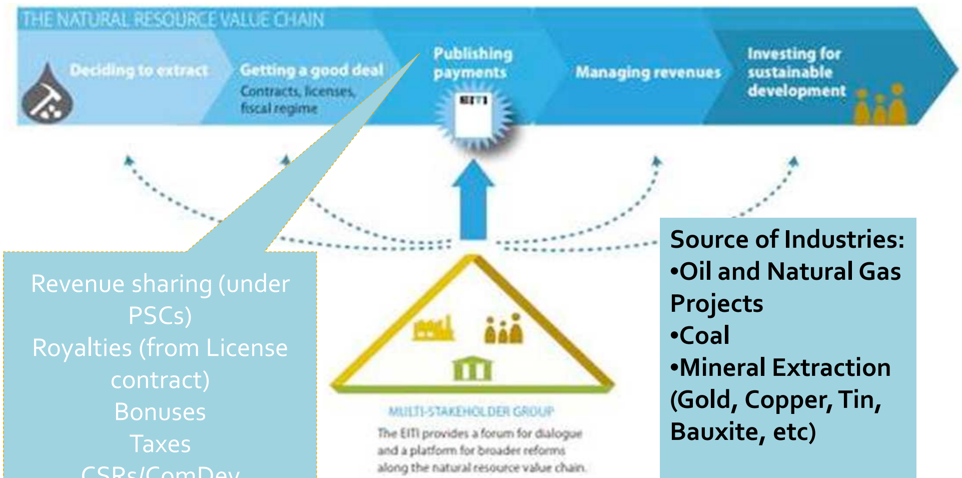
Indonesia AND EITI (2)

- EITI implementation in Indonesia is required by Presidential Regulation, enacted in 2010
- EITI secretariat and implementation team is hosted by Coordinating Ministry of Economics Affairs
- Stakeholders: Central Government's Ministries and Agencies, Local Governments, Companies and Civil Society.
- Sector covered: oil, natural gas, and mineral industries
- Revenues Reporting: project by project basis
- First report due to late 2012/early 2013, based on 2009 audited report

INDONESIA EITI Extractive Industries Transparency Initiative

Kementrian Koordinator Bidang Perekonomian Republik Indonesia

EITI Implementation



Revenue sharing (under PSCs)
Royalties (from License contract)
Bonuses
Taxes
CSRs/ComDev
Etc

Source of Industries:
•Oil and Natural Gas Projects
•Coal
•Mineral Extraction (Gold, Copper, Tin, Bauxite, etc)

EITI Process (1)

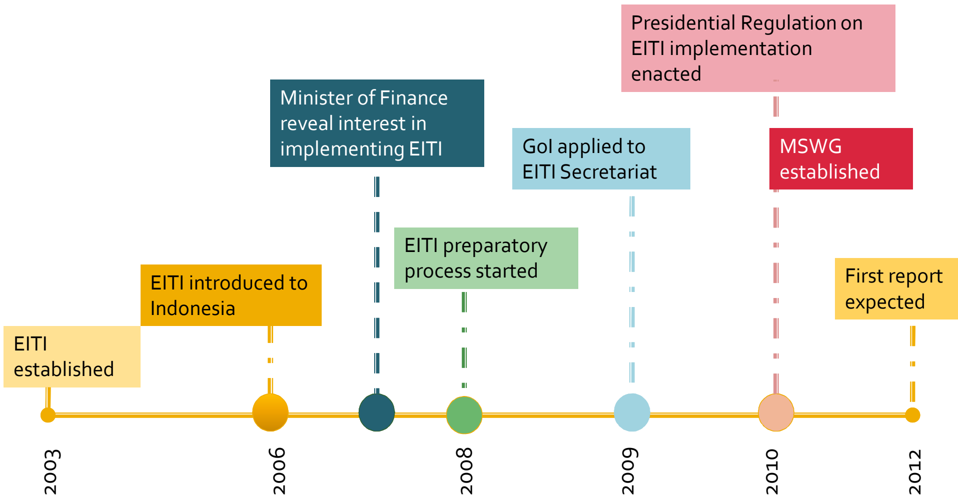
EITI Process (2)

Association of O&G association
Association of Mineral companies
SOE on O&G

Publish What You Pay Indonesia – a coalition of more than 30 NGOs

Ministries and Government Agencies, Local government

Milestone EITI Implementation in Indonesia



GoI: Government of Indonesia MSWG: Multi-Stakeholder Working Group

EITI Limitation and Opportunity (1)

- EITI might prevent corruption but does not necessary effective in addressing corruption in the entire extractive industries' value chain.
  - ....however it helps to detect corruption practices and serve as evaluation tool to improve entire EI governance (transparency, accountability, public participation) along the value chain.
  - EITI report can be excellent source of information to be used by civil society to advocate broader transparency and accountability.
  - Other standard/norms/framework is required to strengthen effectiveness of EITI.
- Required genuine participation of three parties for an effective and sustained result
  - Government must open to engage with CSOs & Companies
  - Strong civil society institutions is a must

EITI Limitation and Opportunity (2)

- Effectiveness of EITI as transparency and accountability tool determine by several infrastructure & material:
  - Data and information of oil, gas, and mineral productions
  - Availability of Extractive Industries contract
  - Clear and transparent revenue flows in the country (companies payment to the government)
  - Government (central and local/state) revenue and expenditure reporting mechanism
  - Government accounting standard and budget transparency
  - Public Accounting Rules and Stock Exchange Regulation
  - Etc……………………
- Effective EITI should be supported by the capacity of Government to manage revenues, and plan the development to ensure the resource rich country to escape from resource curse.

Fabby Tumiwa, Email: fabby@iesr.or.id
www.iesr.or.id
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