

Battle Over Huge Coal Deposit Highlights Risks in Indonesia

Michael Taylor | October 10, 2011 | Reuters

Indonesia contains some of the world's richest mineral deposits, located tantalizingly close to the markets of China and India, but a court battle over a \$1.8 billion coal mine highlights the risks foreign miners face in the country.

London-listed Churchill Mining Plc has been in dispute with Indonesia's Nusantara Group for three years over the right to develop the world's seventh-largest undeveloped coal asset.

The case has reached Indonesia's highest court and could take years more to settle. The 350-sq-km mine site in East Kutai, a coastal district in East Kalimantan province, is said to contain 2.8 billion tons of coal reserves.

"It's a big medium to low-grade thermal coal deposit," Churchill Executive Chairman David Quinlivan told Reuters in a telephone interview.

"That requires a substantial amount of infrastructure to be able to bring it into production.

"But once in production, it will be very much a long-term project -- 50 years or more."

Nusantara Group originally held six licences in the disputed area. According to court documents filed by Churchill, these lapsed between March 2006 and March 2007.

The East Kutai government declared the area open to other companies and Indonesian firm PT Ridlatama received four mining licences, Churchill said.

Between November 2007 and February 2008, Churchill bought a 75 percent stake in Ridlatama's licences and spent about \$40 million on the project.

But after Churchill announced in May 2008 that the project could yield substantial coal, things turned messy.

A few weeks later, the East Kutai regional government granted extensions to the Nusantara Group mining licences that Churchill believed had lapsed.

The undeveloped and potentially highly lucrative coal mine has since become the subject of a series of legal tussles.

But after a March 2011 tribunal ruling in Indonesia, Churchill and minority partner Ridlatama no longer own the East Kutai project.

Churchill filed an appeal on Sept. 26 in Indonesia's Supreme Court. It is unclear how long the court's verdict will take.

"At least months and it can be years," said Rozik Soetjipto, an Indonesia mining consultant on supreme court judgments. "About one or two years, maybe longer if something is very exceptional, but generally less than two years."

Officials at Nusantara were unavailable for comment despite repeated telephone calls and e-mails.

"I'm disappointed more than anything else -- that it had to get to this to try and maintain title," Quinlivan said, adding that Churchill may seek international arbitration.

"The legal process doesn't end in Indonesia."

According to Churchill, Nusantara Group is controlled by former Indonesian Army General Prabowo Subianto.

Prabowo was a former head of the Kopassus special forces and was once married to one of former strongman President Suharto's daughters.

He is the son of a former Indonesian finance minister and data from Indonesia's anti-graft agency shows he had an estimated personal wealth of about \$160 million as of 2009.

The legal tussle between Nusantara and Churchill also highlights the complex bureaucracy of the sprawling country of 17,000 islands.

"If you are going to be on the wrong side of a land acquisition that is in dispute, if it gets blown up in the press, then you will end up with the perception that regulatory risk is getting worse," said Andreas Bokkenheuser, an analyst at UBS.

"But if you look beyond assets in dispute, I actually see the regulatory risk improving in Indonesia."

The government is drafting a rule that would, by 2014, require miners to carry out minimum processing on minerals before export -- part of a mining and coal law introduced in 2009 aimed at making life easier for investors.

Despite these changes, one Indonesia-based analyst estimated there are currently about 100 unresolved disputes involving mine ownership or licences.

"They are trying to clean up the sector," Bokkenheuser said.

"We're seeing enforcement of the law, which is positive ... There is still a concerted effort to make the mining environment more attractive for foreigners to come in and invest."

Indonesia's coal export growth will be fuelled in large part by China and India, where power demand is expected to lift coal imports significantly over the next five years.

Output will hit 340-354 million tonnes for 2011, industry groups say.

The government has also tabled a new land bill to speed up land acquisition, but it may not be effective until 2012 and companies still face risks.

"Number one, don't underestimate the legal due diligence," said Bokkenheuser, referring to foreign miners looking to invest in Indonesia. "Use a combination of Indonesian and foreign guys to do so because you will need local help on that issue.

"Point number two ... you need to make it clear what kind of land you have got -- because land is another regulatory issue -- we still don't have a land reform (bill) in Indonesia that empowers the government to buy land."

For Churchill, the advice may be too late.

"My advice would be, be wary and make sure you've done extensive -- and I mean extensive -- due diligence," Quinlivan said. "Even though, whilst you may have done all this due diligence, and we certainly believe we had, things can turn around that are very unexpected."

"If there is a loophole there, somebody will use it."

(Reporting by Michael Taylor; Editing by Jason Szep and Raju Gopalakrishnan)

Source: <http://www.reuters.com/article/2011/10/10/us-indonesia-coal-churchill-idUSTRE79912J20111010>