The obligation to use national sea transportation company for coal exports

Data from the Indonesian Ship Owners Association reveals that Indonesia’s current export and import shipment has been dominated by foreign Sea Transports, which accounted for 93.7% of the total shipment activities. Responding to such foreign Sea Transports domination within Indonesia’s sea territory, Minister of Trade Regulation No. 82 of 2017 (“Reg. 82”) – which will take effect at the end of April 2018 – was issued to give Indonesian Sea Transport Companies and insurance companies the spotlight.

Since Reg.82 issuance in October 2017, various stakeholders on coal export have voiced their concerns on the readiness of implementation of Reg.82, especially with respect to the availability of Indonesian flagged vessels and detailed implementing procedures that are still missing from Reg. 82. These concerns will be the focus of this article as we explore the issues of Reg. 82 on the export of coal in more details.

Is it correct that Reg.82 prohibits the use of foreign flagged vessels for exporting coal and/or CPO?

Many exporters (in particular, coal exporters) question the effective implementation of Reg. 82 due to the lack of availability of Indonesian flagged vessels. While we can understand their concern, we believe that Reg.82 does not necessarily prohibit the use of foreign flagged vessels for exporting coal.

Article 3 paragraph 1 of Reg.82 states, “Exporters exporting coal and/or CPO shall use Sea Transport which is controlled by Indonesian Sea Transportation Company” for their transportation activity”. Taken at face value, the article seems to suggest that the use of Indonesian flagged vessels is absolute in exporting coal given the all-encompassing language of the article. However, if we refer to the definition of Sea Transportation as stipulated under Law No. 17 of 2008 on Shipping (“Shipping Law”), it does not strictly correspond to the nationality of the vessel being used for the transportation.

Under the Shipping Law, Sea Transportation activities are divided into four activities, which include among other things: (i) domestic Sea Transportation activities; and (ii) international Sea Transportation activities. Highlighting the differences between domestic Sea Transportation activities and international Sea Transportation activities in terms of requirements to use Indonesian flagged vessels will be the key in understanding and interpreting the provisions of Reg. 82.

In essence, domestic Sea Transport activities are subject to the cabotage principle and therefore the use of Indonesian flagged vessel is mandatory. However, the Shipping Law allows international Sea Transport activities - which include export and import activities - to use both Indonesian and/or foreign flagged vessels. The graphic below illustrates the requirements under

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2. The draft Reg.82 is also mentioned in the Economic Policy Package XV as one of four economic policy packages in the ministry level.
3. For example, “Indonesia Palm Oil Association (GAPKI) Secretary-General Togar Sitanggang said in an interview on Jan. 24 that there were several problems with the new rules, noting there were not enough Indonesian-flagged food-grade tankers, and that Indonesian insurers may lack capacity.” Munthe, Bernadette C. (2018, February). Coal buyers spooked by Indonesia’s new shipping rules: https://www.reuters.com/article/us-indonesia-shipping-cabotage/coal-buyers-spooked-by-indonesians-new-
   shipping-rules-assoc-idUSKBN1FS192
4. Based on Reg. 82, an Indonesian Sea Transportation Company means a Sea Transportation Company having Indonesian legal entity status which conducts Sea Transportation activities within the territorial waters of Indonesia and/or from and to foreign seaport.
5. Article 7 as explained under Article 8 and Article 11 of the Shipping Law states that, (i) domestic Sea Transportation activity means, any Sea Transportation activity which is conducted within Indonesian territories by an Indonesian Sea Transportation Company using an Indonesian flagged vessel and manned by Indonesian crew members, (ii) international Sea Transportation activity means, any sea transportation activity which is conducted from and out of Indonesian territories by an Indonesian Sea Transportation Company and/or foreign Sea Transportation Company using an Indonesian and/or foreign flagged vessel.
6. For example, Article 2 of the Joint Regulation between Minister of Trade and Minister of Transportation No. KM 19/2006 (the “Joint Regulation”), states “Transportation of Government’s import goods whose procurement is carried out by an importer must use Indonesian flagged vessel under the control of an Indonesian Sea Transportation Company”. Another example, Article 8 of the Shipping Law, states “domestic Sea Transportation activity means, any Sea Transportation activity which is conducted within Indonesian territories by an Indonesian Sea Transportation Company with using an Indonesian flagged vessel and manned by Indonesian crew members”.

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Based on our discussion with the officials at the Ministry of Trade, the officials also shared the same view that Reg. 82 should not be interpreted to limit the use of foreign flagged vessels. Their concern is more on who owns the vessels, which should be Indonesian Sea Transportation Companies. Indeed, if the Indonesian government truly intends to impose the mandatory use of Indonesian flagged vessels for export and import activities, in line with the basic principle of legal certainty and consistent with other regulations which cover this subject\(^5\), Reg 82 should explicitly state such obligation.

Since Reg.82 does not explicitly require the use of Indonesian flagged vessels for export of coals, arguably coal exporters may still use foreign flagged vessels to the extent those vessels are controlled by an Indonesian Sea Transportation Company. While we think that the above should be the correct interpretation of Reg. 82 provisions, we do note that different officials at the Ministry of Industry or relevant officials at the relevant ports might take a different view. To avoid this possible confusion on the nationality of the vessels, we do think it is crucial for a technical guidance by the related ministry to be issued promptly and provide clarification on this issue.

Will Reg. 82 limit offshore buyer to only use vessels controlled by Indonesian Sea Transportation Companies?

The obligations in Article 3 of Reg. 82 are imposed to exporters and importers in Indonesia. This begs a question whether the requirement to use the vessels owned by Indonesian Sea Transportation Company can be extended to buyers abroad or offshore buyers, which may have their own legal requirements in carrying out import and export activities in their relevant countries.

From legal perspective, Reg. 82 should not be interpreted to restrict offshore buyers from using other vessels, including those that are not owned by Indonesian Sea Transportation Companies. Some arguments that support this notion are:

1. Applicability of Reg. 82 (as also any other regulations issued by Indonesian government) will always be limited by the jurisdiction where it is issued, which is the Indonesian territory. Thus, Reg. 82 cannot bind coal buyers located abroad.

2. Based on the Shipping Law, Government Regulation No. 29 of 2017 (“GR 29/2017”) and Incoterms 2010, any export activities in Indonesia may
use several methods of delivery, among other things: Cost, Insurance and Freight (“CIF”) and Freight on Board (“FOB”). The table below shows terms of delivery under GR 29/2017 and Incoterms 2010:

The obligations to arrange sea transportation and insurance companies in international trade such as coal trading will ultimately depend on the agreed terms of delivery. In FOB term for example, the exporter or seller does not have the right to choose the vessels and insurance as it is only required to deliver the cargo up to the exporter’s port. While in CIF term, the exporter has the obligation to choose the vessels and insurance used to deliver the cargo up to the port of the buyer abroad.

This means that under certain types of method of delivery, such as FOB, offshore buyers have the right to choose their own sea transport and insurance being used for their import activities, and in such case, it is highly unlikely that the provision of Reg. 82 can be applied toward such offshore buyers.

3. In addition, as mentioned above, principally under the Shipping Law, which is a regulation having a higher hierarchy compared to Reg. 82, any international Sea Transport activity may use foreign Sea Transportation Companies and foreign flagged vessels.

**Procedures for exemption on non-availability of vessels**

Article 5 of Reg. 82 grants several exemptions towards the obligations to use Indonesian Sea Transportation Companies in export activities. These exemptions do apply in cases where the number of Indonesian Sea Transportation Companies are limited in availability or completely unavailable. The method to demonstrate such limited availability or unavailability, however, is not discussed in Reg. 82.

Given the silence of Reg. 82, the method stipulated in Ministry of Transportation Regulation No. 100 of 2016 as amended by Ministry of
Cost, Insurance and Freight (CIF)
- means the supplier will arrange for the insurance and delivery of the products to the agreed destination port.
- Supplier will not be liable for any damages incurred as soon as the products are put on board the ship.
- The seller covers the costs of duty unpaid, freight and insurance to the destination port.
- As soon as the goods are placed on the ship then the risk is transferred to the buyer.

Free on Board (FOB)
- FOB means that the seller’s responsibility for the products stops as soon as they are safely loaded onto the ship.
- The sellers will have prepared the customs clearance documents to goods through their domestic requirements.
- The seller goods on goods are transferred is responsible for delivering the board the ship. As soon as the placed on the ship then risk is transferred to the buyer.

Free Alongside Ship (FAS)
- FAS requires a little more effort from the seller to arrange for the goods to arrive at the origin port but the main burden of delivery, costs and insurance will fall on the buyer.
- The seller is responsible for delivering the goods to the designated origin port. Once the goods are alongside the ship then the risk is transferred to the buyer.

Conclusion
The Government intention to enhance the growth of Indonesian Sea Transportation companies and insurance companies through Reg. 82 is a commendable one. To ensure that the implementation of this regulation can be done smoothly, there are certain issues that must still be clarified and improved, including clarification on the use of vessels (namely, that the focus is on the owner of the vessels instead of the vessels’ flag), and the procedures for applying for exemption should it become necessary in the future. We sincerely hope that the Indonesian government can settle these issues before Reg. 82 effective implementation in April 2018.

Authors:
1. Kirana D. Sastrawijaya (Senior Partner of UMBRA – Strategic Legal Solutions)
2. Reggy Firmansyah (Senior Partner of UMBRA – Strategic Legal Solutions)
3. Anaq Pratama (Associate of UMBRA – Strategic Legal Solutions)

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Transportation Regulation No. 115 of 2017 on Guidelines and Conditions for the Issuance of Foreign Vessel Utilization License for other Activities that are not Included as Domestic Transportation for Goods and Passengers ("Reg.100") might be considered as a starting point with further necessary adjustments. Under Reg. 100, in order to obtain the foreign vessels utilization license, the relevant Indonesian Sea Transportation Company is required to demonstrate that it has carried out sufficient procurement efforts to use Indonesian flagged vessels, namely, by showing the procurement announcement. We do understand that in practice, exporters do not normally procure the vessels and apply for the foreign vessel utilization license. Moreover, Reg.100’s scope is for domestic Sea Transportation, while export of coal does not fall under this category (i.e. they belong to International Sea Transport activities). The burden in this case falls to the Indonesian Sea Transportation Company hired by the exporters as they are the ones to procure the vessels that are required by the exporters. Accordingly, further implementing procedures for Article 5 of Reg. 82 is also another pending homework of the Indonesian government to be resolved as soon as possible.

Cost and Freight (CFR)
- means that the supplier will pay the freight costs to get the product to the destination port.
- Similar to FOB, the supplier is no longer liable for any risks or damages as soon as the products have been placed on the ship.
- The seller covers the costs of duty and freight to the destination port. As soon as the goods are placed on the ship then risk is transferred to the buyer.

Free Alongside Ship (FAS)
- FAS requires a little more effort from the seller to arrange for the goods to arrive at the origin port but the main burden of delivery, costs and insurance will fall on the buyer.
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