

NEWSLETTER

6 August 2024

REFORMS ON LOCAL CONTENT GOVERNANCE FOR INDONESIA POWER PROJECTS

Following the longstanding dilemma of balancing the utilization of domestic goods and services in Indonesia with the need to attract foreign investment for infrastructure development, especially for the development of power projects, the Government of Indonesia issued series of regulations related to local content, which reform the governance of local content requirements for power projects development in Indonesia, namely:

1. On 25 July 2024, the Minister of Industry (**MoI**) issued MoI Regulation No. 33 of 2024 (**MoI Reg 33/2024**) which revoked the regulation that previously governed local content threshold (Tingkat Komponen Dalam Negeri) for power projects - MoI Regulation No. 54/M-IND/PER/3/2012 of 2012 on the Guidelines for the Utilization of Domestic Products in the Development of Electricity Infrastructure, as amended several times lastly by MoI Regulation No. 23/M-IND/PER/7/2023 (**MoI Reg 54/2012**). On the same day, however, the MoI issued MoI Regulation No. 34 of 2024 on the Procedures for Calculation of the Value of Domestic Components of Solar Module Products (**MoI Reg 34/2024**).
2. Shortly thereafter, on 30 July 2024, the Minister of Energy and Mineral Resources (**MEMR**) issued MEMR Regulation No. 11 of 2024 on the Use of Domestic Products in the Development of Electrical Infrastructure (**MEMR Reg 11/2024**).

Regardless of different issuance dates, all those three new regulations only came into effect on 31 July 2024.

What are the implications of these series of regulations to local content requirements for power projects development in Indonesia?



Kirana D. Sastrawijaya

Head of Power and Renewable Division

+62 819 3246 4089

(kirana@umbra.law)

Zuhal Dwi Saputra

Senior Associate

(zuhal@umbra.law)

Risca Piscensia Haryanto

Associate

(risca@umbra.law)

Indriyane Vera Natalia

Associate

(indri@umbra.law)

Nabila Ariesanti Cahyarani

Associate

(nabilac@umbra.law)

UMBRA – Strategic Legal Solutions

Telkom Landmark Tower, 49th Floor

The Telkom Hub

Jl. Gatot Subroto Kav. 52

Jakarta 12710 – Indonesia

(+62) 21 5082 0999



UMBRA - Strategic Legal Solutions



www.umbra.law

Our Services:

Mergers & Acquisitions | Capital Market & Securities | Private Equity | Compliance, Governance & Risk Management | Banking & Financial Institutions | Fintech | Corporate & Project Finance | Restructuring & Distressed Assets Management | Power | Infrastructure | Mining & Metals | Oil & Gas | Property & Real Estate | Joint Ventures & Foreign Direct Investment | Telecommunications, Media & Technology (TMT) | State-Owned Enterprises | Employment

Introduction

For years, reports indicate that financing for renewable energy projects has faced inhibition due to issues related to the local content threshold, as the domestic market is skeptical about meeting these requirements.¹ In response, an idea emerged from the government to harmonize regulations amongst ministries in the spirit of reforming local content threshold provisions in the energy sector.² Previously, the local content threshold for power infrastructure was governed by the MoI through MoI Reg 54/2012 and its other related regulations.

These series of revocations and issuances of regulations mark the strengthened commitment of Indonesian governments in addressing the longstanding local content issues for power projects development in Indonesia.

Key Provisions

Local Content Threshold for Power Projects is Now Governed by MEMR instead of MoI

The regulation related to the local content threshold for power projects was initially governed by the MoI through MoI Reg 54/2012. Under MoI Reg 54/2012, any development of electricity infrastructure for the public interest must use domestically produced goods and/or services. Since the enactment of MoI Reg 54/2012, MoI has issued several additional regulations, including those related to the calculation of local content under MoI Regulation No. 04/M-IND/PER/2/2017 on the Provisions and Procedures for Assessing Local Content Levels for Solar Power Plants (MoI Reg 4/2017).

¹ CNBC Indonesia, "TKDN Jadi 'Bottleneck' Investasi Energi Terbarukan, Ini Kata ESDM", accessed on 4 August 2024, <https://www.cnbcindonesia.com/news/20240529121319-4-542078/tkdn-jadi-bottleneck-investasi-energi-terbarukan-ini-kata-esdm>.

² Bisnis.com, "Pinjaman Proyek EBT Seret, Menteri ESDM Akan Terbitkan Aturan Anyar soal TKDN", accessed on 4 August 2024, <https://ekonomi.bisnis.com/read/20240718/44/1783448/pinjaman-proyek-ebt-seret-menteri-esdm-akan-terbitkan-aturan-anyar-soal-tkdn>.

However, the MoI's involvement in regulating local content for power projects led to confusion as the authority for regulating and issuing permits for power projects generally falls under the MEMR. For instance, MoI Reg 54/2012 included provisions on administrative sanctions and financial penalties if the local content threshold was lower than required by the MoI regulations. However, there was uncertainty about how these sanctions would be applied and which government agency was responsible for the enforcement.

It was not until 2023 that MEMR issued MEMR Regulation No. 6 of 2023 on Procedure for Imposition, Calculation, and Payment and/or Deposit of Non-Tax State Revenues at the Directorate General of Electricity (**MEMR Reg 6/2023**). This regulation, among other things, addresses penalties for non-compliance with local content threshold obligations, giving an implied message to the market that the local content is intended to be governed by the MEMR instead of the MoI.

Subsequently, on 13 May 2024, the MoI circulated a plan to revoke MoI Reg 54/2012 quoting, among others, that the revocation is needed as the substance of MoI Reg 54/2012 concerns the development of electricity infrastructure, which falls under the authority of the MEMR instead of MoI.

Finally, the issuance of MEMR Reg 11/2024 further solidifies MEMR's authority as the institution responsible for regulating local content thresholds for power projects.

Under MEMR Reg 11/2024, although each individual local content for goods and individual local content for services in the industry scope will be governed by industrial regulations, MEMR Reg 11/2024 stipulates that the minimum local content requirements of combined goods and services for power projects will be determined by MEMR and will be periodically evaluated by MEMR every three years, or at any time, if needed.

However, as the local content threshold under MoI Reg 54/2012 has been revoked, the MEMR must issue the local content threshold decree soon. Otherwise, there will be a long vacant of regulations on local content threshold for power projects and potential ambiguities regarding the

applicability of higher-level regulations (which might impose stricter thresholds and currently only apply to industrial company). This could create further uncertainties in the market.

Local Content Threshold Now Applies to a Broader Type of Power Projects.

MEMR Reg 11/2024 introduces a broader type of power plants which are subject to the local content threshold compared to the newly revoked MoI Reg 54/2012, as it expands the scope of local content threshold to include wind power plants, biomass power plants, biogas plants, waste-to-energy plants, and gas engine power plants. However, MEMR Reg 11/2024 does not specify the exact local content threshold percentage as this percentage threshold will be determined by MEMR at a later date, likely through a separate MEMR decree.

Exemption of Local Content Threshold for Solar Projects

Given the current conditions in the market, fulfilling local content requirements, particularly for solar projects, presents significant challenges. One major issue is that local manufacturers often struggle to produce solar modules that meet the required quality standards.³ This has led many market participants frequently seek exemptions from these local content thresholds. The difficulty in meeting the stringent local content criteria has led to an increasing number of requests for leniency or exceptions.

For example: (i) in 2019, the requirement to have minimum local content for solar module of 60% in 2019 was postponed until 2021 by MoI - reverting the local content threshold for solar module products to 40%; and (ii) an update to the minimum local content threshold for solar modules was introduced in 2023, which (a) sets the local content threshold for solar modules at 60% starting 1 January 2025; and (b) provided an exemption for local content requirements for solar projects in the new capital city, Ibu Kota Nusantara. For further details, please

³ *Bisnis Indonesia*, "Menilik Alasan ESDM Usul TKDN PLTS Diturunkan Jadi 40%", accessed on 8 August 2024, <https://bisnisindonesia.id/article/menilik-alasan-esdm-usul-tkdn-plts-diturunkan-jadi-40>.

refer to our previous alert here: <https://umbra.law/2023/09/14/client-alert-relaxation-of-tkdn-for-solar-module-and-solar-power-plant/>.

MEMR Reg 11/2024 continues to provide relaxation of the local content threshold for solar projects. This relaxation of local content threshold can be granted until 30 June 2025 for solar projects if (i) the power purchase agreement is signed no later than 31 December 2024, and (ii) the commercial operation date is planned to occur by no later than 30 June 2026, and subject to the following conditions:⁴

- a. the list of solar projects is determined through a coordination meeting held by the Coordinating Minister for Maritime and Investment Affairs (*Menteri Koordinator Bidang Kemaritiman dan Investasi*);
- b. the projects use solar modules produced by manufacturers (either domestic or foreign) who have investment commitment to producing solar modules domestically to meet domestic local content requirements, and committed to complete solar module production in accordance with local content threshold requirements no later than 31 December 2025.

MEMR Reg 11/2024 emphasizes the importance of the solar module manufacturer's commitment to producing solar modules domestically and meeting the mandated local content threshold as a key requirement for this relaxation. This condition is likely intended to support the recent surge in investment in solar module manufacturing in Indonesia, as it has been reported that Indonesia will soon have its first integrated solar cell and solar module manufacturing plant (such as, PT Trina Mas Agra Indonesia's project⁵ and the signing of the Memorandum of Understanding between the Coordinating Minister for Maritime Affairs and Investment and the Inspira Consortium⁶).

⁴ Article 19 of MEMR Reg 11/2024.

⁵ Kontan.co.id, "Sinar Mas Gandeng Trina Solar Bangun Pabrik Sel serta Modul Surya Terintegrasi", accessed on 8 August 2024, <https://pressrelease.kontan.co.id/news/sinar-mas-gandeng-trina-solar-bangun-pabrik-sel-serta-modul-surya-terintegrasi>.

⁶ Investor.id, "Utomo SolaRUV Gandeng Konsorsium Inspira Garap Industrialisasi Rantai Pasok Panel Surya", accessed on 5 August 2024, <https://investor.id/business/324933/utomo-solaruv-gandeng-konsorsium-inspira-garap-industrialisasi-rantai-pasok-panel-surya>.

Local Content Exemption for Projects Funded by Government Offshore Loan/Grant

The local content threshold has also been reported to become a significant obstacle in securing international funding for the development of renewable power projects by multilateral agency such as Asian Development Bank (ADB), World Bank, and Japan International Cooperation Agency (JICA) which are developed by State-owned Enterprises (SOEs) through a sovereign-direct or government two-step-loans or grants. For instance, it was reported that the development of the Hululais geothermal power plant faced delays because JICA, which was planning to provide funding, decided not to proceed with the loan due to the local content threshold requirements not aligning with the agency's procurement guidelines.⁷

MEMR Reg 11/2024 appears to address this issue by allowing local content requirements for power projects funded by foreign loans or foreign grants to follow the requirements as stipulated in the relevant loan or grant agreement, rather than the requirements regulated by the MEMR. This flexibility applies under the condition that the project is intended to meet domestic electricity needs and at least 50% of the loan/grant value originates from multilateral or bilateral creditors (development banks or financial institutions). This includes:

- (i) foreign government grant agreements, government grant forwarding agreements, or direct grant agreements to business entities; or
- (ii) foreign government loan agreements, government on-lending agreements, or direct lending agreements with or without government guarantees to business entities.

However, the reference to “*business entities*” instead of “*SOE*” in the clause suggests that MEMR Reg 11/2024 may be attempting to broaden the scope of this relaxation. It potentially includes not only projects with a sovereign-direct or government two-step-loans or grants to SOEs, but

⁷ Katadata.co.id, “PLN Curhat Aturan TKDN Hambat Pengembangan Proyek EBT”, accessed on 5 August 2024, <https://katadata.co.id/ekonomi-hijau/energi-baru/64c257bdec980/pln-curhat-aturan-tkdn-hambat-pengembangan-proyek-ebt>.

also projects to private business entities securing grants or direct loan from multilateral or bilateral agencies which fulfill the requirements as mentioned above. It remains to be seen how the clause will be interpreted.

Local Content Threshold for Electricity Export Projects

In relation to electricity export, recent reports suggest that the government may introduce a local content threshold of 60% for the electricity export projects.⁸ That requirements have not been previously stipulated in any official regulation. For the first time, MEMR Reg 11/2024 provides umbrella provisions which say that the local content threshold for electrical infrastructure intended for cross-border electricity sales will be subject to a minimum amount specified in a forthcoming MEMR decree.

Local Content Assessment for Solar Module

MoI Reg 34/2024 was issued to replace MoI Reg 4/2017. MoI Reg 34/2024 stipulates that the calculation of local content threshold value for solar modules is based on the assigned value of production factors, such as (i) materials, (ii) manpower, and (iii) factory overhead. While the assigned value for materials and manpower remains unchanged, MoI Reg 34/2024 introduces a new approach for calculating the local content threshold of factory overhead, which is based on the percentage of domestic factory overhead in comparison with the total factory overhead.

Sanctions and Rewards for Local Content Threshold Compliance

Previously, MoI Reg 54/2012 imposed administrative sanctions and financial penalties for non-compliance. In contrast, MEMR Reg 11/2024 outlines specific administrative sanctions for non-compliance with a local content threshold in the form of (i) written reprimand, (ii) interim suspension, (iii) administrative penalties, and/or up-to (iv) revocation of the Business License for Provision of Electricity for Public Interest (*Izin*

⁸ Katadata, "Indonesia akan ekspor 4 Gw Listrik ke Singapura, Minta Syarat TKDN 60%", accessed on 5 August 2024, <https://katadata.co.id/berita/energi/64fd732819a67/indonesia-akan-ekspor-4-gw-listrik-ke-singapura-minta-syarat-tkdn-60>.

Usaha Penyediaan Tenaga Listrik untuk Kepentingan Umum). In another distinction to MoI Reg 54/2012, MEMR Reg 11/2024 now offers the concept of rewards for the achievement of local content threshold (in the form of award certificates; announcements in the mass media; and/or other rewards).

In addition to sanction as stipulated in MEMR Reg 11/2024, as previously explained above, the MEMR has also introduced a non-tax state revenue for local content non-compliance penalty which will be imposed on business entities that fail to meet the local content requirements in MEMR regulation which was issued in 2023.

What's next?

We appreciate the government's efforts to resolve the long-standing issues surrounding the local content requirements which have been reported to cause bottlenecks in the development of renewable projects in Indonesia.

We will closely observe how the market responds to the numerous relaxations introduced by the government. For example, the government has sought to regulate various local content threshold requirements that were previously unaddressed, such as for wind power plants and biomass power plants, and provide clarity on relaxations for solar projects, particularly those currently underway.

Overall, MEMR Reg 11/2024 seeks to strike a balanced approach to local content threshold issues by, among others, (i) developing and encouraging local content threshold for manufacturers that have already invested in Indonesia; (ii) providing relaxations for transitional projects, especially solar projects, to allow time for manufacturers to implement their local manufacture plans; and (iii) offering solutions for projects funded by government two-step or direct loans or grants.

Disclaimer:

This newsletter is intended for providing general information on the latest legal and/or regulatory issues. We have no intention to and do not: (i) provide any legal services to, and (ii) establish any client-attorney relationship with, anyone through this newsletter. We do not guarantee the completeness of all opinions stated in the newsletter and we shall not be liable in any way to you for using any materials contained in the newsletter. If you wish to follow up on any legal matter that is being discussed in this newsletter, kindly contact lawyers that are qualified to practice in Indonesia.

No one may use or reproduce, by any means, any media and materials contained in this newsletter without prior approval from UMBRA - Strategic Legal Solutions.

By reading this article or disclaimer, and/or entering into UMBRA's website, you acknowledge and entirely agree with the content of this disclaimer.