THE PRINCIPLE OF INTERNATIONAL LAW FOR MOST FAVOURED NATION IN THE DEVELOPMENT OF SHALE HYDROCARBON AND COAL BED METHANE

Cut Asmaul Husna TR

Abstract

New energy sources in the future such as Shale Hydrocarbon and Coal Bed Methane are very potential in Indonesia. International companies of natural gas and oil such as United States and Canada have been considering themselves to do investment in this sector since 2005. A global challenge such as oil price deflation in 2017 and 2018 decreases investment value of Indonesia natural gas and oil. It expects that strategies of policy and planning of domestic/foreign investors may invest their assets in Indonesia gas and oil and find many new opportunities such as production development of non-conventional natural gas and oil (i.e., MGNK) by prioritizing the principle of equal treatment without any racial discrimination on its origin based on Article 3 subsection (1) of Act No. 25/2007 about Capital Investment and Ministerial Decree of Energy and Mineral Source No. 26/2017 about the Mechanism of Investment Return on Oild-and-Gas Upstream Business Activities to provide legal assurance in investment climate.

Keywords

investment, non-conventional oil and gas, most favoured nation

* Faculty of Law, Universitas Malikussaleh

Correspondence: Cut Asmaul Husna TR, Faculty of Law, Universitas Malikussaleh, Blang Pulo, Aceh Utara, Aceh, Indonesia. Email: cut2512@gmail.com
**Introduction**

The characteristic of gas-and-oil natural production is valuated based on the tenure of gas-and-oil field. The inclination of such production tends to increase at first and it gradually decreases after reaching the peak of production in accordance to the stock of natural gas and oil. Therefore, it needs efforts to get the peak back in a work field of natural gas and oil. The efforts are such as discovering and developing new field of natural gas and oil. To discover more fields of natural gas and oil in foreign countries, it needs some ways that depend on its profitability. Many fields of natural gas and oil have been found and developed in Indonesia between 1975 – 1980, such as Arjuna, Arun, Minas, Handil, Duri, Bekapai and Cinta.

Many investors consider the potency of global gas and oil as one of their target investment (A.F.M. Maniruzzaman, 2001: 309-310). Although an issue that Indonesia run out its natural gas and oil has spread out, the seismic survey and exploration for the last five years shows the otherwise. Therefore, the government keeps proposing investment in this sector through various ways to make the lifting of gas and oil increase along with its increasing commitment of investment that uses Gross Split Scheme (Buletin SKK Migas, 2019: 3).

In comparison, the biggest lifting of natural gas and oil in 2018 came from three projects. First, it was 209 thousand barrels of oil per day (bopd) (i.e., 98% of the target) from Rokan by PY Chevron Pacific Indonesia. Second, it was 209 thousand bopd (102% of the target) from Block Cepu by Exxon Mobil. Third, it was 79.9 thousand bopd from Pertamina EP. The focus of Pertamina EP was still 93% of the their target in 2018, however, it was bigger than the realization of 2017 lifting at 77 thousand bopd (Buletin SKK Migas, 2019: 7-8).

![Figure 1. Lifting of Natural Gas and Oil](image)

Related to investment, it is targeted in 2019 that domestic and foreign investors will be various. The value of investment in 2019 is likely to be more increasing rather than previous years. The assurance of KKKS (i.e., contractors of cooperation contract) have committed to pay the cost of KKP (i.e., Assured Work Commitment) which has reached more than US$ 2 billion until the end of 2018. The increasing target of lifting on natural gas and oil makes the contribution to National Non-Tax Income (i.e., PNBP) increase by the increasing value of investment on natural gas and oil (Buletin SKK Migas, 2019: 3). Special Executive Unit of Gas-and-Oil Upstream Business Activities (i.e., SKK Migas) notes that the investment value of natural gas and oil per 30th September 2018 has reached US$ 7.9 billion or 56% of the target which was US$ 14.2 billion (Kumparan Bisnis, 2018).

In terms of value, the current investment on gas and oil is more increasing rather than in 2017, along with the increasing realization of primary production development and optimization, such as by Pertamina EP, Pertamina Hulu Mahakam, Chevron Pasific Indonesia, ExxonMobil Cepu, and British Petroleum (m.kumparan.com>skk.migas.cap). With the increasing value of investment in gas-and-oil sector, it expects to distribute budget of investment in non-conventional gas and oil sector. The potency of this sector, especially Shale Hidrokarbon and coal bed methane, may attract many investors to join as well as for the sake of expanding investment in other countries such as Jepang, Korea Selatan, India and Norway (Directorate General of Natura Gas and Oil, 2017:144).

Through Indonesia-Norway Bilateral Energy Consultation in the early 2017, both countries actively discussed the efforts to expand their investment in this sector. The efforts involved the policy of data transparency. They agreed to share experiences in the implementation of this policy. (Directorate General of Natura Gas and Oil, Ministry of Energy and Mineral Source, 2017:145).

The investment should be based on the legal principle as mentioned in Article 3 subsection (1) of Act No. 25/2007 about Capital Investment; Legal Assurance; Transpaency; Accountability; Equal Treatment with no Racial Discrimination; Togetherness; Fair Efficiency; Sustainability; Enviromental Insight; autonomy, and Development Equilibrium and National Economy Unity.

Referring to the principle of Capital Investment in Indonesia, the investment in MGNK deserves to have further concern. According to some researches, the potency of Shale Hidrokarbon and coal bed methane approximately spread out in 14 slopes. Policies for the development of MNK have been set under Ministerial Regulation of Energy and Mineral Source No. 5/ 2012 about the Procedures for Setting and Offering Work Area of Non-Conventional gas and oil. Cooperations in this sector have been pioneered since 2013 by signing a Cooperation Contract of Non-Conventional Gas and Oil. The development of Shale Gas in North Sumatra is one of the examples. In addition, through its subsidiaries company under the name of PT Saka Energi Indonesia, PT Perusahaan Gas Negara (i.e., PGN) has been participating to manage Shale Gas in America. Together with colleges, the government is currently studying the potency of
Shale Gas in 13 areas, including: 7 areas in Sumatra, 5 areas in Kalimantan, and 1 area in Java (i.e., Cepu).

Therefore, this paper would discuss about the basic principle of exploring and developing investment in Shale Hydrocarbon and Coal Bed Methane, and the legal principle as well. It found that the increasing investment in MGNK sector might decrease the volume of oil import from oil-producing countries. In order to attract many investors, the principle of equal treatment in law without any racial discrimination should be in the first place. There should be neither less favourable treatment to any third state not more favourable treatment to national or other parties.

Research Method

The term ‘research’ is defined as effort to reveal, develop, or test the truth of knowledge. It involves an objective activity to find and develop as well as test the knowledge based on principles and theories in systematic ways through an intensive process for the sake of generalization purposes. Discovery of law is an act of concrete rule with particular application.

This research is under a philosophical level to find a legal principle of investment in the development of Shale Hydrocarbon and Coal Bed Methane. Jurisprudence is sui generis science. Therefore, this research aimed to find a coherence truth between legal norms and its principles (Peter Mahmud Marzuki, 2013: 47). The sources for legal studies are classified into primary and secondary materials. The former consists of acts, official transcripts or essay of legislation and judges resolutions. The later consists of any legal publication such as textbooks, legal dictionaries, legal journals, and any comments of judges resolutions (Terry Hutchinson, 2010:39-42).

The Basic Principle of Exploring and Developing Investments in Non-Conventional Gas and Oil


Britanian Law Property Act 1925 distinguishes between legal estates and legal interests. Legal Estates is a proprietary right of land and the owner is called estate owner, while the owner of legal interest has particular interests on other’s land. The term ‘Land’ in Law of Property Act means that “land of any tenure, and mines and mineral, whether or not
help apart from the surface, buildings or parts of buildings (whether the division is horizontal, or vertical made in any other way) and other corporeal heridatements; a manor, an advowson, and easement, right, privilege, or benefit in, over, or derived from land; but not an undivided share in land.” Hence, the term ‘land’ in Britanian Law (i.e., Anglo Saxon) has broad definition, different from the definition of Agraria Regulation, which defines the term ‘land’ in literal meaning.

It is strengthened by the definition of Horizontal Separation Principle between land and things on it. Friedman argues that the system of Modern Law (Britain-America) and Continental Europe Law have particular regulations which may not be classified into either civil or public law, as they contain some elements for public interests. Several states in West Europe such as France, Germany, Dutch, Belgium (i.e., Continental Europe, Civil Law) recognize custom law, as like Indonesia. France has a custom law called “droit de coutumes”, while Dutch has “gewoonterecht”.

The exploration and development of Gas and oil is a long-term business which needs huge fund and very sophisticated technology and operations. Therefore, it needs high professionalism and competent human resources. With this demand, gas and oil companies, especially those participating in upstream sector, are commonly global-scale companies. International people have long been realizing that their huge dependence on fossil-based energy resources (e.g., crude oil, natural gas, and coal) should be diminished as the energy are non-renewable and less go green. The development of MGNK potency uses Production Sharing Contract System, Net Production Sharing Contract with Sliding Scale and Gross Production Sharing Contract with Sliding Scale.

Based on geological and geophysical studies, a location is considered having a prospect of gas-and-oil stock if it encounters every criteria of hydrocarbon system (i.e., petroleum system), which consists of source rock, migration, reservoir, reservoir trap, and seal rock. Referring to the collected data, each criterion has particular valuation score. The result of those studies found that the prospect of hydrocarbon stock should be followed up by drilling the exploration wells in order to find the real stock of MGNK.

The triangle of gas and oil sources in MGNK class consists of extra heavy oil, bitumen, and oil shale, while GNK class consists of coal bed methane, shale gas, and gas hydrate. Heavy oil and thight gas formation are all in transition zone between conventional and non-conventional classes (Benny Lubiantara, 2013:248). Non-conventional hydrokarbon is organic chemical substance which can be in the form of gas, liquid, or solid with C (Carbon) and H (Hydrogen) substances, and it is taken through unusual way (using particular technology that differs from what MGNK uses). It is found in a rock layer with low permeability and/or porosity which is unexpected before. The kind of conventional hydrocarbon is such as Shale Hydrocarbon and Coal Bed Methane.

Shale Hydrocarbon is crude oil that comes from precipitated organisms in shale rocks. The shale rocks was molded since 300 - 400 millions years ago during pre-historical
period in earth history, where the shale was kept as mud sediment beneath the earth layer covered by water. Coal Bed Methane (i.e., CBM) is gas trapped in coal. Coal contains two components, including liquid and gas. To take the gas, the liquid element should be thrown away at first through dewatering process. After throwing away the liquid, the gas may soar and it is usually called by CBM as methane or CH4.

Commonly, non-conventional gas and oil is very latent approximately at 6,000 – 7,000 feet in the bowel of the earth. It is trapped in shale rocks. To take it out of the earth, it needs horizontal drilling and hydraulic fracturing technology. The government may use shale hydrocarbon and CBM to do energy diversification in Indonesia just so diminishing people dependence on natural gas and oil.

Figure 2. The Potency of Non-Conventional Fossil Energy

Developed industrial states such as United States gives their huge concern on this issue and seriously fund the researches that study the utilization of renewable energy including solar, air, and bio-fuels. Much renewable energy has been utilized as the source of electricity such as solar, air, and geotherm. New energy, especially nuclear, has been utilized as the basic material of electricity. The role of nuclear in mix energy is relatively stable between 5 % – 6 % in last three decades. Although some nuclear accidents (e.g., in Three Mile Island, Pennsylvania, United States [1979], Chernobyl Russia [1986], and Fukushima, Japan [2011]) have occurred, the electric supply from nuclear remains relatively stable and quite dominant (Verdict of Constitutional Court with Case number: 001-021-022/PUU-I/2003 about the Judicial Review of Act No. 20/2002 about Electric Source against Act No. 33 of Indonesian Constitution 1945, on 15th December 2004, p. 234)

Indonesia has potential hydrocarbon in 60 sediment slopes. Furthermore, Department
of Geology recently found 128 slopes of gas and oil. The verified stockpile of crude oil in 2014 was 3.6 billion barrel and, considering its recent production level, the age is approximately 13 years. In addition, the verified stockpile of natural gas in 2014 was 100.3 TCF and it will sustain for 34 years long. The tenure of gas and oil stockpile is assumed if no new stockpile is found. Coal Bed Methane (i.e., CBM) is one of non-conventional gas that relatively quite rare and expensive to develop. However, its potency is bigger than the conventional ones (Deputy of Coordination Unit, Management of Energy, Natural Sources and Environment, 2015: 5-6).

The Legal Instrument of Investment

Investment, particularly to gas and oil sector, is one branch of primary international law. States that produce natural gas and oil participate in investment contracts to expand their investment. The law of investment in natural gas and oil recognizes both Private Law (jus privatum) and Public Law (jus publicum). Categorization of those two laws was classified by a Roman philosopher.

Berthold Goldman, Philippe Kahn, and Philippe Fouchard classified those two laws based on the point of interest those laws stand for. Public Law assists public interests related to state’s interest (i.e., the civitas), and Private Law concerns on people interests as an individual or legal corporate (Kusnowibowo, 2013: 2. Cf. Berthold Goldman, 1964:17, Philippe Fouchard, 2004:21).

Based on Article 1 of Act No. 25/2007 about Capital Investment, it mentions that “Foreign investment is investing assets to do business in the territory of the Republic of Indonesia by foreign investors, either in the form of full investment or joint venture with domestic investors.”

The enactment of that article refers to the definition of foreign investment which basically contains several primary elements, as follow.

1. Direct investment;
2. The utilization of capital investment to make business in Indonesia;
3. In the form of full investment of joint venture with domestic investors.

In accordance to the enactment of the article and related to make cooperation with investors, argumentations of law are often proposed that national law of several developing countries sometimes hamper the foreign investment. For instance, some investee states often treat discriminatively. They even give particular criteria that may burden the company (i.e., investment) (Huala Adolf and An An Chandrawulan, 2015:39).

The instrument of international law to protect investment involves Havana Charter 1948 as the product of multilateral negotiation of International Trade Organization (ITO), Organization for Economic Cooperation and Development (OECD) initiated Multilateral Agreement on Investment (MAI), Multilateral Investment Guarantee Agency (MIGA), North American Free Trade Area (NAFTA). North American Global Trade Contract that involves three states including Mexico, Canada, and United States,
Association of South East Asia Nations (ASEAN) Comprehensive Investment Agreement (ACIA), Trade Related Investment Measures (TRIMs) and World Trade Organization (WTO) (Bernard Mommer, 2000:26.).

The Legal Principle of Most Favored Nation (MFN)

Article 3 subsection (1) letter (d) of Act a quo mentions that investment is organized based on: “the principle of equal treatment without any discrimination on original state.” International development, especially in trade and investment, encourages many experts to concern on those two sectors to communicate and propose ideas that deal with international issues of economy and law (Muchammad Zaidun, 2016:5).

Regarding to contracts of economy development in natural sources, both foreign and domestic investors adopt the principle of international law. Capital investment in natural gas and oil is basically cohesiveness between public and private law. The characteristics of this setting bring quite huge consequences on the states’ roles in terms of the interaction of interests among contracting parties.

The chance of investment has successfully eliminated the concept of dominance by the states on their production branches, land, water, and natural sources beneath for people welfare, given no legal protection assurance that the investment will be for people welfare. The capital investors should be responsible on Capital Flight (Verdict of Constitutional Court Case Number: 21-22/PUU-V/2007 about Judicial Review of Act No. 25/2007 about Capital Investment against Article 33 of Indonesian Constitution 1945, on 25th March 2008: 32).

Sornarajah argues that only few international laws that cause controversy, but related to the law of foreign investment (M. Sornarajah, 2011:116). Direct investment involves moving and non-moving assets the investors invest in the area of host country and to get profit through a total control they hold as the owner the assets. In addition, it needs a kind of cooperation between host country and home country to find more new potential stockpile of natural gas and oil (Rudolf Dolzer and Christoph Schreuer, 2008:1-3). International Verdict of Court of Justice (i.e., ICJ) in a case of Anglo-Iranian Oil Company is one of the examples, as follow. “It is this (i.e., the basic) treaty which established the juridical link between the (beneficiary State) and a third-party treaty and confers upon the State the rights enjoyed by the third party. A third party treaty, independent and isolated from the basic treaty, cannot produce any legal effect as between the (beneficiary State) and (the granting State): it is res inter alios acta.” (United Kingdom v. Iran, July 22, 1952).

The coherence between capital investment and natural gas and oil activity in Draft of Law for natural gas and oil should consider the provisions of investment acts. Gas and oil investment is conducted by contractors in order to keep the fairness of production level as mentioned in the agreement of draft of project and/or field development as mandated in Ministerial Regulation of Energy and Mineral Sources of the Republic of Indonesia No. 26/2017 about the Mechanism of Investment Cost Reimbursement in Upstream Business of Natural Gas and Oil.
Article 12 subsection (5) of Act of Capital Investment that deals with the stipulation of open business should be based on the criteria of national interest, such as protecting the natural sources, protecting and developing micro, small, and moderate businesses (i.e., SMEs), and cooperative enterprises, monitoring the production and distribution, improving the capacity of technology, participating on domestic capital investment, and cooperating with corporations the government has assigned for. In particular to capital investment that seeks for non-renewable natural sources (e.g., gas and oil), the investors should allocate their fund in stages for the sake of areal recovery that meets the standard of environmental properness, and the implementation is set under the regulation of capital investment that deals with a purpose to reach national economy welfare. Furthermore, it needs to manage natural resources to accomplish the responsibility that deals with the instrument of international law.

**Conclusion**

Non-conventional gas and oil (i.e., MGNK) is a kind of industry that has been recently becoming a trending topic in many states, including Indonesia. The success of developing MGNK in Canada and United States triggers many states and colleges appointed by their states to increase the value of investment in MGNK sector. It is in line with Ministerial Regulation of Energy and Mineral Sources No. 28/2015 about Acceleration of Non-Conventional Natural Gas and Oil. To find new potential stockpiles of MGNK, it needs a mutual-symbiosis-based cooperation between Home Country and Host Country. The Host Country should give fair protection and treatment on law to every Home Country by prioritizing the principle of international law of MFN.

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