

Phase II Audit Report

Human Rights,
Employment and Social Development
of Papuan People in Indonesia

on the part of

Freeport-McMoRan Copper and Gold, Inc.,
New Orleans, LA
and
PT Freeport Indonesia, Jakarta and Papua



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Introduction

This document is a detailed report of Phase I Follow-up and Phase II of the audit of PT Freeport Indonesia's (PTFI) operations in Irian Jaya, Indonesia. In the first phase of the audit, the International Center for Corporate Accountability (ICCA) analyzed PTFI's compliance with its Social, Employment and Human Rights Policy (SEHR). The first phase of the audit focused on PTFI's internal Security Department, with special interest in the Security Department's human rights training and reporting as well as its relationship with the security forces of the government of the Republic of Indonesia; on general human rights training throughout PTFI's operational units; on the employment, training and recruitment of Papuans within PTFI; and on the administration of PTFI's outreach into the local Papuan communities through the Freeport Partnership Fund and programs the LPMK (the local communities' organization that runs programs using the Freeport Partnership Fund). As part of the audit process, ICCA looked closely at the education unit of the LPMK. The report on the first phase of the audit, along with Freeport's response to the audit was issued in July 2005. The complete text of this report is available on ICCA's web site www.icca-corporateaccountability.org.

As part of the audit process, ICCA made public recommendations to Freeport about corrective actions that Freeport and the LPMK should make to improve adherence to Freeport's SEHR. A follow-up audit on areas of concern was undertaken in August 2006.

The second phase of the audit took place in November and December 2006. It focused on two areas: first, the medical care that PTFI provides for the local population that does not work for PTFI and contractors to PTFI; and second, on the major contractors that provide essential services to PTFI's mining operations. These include catering, housing and hospitality services (PT Pangansari Utama); mining equipment and repair services for equipment (PT Trakindo); specialized mine drilling (PT Sandvik); port services, road maintenance and truck and bus operations/maintenance (PT KPI) and a labor supplier owned and operated by Papuans (PT SAS). As major contractors providing services at PTFI's operations' site exclusively to Freeport, all these contractors are covered by PTFI's SEHR.

A full description of the audit protocols and background about ICCA and its work can be found in the introduction to the first phase audit report. The same protocols were used for the second phase audit. A brief description of these protocols is also contained in individual audit reports of various privatized companies that were suggest of the Phase II audit.

As is noted in the body of this report, ICCA and PTFI have been working on issues surrounding the use of temporary contract workers within PTFI's and privatized companies' workforces. The central issues are how long temporary contract workers can be employed before being transferred to the regular company payrolls and under what conditions temporary contract workers can be paid at a lower rate than fellow workers. These have proven to be difficult, complex and, at times, contentious issues. These discussions have delayed the

issuing of this report. There are still disagreements between ICCA and PTFI about the spirit and letter of Indonesian labor law and how that law should be implemented at PTFI's operations site. ICCA sought and received an independent legal opinion on this matter. This advice was used to review PTFI's policies and practices and those of privatized companies with regard to the employment of temporary contract workers. The legal opinion is offered as an appendix.¹ PTFI has responded to this issue in their reply to this report.

¹ Copies of the relevant memoranda received by ICCA are reproduced in the appendix to this document.

Executive Summary

A. Follow-up to the Phase I Audit

PTFI responded rapidly and effectively to most of the recommendations of presented by ICCA in the Phase I Audit of PTFI's Indonesian operations. This included enhanced training programs for all employees in prevention of human rights violations, the cessation of the practice of PTFI's security personnel driving vehicles for the Indonesian police and military, enhanced training for Papuans who are within the PTFI workforce and for those who wish to work at PTFI's operation in Irian Jaya and reforms within the Education Bureau of the LPMAK-administered and Freeport Partnership Fund-financed community outreach program. Since PTFI has implemented all of ICCA's recommendations in these areas of the Phase I audit, ICCA makes no further recommendations. Since ICCA believes these programs are vitally important for PTFI and the local community, ICCA recommends further audits of these programs should be undertaken in 2008.

In the Phase I audit, ICCA noted that a number of workers that were interviewed said they were performing tasks for PTFI that were similar if not the same as full PTFI employees, but were receiving less pay. Further, some of these employees reported that they had been temporary contract employees for periods in excess of five years. In the Phase I audit ICCA made recommendations to PTFI on a way forward to end this practice. PTFI has put in place a number of programs to end the long-term use of temporary workers and

to bring that area of employment into compliance with Indonesian labor law. However, in the opinion of ICCA there is still a ways to go before PTFI will address this issue fully. Therefore ICCA make the following recommendations with regard to contract labor:

1. The establishment of a high-level management structure to oversee the evaluation of the performance of all temporary contract workers who have worked on the PTFI project for more than three years;
2. The development of concrete plans to transfer as soon as possible all temporary contract workers who are not doing temporary jobs; and
3. The creation of a fair plan to recognize the financial loss of those temporary workers.
4. This process should be completed as soon as possible, but no later than December 31, 2007. Further, ICCA recommends that a further audit of the contract worker practices should be undertaken at the end of 2008.

B. The Phase II Audit

Medical Services to the Papuan Community²

PTFI has supplied medical care to local Papuans since the inception of mining and milling activities in Irian Jaya in the early 1970's. As the number of Papuans who did not work for the company increased in the area surrounding PTFI's operations, PTFI made a commitment to expand the public health and medical care programs available to the local Papuan communities. Since 1996, PTFI has worked with the local community to develop a joint company/community management for the provision of medical care for the Papuan community. *Today, the local community has direct management responsibility for the hospital in the lowland city of Timika (Rumah Sakit Mitra Masyarakat—RSMM) through the Amungme and Kamoro Community Development Institute (LPMAC) and the public health programs for the local community (Public Health and Malaria Control-PHMC). International Security Overseas Services/AEA (ISOS/AEA) and LPMAC share management of the highland hospital (Rumah Sakit Waa-Banti).* PTFI funds these programs through the Freeport Partnership Fund. From 1996 to 2006 the Freeport Partnership Fund provided \$100 million to support medical activities for the local Papuan

² For the purpose of the medical care audit two outside additions were made to the ICCA audit team. The first was Dr. Emon Winardi Danudirgo, an Indonesian physician who is chief of internal medicine at a large, Jakarta hospital and who had formerly worked with the Ministry of Health in Irian Jaya. Dr. Danudirgo provided a context for the auditors with regard to Indonesian medical standards and the delivery of medical care in Papua. The second addition to the auditing team for the medical audit was the Dr. David Lowry, formerly an executive at Freeport in Indonesia and Papua, who advised on access to Papuan villages and people and an understanding of Papuan communities and their needs

communities in and around PTFI's operations. It should be noted that PTFI has no contractual obligation to provide medical care to people who are not employed by the company.

ICCA audited the three major community-based health programs for their effectiveness in improving the health of the Papuans in the local community and the management structure of the LPMK and PTFI's Social and Local Development Department (SLD) for the efficiency of the operation.

The audit concluded that PTFI has fulfilled all its financial and human resources support that the company made in its *Social, Employment and Human Rights Policy* and the *Guiding Principles for Indonesian Operations*. ICCA also found that the medical care providers, the Yayasan Caritas Timika, which operates the RSMM; International ISOS/AEA, which operates the Banti hospital PTFI's Public Health and Malaria Control (PHMC), are deeply committed to the health of the local population. The audit also indicated that, by-and-large, the local community shares in this assessment of the provision of medical care.

ICCA's audit team noted specific areas where significant achievements occurred in reducing the impact of various diseases and in improving the level of wellness among the people and communities involved. At the same time ICCA's audit team observed a number of areas where better planning and efficient implementation should yield further improvements in community health and well-being. Finally, ICCA noted some elements of institutional arrangements and tasks management where a substantial redirection of resources and renewed focus in addressing certain issues would be necessary.

In this Executive Summary, ICCA will give a short description of the audit findings for each program and an outline of the recommendations for improvement in providing medical services to the local community. The enumeration of these recommendations should be viewed in the context of ICCA's overall very positive evaluation of the medical programs offered to the Papuan people through the Freeport Partnership Fund.

A. Overall Provision of Medical Care:

ICCA believes that too much of the focus (and the use of financial and human resources) in the area of wellness is being used for curative care. The budget for the hospitals in Timika and Banti continually increase and the budget for Public Health and Malaria Control decreases. It is ICCA's belief that a well-directed and managed public health initiative in the villages in and around Timika would improve the overall wellness of the people.

B. Management:

LPMAC has provided adequate and thoughtful management of the medical programs through the disbursement of funds from the Freeport Partnership Fund. LPMAC has been well served by the advice offered by PTFI's SLD. Nevertheless, ICCA believes that the following changes will help LPMAC support the medical programs more effectively.

1. LPMAC should employ a medical professional to help evaluate the distribution of money to the three entities the LPMAC supports;
2. LPMAC should allocate funds based on community medical needs and targets;
3. Units receiving funding must deliver on targets based on data collection.

C. Public Health, Malaria Control and Community Clinics

PHMC has provided effective programs within the community to alleviate malaria, tuberculosis and, of late, HIV/AIDS. The funding for PHMC has decreased over the past few years and PHMC has cutback on some programs that, in the opinion of ICCA, would have provided great wellness benefits for little cost. The devotion of the PHMC staff to the well-being of the Papuan people cannot be questioned. ICCA believes that the following recommendations will help the PHMC program provide better services to the Papuan people.

1. PHMC should expand its programs health education within local communities;
2. Community healthcare visitors and community clinics should receive additional funding. These programs should be more carefully monitored to make certain resources are being used wisely and efficiently;

3. PHMC should increase its data collection activities to monitor disease trends in the area;
4. PHMC should look at ways to re-align staff to better serve community needs.

D. Banti Hospital-RSWB

The ICCA auditors were most impressed by the services offered at RSWB. The outpatient and inpatient facilities were impressive. In spite of a large number of people using the facility, the areas were clean and well-run. However, the community was less impressed by the services that RSWB than the auditors thought they would be. It appears that the people in Waa-Banti wish the RSWB to duplicate the services offered at the Tembagapura hospital.)

1. RSWB needs to undertake programs to better educate the local population about the health of community residents;
2. RSWB must look for ways to make the community less dependent on PTFI's Tembagapura hospital.

E. RS Mitra Masyarakat (RSMM)

The RSMM provides services for the large and growing population in the Timika area. The Papuan population in that area is estimated at 50,000. There are no other comprehensive medical facilities in the area, although the government has a small out-patient and inpatient

facility (Puskesmas) and there is a privately-owned maternity clinic that recently opened.

The RSMM was designed for a much smaller population than it presently serves. The attractive campus is no longer as efficient as it once was and there are times when the hospital is overcrowded. The medical staff notes that the hospital as currently arranged does not allow for flexibility during times of high patient load.

That being said, the auditors found that the doctors and other medical staff were committed to providing optimum care for the local population and that the local communities were pleased with the care they received at the RSMM. Based on the audit results, ICCA recommends the following actions to improve the provision of medical services at the RSMM.

1. Give full management responsibility at the RSMM to YCT. This will eliminate overlapping responsibilities now undertaken by various organizations;
2. Expand the number of senior medical and support personnel. Currently too few people have responsibility for too many diverse tasks;
3. Better integrate RSMM with PHMC and others participants in the 'wellness chain;'

4. Create better data that can be used to allocate funding for RSMM and PHMC; and
5. Freeze funding increases for RSMM until it is clear that such funding increases will create overall wellness benefits for the Papuan people in the community.

Recommendations for Follow-up and Compliance Verification

ICCA recommends that PTFI should instigate a follow-up audit towards the end of 2008. This audit would evaluate the efficiency of organizational changes, redirection of budgetary allocation, and operational aspects of RSMM and Public Health programs as agreed to by PTFI.

Privatized Companies

In the early years of its mining operation in Indonesia, PTFI provided all services for itself. As the size of the mining operations increased in the early 1990s, PTFI decided to concentrate on its core business and to have outside companies with specific expertise take over major portions of support activities and some very specific, technical mining operations. Since PTFI already had the physical facilities and the personnel in place for these activities, PTFI sought companies that would take over the management of these functions. PTFI called this process 'privatization' and the companies that managed the operations and personnel came to be called 'privatized companies.' There are three large privatized companies that provide services to PTFI: PT Trakindo Utama, which

provides most of the heavy mining equipment and services the equipment; PT KPI, which provides port services, transportation equipment and maintenance, and road maintenance; and PT Pangansari Utama, which provides canteen and hospitality services. ICCA audited all of these large 'privatized companies' as part of the Phase II audit.

Two other companies that were also audited during Phase II of ICCA audit were PT Sandvik, a small but vital company to PTFI, which does specialized mine drilling; and, PT SAS, a Papuan-owned company, which provides some custodial services for PTFI, but more generally supplies workers with lower-level skills to PTFI and the 'privatized companies.'

The privatized companies are expected to adhere to PTFI's SEHR and GOP. Therefore, the audit of these companies covered the same issues that were covered in the Phase I audit of PTFI's operations. These include adherence to the principles of human rights, enhanced employment opportunities for Papuans and, where applicable, support for the social and economic development of the local Papuan communities.

ICCA's Audit Procedures and Protocols

ICCA's audit of privatized companies' operations and policies followed procedures and protocols that were similar to those applied in all others aspects of ICCA's audit of PTFI's operations. They are designed to undertake a thorough analysis and evaluation of management policies, decision-making systems, and operational procedures and practices. These generally take the form of

Management Compliance Report (MCR) where the facility's management is requested to provide in considerable detail its self-description and analysis of company operations. Every effort is made to understand and appreciate the explanations and assertions made by the senior and operating level managers of the audited unit as to the successes achieved and the challenges still to overcome; their plans for corrective and remedial action; and, the resources they would need to achieve their objectives. ICCA's professional staff undertakes a thorough analysis and evaluation of the MCR's content in preparation for the field audit.

The in-house analysis of MCR data is followed by a field audit, which is comprised of two parallel activities. The first one includes meetings with the management to clarify any statements or data provided in the MCR, which needed further explanation. The second aspect of the field audit includes an analysis of data gathered through detailed, confidential one-on-one interviews with a randomly selected representative sample of the total workforce. All interviews were conducted by a group of teachers and graduate students from the University of Papua in Manokwari. They included both male and female interviewers who were familiar with Papuan culture, spoke Bahasa Indonesian and also understood local dialects. These interviewers were familiar with the culture and dialects of the people to be interviewed and were able to develop excellent rapport with them.

The Phase II audit results suggest that PTFI had not clearly articulated to the privatized companies the responsibilities they had toward the Papuans as a

result PTFI's SEHR. All of the privatized companies fell far short of PTFI in the area of Papuan employment and employee development and most fell short in the area human rights training and employment. However, the most notable feature of the audit of these companies was their use of temporary contract labor, which paralleled PTFI's such of such workers. The overall recommendation for the privatized companies is that they need to make commitment to the SEHR and the GOP on the same level as PTFI's so that they can begin to help the Papuans realize the benefits of PTFI's and their presence in Papua in sustainable ways. In addition, ICCA recommends that PTFI make a greater commitment to work with the privatized companies to help them support PTFI in fulfilling its commitment to the wellbeing of the Papuan people. In addition, ICCA is making the following specific recommendations to the privatized companies based on the audit findings.

PT Pangansari Utama

Because of the nature of Pangansari's work (catering, housing and hospitality), Pangansari should be most able to train and employ Papuans. However, the audit found that fewer Papuan employees than PTFI and that the Papuans employed by Pangansari had not advanced through the company's workforce. The other area of concern that came out of the audit was the purchasing of local goods, especially fruit, vegetables and fish. ICCA recognizes that the growth of the local population in the Timika area may limit the availability of locally purchased foodstuffs, but the auditors believe that before allowing such

a reason to go forward, Pangansari should show that a greater effort has been undertaken by Pangansari to make certain the area is as productive as possible and that the entire population is benefiting from Pangansari's presence at PTFI's operations area. Therefore, the following recommendations have been made to Pangansari and PTFI.

1. PTFI should support Pangansari in increasing the number of Papuan employees who work for Pangansari and assist in the full implementation of PTFI's SEHR by Pangansari. A plan for such support should be in place within three (3) months.
2. Pangansari should take responsibility for increasing the Papuan workforce by 100% in the next five (5) years.
3. Pangansari should also assure that Papuans have upward mobility in the workforce equal to that of Non-Papuan Indonesians. Pangansari should assign a senior executive to oversee these employment and promotion programs and should establish a mechanism to work with Papuan leaders on these issues.
4. PTFI and Pangansari should develop a joint plan to fully evaluate the potential of increased local purchases and do feasibility studies for increased productivity in farming the local land. Such a plan should be in place within three (3) months of the issue of this report.
5. Pangansari should develop a mechanism to monitor achievement in the area of local economic development through farming and fishing. A senior executive should have responsibility for the plan and should

work with PTFI's SLD Department and the LPMK in implementing the plan.

PT KPI

PT KPI operates PTFI's Portsite and truck and bus transportation. It also provides light vehicle maintenance and the upkeep of PTFI's roads. Most of PT KPI's workers are skilled. In general worker satisfaction at KPI was good and KPI had made a good-faith effort to implement PTFI's SEHR. The two major issues raised in the audit were the employment of Papuans among the staff employees of KPI (KPI had done an acceptable job in employing Papuans in non-staff positions) and the use of temporary contract workers with salaries lower than those of regular KPI employees and for periods in excess of those permitted by Indonesian labor law. It is in these areas that ICCA is making recommendations to KPI.

1. KPI must develop a career path plan for Papuan employees to move Papuan non-staff employees to staff positions. This should include intensive on-the-job training and mentoring programs.
2. KPI must create a plan to transfer temporary contract workers to the KPI payroll in accordance with Indonesian labor law. In addition, all temporary contract workers who do the same work as KPI employees should receive equal wages as required by Indonesian labor law. Plans

to implement these actions should be complete within six months and implementation of the programs should be formally evaluated within 12 months of the acceptance of this report.

PT Sandvik

Sandvik provides specialized mining services for PTFI. Because of the nature of their work, Sandvik has a number of highly skilled professionals, a number of whom are expatriates, and a greater number of skilled assistants that provide services to the specialized mining professionals and a number of semi-skilled workers. There are relatively few Papuans (8.6% of the workforce) who are employed by Sandvik. Most of those fall in the last category of employees. Although Sandvik's management report states that the company has active on-the-job and developmental training programs, nearly half of the employees state that they have had little or no training geared toward advancement in the workforce. However, virtually all employees agree with the company that they have received safety training.

Sandvik employees are divided along staff and non-staff lines as to whether Sandvik is a good employer: staff employees say they are happy about their employment; non-staff employees say they are less happy. A similar divergence of opinion exists among employees of Sandvik about the company's commitment to human rights: staff believe the commitment is real and vital; non-staff are less certain.

However, the major issue that ICCA has focused on with Sandvik (as with PTFI and some of the other contractors) is the use of temporary contract workers. For Sandvik the issue is one group of workers doing a single task for more than three years, but still deemed 'temporary.'

Based on the audit findings, ICCA makes the following recommendations to Sandvik:

1. Prepare a detailed plan of action that provides targets toward hiring, training and promotion of Papuan workers. This plan should be in place within six (6) months from the formal acceptance of this report.
2. Implement program aimed at on-the-job and developmental training for all employees and especially for Papuan workers; and
3. Develop a plan of action for contract workers to bring Sandvik into compliance with Indonesian labor law, including transfer of all temporary workers who have worked with Sandvik on temporary status for more than three (3) years, compensation to such workers for lost wages and a policy for the future use of temporary contract workers.
4. These plans should be audited within one year of the acceptance of this report to assure implementation.

PT SAS

PT SAS manages a few functions, including a cattle ranch and some general maintenance functions, but PT SAS is mainly a labor provider. However,

the most notable aspect of PT SAS is that it is owned and operated by local Papuans. PT SAS is a great success story for the joint efforts of PTFI and the local community to establish locally-owned and operated businesses.

That being said, ICCA was surprised and disappointed that PT SAS employed relatively few Papuans. Therefore, ICCA recommends that SAS work to increase the employment of Papuans by developing an agreement with PTFI to enhance the recruiting and training of Papuans. Since most of the workers employed by PT SAS work in semi-skilled positions, it should be relatively easy to realize the goal of adding Papuans to PT SAS' roster of workers.

PT Trakindo

Trakindo, which sells and services mining equipment used by PTFI, has worked at PTFI's operations' site for 27 years. Over the past five years, the presence and scope of activities at PTFI has substantially increased. Because of the length of time that Trakindo has provided services for PTFI, it might be expected that Trakindo would be further advanced in compliance with PTFI's SEHR. The audit suggested that that was not true. Trakindo lagged behind other contractors in their employment of Papuans, both in the staff and the non-staff areas. In addition, Trakindo had not yet implemented a robust implementation of human rights training and monitoring. Finally, Trakindo, like PTFI and some of the other privatized companies, used temporary contract workers in ways in which ICCA considered contrary to Indonesian labor law. On the positive side, most of Trakindo's staff employees expressed satisfaction with

Trakindo as an employer and stated that they believed Trakindo treated Papuans well. Non-staff employees were less positive toward Trakindo as an employer and with regard to the company's treatment of Papuans, but they were still fairly positive in their assessment.

The following recommendations focus on the areas of Papuan employment, advancement in the workforce and the general issue of the use of temporary contract workers.

1. Bring Trakindo's employment standards and commitment to Papuan employment and employee development into line with PTFI's commitments to the Papuan community as set out in PTFI's SEHR.
2. Trakindo should adhere to Indonesian labor law with regard to temporary contract workers.
3. Trakindo should develop a comprehensive education, recruitment and training programs for Papuans.
4. Trakindo should fully implement the human rights provisions of PTFI's SEHR.

Chapter 1

Phase I Follow-up Audit Report

I. INTRODUCTION

This document presents the findings of a follow-up audit conducted by the International Center for Corporate Accountability, Inc. (ICCA) during August 20-23, 2006. The Phase I Audit was concluded at the site of PT Freeport Indonesia (PTFI) mining operations in Papua, Indonesia, during the period of November 23 – December 1, 2004. It was designed to evaluate PTFI's performance in the areas of human rights, hiring and employment opportunities for the Papuan people, and social and economic development of the Papuan community. Freeport's commitments to these areas are described in detail in the company's Guiding Principles of Operations in Indonesia (GPOI – 1) and its Social, Employment and Human Rights Policy (SEHR).

ICCA's report of the Phase I audit commended Freeport on meeting a substantial part of its commitments to the Papuan people in terms of employment and skill-based training, general education, public health and medical care, and economic development. At the same time, Phase I audit found certain areas where progress was inadequate and further action was needed. In response, Freeport committed itself to undertake the necessary changes in its policies and programs.

It was also agreed that ICCA would undertake a Follow-Up Audit. The purpose of this follow-up audit would be to verify that appropriate actions had

been or were being taken by Freeport McMoRan Copper and Gold, Inc. (Freeport) and PT Freeport Indonesia (PTFI) in response to ICCA's recommendations in the Phase I Audit Report.

This report has been prepared in two parts. The first part of the report was completed and formally submitted to Freeport on March 14, 2007. This segment of the report generally confirmed that Freeport had positively responded to the ICCA's recommendations and had taken the necessary corrective action, which also included establishment of new policies and procedures that would prevent the reoccurrence of similar problems in the future. ICCA is satisfied with Freeport's responses and have so indicated in the body of the report that follows.

There is, however, one area where ICCA believes that Freeport's actions after the first phase of the audit have been inadequate. This is the area of temporary, contract workers. Freeport began intensively using contract workers in the early 1990s when rapid expansion of the mine and mill required the use of a great number of temporary employees. Because there were no Indonesian-based construction companies that were able to provide 'turn-key' project management the expansion of the mine, mill and support facilities, Freeport chose to use a variety of companies for the construction projects with Freeport providing general and overall management. The temporary nature of the construction projects made it desirable for Freeport and its sub-contractors to use temporary labor providers to employ workers. All of this was in compliance with Indonesian labor law and practice, which permits the use of temporary, contract employees for periods up to three (3) years under clearly defined work situations

and also require that these workers were not doing permanent work alongside a company's regular employees. ICCA's conclusion in this regard has been further confirmed through independent legal advice on the interpretation of pertinent Indonesia's employment laws.³

After completion of the construction projects in the mid-1990s, however, Freeport continued to use contract labor to perform jobs that were permanent in nature and for periods that were far in excess of what Indonesian labor law provided. The first phase of the audit, completed in 2005, noted problems with the use of temporary contract laborers. In this report, ICCA cited examples of workers who had been working side-by-side with Freeport employees for many years and were paid wages that were substantially below those provided to Freeport's regular employees. ICCA believes that the Indonesian labor law is clear with respect to the time limits and nature of employment conditions for temporary, contract employees. Therefore, even if all actions taken by PTFI to date are accepted at face value, the company would still be considered largely in violation of Indonesia employment laws and PTFI's SEHR policies.

As a result of the audit, PTFI made a number of commitments with regards to contract employees. These included evaluations of all contract employees to determine whether their work performance met PTFI's employment standards and, if contract employees met those object standards, hiring them as regular PTFI employees; internal development plans to reduce contract labor

³ Copies of the relevant memoranda received by ICCA legal counsel are reproduced in the appendix to this document.

through training programs and by careful adherence to the company's already developed policy on contract labor.

However, the follow-up audit showed less improvement in the area of contract employees than ICCA had expected as the basis for reasonable compliance with Indonesia employment laws and Freeport's SEHR policies. Freeport had raised the pay scale for all contract employees first to 63% of Freeport employees and then to 73%; the company had also transferred some long-serving contract employees to the PTFI payroll. These wage rates and transfers, however, remained below those mandated by the Indonesia employment laws. There were also many employees who had served far longer than three years with contract labor suppliers who remained outside the PTFI employment structure and many others whose pay for doing the same work as PTFI employees remained substantially below that of PTFI employees. Therefore, ICCA has made further recommendations to Freeport about what Freeport must do to rectify this labor situation.

II. SCOPE OF THE FOLLOW-UP AUDIT

The scope of the follow-up audit covered four major areas where additional action was indicated on the part of PTFI. These are: (a) insufficient training and comprehension on the part of many employees with regard to PTFI's human rights policies and their implementation; (b) use of PTFI's Security Department (SD) drivers for transporting Indonesian military personnel in the area of PTFI mining operations; (c) increasing employment opportunities and

upward mobility for Papuans through increased training and other approaches to skill enhancement; and, (d) clarifying policies and streamlining the process of hiring contract labor and ensuring that all workers (both PTFI and contract) are paid similar wages and benefits for doing similar work.

Another part of the Phase I Audit follow-up was devoted to the education-related programs and activities of the Lembaga Pengembangan Masyarakat Amungme dan Kamoro (LPMMAK).⁴ ICCA's formal audit revealed a number of deficiencies in the LPMMAK's education policies and programs and called for a series of corrective actions on the part of LPMMAK. Education is an important part of PTFI's efforts to support the socio-economic development of the Papuan community - especially that of Seven Suku - and education programs account for about 30% of LPMMAK's annual budget.

III. AUDIT FINDINGS – Part I

As noted earlier, ICCA's findings contained in Part I were submitted to Freeport on March 14, 2007. They are reproduced here so as to create a complete public record of the Phase I Follow-Up Audit.

Human Rights Training

ICCA's follow-up confirms that Freeport's Human Rights training program has been revised to focus on effective learning and continuous enhancement of human rights compliance. As part of this process, PTFI has appointed a Senior

⁴ LPMMAK is an organization set up to manage the Freeport Partnership Fund (formerly referred to as the "1% Fund") with focus on the educational, social, and economic development of the seven local indigenous tribes (or suku), particularly the Amungme and Kamoro people.

Human Rights Compliance Officer, a distinguished Papuan, whose role is to ensure that company's training and communications efforts are effective, appropriate, and ongoing. PTFI has also initiated a program for human rights "trainees" who assist the Senior Human Rights Compliance Officer in providing regular human rights training to all PTFI and privatized company employees, contract workers, and trainees.

Training in human rights issues is conducted annually for all PTFI departments, except for the Security and Social Local Development Departments, where the training is conducted twice a year. All new hires participate in human rights training as part of their mandatory employment induction.

Information billboards and posters outlining six key basic human rights provisions are placed in public areas, such as offices and workers' mess halls. Posters are published both in English and Indonesian. Security Department personnel also carry cards noting the six major human rights principles along with their ID cards.

ICCA is satisfied that PTFI has taken appropriate actions in response to ICCA's initial audit recommendations and that PTFI's new program and procedures should create improved understanding and more effective implementation of the company's human rights policies. The important point to emphasize here is that PTFI must continue to devote the necessary monetary and human resources on an ongoing basis to ensure that protecting human

rights becomes an integral part of PTFI's corporate culture and embedded into all aspects of PTFI's operations and human resources management.

Security Department (SD)

Assignment of SD Drivers to the Indonesian Military Units: ICCA confirms that PTFI's SD has discontinued the practice of providing drivers to the Indonesian government security personnel. Instead, the SD provides specialized training to government drivers. This situation is necessitated by the fact that driving conditions in the mining area are quite hazardous given the mountainous terrain and constant flow of heavily loaded trucks. All drivers operating in the mining area must undergo this training to ensure safe driving and to minimize road accidents.

Security Department Training in Human Rights Policies and Programs: ICCA confirms that PTFI has devoted significant resources to improve the quality and effectiveness of human rights training for the SD workers. ICCA has also verified that all employees of the SD have received human rights training and carry human rights principles cards with them at all times. The SD personnel are not allowed to carry guns or use physical force. All cases of human rights violations are reported and forwarded to the appropriate department or agency for follow-up. According to the SD management, in the last 18 months, there were only a handful of reports filed. However, none of these reports could be classified as human rights violations and none involved actions taken by any PTFI employee or an employee of a privatized or contractor company.

Papuan Employment

ICCA's Phase I Audit had identified significant discontent among PTFI's Papuan employees as well as Papuan community leaders with the company's efforts in providing jobs for the Papuan people. While Phase I Audit showed that PTFI had met its numerical targets, the same could not be said for upward mobility at rates that were consistent with promotion rates of Non-Papuan employees with comparable seniority and work experience.

PTFI considers inadequate basic education and lack of technical training to be the primary cause of poor progress on the promotional ladder for some Papuan employees. To this end, PTFI is focusing on creating development programs for its employees and potential employees - both through on-the-job training and off-site education programs. According to PTFI, the company spent approximately US \$22 million on training and development programs in 2006.

One such program, called the Graduate Development Program, was launched in 2004 in collaboration with a number of Indonesian universities. This program targets the top graduates of the best Indonesian universities and provides them with a 1-3 year structured development program with a focus on business skills development and future employment at PTFI. To date, about 100 graduates have joined the program, and about 20% of these are Papuan.

Another program called the Affirmative Action Program, gives about 50 Papuan employees between 6 and 12 months of release time from the job to participate in focused skills training. The intent is that with additional

competencies, these Papuans who are mainly long in service but low in skill, can return to the workplace in higher level positions.

The Nemangkawi Mining Institute (NMI), which was established by PTFI in 2003, offers pre-apprentice, three-year apprentice, and adult education programs. NMI focuses on technical training and currently has more than 1,000 students, over 95% of them Papuan, and more than half of these from the 7 Sukes. The company expects that of those who successfully complete the program, at least 10% would be capable to advance to supervisory and managerial level positions. At the time of the follow-up audit, 175 apprentices had been hired as employees of PTFI or one of the PTFI's partner companies. Capital spending for Nemangkawi facilities totaled over \$3 million as of 2006.

A new performance evaluation system for non-staff (hourly) workers was introduced in April 2006. In addition to the evaluation of current job performance, the new system emphasizes demonstration of competency and high levels of performance. Staff performance appraisals, conducted annually, specifically cite succession planning as criteria for success of all staff.

The company has invested considerable resources in the development of succession plans for every department. In 2006, as a result of the recommendations made by ICCA, PTFI integrated a Papuan Development component into every department's succession plan. These set out specific and aggressive targets for increasing the proportion of Papuans among both staff and non-staff workers throughout the company over a 5-year period. The plans are reviewed twice per year by each department and by senior management.

Departments not meeting their goals were required to provide a satisfactory explanation and a plan to rectify the situation. Management in each department is held accountable for results and achievement in this area is a factor in management's incentive compensation decisions.

These efforts are beginning to bear fruit. Data show that the proportion of Papuan staff has gone from 7.7% at the end of 2005 to 12.4% as of August 2006. The proportion of Papuan non-staff has increased from 19.8% to 30.8% during the same period. Papuans are being hired and promoted at the same rates as Non-Papuans. Papuans are also receiving significantly higher training opportunities than Non-Papuans.

Overall Observations and Recommendations

ICCA confirms that Freeport McMoRan Copper and Gold, Inc (FCX) and PT Freeport Indonesia (PTFI) have taken appropriate follow-up actions based on the recommendations made by ICCA in the Phase 1 Audit.

PTFI has taken positive and affirmative action to rectify the areas of concern that were identified by the International Center for Corporate Accountability (ICCA) in the first phase of the audit. Five major areas were identified by ICCA that required remedial actions:

1. The effectiveness of human rights training, especially in PTFI's Security Department has been considerably enhanced and there is greater understanding of human rights principles and the reporting of potential

- human rights violations. PTFI would need to continue to improve all aspects of human rights training, reporting, and investigations.
2. Transportation of Indonesian security forces in PTFI vehicles. PTFI has ended this practice. As ICCA has noted, PTFI has developed a special driver's training program for all non-PTFI drivers on roads under the supervision of PTFI. Because of the unique driving conditions in areas, difficult terrain, and the specially outfitted vehicles required to traverse such terrain, it is important that all drivers have the requisite skills to protect the safety of all. PTFI management continues to monitor the drivers' training program and the separation of PTFI security personnel and equipment from the activities of security forces of the Government of Indonesia.
 3. There has been considerable progress in integrating Papuans into PTFI's workforce. ICCA noted that PTFI had exceeded its numerical targets for hiring Papuans. However, while PTFI has been making tremendous effort in giving preference to Papuans in its hiring program, it has not made enough progress in retaining Papuan workers. For example, 331 Papuans were hired during the period between November 1, 2004, and July 31, 2006, but 309 Papuans left the company during the same period. Also, ICCA continues to be concerned about the movement of Papuan into more important roles in the company. PTFI takes seriously the commitment to ensure that Papuans are fully represented within all levels of our workforce. PTFI has indicated that it would actively seek qualified

Papuans for every open position, and the company would invest considerable resources on an ongoing basis to help its Papuan employees develop the skills and experience that would allow them to assume increasingly higher levels of responsibility.

Based on its extensive experience with other companies around the world, ICCA maintains that once initial recruitment has been properly made, further progress depends, to a great extent, on on-the-job training, mentoring, and a supportive work environment. Therefore, managers at all supervising levels must be held responsible for developing Papuan employees to ensure that their progress on the promotion ladder is commensurate with their numbers at lower supervisory levels.

ICCA recommends that PTFI continue to include Papuan employee development and promotion as an integral part of management performance evaluation and compensation. A failure to find employees capable of being promoted should be considered a failure on the part of supervisors in hiring, training, and mentoring Papuan employees under their supervision.

This requires that PTFI establish clear targets of achievement to which all department heads are held accountable. These efforts should focus on “targets achieved” and not merely “efforts expanded”. PTFI should create a system of rewards and penalties that would accompany target achievements. Otherwise, if the past is any guidance, the new emphasis is unlikely to deliver on its promise.

ICCA recommends that the success of these programs should be evaluated through a second audit during the period of January-March 2008 to measure their impact in providing more upper level jobs to Papuans and also improve their success in gaining upper level mobility in the jobs currently held by them. This initiative should be made an integral part of the second round of audits of PTFI's facilities and operations.

It should be noted here that in Freeport's agreement to undertake independent external audits, the company had committed itself to making such audits an integral part of their self-assessment and public disclosure on a regular period basis. The first round of audits, by their very nature, was complicated and subject to unforeseen difficulties in audit design and implementation. However, these difficulties have been largely overcome. ICCA recommends that Freeport should maintain a four-year cycle for such audits that would also include its privatized companies.

The Lembaga Pengembangan Masyarakat Amungme dan Kamoro (LPMAK) Education Bureau

In its Phase 1 formal audit of LPMAK's Education Bureau (EB), ICCA found performance deficiencies in almost every aspect of EB's operations. In particular, there was lack of focus on priorities in terms of the critical educational needs of the Papuan community, inadequate long-term planning, poor execution of current programs, inadequate record-keeping, lack of administrative oversight on field operations, poor overall management, and a relative absence of

accountability for performance at all levels of management. This has resulted in loss of accountability for substantial sums of money spent in scholarship programs, poor management of dormitories, in addition to other deficiencies.

ICCA's follow-up audit of the EB revealed that LPMMAK has taken appropriate action in response to ICCA's original findings and recommendations. Sufficient financial and manpower resources have been directed to addressing the deficiencies of the EB. In ICCA's views, these efforts have produced tangible improvements in the activities of the EB.

Organization Structure: Following ICCA's recommendations, LPMMAK reorganized the EB's structure in November 2005. Several functions were consolidated or terminated, which resulted in a streamlined organization, and reduced the number of sub-sections from the original eight to the current four. Nearly all staff members also received special job training. In addition, all employees of the EB now undergo performance evaluations, leading to replacement of some staff members with newly hired people. Performance evaluation is conducted on a regular basis to facilitate productivity and responsibility at the workplace.

Academic Scholarships Program: At the time of ICCA's audit in 2004, the scholarship program was found to be poorly managed. No tracking system existed to verify the status of participating students' and their progress in pursuing program of studies for which they had received scholarship grants. Financial records were often missing. The scholarships were not linked to employment opportunities in Papua.

The EB has completely revamped its scholarship program. There is greater emphasis on the quality of students, relevance of the program to the potential job market, and an insistence on timely completion of degree requirements by the scholarship recipients. The EB has created a new Scholarship Policy Manual. It has tightened application procedures and academic standards. A number of students that did not meet the new requirements were released from the program.

Another important modification in the scholarship system has been the transfer of the application approval responsibility from LPMAC to various accredited universities where students are expected to pursue their academic studies. Educational program approvals have been revised to make them more relevant to the potential business and employment prospects in the Mimika region. EB is also working with the Quality Management Services Department of PTFI to better predict employment needs of PTFI. Data on graduate students is submitted to PTFI's Human Resources Department and other potential employers. LPMAC is also planning to hold regular Career Fairs.

EB has taken steps to facilitate financial transparency of the scholarship program. With technical assistance of the DotNet Company, LPMAC has set up a database to keep track of each scholarship recipient. The system offers a built-in approval mechanism if all necessary requirements are met by students. Two employees (one LPMAC and one PTFI) have received technical training to ensure the database is maintained properly.

Basic Education Programs: A major problem in the Mimika area of Papua is the lack of basic education. This problem is not easily resolved due to certain governmental regulations in the region. All elementary schools as well as teachers and supporting personnel are obliged to receive government certification and approval. This greatly impacts LPMMAK's efforts to develop and support basic schooling.

LPMMAK is looking at ways to increase the quality of schools through establishing partnerships with outside professional and religious organizations. EB is optimistic about establishing professional ties with local government agencies to facilitate basic schooling. The Indonesian government has established a priority in 2006 toward creating basic education programs in rural areas. Local governments are setting up new education programs. Based on this commitment, LPMMAK and PTFI are collaborating with the United States Agency for International Development (USAID), local government representatives, and professional and religious organizations in developing such programs.

Student Dormitories: The conditions observed in the student dormitories during the initial ICCA's visit were one of the major concerns of the audit team. ICCA strongly recommended that LPMMAK take immediate action in improving conditions for the students living in these dormitories, which mostly housed high school age boys and girls. Following ICCA's recommendations, LPMMAK has revised its dormitory standards. However, a large number of dormitories were in such poor condition that their rehabilitation was economically imprudent.

Consequently, five dormitories were closed and six new dormitories are now at various stages of construction. All of the dormitory buildings and supporting structures are expected to meet LPMak requirements. LPMak has also set up a tender system to provide high level of supervision and maintenance of the dormitory buildings. The new system allows independent management professionals, private companies, and churches to compete for best management plan for the dormitories.

Overall Observations and Recommendations

ICCA recognizes the efforts made by all concerned in improving the operations of LPMak's Education Bureau. This is quite important since the Education Bureau accounts for a very large portion of LPMak's annual budget. Moreover, the success of its efforts is vital to the long term improvement in the economic prospects of the Papuan community.

The early phases of the success are largely noted in terms of program planning, initial implementation, and improvements toward eliminating deficiencies noted in the ICCA's Phase I audit. The real test would come when the efficiency of the Education Bureau is measured in terms of results achieved. In the past, LPMak has made similar efforts toward restructuring its Education Bureau with mixed results at best.

ICCA, therefore, recommends that LPMak's Education Bureau should be included in the PTFI's second round audit in 2008. Freeport should also identify various PTFI departments whose program and oversight activities have a bearing

on the success of LPMMAK's Education Bureau. These departments should also be required to establish clear-cut targets of achievement with regard to their actions pertaining to LPMMAK's Education Bureau. ICCA also recommends that these activities should be scheduled for second round audit at the same time that LPMMAK's Education Bureau would be audited.

IV. AUDIT FINDINGS – Part II

Treatment of Contract Workers

ICCA's initial audit had indicated that PTFI was employing temporary workers who were hired through independent contract labor providers. These workers generally worked alongside PTFI's own employees performing more or less similar jobs. And yet, these contract employees were invariably paid lower wages and given lesser benefits in comparison with PTFI's own employees doing similar work under identical circumstances.

A careful analysis of the data pertaining to the hiring, retention, promotion, and treatment of contract workers in terms of wages, benefits, and promotion policies has led ICCA to conclude that PTFI's policies and practices are in violation of the Indonesian employment law and also Freeport's own commitment embodied in the company's Social, Economic and Human Rights (SEHR) policies and Freeport's Policy on Secondment of Managed Contractors' Indonesian Employees to PTFI. ICCA consulted with an Indonesian law firm specializing in labor law to get a legal opinion about Indonesian labor law as it governs the use

of temporary, contract workers. The legal opinion can be found in the appendix of this audit report.

PTFI's Response to ICCA Phase I Audit

PTFI responded to the issue of contract employees raised by ICCA's audit in three ways. First, Freeport stated that "since 2004, [PTFI has] been systematically and objectively evaluating each worker to determine whether he or she meets [PTFI's] current standards for hiring [contract workers] as employees. If a contract worker achieves these standards, the individual [will be] hired as an employee of PTFI."

Further, PTFI stated it "has developed plans to reduce its use of contract labor and to recruit all hourly employees from students that graduate from the Nemangkawi Mining Institute.

Finally, PTFI stated in their response to the audit that the company "has established guidelines which are set forth in [PTFI's] Policy on the Secondment of Managed Contractors' Indonesian Employees to PTFI." This Policy, Freeport asserted "has been recently revised to incorporate new practices and changes in response to the audit's recommendations."

The follow-up audit revealed that has made some progress with regard to contract workers, but that the improvements have been piecemeal and implemented at a very slow rate. These observations were borne-out not only in the follow-up audit, but also in the Phase II audit undertaken almost a year after the follow-up audit and two years after the Phase I audit.

PTFI has submitted evidence to ICCA that it has reduced the number of contract labor providers from six to two to serve its core business units.⁵ This has been accomplished by having work that is not part of PTFI's core business outsourced to local service providers.⁶ These contractors are paid on a unit rate or fixed fee basis.

PTFI's manpower reports state that the overall contracted manpower has been reduced by 13% from year 2004 to 2006.

Years of Service (YoS)	2006	2005	2004
<1	751	377	579
1-3	500	554	450
>3	300	650	760
Total	1,551	1,581	1,789

In addition, as a part of the overall process of contract work elimination, PTFI reports that it is shifting its recruitment from contract labor providers to its development programs (Nemangkawi Mining Institute and the Graduate Development Program).

PTFI has indicated that a new performance evaluation system for non-staff was introduced in April 2006 and is now conducted semi-annually. All contract workers must meet PTFI employment standards before being transferred to PTFI payroll.⁷ In case a contract worker does not meet such

⁵ It is not clear to ICCA as to how a reduction in the number of contract worker suppliers would improve the legality or the contract worker program.

⁶ PTFI would need to clearly define the type of jobs defined that are categorized as non-core jobs and nature of their distinctiveness and seasonality as defined in the Indonesian employment laws.

⁷ On the face of it, this situation seems arbitrary and unjustified. As ICCA has noted in other parts of this report, a large number of contractor supplied workers have been continuously employed for long periods of time with some exceeding 12-13 years. Furthermore, ICCA's audit has confirmed that a large majority of these workers have been employed alongside PTFI's regular employees doing essentially similar work and under essentially similar work environment. Therefore, one must assume that these workers had to be fully qualified. Otherwise, their employment should have been terminated a long time ago since temporary workers by definition had no job security.

requirements, he/she is given another chance to reach the required standards of employment. Non-Papuan workers are generally given six months to meet PTFI's standard, while Papuan workers may take up to one year for such preparation.

With regard to salary, PTFI reports indicate that there is still a significant, although decreased, difference between PTFI employees and contract workers. Freeport has revised its labor agreement with its two labor supply services to reduce management fees and thereby increase contract workers' wages. PTFI states that contract labor wages are determined on the basis of an initial competency assessment given to contract workers. These wages are adjusted upward as the contract workers develop additional competencies. This explanation, however, does not reflect facts as observed by ICCA. PTFI's own data shows that contract workers' salaries, on average, were only 63% of PTFI workers' salaries for comparable work. Even with an increase in pay for contract workers during the period since the first audit, temporary, contract workers are only receiving 73% of the salaries of PTFI employees doing the same work. Therefore, contract workers doing similar jobs are not equally paid compared to their counterparts on the PTFI payroll.

It should be noted here that ICCA has not verified the accuracy of this information or the state of its current and planned implementation. ICCA is simply noting this information as part of PTFI's formal response to ICCA's findings.

ICCA's Response to Freeport's Remedial Actions to Contract Labor Issues

ICCA believes that a satisfactory resolution of the contract labor issue has two dimensions: the first is compliance with the specific provisions of the Indonesian employment laws with regard to temporary (contract) workers. The second one deals with proper and equitable treatment of temporary contract workers who have been disadvantaged by their status within the Freeport system.

ICCA believes that PTFI has not yet dealt fully and effectively with either of the main issues that affect the employment of temporary contract workers. There have been too many programs (which may or may not be effective in changing the way in which temporary contract workers are employed) and too little effort put into actually moving those workers into working conditions that comply with Indonesia labor law and PTFI's internal labor policies. These observations have been reinforced by the results of the Phase II audit conducted by ICCA in December 2006. Although PTFI reports that the company has decreased the number of temporary contract employees who have worked for more than three years from 700 to 300 over a two-and-one-half year period (2004 to 2006), ICCA believes that there is no reason why to number should not have been reduced to zero, considering the seriousness of the issue.

Overall Observations and Recommendations

In making these recommendations, ICCA has taken into consideration the long history of the temporary worker situation, which arose from the conditions

prevailing at the time of the start-up and construction phase of the mine, which required fast ramping-up of the employment. It is also recognized that many of those jobs would be eliminated once the construction phase is completed and the mine is in operation. Notwithstanding, the fact remains that temporary workers phenomenon has become an integral part of the company's operations and has results in causing significant financial harm and loss of benefits accruing from regular full-time employment with PTFI that have rightfully earned.

ICCA feels that Freeport recognize the inherently unfair condition of the temporary workers and take prompt steps that are both fair and equitable to the workers and also adhere to the company's own policies and commitments with regards to human rights and fair employment polices (SEHR).

1. PTFI should establish a small committee under the supervision of a senior HR executive and two independent outside experts knowledgeable with applicable Indonesian employment laws and also worker job-classifications. The committee should also include a member of the Papuan community leadership.
2. This committee would examine each and every job classification to determine whether or not it meets the specific conditions permissible for the hiring of temporary workers under the pertinent Indonesian laws. The task of the committee would also include "outsourcing" jobs to ensure that these do not become a back-door method of continuing with violation of temporary worker employment policies.

3. All decisions made by the committee with regard to job-classifications would be fully transparent and made public.
4. PTFI would also set up an appeal process that would allow workers an avenue for seeking redress for unfair treatment.
5. PTFI would suspend any new hiring of temporary workers unless the new system has been set in place and is fully operational.
6. With regard to current temporary workers:
 - (a) PTFI would take immediate steps to transfer all the temporary workers to the PTFI payroll who had been in continuous employment with PTFI and also with its affiliated privatized companies. For these workers, there can be no competency test or “fitness for job” requirement.
 - (b) PTFI would take immediate measures to calculate the “loss of pay” for these workers beyond the three-year period on basis of what they would have earned had they been in the employment of PTFI as full time employees. PTFI would ensure that all these workers receive the appropriate amount of compensation together with a reasonable rate of interest for lost income. This process should be completed as soon as possible but no later than December 31, 2007.
 - (c) For workers with tenure of less than three years, PTFI would endeavor to determine their eligibility for regular, full time employment. The criteria for determining such eligibility would

also be subject to the approval of the aforementioned committee; allow for worker appeal; and be fully transparent. PTFI would also make every effort to provide training and otherwise help these workers to acquire the necessary skills and thus become eligible for full-time employment with PTFI.

- (d) Notwithstanding, the issue of continued employment, these temporary workers would be entitled to receive the “back pay” plus accrued interest for the wages lost due to pay differences between temporary and regular workers doing essentially similar work and essentially similar work environment.
- (e) In all situations described above, the burden of proof would be on the company to demonstrate as to the lack of eligibility on the part of a single worker or a group of workers.
- (f) Any worker, who is unhappy with the committee’s decision, would have the right to appeal to the head of PTFI’s Human Resources Department.

7. Once this process is complete and has been so certified by Freeport, there should be a formal audit to ensure the implementation of agreed upon ICCA’s recommendations by Freeport and PTFI. The findings of such an audit would also be a matter of public record.

Chapter 2

Public Health and Medical Care

Scope of the Public Health and Medical Care Audit

This audit report is part of Phase II audit of the mine site facilities and operations of PT Freeport Indonesia (PTFI), and also a number of privatized companies affiliated with PTFI that provide specialized services to PTFI at the mine site and the surrounding community. This field audit was carried out at the mine site on December 6, 2006.

The focus of the ICCA audit of PTFI's public health and medical care is limited to the communities surrounding the mine site and, in particular, members of the 7-sukus. This audit does not cover PTFI's employees and those of the privatized companies. These are covered under PTFI's contract of work with the Indonesian government.

PTFI has had a long history in creating disease-prevention infrastructure and providing for the health maintenance and curative care for its employees; the Papuan community surrounding the mine site and its ancillary operations in general; and, those of the 7-tribes (sukus) in particular. This commitment has been driven by three sets of factors.

1. Physical environment surrounding the PTFI's operations is a fertile breeding ground for water and airborne diseases e.g. malaria, tuberculosis, diarrhea and upper-respiratory diseases, and, of late, HIV/AIDS; a population that has little experience with disease control and

- prevention; and where caring for the health of the local population is a continuing challenge.
2. The living conditions and poor hygiene in the local communities are further exacerbated by unplanned growth, people migration, and higher population densities than could be supported by the previously scattered and thinly populated village structure of the Papuan tribes.
 3. The rudimentary character of healthcare provided by the local government bodies has always been inadequate and has become even more so with the increasing demand from the growing community.

In many ways, the public health and preventive care efforts for the community inter-mingle with those undertaken directly by the company in its contract of work area. This is a natural and desirable outcome because water and airborne parasites are not constrained by artificial boundaries. Similarly, given the extent and somewhat stretchable definition of extended family among the Papuan tribes, PTFI's employee-oriented medical facilities often become an extended back-up support system for the company's programs intended for the non-employee Papuan community.

This audit report provides ICCA's findings and overall assessment of three aspects of the public health and medical care programs in the areas surrounding the mine site, facilities covered by its ancillary and affiliated operations, including the burgeoning township of Timika. The three program elements covered are:

- (a) Public Health, Health Education, Malaria Control, and Community Health Centers;

(b) *Ruma Sakit Banti* – Banti Hospital; and,

(c) *RS Mitra Masyarakat* - RSMM Timika Hospital.

ICCA's Audit Procedures and Protocols

ICCA's audit of LPMAK's public health and medical care policies and programs followed procedures and protocols that were similar to those applied in all others aspects of ICCA's audit of PTFI's operations. They are designed to undertake a thorough analysis and evaluation of management policies, decision-making systems, and operational procedures and practices. These generally take the form of Management Compliance Report (MCR) where the facility's management is requested to provide in considerable detail its self-description and analysis of company operations. Every effort is made to understand and appreciate the explanations and assertions made by the senior and operating level managers of the audited unit as to the successes achieved and the challenges still to overcome; their plans for corrective and remedial action; and, the resources they would need to achieve their objectives. ICCA's professional staff undertakes a thorough analysis and evaluation of the MCR's content in preparation for the field audit.

The field audit is comprised of three parallel activities. The first one includes meetings with the management to clarify any statements or data provided in the MCR which needed further explanation. The second aspect of the field audit is on-site visit carried out by a team of ICCA's professionals. In the current instance, ICCA's audit team was augmented by Dr. Emon Winardi

Danudirgo, a specialist in internal medicine at Saint Carolus Health Services - a 543 bed hospital – located in Central Jakarta. Dr. Danudirgo is an internist at St. Carolus. It is a 543 bed hospital, which is located in central Jakarta. Dr. Danudirgo had also worked for the Ministry of Health in Papua (Irain Jaya) from 1986 to 1990 and is quite knowledgeable about Papuan medical issues. The on-site visit covers a thorough examination of all physical facilities and how they are being operated when measured against relevant benchmarks and/or standards established by local government and regulatory authorities and accepted by all concerned as the appropriate standards for performance evaluation.

The third aspect of the field audit includes an analysis of data gathered through detailed, confidential one-on-one interviews with a randomly selected representative sample of the population, which is the intended beneficiary of these programs. Creating a representative interviewee sample of the community presented some unique challenge. The communities involved did not have any method of identification along the lines of street names or house numbers. The character of individual families and number of family members in a household also constantly fluctuated. Therefore, the selection process focused on:

- (a) Interviews with members of households in communities that were domiciled by Papuans and especially members of the 7-sukus.
- (b) People selected to be interviewed had made use of various healthcare facilities during the previous six months.

(c) Interviews were conducted on location where the interviewees actually lived; the interviewee was the head of the family, and, was generally surrounded by family members.

(d) Interviews were conducted by Papuans (university teachers and graduate students) and included both male and female interviewers. These interviewers were familiar with the culture and dialects of the people to be interviewed and were able to develop excellent rapport with them.

Briefly described, the interviewee group consisted of 91% Papuans and 9% Non-Papuans. Among the Papuans, 53% were Amungme, 43% Kamoro and the remaining 4% belonged to other tribes. Male interviewees accounted for 81% of the group with an average age of 35 years for males and 25 years for females. For the most part, interviewees were married (91%) with 3.4 children per family.

A very large majority (86%) reported to have been sick at least once over the previous six months and when sick, 96% of them had sought medical help. Among the illnesses most reported by the interviewees were: Malaria (75%), Diarrhea 30%, Headache (25%), Coughing (20%), and Fever (15%).⁸

⁸ A large number of interviewees reported multiple incidents of illness for which they sought medical care.

Challenges for PTFI in Developing Public Health and Medical Care Programs

From its very inception, PTFI recognized that it must address the community public health and medical care problems both as a matter of necessity to control the spread of disease in the communities surrounding the mine site, and to protect the health and well-being of its potential pool of workers. Equally important, PTFI had recognized its responsibility in dealing with the Papuan community's general health and medical care problems as a matter of good corporate citizen.

The scope of magnitude of PTFI's commitment is quite unique among such healthcare programs supported by multinational corporations anywhere in the world. Available data show that over the past ten years, PTFI has provided approximately \$100 million through the Freeport Partnership Fund for the buildings and operations of hospitals, community health clinics and related facilities. On a continuing basis, the Freeport Partnership Fund has provided nearly US\$8.0 million per year the LPMAC (the local community organization that manages the programs funded by the Freeport Partnership Fund) to support two hospitals and a public health program for the residents of the Timika and Banti areas in West Papua.

LPMAC, with the support of PTFI and International Security Overseas Services (ISOS/AEA), has established management structures for the administration of curative and public health initiatives. Medical facilities have been built and are being properly maintained. Professional staff has been

recruited and numerous health care and health education programs have been established. These facilities and programs make available to all residents with low cost medical care; and for the indigenous Papuans from the seven sukus, this care is provided virtually free of charge. ICCA's field audit has confirmed as to the net effect of this effort in terms of improved healthcare facilities for the vast majority of Papuans living in Timika and the communities surrounding PTFI's mine site. ICCA's audit has noted that PTFI's activities in this context are not legally mandated. PTFI's Contract of Work requires the company to provide medical care for all of its employees, dependents of 'family-status' employees, and government employees assigned to PTFI's operations' area. Notwithstanding, PTFI has been providing emergency medical care to local residents, since the inception of mining operations in 1972.

In 1992, when PTFI was expanding its operations after the discovery of the Grasberg deposit, the company expanded its public health programs to cover malaria control, including out-patient treatment for those infected with the parasite in indigenous communities that were in close proximity to PTFI's residential and work sites. PTFI was concerned that endemic malaria in areas surrounding PTFI's facilities would endanger the health and well-being of employees and their dependents. These programs have been recognized to be amongst the most effective in Southeast Asia and the Pacific.

Organizational and Financial Oversight of Public Health and Medical Care Programs

All PTFI supported programs intended for the benefit of the Papuan community in general, and the 7-sukus in particular, are funded through Freeport Partnership Fund, which is managed by a Papuan organization called the Amungme and Kamoro Community Development Institute (LPMMAK). The LPMMAK was established in 2001 for the express purpose of managing the funds that PTFI agreed to make available to the local community to aid PTFI's neighbors in developing community health, education and infrastructure. The LPMMAK gives a strong voice to the two indigenous Papuan groups in PTFI's area of operations. All indications are that the LPMMAK is gaining capacity to manage not only the Freeport Partnership Fund, but also the rapidly changing social and political world in which LPMMAK operates.⁹

Healthcare and Education Programs constitute the two largest programs supervised by LPMMAK. For example, in 2004 total spending on all healthcare programs accounted for approximately 30% of LPMMAK's budget. It was increased to 36% of LPMMAK's budget in 2006 and is projected to increase to 42% in 2007.

LPMMAK is governed by representatives of the Papuan community and operates relatively independently in terms of program priorities and funding allocations. This has been both its strength and its weakness. The strength lies in its responsiveness to the community while its weakness emanates from its

⁹ For further details on the organization structure, programs and policies, and operations, please see ICCA's PTFI Phase I Audit Report: www.ICCA-CorporateAccountability.org

relative inability to make operational decisions unaffected by socio-political factors based primarily on objective and efficiency driven considerations.

In the case of healthcare programs, LPMAK's decision-criteria are almost entirely allocative, i.e., LPMAK responds to annual funding requests from individual operating units, i.e., Public Health, Health Education, and Malaria Control; Satellite Clinics and Community Health Centers; *Ruma Sakit Waa-Banti* (Banti Hospital); and, *RS Mitra Masyarakat* (RSMM Timika Hospital). The budget allocation becomes a negotiating process where the relative influence and bargaining power of the operating units determine the outcome of the allocation.

When it comes to public health and medical care programs, a similar situation prevails. To wit, LPMAK does not employ independent expertise with which to evaluate the relative contribution of each preventive health and medical care program in the context of overall health and wellness of the entire community. Instead, it reviews budgetary needs of each program as if these units were stand alone entities and operate without any consideration of how their actions would impact other program entities, and even more important, the standard of general health of the entire community. This approach often results in unintended negative consequences to their intended purpose. For example, it is universally recognized that measures of preventive healthcare are least expensive and most effective in improving the overall quality of wellness in the Papuan community. And yet, while most healthcare programs had increased their budget allocations, public health and malaria control program actually recorded a decreased allocation, i.e., its funding level declined from nearly

US\$353,000 in 2004 to US\$120,000 in 2006 – a loss of almost two-third over a 2-year period.

Overall Observations and Recommendations

1. LPMMAK should retain the services of an experienced medical professional with a comprehensive and objective perspective to establishing the overall level of community wellness that it aims to achieve over a 5-10 year period and how this objective might be translated into yearly targets.
2. Budgetary allocations of all operating units must be considered in the context of LPMMAK's overall community wellness targets. In particular, operating units should be required to provide trade-off values between budgetary allocations and the individual unit's contributions to the community wellness goals.
3. Individual operating units must be held responsible for delivering on their performance targets in terms of their own operations and also their contributions to the community wellness targets.
4. System of data collection and analysis should be established to generate information that goes beyond book-keeping and instead becomes a management tool for informed decision-making.

Public Health, Malaria Control and Community Clinics

Public Health and Malaria Control (PHMC) has two functions and is dually managed. One function is to provide public health activities directly for PFTI, its employees and their dependents. This function is funded by PTFI and managed by PTFI and ISOS/AEA. The other function of PHMC is to provide public health activities to local communities in the area of PTFI's operations. In this case PHMC is managed by LPMMAK and operated by ISOS/AEA. Hence, PHMC has a complex structure. The ICCA audit did not cover the PHMC operations for PTFI's operations. The audit looked only at PHMC activities provided for the local community and the relationship of PHMC with the two curative care facilities that are managed by LPMMAK.

These activities are the first-line of defense against water and airborne diseases, and diseases emanating from poor hygiene and improper waste management. Operating under inhospitable environmental conditions, a mining operation like PTFI must build and maintain disease control systems to protect the community and also ensure the availability of a healthy pool of workforce.

PHMC works on a wide range of public health issues that are relevant to the community and the employees located at the mine site. Historically, the department's most important activity has been the integrated malaria control within and outside the area of operations. PHMC's role in the area of public health has since been considerably expanded. Basic health services are now provided to a number of sponsored communities, and a TB control program and an STD/HIV control program are operated by PHMC. The environmental health

section of the department works mainly with food safety and water quality for employees but has had significant input into the provision of clean water to local communities. All of these activities are supported by active health education and health promotion activities.

Overall Observations and Recommendations

ICCA confirms that PTFI has fulfilled all its financial and human resources support commitments toward community health that the company made in its *Social, Employment and Human Rights Policy* (1999, rev. 2001), and in the *Guiding Principles for Indonesian Operations* (2003). The audit found that PTFI's Social and Local Development Department (SLD) has provided professional guidance to the Health Committee of the LPMAC in a sensitive and caring way. The audit further found that the professional medical care providers, the Yayasan Caritas Timika (YCT), which operated the RSMM in Timika, International SOS/AEA, which operates the Banti Clinic and PTFI's Public Health and Malaria Control, which provides public health services to PTFI and to the local communities to be deeply committed to the health of the local population. The audit also indicated that, by-and-large the local community in this positive assessment of PTFI, LPMAC and their agencies providing public health and medical care services.

ICCA's audit team also noted specific areas where significant achievements occurred in reducing the impact of various diseases and in improving the level of wellness among the people and communities involved. At the same time, ICCA's audit team observed a number of areas where better

planning and efficient implementation should yield further improvements in the community health and well-being. Finally, ICCA noted some elements of institutional arrangements and tasks management where a substantial redirection of resources and renewed focus in addressing certain issues would be necessary.

Health Program Initiatives

Public health initiatives in the local communities are centered in the primary care clinics in villages that are on the outskirts of Timika. Public health workers canvas individual households in villages to seek-out people who are sick. For those who show potential signs of malaria, blood smears are taken and analyzed at the local clinic. Where the tests for malaria are found to be positive, the public health worker further conducts additional tests and analysis. Anti-malarial medications are provided as necessary. Where tuberculosis is suspected, a sputum test is administered and if the results are positive, the patient is referred to the tuberculosis center (jointly administered by the government health services and PTFI's Public Health Department) in Timika. If, in the judgment of the medical personnel at the tuberculosis center, the patient required hospitalization, the patient is transferred to the RSMM. The Public Health and Malaria Control Department also seek out potential cases of HIV. The government health services and PTFI's Public Health Department jointly operate a sexually transmitted disease center in Timika where patients suspected of suffering from HIV and other sexually transmitted infections can

receive treatment. In the near future it is expected that the government will begin providing anti-retroviral medications for those who have contracted HIV.

Another role played by PHMC in the local communities is the control of the malaria vectors. This is accomplished through the elimination of standing water by placing larvicide in places in where anapholine mosquitoes breed and, when necessary, spraying residential areas when there is an outbreak of malaria. Beyond these normal public health activities, the Public Health Department has also been active in malaria research, partnering with the World Health Organization and the Menzies School of Public Health (in Darwin, Australia) in clinical trials of new malaria medications.

The senior management of PHMC considers the current program to be adequately staffed and financed. The department is in the process of strengthening its ranks of professional/medical staff. The department has employed a significant number of Papuan community health workers (public health men and entomology crews) and enjoys strong external (research and training) participation in programs, mainly from the national institute of health research (LitBangKes) and Menzies School of Health Research. Staff satisfaction is strongly related to job security and compensation levels. PHMC claims to receive high marks for patient satisfaction because of its emphasis on quality care and the fact that its staff is adequately compensated and highly motivated. However, as we note in the latter part of this action, this assertion is not fully supported by the community members interviewed on site by the ICCA audit team.

ICCA's analysis of quality and dispersion of services, however, suggests that the PHMC staff and facilities are not efficiently distributed throughout the area. The farther away from the densely populated areas around Timika, the more likely there is to be an active public health program. While there is some logic behind this placement of public health resources, a strong case can be made that equal public health (or, most probably) greater public health challenges exist in the villages contiguous to Timika and within Timika itself. It is presumed that people closest to Timika have access to the hospital and curative care. However, the downstream medical care given at the hospital is expensive and because the hospital is still quite a distance from many villages close to Timika, people are less apt to seek medical care early when a lengthy trip is required to reach the hospital.

ICCA's analysis also suggests that PHMC has not fully embraced the notion that health education must be a major part of its priorities. Although, there are some good public health education programs currently in place; it is also apparent that these program do not give enough emphasis to the fact that it is more desirable for a person to be healthier and thus require less curative care. ICCA's audit team considers this lack of emphasis on comprehensive health education to be a lost opportunity for all parties and especially the local community.

Interviews with community members have provided a decidedly mixed picture about their experience with PHMC. There is a credibility gap between the PHMC's self assessment of community's satisfaction with its services, and the

level of satisfaction reported by the community members in interviews with ICCA. When asked as to how many visits were made by the public healthcare staff during the previous six months, 6% indicated healthcare staff visits of once a week, another 6% indicated twice a week, and 3% indicated once a month. The sporadic and inconsistent nature of healthcare staff visits also reflected poorly on the overall level of satisfaction with the public health staff, which was rated at 2.85 on 5-point scale with 1 being highly dissatisfied and 5 being highly satisfied.

In conclusion, the audit team believes that the successes of the Public Health and Malaria programs do not go far enough and must be enhanced if PTFI and the community is to gain benefits from an increase in the preventative care and wellness program.

1. Health education must become a more important element of the PHMC department. It should be carefully organized and monitored to ensure maximum outreach and to measure learning and retention of educational elements on the part of the recipient community.
2. Programs for community healthcare visitors and establishment of additional healthcare clinics should receive a major infusion of new funding. It is important that these programs are carried out and monitored with the intensity of planning and implementation similar to the one currently applied to Malaria control. Otherwise, a redirection of resources from curative to preventive care will not succeed.

3. The PHMC department must enhance its data collection and analysis to monitor the trends not only in disease control, but equally important, on the levels of community well-being. For example, although copious statistics have been collected over the past years about malaria, tuberculosis, mother and child health, and, of late, about HIV/AIDS; there has been no attempt to show the effect of public health initiatives upon morbidity and mortality in the communities served. Therefore, no one can show whether the overall health of the communities is really better, and if so, how it relates to the enormous outlay of funds on public health initiatives.
4. PHMC should consider launching two longitudinal studies to track its efforts in improving the overall health and well-being of the community.
 - (a) It should monitor groups of infants through the first five years of their lives. This would include, any other types and frequency of illnesses, weight gain/loss, infant mortality rates, and how children born at one time period (t_1) compare with children born at t_2 and t_3 , etc., over a 5-year period.
 - (b) It should collect regular data on deaths, including age, sex, causes of death and other relative factors that would denote the overall level of community health well-being as indicated through mortality statistics.

5. ICCA would strongly urge that PHMC should immediate measures to realign its staff and resource allocation priorities along the lines indicated on this section. We also recommend that LPMAC and PHMC secure short-term services of one or more professional experts to implement these recommendations.
6. ICCA recommends that these program changes should be fully implemented by the end of 2007. ICCA would like to include a review of this progress in these and related areas in the proposed follow-up audit visit during the period January – May, 2008.

RSWB (Banti Hospital) – Highlands

The second largest unit in overall LPMAC Healthcare Program budget allocation is RS Waa-Banti Hospital (RSWB). On average, RSWB receives 20% of the total Healthcare budget with an annual increase in the budget allocation of 5%.

Banti village is located approximately five kilometers from PTFI's residential and administrative site of Tembagapura. Banti's residents, for the most part, are members of the Amungme tribe, which is the group that has resided in the area of the mine for a number of generations. Although, Banti has grown substantially since the inception of mining by PTFI in 1972, it has not seen the rapid and unrelenting growth that has been characteristic of Timika over the past decade.

Banti is located at approximately 6000 ft above sea level and has a temperate climate. It has different disease vectors than the lowland villages have. Malaria is seldom transmitted in Banti. However, since there is now regular movement of people between Banti and Timika, cases of malaria are found in the community. Banti is very damp and has over 250 inches of rainfall each year. Therefore, there are many cases of upper-respiratory infections that require treatment. In the past few years there have been cases of HIV in Banti and the surrounding areas. Because of movement of people between Banti and Timika, it is expected that the incidence of HIV and AIDS in Banti will continue to increase.

Historically, Banti has had a clinic, operated by PTFI and/or PTFI's medical services provider, ISOS/AEA. During the late 1990s and early 2000s, the clinic referred many cases to PTFI's Tembagapura hospital, which was intended to provide medical services to PTFI employees and their dependents. Because of overcrowding at the Tembagapura hospital, PTFI decided to expand the Banti clinic to provide in-patient care. In 2002, the expanded Banti clinic became the Banti hospital. RSWB is a 74-bed hospital located in Banti. The primary task of RSWB is to provide health services to the members of the 7 tribal communities residing in the highland regions of Mimika and to reduce their reliance on PTFI's Tembagapura hospital. RSWB hospital runs a nutrition program for all malnourished children who are hospitalized, a maternity care program (Mother and Child Health), an immunization program, pre-natal care, and family planning and micronutrient supplementation programs. The hospital

operates a special program for handling tuberculosis patients. Infected patients are provided with direct treatment, observation and supervision. The hospital tracks down and conducts medical check-ups of the suspected people who have been in contact with tuberculosis patients. In addition to curative programs, RSWB hospital has a health education program that offers information on children's health, infectious diseases etc. Over the last few years, the facility has grown to provide larger scope of medical services, including out-patient and in-patient services, emergency room, laboratory, x-ray, and referral to Tembagapura hospital for severe medical problems, surgery and childbirth. The Banti hospital does not have facilities for acute care. In cases where acute care is required, patients are referred to the Tembagapura hospital or the RSMM.

Unlike RSMM, which is administered and staffed by YCT, the Banti hospital is administered and staffed by ISOS/AEA. LPMK and ISOS/AEA have a contract which provides for ISOS/AEA oversight for the Banti hospital until December 31, 2009.

Physical Facilities and Personnel

The in-patient department of the Banti hospital serves on average 250 patients from the 7 tribes each month. Of these, the majority (about 230 patients) is treated in the General ward, and about 15 to 20 patients receive treatment in the Tuberculosis ward.

The hospital's self-assessment of staffing levels report that the number and distribution of medical and support staff is satisfactory. In general, hospital

management believes that there is sufficient staff allocation in all of its units, while some extra personnel would be helpful in administrative section, out-patient reach, and general ward.

Physical Inspection of the RSWB Medical Facilities

The ICCA audit team visited the Banti hospital during one of its busiest times of the day when medical and support staff were involved in the evaluation and treatment of patients. The hospital was teeming with patients, including many children. The audit team had a number of immediate impressions. First, the hospital was bright and clean. A custodial crew was at work throughout the visit. Unlike the RSMM, which is built in pods with long walkways between units, the Banti hospital is compactly built. Second, the staff appeared to be positively involved in patient care. There were no complaints about the physical condition of the hospital facility and the work conditions.

ICCA's audit felt that Banti benefited from its reliance and support from the medical staff of PTFI's Tembagapura hospital, including access to an experienced, professional medical administrator. Further, and unlike the case with RSMM, the Banti clinic also enjoyed access to medications and other group purchasing agreements through ISOS/AEA. ICCA's medical consultant noted that the Banti hospital was superior in facilities and medical services rendered to the average private and government hospitals in Indonesia.

Banti hospital serves a more critical community need when compared with the lowland Timika area. There is little public health available in and around the

Banti area. The medical staff noted, as had the medical staff at the RSMM, that a significant part of their patient-load comprised of patients with diseases and/or conditions that could have been addressed by health education, disease prevention and/or village-based primary care medicine.

LPMMAK is starting to institute some public health programs in the Banti area and ISOS/AEA has agreed to support these efforts, which is a salutary development.

Papuan Assessment of Services Provided by the Banti Hospital

Among the Papuan community members interviewed by ICCA, approximately 50% stated that either they or one of their family members had received treatment at the Banti hospital. Interviewed respondents' views of the quality of service and facilities were quite mixed. When asked their views as to the overall quality of services provided to patients at the Banti hospital, the respondents rated the Banti hospital at 2.6 on a scale of 1 to 5, where 1 indicated highly unsatisfactory and 5 highly satisfactory. Their ranking as to the attentiveness of the medical staff was even lower at 2.2. When asked about the quality of services in different hospital units, they ranked in-patient and out-patient services at 2.6 and emergency services at 2.9.

This situation is quite ironical due to the fact that ICCA team's own expert considered the Banti facilities to be far superior to the RSMM hospital at Timika. ICCA's expert also considered the resource availability and services provided to

patients at Banti to be of higher quality when compared with similar facilities at the RSMM hospital.

Major Challenges

The management of the hospital offers several possible explanations to this state of affairs. According to the Banti Hospital's senior medical staff, most of the problems that occur between the hospital and its patients had to do with poor communications. They contended that quite often patients would not recognize the seriousness of their illness; they would refuse hospitalization; and, would not show-up for the medical appointments. In many cases, there was literally a language barrier between the patients and the medical staff. Many patients would insist on being referred to the larger hospital in Tembagapura, although their medical needs could be easily met by the services offered at Banti.

There are other possible explanations for which parallels could be found in other localities experienced by ICCA. The first one has to do with the level of expectations, which are built either on what is currently available or what is perceived to be available by the user in comparable situations. Papuan patients at the Banti hospital had knowledge and familiarity with the Tembagapura hospital, which they perceived – rightly or wrongly - to be far superior to the Banti facility. Second, the Banti patients had become used to a higher level of service and thus would take it for granted and thereby expect constant improvement. Third, the situation is also afflicted by the condition of infinite demand. Since the Banti patients receive all medical services free of charge, they have little concept

of what it costs to provide such services and therefore do not consider it unreasonable to demand a continuously higher level of service.

The challenge for the Banti hospital and the LPMMAK lies in the element of education. In the current scheme of things, curative services are considered entitlements, which must be made available in ever increasing quantity to the entitled group. However, under the framework of “wellness” as espoused in an earlier section of this report, hospital visits would be seen as a failure of the “wellness program”. In other words, the best solution, and perhaps the most viable solution to the rising health care costs – which are not necessarily related higher level of wellness – would promote good health and reward people for having improved health and not needing hospital care. Clearly, health-related public education and general conditions of healthy living should receive priority in the Papuan community’s public health and medical care programs.

RS Mitra Masyarakat – RSMM Hospital

RSMM (*RS Mitra Masyarakat*) Timika hospital was built with funds provided by PTFI in 1998. The building of the hospital was preceded by civil unrest in 1996, which took place in and around the PTFI operational area. Responding to some of the community's concerns, PTFI expanded and transformed its outreach programs including its health-related activities for the local community. In consultation with the Government of Indonesia and leaders of the local community, PTFI helped to expand the public health programs that had begun several years before and planned a hospital in the rapidly expanding Timika area.

RSMM is the primary curative care medical facility in the lowlands area of Kabupaten Mimika. It is located in the outskirts of the city of Timika, which is a primarily urban community with an estimated current population of over 100,000 people and growing at the rate of 15% a year. RSMM's primary responsibility is to serve the medical needs of the Papuan people. These account for approximately 50,000 or one-half the population of Timika. All Papuans receive low cost medical care at the RSMM. Papuans from the seven tribes (*sukus*) that border PTFI's area of operations, receive medical care that is virtually free of charge. The majority of the Non-Papuan Indonesians in the area do not choose to go to the RSMM, preferring to receive medical care from the approximately 20 private physicians who have set up practice in Timika. The RSMM has 100 beds. In addition, it provides emergency and out-patient services. The hospital is in the process of seeking certification from the Ministry of Health as a "class 'C'

hospital.” As a “class ‘C’ hospital” RSMM will be required to have medical staff certified in internal medicine, pediatrics, surgery and obstetrics/gynecology. At present RSMM does not have a fully functional internal medicine specialty and the surgical procedures are limited by the lack of a full-time anesthesiologist.

Physical Facilities and Financing

RSMM’s almost entire budget is paid for by the Freeport Partnership Fund, which is controlled and managed by LPMAC. RSMM is the largest component in LPMAC’s Healthcare Program budget. In 2006, RSMM budget accounted for over 52% of LPMAC’s total healthcare budget. According to the data provided by RSMM, the hospital’s operational budget in 2004 was US\$4.2 million and was projected to increase to US\$4.6 million in 2007, representing an increase of 9.5% over a 3 year period.

The chief medical officer of the hospital is also responsible for overseeing the financial (budgetary) aspects as well as physical plant maintenance. This is highly unusual for a facility of this size and places an inordinate burden on the time, resources and abilities of the responsible individual. Data provided by the hospital administration indicates that, RSMM has had significant growth in its personnel at all levels, which is consistent with the sharp increases in its budget as previously indicated. Table 2.1 shows that RSMM’s overall staff levels increased from 275 to 316 in 2 years – an increase of 15% and are projected to increase further to 353 or an overall increase of 28% over a three year period.

Notwithstanding, this encouraging scenario of financial resources and an expanded medical staff and support personnel, the hospital management's self-assessment paints a rather discouraging picture of its resource-capabilities when compared with the current and future demands for its services.

Table 2.1

Profile of Administrative, Medical and Professional Staff

	2004 (actual)	2005 (actual)	2006 (current)	2006 (projected)	2007 (projected)
Medical Staff	13	14	17	18	18
Nursing Staff	128	147	146	156	169
Medical Support	36	34	37	37	42
Non-medical Staff	98	104	116	116	124
Total	275	299	316	327	353

According to the self-assessment provided by the hospital's management:

(a) The hospital is overcrowded and cannot cope with linearly increasing load of patient activity. This over-crowding has been persistent since 2003 and the hospital has not been able to accommodate linearly increasing loads of activity. Current physical facilities are not up to the medium-sized hospital standards.

- Hospital wards and rooms are overcrowded and at times patients have to be treated in the corridors or outside the building.
- Not fully recovered patients have to be discharged from the hospital, because new patients are lining up.
- There are no separate rooms for male and female patients.

- Patients with and without infectious disease are not separated causing frequent instances of nosocomial infection.
- (b) The hospital suffers from insufficient funds, lack of long-term dependable funding and a rigid budget system, which limits management/employee’s initiative and innovation/creativity; and,
- (c) At present, the management activities at the hospital revolve around routines that are short term/survival oriented. The hospital’s long term development is uncertain and unclear.
- (d) Finally, the hospital management’s own assessment of the current (2006) adequacy of staffing provided in almost all aspects of its operations is “generally not sufficient” or “completely insufficient”. These observations on the part of RSMM’s management are summarized in Tables 2.2 and 2.3.

Table 2.2

Current (2006) Quality of Staffing at RSMM Hospital

All Hospital Staff	Generally Insufficient	Completely Insufficient
Administrative Staff		X
Medical Staff		X
Other Professional Staff		X
Other Professional Non-Staff		X
In-Patient Services		X
Administrative Staff		X
Medical Staff		X
Other Professional Staff		X
Other Professional Non-Staff		X
Out-Patient Services	X	
Emergency Services	X	

Table 2.3

**Quality of Physical Facilities at RSMM in Relation to
Patient's Current and Future Needs**

A. Patient Service Facilities		<i>Current</i>	<i>Projected</i>
Special Depts./Hosp. Wings		Unsatisfactory	Unsatisfactory
In-Patient Services	Maternity Ward	√	√
	TB Ward	√	√
	General Ward	√	√
	Pediatric Ward	√	√
	Internal Ward	√	√
	Surgery/Operation Ward	√	√
	High Care/ Intensive Care	√	√
Out-patient Services	General Polyclinic	√	√
	Special Polyclinic	√	√
	Medical Check Up	√	√
Emergency Room	√	√	
B. Administrative Facilities			
In-Patient Administration		√	√
Out-Patient Administration		√	√
Emergency Room Administration		√	√
Preventive Care Administration		√	√
C. Staff Housing Facilities			
Admin. Staff Housing:		√	√
Medical Staff Housing:		√	√
Other Professional Staff Housing:		√	√
Other Professional Non-Staff Housing:		√	√

Physical Inspection of the RSMM Medical Facilities

ICCA audit team found the hospital's building design to be a challenge in providing optimum medical care. The hospital is set up in pods connected by long, exterior hallways. Hospital management suggested that the design of the hospital was acceptable when the hospital was first built, but increased use of the hospital over the past few years has presented medical and logistical challenges. Although the architecture is pleasing to the eye, it leaves interconnected medical personnel and procedures distant from each other. For example, patients leaving surgery must be transported to a different pod for post-surgical recovery; more importantly, if a post-surgical patient has a medical crisis, the patient must be wheeled quite a distance to be returned to surgery.

This is only one of a number of examples of how less-than-optimum planning of the hospital's architecture makes patient care difficult and complex. Another example of how hospital architecture negatively affects patient care is that when a unit is overcrowded, it is not easy to 'borrow' space from another unit, since each unit is self-contained in a pod. At times the medical staff reports that highly infectious patients have mingled with other patients in a way that is harmful to the well-being of both patients. The inflexibility of the pod-architecture has also compromised privacy by placing patients of different genders in the same rooms for treatment.

Unfortunately, there is no easy solution to the problem of poorly designed hospital building. Moreover, as we would explain in a later section of this report,

our analysis indicates that an extension of the facility to alleviate overcrowding is not a feasible, practical or even a desirable solution.

There is also a medical 'unknown' that must be noted. The local government (Kabupaten of Mimika) is in the process of building a 200+ bed hospital south of Timika. The building is most impressive and the unofficial word around Timika is that the hospital will open in 2007. The other word around Timika is that there is no budget to purchase equipment and operate the hospital. If the hospital opens and provides reasonably good medical services for the people in Timika, the entire dynamic of the health and medical care in the areas around PTFI's operations would change. However, the history of government-provided medical care in Timika (and elsewhere in Papua) is not good. There is no certainty as to whether and when the hospital will open and the extent to which meet the community's projected medical care needs.

Operational Issues

In meetings with RSMM's medical and administrative personnel, ICCA's audit team and medical experts found that the medical and administrative personnel were committed to the provision of professional medical care for the people in the communities serve by the hospital. Nevertheless, the administrative procedures, when combined with poorly planned and constructed physical facilities, have given rise to further operational problems which require prompt attention on the part of the hospital's medical and administrative staff.

RSMM's chief medical officer also serves as its top administrative officer. This is a burdensome responsibility and distracts him from giving full attention to the medical aspects of RSMM. The two jobs require different types of management expertise and operational skills. A more decentralized and focused organizational system would most likely improve operational efficiencies. It would also enhance transparency, accountability and performance evaluation.

It was further noted that during the audit team's visual inspection of the hospital (which was done during a light patient load), the cleanliness of the facility was not up to acceptable Indonesian and international standards. In comparison with PTFI's hospitals (at Tembagapura and Kuala Kencana) and the Banti Hospital (funded by LPMK and operated by ISOS/AEA), RSMM was far less clean than the other facilities. The lack of general cleanliness at the RSMM raised questions whether proper sterilization and infection control was being practiced at the hospital.

ICCA's team also confirmed the existence of many problems pertaining to patient care – in addition to insufficient cleanliness – that have the potential of causing adverse medical impact on the patient population. These problems were also recognized by the hospital's senior medical and administrative staff and have been referred to in an earlier section of this report. However, the hospital administration had attributed all these problems to overcrowding and lack of adequate resources. ICCA's analysis, however, indicate that a significant number of these problems could be resolved through greater emphasis to better housekeeping. Even if there was overcrowding, this must not be allowed to

expose hospital patients to added risk of infection and other medical complications.

Experiences of the Papuan Patients at RSMM Hospital

Among the Papuans interviewed by ICCA team a little over one-third (32%) had visited RSMM hospital. Interviewers were asked to rate their experiences on a 5 point scale with 5 being highly satisfied and 1 being highly dissatisfied.

In general, the opinions of the patients with regard to their experience at the RSMM hospital ranged between 3 and 4, i.e., from neither satisfied nor unsatisfied (3) to somewhat satisfied (4) (Table 2.4).

Table 2.4

Level of Papuan Patients Satisfaction with the

Quality of RSMM Hospital's Services

Category of Experience	Rating
Overall Quality of In-Patient Medical Care	3.6
Overall Quality of Out-Patient Medical Care	3.4
Overall Quality of Emergency Care	3.9
Overall Attention and Care from the Medical Staff	3.8

Analytical Observations

RSMM hospital is facing a unique set of challenges and opportunities in the context of providing medical care to the Papuan community. Clearly, the hospital is overcrowded and could use better facilities and an increase in medical and support services and staff. This is the path that has been followed until now

by RSMM, where LPMMAK has continued to devote an increasing portion of its budget to healthcare and, in particular, to RSMM hospital. Furthermore, RSMM has argued in favor of a similar approach in the future by requesting further increases in its budget to meet the growing medical needs of the Papuan community. As a matter of fact, as we have noted in an earlier part of this report, RSMM's senior medical and administrative staff considers all aspects of its current operating environment to be quite unsatisfactory and need substantial improvements regarding potentially large sums of money.

However, in ICCA's opinion this strategy for further growth is not sustainable as the basis of improving medical services. It is equally unfeasible on financial grounds. Furthermore, this strategy is based on the faulty promise that an extension of RSMM hospital or a greater allocation of LPMMAK's financial resources to RSMM would improve the overall health of the Papuan community including the 7-sukus.

In a broader social context, healthcare is better defined as "level of wellness" in the community – a concept that is quite different from the curative aspects of disease management. People wellness - which is defined as fewer incidents of disease and prevention of disease in early stages – disease prevention and sickness avoidance can be viewed as parts of continuous chain starting with health education to better hygiene, preventive healthcare, early detection and treatment, and in-hospital care as the last resort.

Treatment at the hospital, therefore, should not be viewed as a discrete event, but one which is greatly influenced by actions taken at the

previous points in the wellness chain. It should also be apparent that hospital treatment is the most expensive item in the wellness chain and, therefore, should be resorted to only when other options have been tried.

According to RSMM, approximately 50% of the hospital's patients suffer from preventable diseases, i.e., diseases that can and should be better controlled through public health, e.g., malaria control, consumer education, better hygiene and early detection and treatment. In other words, a significant number of these patients can be treated without resorting to staying in the hospital. ICCA had requested RSMM for the data that would show the actual number of bed-days per year devoted to patients with preventable diseases and the financial costs associated with their staying at the hospital. Unfortunately, the hospital indicated that it could not provide us with this information. Notwithstanding, it should be apparent that financial costs must be quite substantial and constitute an enormous financial and medical staff burden on the hospital's resources.

There is another important reason as to why a strategy of allocating more resources to RSMM is doomed to failure. This is based on the economic logic of supply and demand. At RSMM, hospital care for the Papuan people is virtually free. Therefore, the demand for such service is infinite and no amount of increase in supply will satisfy this demand. As a matter of fact, increased supply would by itself create greater demand for the hospital services as people become accustomed to a certain level of service and continuously demand ever higher level of service since this demand for service does not require any expenditure on their part. Similarly, the hospital is equally motivated to expand its size and

services offered since it does not have to worry about increased costs or rationalize these costs in terms of alternative and potentially less expensive approach to enhancing level of wellness in the community. This phenomenon is well-known in economics as “Say’s Law” which stipulates that increased supply leads to expansion in demand when the customer does not have to pay for extra services – which soon become “must have” necessities rather use of scarce resources used judiciously.

When considered exclusively in the context of RSMM, increased funding is justified to alleviate the problem of overcrowding and to improve the quality of medical care. However, when considered in the context of improving the overall level of wellness in the community, a better approach would be to restrain spending at the downstream, i.e., at the hospital level and increase spending at the upstream, i.e., in the preventive, early stage detection and treatment level of wellness chain.

Overall Observations and Recommendations

1. Serious consideration should be given to handing over full responsibility for RSMM to YCT. At present there are too many organizations that have a hand in the management of RSMM and yet no one organization has full responsibility for the operation. The Freeport Partnership Fund and LPMAC must have responsibility for the effectiveness and professionalism of the RSMM in their role as fund providers for the RSMM, but day-to-day operations should be in the hands of YCT.

2. RSMM should give serious consideration to expanding its senior management to give it better focus and align complex job responsibilities with appropriate skill levels; and create greater accountability for performance. We recommend that RSMM's overall management be divided into three positions:
 - (a) Director of Medical Services
 - (b) Director of Administrative Services
 - (c) Director of Finance and Information Services
3. RSMM should not be treated as a "stand alone" entity. Instead, the scope and manner of its operations must be integrated in an overall design of "community wellness" and implemented at the LPMAK level in cooperation with organizations responsible for other elements of the community wellness chain.
4. A careful analysis should be undertaken to assess the trade-off between cost savings and community wellness by shifting resource allocation to the upstream elements of the wellness chain.
5. RSMM should generate data that would provide a more accurate assessment of medical costs associated with patients suffering from preventable diseases.
6. RSMM's budget should be frozen at the current level to induce the hospital to participate in developing and implementing programs that would effectively reduce the number of patients that must be hospitalized from preventable diseases.

7. RSMM should be allowed to use savings generated from this approach toward enhancing overall quality of medical care for those patients for whom hospital care is necessary and must be provided.
8. PTFI, LPMAK and RSMM should jointly agree and prepare a plan of action to implement ICCA's recommendations contained in this report. Furthermore, to ensure its effective execution, the following steps should be incorporated into the plan document:
 - (a) Series of specific actions that must be taken and a time-line to indicate when individual actions are to be completed.
 - (b) Where necessary, the budgetary implications of various changes should be carefully considered and appropriate budget provided to implement the plan.
 - (c) The implementation plan must identify individuals who would be held accountable for meeting plan targets. This is an absolute must otherwise the plan would risk failure under the burden of bureaucratic turf fighting and blame shifting. It is also important that responsible executives would have a strong incentive – both positive and negative - to complete the plan on time and in budget.
 - (d) The RSMM should be subjected to a follow-up audit by ICCA following a 12-month implementation period.

Chapter 3

PT PANGANSARI UTAMA

Company Profile

PT Pangansari Utama is an Indonesian company with headquarters in Jakarta. Its main business is Field Catering, Housekeeping, Recreational Facilities and other forms of Support Services. The company operates in many parts of Indonesia and in several overseas locations. It provides services to schools, hospitals, factories and airlines. It has food manufacturing facilities and food distribution outlets operating in Caltex Riau, British Petroleum Java Sea, Pagerungan, INCO Soroako, Total Indonesia Balikpapan, and has overseas projects in Vietnam and Yemen.

For PTFI's Indonesian area of operations, Pangansari provides housekeeping, catering, and maintenance of recreational facilities. Its operations are spread over 36 different locations within PTFI's contract of work area. According to the data provided by the company, Pangansari's annual revenues from PTFI operations in 2006 were approximately US\$30.0 million, a figure which has remained relatively stable over the previous three years.

In addition to its catering and housekeeping services, Pangansari has close association with two major local companies operating in the Timika area:

1. Pangansari Industri Mitra Ternak (PMIT) operates a cattle ranch which is located about 20 km outside of Timika. PMIT's output of beef is consumed by the PTFI Project.

2. Koperasi Karyawan (Kopkar) Sarima collects fresh fish caught from within the Timika/Mimika areas. All the fish is processed under the supervision of PTFI's Public Health Department at the Kopkar Sarima processing plant and is served in PTFI's Mess Halls.

Unique Characteristics of Pangansari

Pangansari possesses a unique set of operational characteristics that could admirably serve PTFI's goals in terms of:

1. Increasing employment opportunities for the Papuan people and their integration into the more modern industrialized economic system, i.e., finding jobs for relatively low-skilled workers and providing them with opportunities for further skill enhancement that would be consistent with the absorptive capacity of the Papuan workers and Pangansari's needs for enhanced skilled workers.
2. Enhancement and protection of human rights for all workers in general and Papuan workers in particular.
3. Contribute to the economic development of the Papuan community through the creation of business opportunities by supplying goods and services to PTFI and its privatized companies.

Among the privatized companies affiliated with PTFI, Pangansari employs the largest number of workers. It is only second to PTFI in terms of workers directly employed on its payroll. However, its ranking falls to third among the privatized companies when contractor supplied temporary workers are included

in the total employment figures. Pangansari is admirably situated to use its hands-on experience and close contact with the Papuan community to become a role model for implementing PTFI's human rights policies. These include: equitable and non-discriminatory treatment of Papuans in employment and promotion at the workplace, and, contributing to the economic development of the Papuan community in PTFI's contract of work area.

Finally, a large part of Pangansari's procurement needs are comprised of raw produce, e.g., vegetables, fish, poultry, meat and rice. These have the potential of substitution from imports to local production.

Employment Policies and Their Effectiveness

At the time of this audit Pangansari employed 1421 workers directly and provided employment for an additional 100 workers through PMIT. A majority of Pangansari workers are employed in support of catering services (47%) and housekeeping (47%) functions. The remainder 6% worked in warehousing and administration. Approximately 90% of all employees are low-skilled workers. The remaining 10% comprise of supervisors and management personnel.

Pangansari's total headcount of workers has remained fairly stable since 2003. Overall employment on January 1, 2006 was 1381 compared to 1314 in 2003. A similar situation exists with regard to Papuan employment – 21% of the total workforce in January 1, 2006 - which is essentially unchanged from 2003. Barely 10% of Papuans fill supervisory positions while the remaining 90% work in

low-skilled or unskilled jobs - a proportion consistent with the overall company profile.

The overall turnover rates amongst Pangansari's workers are extremely low, i.e., less than 5%. However, among the Papuans, the company claims to have experienced very high turnover rates. The reasons offered by the company for this situation are quite predictable and would apply to any community at the early stages of transformation from a subsistence culture to a more modern economy. These include: lack of work discipline, tribal disputes, and requirements of extended family. To this, Pangansari has added one more explanation, i.e., the recent allure of itinerant gold-panning, which is significantly more profitable.

The important question that must be asked here is not the relative low-skilled character of Papuan labor force, which was apparent and easily anticipated. Instead, the focus should be on what Pangansari could have done to prepare the Papuan workers through training to become productive members of its workforce.

On the surface at least, Pangansari has in place the necessary policies and programs to support Papuan employment efforts. The company has established extensive policies and procedures for job training. Each new hire goes through a 6-week on-the-job training period. A special program is in place to aid Papuan employment, through which 10 Papuans from the local villages are sent to Pangansari's Jakarta training facility. All successful graduates who return

to Timika are offered employment by the company. The company, however, states that many graduates decline these job offers.

Pangansari has also established detailed job descriptions and qualification criteria for all of its 86 functional positions. Its operations consist of 16 departments based on functionality and geography, using 10 job grades, ranging from 'junior employee' to 'senior manager'. Every position has a detailed work schedule, describing off-days, shift assignments, etc. The company's projections foresee a 1% increase in total employment for its PTFI operations during 2007.

These efforts, however, have not yielded desired results and Papuan employment levels at Pangansari remain low. For example, during the 3-year period between 2003 and 2006, the number of Papuan workers – both at the staff and non-staff levels – has essentially remained unchanged. This is especially discouraging since 90% of the Pangansari's workforce consists of unskilled and low skilled workers. Pangansari's failure in this regard cannot be blamed entirely on the characteristics of the Papuan culture, which were already well-known and, therefore, must be treated as given.

Although the ICCA audit has a special interest in the treatment of Papuans and their advancement in the workforce, it is impossible for ICCA to gather data about operations without interviewing a cross-section of employees. When ICCA interviewed Papuan and Non-Papuan employees about their perception of fairness of treatment with regard to salary and promotions, nearly half (49%) of the interviewed workers expressed their dissatisfaction. This includes over half

of the Non-Papuan workers (55%) and over one-third of Papuan workers (36%) (Table 3.1).

Table 3.1

Negative perception of workers about fairness of treatment with regard to salary and promotion

	Workers holding negative opinion of Pangansari; % of total sample
Papuans	36%
Non-Papuans	55%
Staff	59%
Non-Staff	47%
Total	49%

Among the complaints mentioned in regard to unfair treatment, the one most often stated was nepotism and favoritism in hiring and promotion (Table 3.2). This feeling was prevalent both amongst the Papuan as well as Non-Papuan workers. Non-Papuan workers complained that Papuan employees were unfairly favored; Papuans complained that employees of certain tribes received preferential treatment. Both groups noted that hiring and promotions were often affected by the personal whims of management and not by performance. Some anecdotal comments reproduced here are indicative of the general mood amongst the interviewed workers.

- The boss chooses people from the same tribe to fill the position.
- The employee closest to the boss gets promotion.
- Outsiders are hired for all important positions.
- Priority in promotion is based on ethnicity.
- There is too much nepotism.

- Tribal favoritism, family relationship, closeness to the boss.
- Someone held a position not because of his qualifications but because he/she is a Papuan.
- They treat Papuan workers better than Non-Papuan.

Table 3.2

Workers responses of unfair treatment with regard to salary and promotion

Category	% of total responses
Nepotism and favoritism	34%
Unequal treatment of Papuans and Non-Papuans	11%
Unequal treatment of old and new workers	11%
Unequal treatment of staff and non-staff employees	6%
Other complaints	39%

It is important to recognize that starting with the same population, PTFI has made been more successful in increasing the number of Papuan workers on its payroll than Pangansari has been. The same could be said for a number of other privatized companies where the level of required skill-set is higher than Pangansari. Pangansari's challenge is to find a more successful way in which to attract train and employ an increasing number of Papuans. At the same time, ICCA considers that PTFI must share certain responsibility when one of its privatized companies - and the one with the highest potential for providing entry level jobs to Papuans – has been unsuccessful in making demonstrable progress in this area. It is hoped that PTFI will use it own experience in increasing its Papuan workforce to help Pangansari's management meet its obligation toward greater employment and upward mobility of Papuan workers.

Pangansari's Projections for Future Employment

It was previously stated that Papuan workers represented only 21% of Pangansari's current workforce – a rather small number given the composition of tasks performed by the company. Notwithstanding, Pangansari's management indicates that it expects to increase Papuan employment at Pangansari from a current 21% to 35% in the next 5-6 years. Pangansari's management further indicates that the company would even like to increase this proportion to 50% of its workforce provided suitably trained Papuan workers could be found.

Pangansari states that to date it has failed to find "suitably trained" Papuan workers as a major reason for its low level of Papuan employment. In reality, however, PTFI and other companies working for PTFI have had to make a commitment to train Papuans for employment. Although Pangansari jobs do not, in many cases, require high job skills, Pangansari does require Papuans to do work that is not culturally accustomed in many parts of Papua. Diets in Papua are different, as are cooking techniques. Papuans will require cultural orientation and training as well as specific job training to be helpful workers in many of Pangansari's operations. Therefore Pangansari cannot look for Papuans with ready-made skills; Pangansari must train Papuans to fit into Pangansari's job requirements.

Given its employment needs, it would seem that Pangansari should put maximum effort in creating large scale training programs, which would be economically justified given the number of Papuans it needs to hire to meet the company's own optimistic projections. It is also possible that Pangansari's lack

of progress in hiring Papuan employees might be found in the fact that Papuan workers, who do not have many of the skills necessary to do the more important and interesting jobs with Pangansari, have been confined to dead-end jobs with no prospect of promotion and growth. It is, therefore, not surprising that workers tend to leave these jobs more frequently than would otherwise be the case.

The importance and success of good training programs in preparing Papuan workers has been successfully demonstrated by PTFI, which has had much more success in identifying and training Papuans for employment in higher-skilled areas of work. Therefore, Pangansari should be able to create the necessary training programs for the Papuans and hire more Papuans. A more vigorous commitment by Pangansari's management commitments should help change the Papuan employment situation for the better.

Human Rights Policy Implementation

PTFI requires that all of its business units and contractors follow the company's Social Employment and Human Rights (SEHR) policy and that all staff employees sign the HRAL document, indicating their understanding of the SEHR policy. As of December 15, 2006, almost one-half (49%) of Pangansari's staff employees had signed the HRAL document. Pangansari's management has made a self-assessment of PTFI's SEHR training and expects all of its employees to be aware of the SEHR. In reality, while most are familiar with these policies and believe its effectiveness, only a small number of employees claim to understand the major provisions of the SEHR.

The gap between Pangansari’s record of providing human rights training programs and the understanding by Pangansari employees of the company’s human rights commitment is quite significant. It indicates that the company has been less than effective in implementing these programs. ICCA discovered the same phenomenon when it did its first human rights audit of PTFI employees two years ago; many hours of training had taken place with little effect upon employee and their understanding of human rights.

The data ICCA collected from the workers’ interviews points to a need to improve the company’s human rights program implementation. Interviewed workers were asked to evaluate their level of satisfaction with the way Pangansari acts to protect human rights of its employees. The question was further broken down into two categories: protection of Papuan workers and protection of Non-Papuan workers. The answers were rated from 1 – “Strongly Dissatisfied,” to 5 – “Strongly Satisfied” (Table 3.3).

Table 3.3

Workers responses in regard to how Pangansari acts to protect

Human Rights of its employees

	Staff	Non-Staff	Total
Non-Papuan	3.1	3.0	3.0
Papuan	3.7	3.1	3.4
Total	3.2	3.0	3.2

Overall, interviewed workers gave Pangansari a cumulative rating of 3.2, which is slightly above the middle point of the opinion range. There is a small variation between Papuan and Non-Papuan workers (Papuan workers

believe that Non-Papuans are treated and protected better while Non-Papuan workers believe that Papuans' rights are better protected).

Another notable point is the number of workers who expressed a clearly negative ("Highly Dissatisfied" and "Somewhat Dissatisfied") or clearly positive opinion ("Highly Satisfied" and "Somewhat Satisfied") about Pangansari's record of respecting human rights. Table 3.4 shows that employees had a strongly split opinion about Pangansari's overall respect for human rights.

Table 3.4

Intensity of employee opinions about Pangansari's respect for Human Rights

	Clearly Negative	Neutral or No Opinion	Clearly Positive
Staff	41%	18%	41%
Papuans	33%	34%	33%
Non-Papuans	43%	14%	43%
Non-Staff	39%	22%	39%
Papuans	27%	34%	39%
Non-Papuans	44%	18%	38%
Total	39%	22%	39%

Support for the Papuan Community Economic Development

Pangansari and PTFI have made an effort to enhance the economic development of the local Papuan community through purchasing vegetables, fruit, fish, poultry and beef within the area around PTFI's operations. Pangansari's management asserts that it has a strong commitment to developing local enterprises and to allocate more of its purchasing requirements to local farmers and producers of other products and services. According to Pangansari,

the total value of purchases made by the company for its catering operations has increased from US\$25.2 million in 2004 to US\$32.1 million in 2006. During the same 3-year period, the company's share of local Papuan purchases increased from \$6.0 million to \$6.7 million. However, in percentage terms, purchases from Papua actually declined from 24% to 21%.

Projections for Future Growth

Pangansari has expressed its intention to increase local purchases from Papuan-owned and controlled organizations. Pangansari projects its local purchases to increase from the current level of 21% to 56% in 2007. This is based on the successful completion of two projects currently under development. These are: creation of rice paddies to grow rice locally, and, the establishment of a frozen vegetable processing plant. A rudimentary calculation, however, shows the fallacy of these projections. Pangansari's value of current total of monthly purchases is approximately US\$2.70 million, with procurement from Papuan sources accounting for about US\$557,000. Of this amount, rice and frozen vegetables account for only US\$243,000 per month. These items are targeted to be purchased locally in 2007. It is difficult to see how Pangansari plans to raise the local purchasing share from 21% to 56% by a mere addition of US\$243,000 per month.

Pangansari notes that the rapid increase in population in the areas around PTFI's operations has increased the demand for locally produced food in the local market, making it more difficult for food from the local area to be obtained

by Pangansari. Further, Pangansari notes that if the company obtained as much locally produced food for PTFI's operations the cost of food in the local market would increase. These are all valid points that need to be carefully considered. However, it is essential that these considerations not become an excuse for Pangansari to take the easy way out and obtain food from other parts of Indonesia and from Australia to the detriment of the local Papuan economy.

Overall Views of Pangansari

As part of employee interviews, ICCA asked all Pangansari workers a set of general questions. These were intended to elicit workers' overall opinion of Pangansari. The first question related to their overall opinion of Pangansari as a good employer. These findings are noted in Table 3.5.

Table 3.5

Intensity of employee overall opinions about Pangansari as a good employer

	Clearly Negative	Neutral	Clearly Positive
Staff	24%	23%	53%
Papuans	33%	34%	33%
Non-Papuans	21%	22%	57%
Non-Staff	44%	18%	38%
Papuans	30%	18%	52%
Non-Papuans	51%	19%	30%
Total	41%	19%	40%

We also asked the workers about their views of Pangansari as a good company for the Papuan people. The data are presented in Table 3.6.

Table 3.6

**Intensity of employee opinions about Pangansari as a good employer
for the Papuan people**

	Clearly Negative	Neutral	Clearly Positive
Staff	82%	6%	12%
Papuans	33%	0%	67%
Non-Papuans	93%	7%	0%
Non-Staff	18%	21%	61%
Papuans	24%	15%	61%
Non-Papuans	14%	24%	62%
Total	27%	19%	54%

Finally, we asked Pangansari workers about their opinion of PTFI. Our intention was to observe any differences in workers' views of Pangansari when compared with PTFI. The findings are presented in Table 3.7.

Table 3.7

**Intensity of employee opinions about PTFI as a good employer
for the Papuan people**

	Clearly Negative	Neutral	Clearly Positive
Staff	6%	6%	88%
Papuans	33%	0%	67%
Non-Papuans	0%	7%	93%
Non-Staff	10%	14%	76%
Papuans	21%	12%	67%
Non-Papuans	5%	14%	81%
Total	10%	12%	78%

These findings are quite troublesome and should raise a "red flag" in terms of serious problems for Pangansari. The data in Tables 3.5 – 3.7 show that:

- (a) Only 40% of all workers hold a positive view of Pangansari.
- (b) Both Papuans and Non-Papuans report a large measure of distrust in Pangansari as a good employer. This feeling appears to be more pronounced among Non-Papuans who constitute almost 80% of Pangansari's workforce
- (c) There is the prevalence of highly negative views of the company "as a good employer for the Papuan people." Among the staff, i.e., supervisory personnel, 82% had a negative opinion of Pangansari, while a majority of the non-staff (54%) expressed a positive opinion.
- (d) Finally, Table 3.7 highlights another anomaly as to the perspective of Pangansari workers about "PTFI as a good employer for the Papuan people." When compared with the generally negative expressions about Pangansari, an overwhelming majority of the workers had a highly favorable view of PTFI. Although, this feeling was less pronounced among the Papuan workers when compared with Non-Papuan workers.

ICCA's Concluding Observations and Recommendations

for Corrective Action

ICCA's detailed analysis of Pangansari's operational practices and business model suggest that Pangansari has not realized its potential of maximizing employment opportunities for the Papuan people. The company's employment levels of Papuan people are far below what could be expected given

its needs of essentially low skilled or unskilled workers and the large pool of Papuan workers that would fall in this category.

A similar situation exists with regard to local purchasing of agricultural products for catering at PTFI. ICCA recognizes that Pangansari has outlined a number of programs with a view to increasing local purchases. Unfortunately, these efforts to date have not resulted in a meaningful contribution to Pangansari's overall purchases of goods and services under its contract with PTFI.

A. Papuan Employment and Human Resources

In ICCA's opinion, Pangansari's operations – especially in the area of Papuan employment – represent an area of missed opportunity that could have been enormously beneficial to the Papuan community without any adverse financial impact on Pangansari or PTFI. The responsibility for this poor level of performance must rest with Pangansari's management for not meeting its commitments toward increased levels of Papuan employment.

Pangansari's claims of unskilled character of Papuan workers is implausible when confronted with the fact that a majority of Pangansari jobs can be satisfied with low-skilled workers, which is also the largest pool of potential Papuan workers. Pangansari's claim of non-availability of "suitably trained" Papuan workers is also untenable given the fact that both PTFI and other privatized companies have been quite successful in hiring training and retraining Papuan workers at successive level of higher skills. Furthermore, Pangansari

has largely failed in implementing its human resource policies and procedures in a manner that would give its employees a feeling of trust in their company's actions.

Pangansari's optimistic projections for future growth are quite unrealistic based its past performance with regard to employment of Papuans. In ICCA's opinion Pangansari's future employment growth prospects must be linked to a comprehensive recruitment and training program and strict and enforceable performance measures.

We strongly urge PTFI to support Pangansari in the development of policies and programs that will increase the number of Papuan employees on the company's payroll. Furthermore, implementation of these recommendations should be made an integral part of Pangansari's obligation of "satisfactory performance" under its contract with PTFI.

In ICCA's opinion, PTFI management has not exercised sufficient due diligence with regard to Pangansari's management concerning employment training and promotion of Papuan employees. In this regard, PTFI should identify management personnel in its own ranks who should be responsible for Pangansari's performance. ICCA also believes that PTFI should actively support Pangansari's implementation of the PTFI's SEHR policies.

Finally, it is important for PTFI to recognize and accept the fact that Pangansari's management PTFI's active support to bring about changes in Pangansari's culture and *modus operandi*.

1. Pangansari should be required to increase its Papuan workforce by 100% during the next five years, i.e., June 30, 2012. Furthermore, Pangansari should be held accountable for increasing its Papuan payroll by 20% per year to ensure the continuity of its contract with PTFI.

PTFI should ensure that Pangansari's efforts at Papuan employment are based on good training, better employee relations, and long-term employee tenure. This would mean that Pangansari should also demonstrate that its Papuan employee turnover rates are no higher than those of the Non-Papuan employees in specific job categories..

2. Pangansari should also be required to ensure that during this 5-year period, upward mobility among Papuan employees, i.e., from hourly workers to staff positions, and from staff positions to supervisory positions, are similar to those of non Papuan employees. If anything, Pangansari should demonstrate a more accelerated rate of upward mobility among the Papuan workers since its current record is quite deficient in this respect.

3. Pangansari should appoint a senior executive with the primary responsibility for implementing these recommendations. This executive's performance evaluation, promotion and salary increases should be determined based on his success in implementing these recommendations.

4. Pangansari should establish a committee of Papuan leaders to advise and assist Pangansari in the recruitment, training, and retention of Papuan employees. This committee should work closely with Pangansari's management

and also help Pangansari toward building better relations with the Papuan community.

ICCA's Follow-up Activities

ICCA recommends that both Pangansari and PTFI jointly create a plan of action with necessary standards and conditions of performance evaluation and target achievement. This plan should be completed within three months from the date of the formal acceptance of this report by PTFI and Pangansari.

B. Procurement from Papuan and other Local Sources

Pangansari has offered an optimistic and ambitious plan for creating greater business opportunities through changes in its procurement policies to encourage Papuan economic and business development. ICCA's preliminary analysis indicates these plans would be very difficult to implement. Therefore, ICCA recommends the following:

1. Pangansari should provide PTFI with carefully developed feasibility studies of all such projects to ensure that they are operationally sound and economically viable.
2. PTFI should hold Pangansari accountable for meeting its achievement targets specified under the plans. PTFI's performance evaluation should focus primarily on the "deliverable outcomes" rather than efforts made. These performance standards should be made an integral part of Pangansari's obligation of "satisfactory performance" under its contract with PTFI.

3. Pangansari should appoint a senior executive with the primary responsibility for implementing local procurement plans and initiatives toward Papuan economic development. This executive's performance evaluation, promotion and salary increases should be determined based on his success in implementing these recommendations.

4. It is highly desirable that Pangansari's local procurement and Papuan economic development activities should be implemented in cooperation with PTFI's Contracting Department, Social and Local Development (SLD) Department, and also Amungme and Kamoro Community Development Institute (LPMK).

5. Pangansari should establish a committee of Papuan leaders and local businessmen to advise and assist Pangansari in these efforts. This committee should work closely with Pangansari's management and also help Pangansari toward building better relations with the Papuan community.

ICCA's Follow-up Activities

ICCA recommends that both Pangansari and PTFI jointly create a plan of action with necessary standards and conditions of performance evaluation and target achievement. This plan should be completed within three months from the date of the formal acceptance of this report by PTFI and Pangansari.

Chapter 4

PT KUALA PELABUHAN INDONESIA (PT KPI)

Company Profile

KPI has been providing services to PTFI and its affiliated companies since 1995. These services include marine and stevedoring; cargo handling; levee and road construction and maintenance; repair and maintenance of mining equipment; and, light vehicle maintenance. KPI's business with PTFI has been in a state of gradual reduction. Annual revenues have gone down from US\$6.0 million in 2004 to US\$2.25 million in 2006, and are expected to stabilize around to US\$2.0 million by 2008.

Workforce Profile

Notwithstanding the reduction in the annual value of contracted work, KPI has shown a modest increase in its workforce numbers. Total number of workers has increased from 1452 in 2004 to 1530 in 2006 and is projected to increase to 1556 by 2008. As of June 2006, 14% of the 1482 employees were at the staff level.

A majority (74%) of KPI employees are Indonesians who have come from outside of Papua. They are also mostly male. As of June 2006, 369 of the 1475 employees were Papuan Indonesians. The number of local Papuans from the 7sukus was 169 or a little over 11% of the total number of workers at KPI.

Terms of Employment, Hiring, Wages and Promotion Policies

KPI's employee relations are governed by a collective bargaining agreement with the Indonesian Chemistry and Mining Trade Union. KPI's terms of employment details hiring, promotion, training, work hours, pay, benefits, promotion and disciplinary policy, and other rules and regulations governing employee rights and responsibilities.

Company policies give first preference in hiring to those trained by the PTFI apprentice program, followed by Papuans of the 7 suku, Papuans in general, then Indonesians. Hiring decisions are based on applicants' skills assessment test performance. KPI also gives preferential treatment to local Papuans in case the test results are marginal and the job in question is relatively narrow in scope. In 2005, KPI has promoted a total of 5 Papuan and 3 Non-Papuan employees from non-staff to staff positions. These were chosen from approximately 147 eligible employees. Likewise, during the same period, 59 Papuans and 94 Non-Papuans were promoted within non-staff positions.

KPI employees' base salary scale consists of 7 job grades, with 2-5 steps within each grade. As a general rule, contracted employees receive 36-38% less than KPI's own employees.

In the sample of interviewed workers, about 26% of the people stated that they were dissatisfied with the level of treatment that they had received from the company with regard to salary and promotion. Among these people, 35% were Papuan workers. Complaints included favoritism on the part of the management and unequal treatment between Papuans and Non-Papuans.

Training Programs

All of KPI's job-related training programs are implemented in coordination with PTFI's QMS department. If certain types of training are not included in the QMS training program, KPI works with the QMS department to design and implement customized programs. During 2006, 1107 KPI employees logged 27,000 training hours in QMS managed training programs.

KPI is also an active participant in QMS' apprenticeship and on the job training programs; at the time of ICCA's audit 42 QMS apprentices were assigned to KPI. Most of the workers interviewed by ICCA (92%) confirmed that they had received some type of job-related training at KPI. Among the workers interviewed by ICCA, a little over one-third (37%) confirmed their participation in QMS training program. This number included 13% of Papuan and 48% of the Non-Papuan workers in the total sample.

In addition, all new hires undergo a mandatory safety training program, which is applicable to the PTFI area of operations in Timika. This fact was unanimously confirmed by the majority of the workers interviewed by ICCA (95%).

Contract Workers

KPI employs workers on its own payroll as well as contract workers on a temporary basis from local labor suppliers. The number of contracted workers has more than doubled over a 2-year period, i.e., from 137 in 2005 to 280 in 2006.

The organizational rationale and legal justification for hiring temporary workers is to be found in the seasonal nature of work or specialized projects that are not part of the company's core operations and thus do not require regular full time employees. Indonesia's employment law allows for the hiring of temporary workers under the provisions generally described as Employment Agreement for Predetermined period (PKWT).¹⁰ A review of KPI's temporary contract workers leads ICCA to conclude that KPI's employment practices and program do not meet the required criterion under the Indonesian Labor Law (Table 4.1).

Table 4.1

Length of Service with KPI before being transferred to the company's regular workforce (in years)

	2004	2005	2006	Total
Average years of service as a contractor (yrs.)	8.8	7.7	4.8	7.5
Less than 3 years	1%	3%	21%	7%
3 - 6 years	14%	35%	61%	30%
More than 6 years	85%	61%	18%	63%
Total No. of workers	146 (100%)	62 (100%)	71 (100%)	279 (100%)

Data provided in Table 4.1 shows that in 2004, 85% of the temporary workers had worked with KPI for over 6 years prior to being transferred to the company's regular workforce. Even in the year 2006, the most recent year for

¹⁰ Based on the Law Number 13 Year 2003 re: Employment ("Law 13/2003"); Decree of Minister of Manpower and Transmigration Number KEP.100/MEN/VI/2004 re: Implementation Provisions of Employment Agreement for Predetermined Period ("Decree 100/2004"); Decree of Minister of Manpower and Transmigration Number KEP.101/Men/VI/2004 re Procedures of License of the Worker/Labor Supplier Company ("Decree 101/2004"); and Decree of Minister of Manpower and Transmigration Number KEP.220/MEN/VI/2004 re: Prerequisites of Hand-Over of Some of Implementation Works to Other Company ("Decree 220/2004").

which data are available, the average tenure of temporary workers was 4.8 years before being transferred to the company's regular payroll. Analysis of the data further shows that:

- (a) These temporary workers have been employed in almost every department of the company.
- (b) There is no evidence to suggest that these workers were employed in seasonal work or non-core projects.
- (c) The only justifications for keeping all these workers in the temporary status appear to be their wages, i.e., these workers are paid lower wages for comparable work at KPI. As a matter of fact, the company has comparative tables for wages in different grades (steps) that mirror those of regular employees and maintain 35% wage differential across the board.

Transfer of Workers from Temporary to Permanent Employees Payroll

According to KPI, the transfer eligibility is based on skills, occupational assessment, and length of service with KPI while on the contractors' payroll. KPI uses the following criteria to determine the eligibility of temporary contract workers for transfer to the company's payroll:

- (a) Only contract employee who fulfills transfer requirements can be proposed to be employed as permanent employee.

- (b) The proposed contract employee must follow series assessments (SHL/Q test, Competency test), medically suitable, and must not be under the disciplinary action period.
- (c) Contract employee can only be transferred to permanent employee after working at company for at least 1 (one) year of service.
- (d) Remuneration (salary, benefits, etc) offer to contract employee should be at least same as previous remuneration at contractor. In special case, higher remuneration or grade can be offered to contract employee in line with; competency test result, budget and subject to Corporate Management approval.
- (e) All contract employees who are transferred to permanent are subject to probationary period for maximum 3 months.

From ICCA's perspective, these criteria are subjective and lack transparency. If a temporary worker can give satisfactory performance over a period of 3-8 years, it is illogical to suggest that he has not mastered the required skills to perform the tasks that he is already performing and that he must undergo further tests including a mandatory probation period of up to 3 months.

The question that needs to be asked from legal and practical perspective should be not about the conditions under which transfers will be made by KPI, but about the conditions under which KPI would be legally allowed to keep workers in the temporary status for such long periods.

Human Rights Policy Implementation

KPI's policy regarding human rights violations is to refer all complaints to the PTFI's human rights office. Of the 210 staff employees, all have signed the PTFI's Human Rights Assurance Letter as required by PTFI. KPI management's self-assessment indicates that only some employees possess awareness, familiarity, and understanding of PTFI's Social Employment and Human Rights policy and belief in its effectiveness.

Worker familiarity with KPI's human rights policies also reflected in their highly positive views of KPI in terms of the company's respect for human rights. Table 4.2 indicates that staff workers were unanimous in their positive opinion of KPI for its respect and protection of employees' human rights. Similarly, non-staff employees gave KPI a positive ranking by large majorities (Papuan 63% and Non-Papuans 88%)

Table 4.2

Interviewed Workers' Opinions about KPI's Respect for Human Rights

	Clearly Negative	Neutral	Clearly Positive	No Response
Staff	0%	0%	80%	20%
Papuans *	0%	0%	0%	100%
Non-Papuans	0%	0%	100%	0%
Non-Staff	6%	15%	76%	3%
Papuans	13%	19%	63%	6%
Non-Papuans	0%	12%	88%	0%
Total	5%	13%	76%	5%

* Data for Papuan staff workers is not reliable because of their very small number in the sample of interviewed workers

Support for the Papuan Community

a. Employment

Since 2003, KPI has been actively recruiting Papuan workers at a rate of 50% of its total hires. Company projections estimate that Papuans will comprise 30% of the total workforce by 2008. This projection involves the replacement of approximately 60 Non-Papuan Indonesians with workers of Papuan origin over the next two-year period. Given that the annual employee turnover rate at KPI has been around a steady 3% or 45 workers yearly, this target assumes that 66% of all new hires will be Papuans during 2007 and 2008. In fact KPI management, in its Management Compliance Report to ICCA, explicitly states that the company's target for new employment is to hire 75% of all new workers from the Papuan community. During 2006, KPI has succeeded in recruiting 70% of its new hires from Papuans. This is a commendable feat, considering the hurdles reported by PTFI and its other contractors in increasing their hiring levels from the Papuan community.

KPI has also designated specific job categories for Papuan recruitment in the next two years. To this end, the company has incorporated PTFI's apprenticeship program (through Nemangkawi Mining Institute) where on-the-job training programs are used to identify high-potential participants for future hiring. TKPI also has instituted specific training programs toward accelerated career development for the Papuan employees.

KPI's management considers poor literacy rates and relatively unskilled character of Papuan workers to be a major impediment to its recruitment efforts.

The company also cites lack of certain trade expertise and training at the QMS apprenticeship program, the need for significant training required to promote Papuans to staff positions, and long lead times involved in identifying eligible Papuan employees during the recruitment and training process.

b. Local Economic Development

KPI's local purchases of goods and services are managed through PTFI. These purchases are largely made through Indonesian-owned companies. Local purchases made from Papuan-owned companies represent a negligible portion (less than 1%). The company attributes their inability to channel any meaningful business to local enterprises to the supply chain management protocols of PTFI, which manages KPI purchases.

Overall Views of KPI

We asked workers a series of general questions about KPI. These were included to the workers' overall opinion of the company. The first question related to their overall opinion of KPI as a good employer. These findings are noted in Table 4.3. We also asked the workers about their views of KPI as a good company for the Papuan people. The data are presented in Table 4.4. Finally, we asked KPI workers about their opinion of PTFI. Our intention was to observe any difference in workers' views of KPI when compared with PTFI. The findings are presented in Table 4.5.

KPI consistently scores high marks from its employees both as a “good employer” and as a “good employer for the Papuan people.” Overall 68% of all non-staff workers interviewed by ICCA had a positive view of KPI as a good employer with 81% Papuan employees falling in this category compared to 53% of Non-Papuan employees.

Table 4.3

Intensity of employee overall opinions about KPI as a good employer

	Clearly Negative	Neutral	Clearly Positive	No Response
Staff	0%	0%	80%	20%
Papuans *	0%	0%	0%	100%
Non-Papuans	0%	0%	100%	0%
Non-Staff	12%	18%	67%	3%
Papuans	25%	13%	81%	6%
Non-Papuans	0%	24%	53%	0%
Total	11%	16%	68%	5%

* Data for Papuan staff workers is not reliable because of their very small number in the sample of interviewed workers

ICCA findings in Table 4.3 indicated positively about KPI as an ‘overall employer.’ Table 4.4 indicates that KPI is also considered a good employer of Papuans, although at slightly less robust level. Among the non-staff workers, 61% of the interviewed workers held a clearly positive opinion of KPI as a good employer for the Papuan people (38% Papuan and 82% Non-Papuan).

It is interesting to note that among the privatized companies audited by ICCA, KPI stands out as the only company where workers’ approval of KPI ranks favorably with their appreciation of PTFI as a good employer for the Papuan people. (Tables 4.4 and 4.5).

Table 4.4

Intensity of employee opinions about KPI as a good employer of the Papuan people

	Clearly Negative	Neutral	Clearly Positive	No Response
Staff	0%	0%	80%	20%
Papuans *	0%	0%	0%	100%
Non-Papuans	0%	0%	100%	0%
Non-Staff	21%	15%	61%	3%
Papuans	38%	19%	38%	6%
Non-Papuans	6%	12%	82%	0%
Total	18%	13%	63%	5%

* Data for Papuan staff workers is not reliable because of their very small number in the sample of interviewed workers

Table 4.5

Intensity of employee opinions about PTFI as a good employer of the Papuan people

	Clearly Negative	Neutral	Clearly Positive	No Response
Staff	0%	0%	80%	20%
Papuans *	0%	0%	0%	100%
Non-Papuans	0%	0%	100%	0%
Non-Staff	9%	0%	88%	3%
Papuans	19%	0%	75%	6%
Non-Papuans	0%	0%	100%	0%
Total	8%	0%	87%	5%

* Data for Papuan staff workers is not reliable because of their very small number in the sample of interviewed workers

ICCA's Concluding Observations and Recommendations for Corrective Action

1. KPI's results demonstrate a good faith effort in hiring and training workers, especially the Papuan workers at the entry level jobs.
2. KPI's commitment to improve its Papuan employment efforts are based on reasonable assumptions and backed by planning and training effort to ensure that these targets would be achieved as planned.
3. KPI's efforts with regard to promotion of Papuan employees to staff level positions needs to be strengthened.
4. ICCA believes KPI is in violation of Indonesian labor laws with regard to contracted workers in terms of wages and conditions of employment. The fact that this practice has continued for such a long time requires further study and understanding.
5. KPI has not demonstrated a robust effort toward economic development of the Papuan community through its local purchasing program.

Recommendations

1. KPI must develop an actionable plan to create career path planning with specific targets of achievements for promoting Papuan employees to staff positions over a 3-year period, i.e., 2007-2009. Moreover, these promotions should represent a justifiable proportion of the total Papuan employees in KPI's payroll. This should include intensive training and on-

the-job mentoring to ensure that sufficient number of Papuans is available to fill these positions.

2. KPI should also create a plan of action with clear-cut criteria and achievement targets for transferring qualified contract workers to the KPI payroll. KPI should be prohibited from keeping contract workers as temporary employees for lengths of time beyond those allowed by law and PTFI's policy.
3. KPI should be prohibited from paying comparably skilled and experienced contracted workers wages and benefits that are different from KPI's own workers for similar work. Any administrative fee paid to the contract agency should not impact contract workers' wages.
4. ICCA also recommends that KPI prepare a plan of action – in cooperation with PTFI – to remedy issues identified in this report. This plan of action should be readied for implementation within six months from the date of the formal acceptance of this report by PTFI. ICCA recommends a verification follow-up audit within the 12 months to evaluate KPI's implementation of the action plan.

Chapter 5

PT SANDVIK SMC

Company Profile

PT Sandvik is a wholly-owned subsidiary of Sandvik Group, Sweden. Started in 1996, the company's operations in Papua are dedicated to providing services exclusively to PT Freeport Indonesia. These services include, among others, blast hole drilling, operating and maintaining ore flow equipment, maintenance of AB tunnel, and support services for other drilling, equipment maintenance and support services for milling operations. The value of these services has grown from US\$16.0 million in 2004 to US\$30.0 million in 2006. It is projected to grow by another 25% to reach US\$40.0 million by 2008.

Workforce Profile

The workforce at Sandvik consists largely of relatively skilled and experienced workers. They operate complex and expensive machinery under hazardous work conditions. Therefore, worker training and workplace safety are considered a top priority by the company.

Sandvik's workforce has grown from 216 workers in 2004 to 267 in 2006. It is expected to reach 309 by 2008. This growth reflects the expansion in the variety and value of services it provides to PTFI.

A majority of the Sandvik workers are hired directly by the company. The workforce is predominantly comprised of male Indonesians. The composition of

the workforce is Staff (21%), Non-Staff or hourly workers (73%), and Expatriate (6%). Of these, 22 or 8.6% are Papuan. It is also notable to emphasize that this proportion has remained essentially unchanged since 2004. Among the current 54 Staff employees only 3 are Papuan. The number of Papuan employees (both staff and non-staff) from the local tribes has increased from 4 in 2004 to 7 in 2006, and is projected to reach 17 by 2008.

**Training for Skill Enhancement, Promotion Policies,
and Workplace Discipline**

According to Sandvik's MCR, the management of the company recognizes the importance of workers' competency development. The company emphasizes continuous skill enhancement on the part of its workers, which would enable them to adjust to the technological innovations and new equipment used by the company. To upgrade the skills and effectiveness of its workforce, the company has developed and implemented skilled and semi-skilled training programs customized to the department needs with PTFI's QMS Department.

Interviews with a representative group of workers indicated that Sandvik's emphasis on job-related training has not been sufficiently translated into practice. Among the interviewed workers, almost 50% stated that they had not received any initial job-related training at the time of hiring. Another 35% indicated that there was no on-the-job continuous training or skill enhancement program offered to the workers.

Sandvik's emphasis on safety training, however, was quite evident. Interviewed workers were unanimous in stating that they had received safety-related training. Sandvik also participates in the skill enhancement programs developed by PTFI's QMS department. These programs are customized to meet PTFI's needs and also those of the privatized companies. Among the interviewed workers, almost one-half (45%) stated that they had participated in QMS development program. It is noteworthy, however, that none of these workers were Papuan, which is ironical since an important goal of the program was to help Papuan workers acquire technical skills and thereby get better jobs.

Another important aspect of the QMS development program is to prepare workers to pass a "proficiency test". This test is designed to equip workers with basic literacy and related skills in order to take more complex job related skills programs. This test has been somewhat controversial among the workers. While some workers regard this as a useful tool for learning, many others, notably older workers, have had difficulty passing the test. They also question its relevance for the more experienced workers who have already proved themselves through their on-the-job performance. Among the interviewed workers at Sandvik, a large majority (70%) indicated their belief that the proficiency test was a fair assessment of their skills, while another 30% did not agree with this assessment.

Sandvik has formal promotion policies for both staff and non-staff workers. These policies evaluate employees on the basis of their education, training, and tenure with the company, disciplinary records, and performance appraisal

reports. According to Sandvik’s Management Compliance Report, all eligible employees have been promoted from non-staff to staff positions during the past two years (6 in 2005, and 10 in 2006). In addition, in 2006, 7 employees were promoted within staff ranks, and 13 employees were promoted within non-staff ranks.

Here again there is a credibility gap between the company’s professed policies with regard to promotion and as they are perceived by the employees. When asked about the fairness of worker treatment by the management in regard to salaries and promotions, almost one-half of the interviewed workers expressed their dissatisfaction with Sandvik’s practices in granting salary increases and promotion to the employees. A majority of the complaints pertained to lower salaries at Sandvik when compared to other companies and also a more favorable treatment given to newly hired employees than older employees who had been with the company for a longer period. Workers also complained about lack of clear and objective criteria as they were applied in practice. Other complaints mentioned by the workers included favoritism in hiring and promotion practices. These complaints are summarized in Table 5.1.

Table 5.1

Worker Complaints with regard to Salary and Promotion Polices

Category	% of total negative responses
Low salary	50%
Unclear promotion practices	20%
Favoritism	10%
Other complaints	20%

Sandvik's employee discipline policies involve progressive action, starting from oral warnings, continuing with up to four written warning letters, up to termination. These policies and procedures are formally defined in the employee handbook along with applicable offenses and transgressions in the workplace.

Contract Workers

Sandvik also hires temporary workers through labor contractors. In 2006, there were 34 temporary workers comprising 12% of the workforce.

Sandvik states that it has a policy of transferring sub-contracted workers to permanent positions based on business needs and employee' qualifications. The number of transfers of temporary workers to regular Sandvik payroll is rather small: 8 people were transferred in 2004, 10 in 2005, and 2 in 2006.

According to Sandvik's management, these workers had remained on the temporary status for periods ranging between 1 to 3 years. The company also states that there is no fixed rule for maximum allowable period, which depends on the needs of various business units and job sites.

According to Sandvik, an important consideration in hiring temporary workers is the situation where Sandvik is not guaranteed full time work by PTFI. Under these circumstances, the company manages this business with the help of its own supervisors by hiring additional workers through labor supply contractors. Sandvik management states that the company has

“previously approached Freeport to recommend they hire a permanent crew to cover this type of work. Freeport has done so but there continues to be a requirement from Freeport to utilize

this labour source. This is the greater percentage of the contract workers.”

Sandvik’s explanation with regard to the hiring of temporary workers is understandable if PTFI does not feel the work is permanent. Notwithstanding, ICCA would request further explanation from PTFI with regard to its instance on the work being temporary where Sandvik considers a full time crew can be justified.

Indonesian Employment Law stipulates rather well defined conditions under which temporary workers may be hired by an employer.¹¹ At this point, ICCA does not have sufficient information to evaluate the appropriateness of Sandvik’s hiring of temporary workers.

Human Rights Policies

Sandvik has a formal code of conduct involving company and employee behavior in the areas of human rights, fair treatment of workers, employee harassment, equal opportunity, safety of work environment, and ethics in financial dealings. In the area of human rights, the company has made a self-assessment, and reports that all its employees possess awareness and understanding of PTFI’s Social Employment and Human Rights Policy.

¹¹ Based on the Law Number 13 Year 2003 re: Employment (“Law 13/2003”); Decree of Minister of Manpower and Transmigration Number KEP.100/MEN/VI/2004 re: Implementation Provisions of Employment Agreement for Predetermined Period (“Decree 100/2004”); Decree of Minister of Manpower and Transmigration Number KEP.101/Men/VI/2004 re Procedures of License of the Worker/Labor Supplier Company (“Decree 101/2004”); and Decree of Minister of Manpower and Transmigration Number KEP.220/MEN/VI/2004 re: Prerequisites of Hand-Over of Some of Implementation Works to Other Company (“Decree 220/2004”).

A description of human rights policies is included in the workers' contracts, which are signed by all new hires. Although, Sandvik's management communicates the importance of human rights policies to all its employees, there is no follow-up program currently available, which would assess the level of understanding and familiarization of the workers with the company's human rights policies.

Among the interviewed workers, a very large majority (75%) indicated that they were not given any information on the company human rights policies during orientation or subsequently in any other programs. We also asked the workers about how satisfied they were with the way Sandvik acts to protect the Human Rights of its employees. The answers were rated from 1 – "Strongly Dissatisfied," to 5 – "Strongly Satisfied". These findings are summarized in Table 5.2.

Table 5.2

Interviewed Workers' Opinions about Sandvik's Respect for Human Rights

	Clearly Negative	Neutral	Clearly Positive	No Response
Staff	29%	14%	57%	0%
Non-Staff	38%	23%	31%	8%
Total	35%	20%	40%	5%

A note of caution is necessary in the interpretation of data provided in Table 5.2. The data did not include any Papuans in the staff category and only two Papuans among the non-staff. Therefore there is no break-out of Papuan and Non-Papuan employees. Among the staff members, a majority (57%) held a

positive view of the company's human rights policies. Among the non-staff, however, opinions about Sandvik's human rights performance was less positive (31%).

Future Growth in Papuan Employment

Sandvik has identified three major job categories where the company plans to establish a preferential hiring program for the Papuans. These job categories are in the area of security, warehousing and mechanics. These plans are projected to add 12 Papuans to the company's payroll in 2007 and another 12 in 2008. In other words, under the most optimistic estimates, Sandvik expects to increase its employment of Papuans from a total of 12 workers in 2004 to 45 in 2008.

Overall Views of Sandvik

Toward the conclusion of each interview, workers were asked their overall opinion about their employer. Once again, the data provides a different picture about Sandvik when viewed from the perspective of the workers when compared to the self-assessment on the part of Sandvik's management. When asked their opinion about Sandvik as a good employer, 57% of the staff employees responded that the company was clearly a good employee. Among non-staff employees the opinion was much different, with only 15% of the employees reporting that Sandvik was a good employer.

Table 5.3**Intensity of employee overall opinions about Sandvik as a good employer**

	Clearly Negative	Neutral	Clearly Positive
Staff	14%	29%	57%
Non-Staff	39%	46%	15%
Total	30%	40%	30%

However, when we asked the interviewed workers about their views as to the extent the company is good for the Papuan people, there was a similar discrepancy between the opinions of staff and non-staff as was seen with regard to Sandvik as a generally good employer. Staff employees were far more positive about employment with Sandvik than were non-staff (57% of staff were clearly positive against only 15% of non-staff). Again, there were too few Papuans in the sample to use them as a separate category.

Table 5.4**Intensity of employee opinions about Sandvik as a good employer of the Papuan people**

	Clearly Negative	Neutral	Clearly Positive	No Response
Staff	29%	0%	57%	14%
Non-Staff	31%	46%	23%	0%
Total	30%	30%	35%	5%

Finally, an expression of workers' confidence in Sandvik as an employer of Papuans can be elicited from Table 5.5. Sandvik employees were asked about their opinion of PTFI as a good employer for the Papuan people. Workers'

opinions in this case stand in sharp contrast to those expressed toward their immediate employer, i.e., Sandvik. A majority (65%) of workers in all categories indicated a positive view of PTFI's employment of Papuan people over against 35% for Sandvik.

Table 5.5

Intensity of employee opinions about PTFI as a good employer of the Papuan people

	Clearly Negative	Neutral	Clearly Positive	No Response
Staff	0%	14%	86%	0%
Non-Staff	23%	15%	54%	8%
Total	15%	15%	65%	5%

ICCA's Concluding Observations and Recommendations

for Corrective Action

1. ICCA's finds that the implementation of programs and policies by Sandvik in the areas of hiring, training, promotion, and respect for human rights falls short of the high goals and expectations that the company has set for itself and has shared with PTFI and its own employees. The company's management has not put in place the structures, controls and monitoring necessary to implement its own policies and programs. Because there were too few Papuans in the sample of those interviewed to comment about how Sandvik's Papuan employees feel about Sandvik, but among the Sandvik employees in general, there is dissatisfaction about employment conditions (especially among non-staff) and treatment of Papuans (again, especially among non-staff). It is hoped that Sandvik's management will

take these employee-driven comments and seek ways to address the issues articulated in the employee surveys.

2. ICCA also feels that PTFI should have exercised greater oversight in ensuring that workers in Sandvik and other privatized companies are treated fairly and that all decisions pertaining to hiring, training, salaries and promotion are objectively made and are transparent to the workers.
3. ICCA also concludes that Sandvik's record is unsatisfactory when it comes to the hiring, training, and promotions of Papuan workers. Since 1966, when PTFI made a strong commitment to employ Papuans, Sandvik did not follow PTFI's lead. It is time for Sandvik to match PTFI's commitment to the Papuan people. It is important that Sandvik make public commitments to Papuan employment and the match those commitments with transparent disclosures of programs and numbers of Papuans added to the workforce.

Within six months from the formal acceptance of the report, Sandvik should submit a detailed plan of action that would:

- a. provide specific yearly targets of achievement toward hiring, training and promotion of Papuan workers, especially promotion to staff ranks;

- b. implement an improved plan of training to enhance awareness of and sensitivity toward human rights issues at all levels of supervisory and management staff; and,
- c. create and implement a plan of action in terms of contract workers that is in accord with Indonesian labor laws and PTFI policies. This would include, among others (i) an immediate transfer to Sandvik's regular payroll all contract workers whose terms of employment have met or exceeded the condition provided under the Indonesia employment laws; (ii) consideration in some form to compensate for the loss of income suffered by these employees during their contract worker status; and, (iii) a clear-cut policy with regard to future hiring of contract workers that comply with the condition stipulated in the Indonesia employment laws for hiring and retention of such workers.

These plans should be reviewed for their specificity and adequacy, and the plans should be audited within one-year of the plan's introduction to ensure a satisfactory level of implementation and achievement.

Chapter 6

PT SALJU ABADI SEJAHTERA (PT SAS)

Company Profile

PT SAS is an Indigenous Amungme Papuan company, which provides temporary manual labor to PTFI and other organizations. The company was founded in April 2004. In addition, PT SAS manages a cattle rearing project. The cattle project, located at mile 22 in the Timika region, is an integral part of PTFI's reclamation program. PT SAS is headquartered in Timika and maintains a local office in Tembagapura and a representative office in Jayapura, Papua.

The company derives over 95% of its revenue as supplier of temporary workers to PTFI and KPI. PT SAS has had a remarkable growth in revenue, which has increased from US\$580,000 in 2004 to over US\$1.53 million in 2006. PT SAS management projects this high growth rate to continue with annual revenue increasing to US\$1.81 million in 2007 and US\$2.22 million in 2008.

Worker Profile

PT SAS employee payroll has increased from 162 in 2004 to 325 in 2006. Over this period, Papuans have generally constituted between 25-28% of the total workforce. Currently, approximately 30 employees (majority of whom are Papuan) work directly for PT SAS administration and at the cattle ranch. Therefore, this rapid increase in the company payroll can only be attributed to the

growth in the number of workers who are assigned to work in PTFI's business units and KPI.

Employment Terms

PT SAS has established policies, made available to its workers in the form of an employee handbook which outlines the terms of employment, work rules, applicable taxes and deductions, insurance provisions, wage and allowance schedules, and other regulations governing employee conduct and responsibilities.

Wages and Benefits

PT SAS workers' wages are based on a service agreement with PTFI. This agreement is based on six grades, and up to five steps within each job grade. PT SAS reports that their workers who perform comparable jobs to those of direct employees of PTFI receive 15% less pay than PTFI employees receive. With regard to employee benefits, most benefits are identical to those offered by PTFI. The major differences are that PT SAS offers medical and home-leave benefits only for workers. PTFI's coverage medical and home-leave policy includes dependents as well.

Employee Training

PT SAS does not offer any employee development or training programs to its workers. However, PT SAS can and does take advantage of job training provided through PTFI's QMS Department.

Hiring and Promotion Policies

PT SAS follows PTFI guidelines with regard to the implementation of hiring, promotion, retirement, and termination policies.

Human Rights Policy Implementation

Company policy states that any report received by PT SAS regarding human rights violations will be referred to the PTFI Human Rights Officer for review. Company management has indicated that human rights training has been scheduled for August 2006; the training will be provided through PTFI's Human Rights Compliance Office and will be identical to that provided to PTFI employees.

Among the interviewed workers, opinions were about equally divided between those who felt that SAS protected employees' human rights and those who disagreed with this assessment (Table 6.1). Almost 20% of the interviewed workers were neutral with regard to their evaluation of the company's respect for human rights.

Table 6.1**Interviewed Workers' Opinions about SAS's Respect for Human Rights**

	Clearly Negative	Neutral	Clearly Positive
Total	41%	18%	41%
Papuans	25%	25%	50%
Non-Papuans	43%	18%	39%

Overall Views of PT SAS

During the field audit, we asked workers a series of general questions about PT SAS. These were included to the workers' overall opinion of the company. The first question related to their overall opinion of SAS as a good employer. These findings are noted in Table 6.2. We also asked the workers about their views of SAS as a good company for the Papuan people. The data are presented in Table 6.3. Finally, we asked SAS workers about their opinion of PTFI. Our intention was to observe any difference in workers' views of SAS when compared with PTFI. The findings are presented in Table 6.4.

Table 6.2**Intensity of employee overall opinions about PT SAS as a good employer**

	Clearly Negative	Neutral	Clearly Positive
Total	37%	22%	41%
Papuans	0%	25%	75%
Non-Papuans	43%	22%	35%

Table 6.3**Intensity of employee opinions about PT SAS as a good employer of the Papuan people**

	Clearly Negative	Neutral	Clearly Positive	No Response
Total	33%	19%	44%	4%
Papuans	0%	25%	75%	0%
Non-Papuans	39%	17%	39%	4%

Table 6.4**Intensity of employee opinions about PTFI as a good employer of the Papuan people**

	Clearly Negative	Neutral	Clearly Positive
Total	7%	4%	89%
Papuans	25%	0%	75%
Non-Papuans	4%	4%	91%

The company generally receives a favorable assessment as a good employer and as a good employer for the Papuan people. These findings, however, should be considered with a note of caution because of the relatively small proportion of SAS workers who are Papuans. Notwithstanding, it is also clear that Non-Papuan SAS workers by majority hold a positive opinion of PTFI as a good employer for the Papuan people when compared to their opinion of SAS.

ICCA's Concluding Observations and Recommendations for Corrective Action

There is something special about PTSAS because it is an Amungme (local, 7 suku) business enterprise. One might hope that it would employ more local Papuans and that it would do a better job with employee development, but it is a hopeful sign that there is a Papuan entity doing business with PTFI. With the exception of PTSAS' direct management of the cattle farm and its own internal management function, PTSAS is contract labor supplier to PTFI and to a larger company providing services to PTFI, KPI. As a contract labor supplier, PTSAS is involved with the same issues of compensation that other, larger and longer established contract labor suppliers face—that is, full compliance with Indonesian labor law with respect to duration of service and compensation of temporary, contract workers.

As PTFI and contractors to PTFI struggle with the issue of coming into full compliance with Indonesian labor law as it governs the use of temporary contract labor, PTSAS will be swept along with the tide. ICCA does recommend that PTSAS work diligently to increase the Papuans who are employed through the company. Since most of those employed through PTSAS provide basic labor, it should be relatively easy to recruit from Papuans in general and 7 suku Papuans more specifically. To effect this increased use of Papuans in PTSAS, the company should establish a working agreement and program with PTFI to enhance the training of local Papuans.

Chapter 7

PT TRAKINDO UTAMA

Company Profile

PT Trakindo Utama is one of the oldest privatized companies among PTFI's contractors. The company has been a dedicated supplier of Caterpillar equipment including after-sale support and maintenance services to PTFI for over 27 years – almost since the start of mining operations in Papua. Trakindo is responsible for providing PTFI with most of its front line maintenance, component and machine rebuilding, parts and logistics, machine rental services and the provision of equipment operators for all types of Caterpillar machines.

In 2002, Trakindo signed a Life of Mine Strategic Alliance Partnership including a Maintenance & Repair Contract (MARC) with Freeport. This led to a large increase in Trakindo facility investment and employee count at the mine site. The total value of Trakindo's services to PTFI has been around \$130 million/per year since 2004. Trakindo projects this number to increase to around \$170 million by the year 2009.

Workforce Profile

Trakindo's overall workforce has been increasing on average 11-13% per year during the last 4 years. As of July 1, 2006, Trakindo employed over 1500 people. This includes workers directly employed by Trakindo (78%) and those hired by the company as contract employees (22%). Trakindo's workforce is

almost entirely male (97%). It is also 95% Indonesian. Among Trakindo's workers, Papuans represent about 6.5% of the workforce. Papuan workers belonging to 7-suskus constitute 2.5% of the Trakindo workforce.

Contractor-Supplied and Outsourced Workers

Trakindo relies on temporary workers via two classifications: outsourced employees and temporary contract-supplied workers. The outsourced employees are in effect 'job shop' employees and are employed by three 'job shop' companies, who then assign them to work for Trakindo on specific projects. Contract employees work under direct control of Trakindo, but are not considered company employees. The company has been gradually reducing the number of both the contractor-supplied temporary employees and outsourced workers.

The distinction between the two groups is worth noting. Contract employees are "temporary workers" provided to Trakindo by the contractor. In the case of "job shop," Trakindo hires an outside company to perform a particular task or handle a specific project. The outsourced company provides labor to work on such projects. In addition, outsourced workers are also paid directly by their employer, e.g., labor supply company, while contracted workers received their payment from Trakindo.

The primary rationale for the use of non-company workers is the flexibility it offers to the company to adjust for variable work loads. The company also argues that contract workers are necessary in the initial hiring stage since Trakindo does not want to hire untrained people directly on its payroll.

At the end of a fixed-term contract with an outsourced or directly contracted worker, Trakindo routinely considers transferring the worker to its own payroll as a permanent employee. During 2006, 88 of 538 (or 16%) of such workers were transferred as permanent employees of Trakindo.

In 2006, contract and outsourced workers accounted for 33% (6% contracted and 27% outsourced) of Trakindo's workforce. This percentage went down from 38% in 2005 and 40% in 2004. However, Trakindo's management states that the proportion of temporary workers (contract and out-sourced) is likely to remain at this level through the foreseeable future.

Employment Policies

Trakindo has established a formal set of Employment policies. Each employee receives a handbook, which contains detailed information on the working conditions, wages and benefits, training and promotion, and disciplinary procedures applicable to Trakindo's employees.

Trakindo's workers are classified as non-staff (job grades 1-5) or staff (job grades 6-12). Differences in job grades translate into basic salary and incentive differentials. All candidates must meet the position qualifications determined by Trakindo and successfully pass a formal selection process/employee recruitment interview. Typically all new employees have to serve a 3 months probation period, which leads to confirmation of permanent employment upon demonstrated suitability.

Employee turnover at Trakindo has ranged between 12-19% for non-staff and 3-6% for staff positions over the past three years. However, these include many Trakindo employees who were relocated to other operations that Trakindo has within Indonesia. The actual percentage of employees that leave Trakindo is very low.

Wages and Benefits

Trakindo's wage rates for contracted and outsourced workers differ from those of the company's own employees. The company states that its hourly rates for temporary and out-sourced workers are generally equal to the wage rates paid to the company's own employees doing similar work. Trakindo's management also states that it must deduct from these wages an appropriate amount of attributable to "management fee", which is payable to the 'job shop' company. Therefore, it should be apparent that the net take-home pay of contract and outsourced workers would be less than Trakindo's own employees. The company asserts that for some job classifications, Trakindo makes up the differential in take-home pay and passes on the extra expense to PTFI.

There also exists a significant difference between outsourced workers and Trakindo employees in the area of fringe benefits. The company also differentiates between local and non-local workers in terms of their eligibility for certain benefits. Almost all Papuan workers are considered to be hired locally, s even though there some Papuans may actually live further away (in time of travel if not in distance) from PTFI's operations site.. The company acknowledges that

an equity problem exists and states that they are in the process of correcting any inequities.

Promotion Policies and Procedures

All Trakindo employees receive a formal annual appraisal, which must be documented and filed by the Divisional HR Dept. To obtain a promotion, an employee must demonstrate the skills and ability to take on the new responsibilities and has two consecutive service years of satisfactory work performance in his/her current job.

During the past 18 months, 50 employees (3 of whom were Papuan) were promoted from non-staff to staff positions, 32 were promoted within staff positions, and 308 (43 of whom were Papuans) were promoted within non-staff positions.

Training Programs

All Trakindo employees undergo basic induction and safety training before entering the work-place. In addition, there are a number of technical training programs that are designed to provide employees with the skill sets required to do specific jobs. Trakindo has a full time training department on site. It is supported by Trakindo's Corporate Training Division located in Jakarta and at its residential Training School in Cileungsi, West Java. Technical training involves classroom, on-the-job-training and self-paced interactive training. Trakindo also conducts training for supervisory and management skills. Of the interviewed

workers, a large majority (80%) confirmed that they had received some type of job-related training.

Trakindo also works with PTFI's QMS department whose technical training is mostly based on the Trakindo/Caterpillar programs. Several QMS trainers have been certified to conduct Trakindo/Caterpillar's technical courses by attending a trainers' program at Trakindo's residential training school in Cileungsi. At the PTFI site Trakindo and QMS share training facilities and materials and many training classes involve employees from both companies, as well as those from other Privatized Companies and Contractors working on the job site. In the sample of workers interviewed by ICCA team, 22% of the respondents stated that they had participated in the QMS training. However, all of these workers were Non-Papuan.

Employee Complaints and Disciplinary Procedures

Disciplinary procedures are formally established, made available to all employees, and outline the process with which workers' undesirable behavior is managed. The basic process is a progression of verbal warnings, followed by formal letters, suspension, and temporary or permanent termination if deemed necessary.

Employee Complaints about Trakindo's Salary and Promotion Policies

Workers interviewed by ICCA voiced a variety of complaints about Trakindo's management on issues of salaries, promotion, and unequal treatment.

The type and range of these complaints were quite similar to those expressed by workers in other privatized companies. By far the largest number of complaints referred to favoritism (25%) followed by unequal treatment of local (Papuan and Non-Papuan) workers (15%). Workers also complained that overall salary levels at Trakindo (for similar type of work) were lower than at PTFI and other privatized companies (15%).

Another significant topic of complaint was unequal treatment of older employees when compared to new hires and between staff and non-staff workers (10%). Almost one-in-five (19%) of the interviewed workers also stated that salary policies and promotion rules were not clear and easily understood.

Human Rights Policy Implementation

PTFI requires that all privatized companies comply with PTFI's Social Employment and Human Resources (SEHR) Policies:

- (a) Everyone should be treated fairly and equally.
- (b) There should be no discrimination based on race, sex, or ethnicity.
- (c) All Papuans and Non-Papuans should be equally treated with respect.
- (d) Everyone should have the right to join a group, or not join a group.
- (e) No one should be forced to work against his/her wishes.
- (f) There should be no discrimination between Papuans and Non-Papuans in employment, promotion and training programs.

All managerial staff members in PTFI's area of operations are required to undergo training in PTFI's Social Employment and Human resources (SEHR) policies and sign the Human Rights Assurance Letter (HRAL), indicating their commitment to follow the SEHR policy.

ICCA's audit revealed that Trakindo had been lagging in its effort to comply with PTFI's policies in this area. As of February 2007, no staff employee of Trakindo had received the SEHR training, and with the exception of the General Manager, none had signed the HRAL letter. However, Trakindo states that the company had posted the HRAL document on its web site, circulated it to the business unit managers, and had provided human rights awareness training to the department head and one non-managerial employee at the highland location.¹²

ICCA's findings from worker interviews indicate that different worker groups held divergent views with regard to Trakindo's respect for human rights (Table 7.1). Among the staff employees, almost one-third had a neutral opinion of Trakindo's human rights policies and program. Two-thirds of the Papuan staff members had a positive opinion of Trakindo in this area, while another one-third was neutral. However, in the case of non-staff workers, Papuan workers had the smallest proportion of those with clearly positive opinion of Trakindo (29%). Among the remainder, 43% of Papuan workers held a clearly negative opinion, 21% neutral, 29% positive, and 7% gave no response to this question.

¹² PTFI's practice has been to have the head of each of the major contractor and privatized companies participate in the human rights training and annual assurance. These companies could also elect to expand the scope of training and annual assurance, as Trakindo did late in 2006. PTFI's intent is to expand the scope of the human rights training and assurance to include all workers at its Indonesian operations over a three-year period.

Table 7.1

Interviewed Workers' Opinions about Trakindo's Respect for Human Rights

	Clearly Negative	Neutral	Clearly Positive	No Response
Staff	21%	33%	46%	0%
Papuans	0%	33%	67%	0%
Non-Papuans	23%	33%	44%	0%
Non-Staff	31%	22%	43%	4%
Papuans	43%	21%	29%	7%
Non-Papuans	27%	23%	48%	2%
Total	27%	26%	44%	3%

Support for Papuans*a. Employment Opportunities:*

Trakindo's commitment to the local population is targeted for Indonesians in general. The company does not have any specific policies that target Papuans or the local 7-sukus. The company has recently staffed a newly created position of 'Papuan Development Superintendent.' This person is charged with the task of recruiting and developing Papuans for employment at Trakindo through collaboration with local Papuan development organizations, including PTFI's Nemangkawi Mining Institute.

Trakindo's lack of specific support for the Papuan community is evident from the low level of Papuan representation in the company's payroll. Of the skilled jobs at Trakindo, Papuans' share has declined from 10% in 2003-2004 to 8% in 2006, and is targeted to stay at this level through 2008.

Although Trakindo has the longest period of experience (over 27 years) working with PTFI, it has one of the poorest records with regards to Papuan recruitment, training and employment. The company has stated that they have

been stymied by Papuan “reluctance for self-development” and “low basic education levels.” However, the company has not shown that it has developed programs to enhance the basic education and the work skills of the Papuans to help them be employed by Trakindo. Trakindo has not provided ICCA with any plans indicating company’s expectations with regard to Papuan employment for the next 2-3 years and how those expectations are to be realized.

b. Local Purchases:

Trakindo does not have any formal policies, goals, or targets to assist Papuans in developing their local economy. Company management states that they will prefer to purchase goods and supplies locally provided that their quality requirements are met. However, Trakindo defines its local purchases as those procured from Indonesian sources in general, and does not make any special provision with regard to Papuan-owned enterprises. Trakindo would prefer an Indonesian source over imports where the price differential is within 10%. Otherwise, Trakindo relies on its corporate purchasing channels to satisfy its procurement needs. During the last 2.5 years, Trakindo’s total purchases were approximately \$7 million. Of this amount, about \$2.2 million were purchased from outside of Papua, and \$4.5 million were purchased from Non-Papuan businesses operating in Papua. Papuan businesses’ share of Trakindo purchases during this period represents approximately 1%.

Overall Views of Trakindo

During ICCA interviews, we asked all Trakindo workers a set of general questions as to the workers' overall opinion of the company. The first question related to their overall opinion of Trakindo as a good employer. These findings are noted in Table 7.2. We also asked the workers about their views of Trakindo as a good company for the Papuan people. The data are presented in Table 7.3. Finally, we asked Trakindo workers about their opinion of PTFI. Our intention was to observe any difference in workers' views of Trakindo when compared with PTFI. The findings are presented in Table 7.4.

Among the interviewed workers, employees' opinions differed between staff and non-staff workers. Staff level employees were clearly more positive in their views of Trakindo as a good employer, with Papuan staff members unanimously holding this opinion (Table 7.2). In this category, almost twice as many Non-Papuan employees had a neutral opinion compared to a clearly negative opinion of Trakindo as a good employer.

Table 7.2

Intensity of employee overall opinions about Trakindo as a good employer

	Clearly Negative	Neutral	Clearly Positive	No Response
Staff	12%	21%	67%	0%
Papuans	0%	0%	100%	0%
Non-Papuans	13%	23%	63%	0%
Non-Staff	26%	26%	47%	1%
Papuans	36%	21%	43%	0%
Non-Papuans	23%	27%	47%	2%
Total	21%	24%	54%	1%

The reported findings were different among hourly workers. Among the non-staff workers, the proportion of Papuans holding a positive opinion of Trakindo was 43%. However, when it came to holding a clearly negative opinion, 36% of Papuan non-staff workers felt this way as compared to Non-Papuans (23%).

Table 7.3

Intensity of employee opinions about Trakindo as a good employer of the Papuan people

	Clearly Negative	Neutral	Clearly Positive	No Response
Staff	3%	27%	70%	0%
Papuans	0%	33%	67%	0%
Non-Papuans	3%	27%	70%	0%
Non-Staff	28%	24%	43%	5%
Papuans	64%	21%	14%	0%
Non-Papuans	16%	25%	52%	7%
Total	19%	25%	53%	3%

The contrast of opinions between Papuan and Non-Papuan workers was clearly noticeable when asked about workers' opinion of Trakindo as a good employer for the Papuan people (Table 7.3). In the sample of interviewed workers, 64% of the Papuan hourly workers held a clearly negative opinion of Trakindo, and only 14% held a clearly positive opinion. The remaining 21% were neutral opinion about Trakindo.

Table 7.4

Intensity of employee opinions about PTFI as a good employer of the Papuan people

	Clearly Negative	Neutral	Clearly Positive	No Response
Staff	6%	18%	76%	0%
Papuans	33%	33%	33%	0%
Non-Papuans	3%	17%	80%	0%
Non-Staff	10%	14%	69%	7%
Papuans	7%	14%	71%	7%
Non-Papuans	11%	14%	68%	7%
Total	9%	15%	71%	4%

Trakindo employees were also asked about their opinion of PTFI as a good employer of Papuans. The data presented in Table 4 indicates the overall level of trust held by all categories of Trakindo's workers as to PTFI as a good employer for the Papuans. A majority of hourly workers (71% Papuans, 68% Non-Papuans) expressed their clearly positive view of PTFI. However, it is worthwhile to note that Papuan staff employees of Trakindo were about equally divided in their opinion of PTFI: 33% had clearly positive opinion, 33% - neutral, and 33% - clearly negative.

ICCA's Concluding Observations and Recommendations**for Corrective Action**

Whether the fault lies with PTFI for not impressing upon Trakindo the standards for employment and positive action toward implementation of PTFI's SEHR or with Trakindo for not taking seriously PTFI's operations site standards,

the reality is that PTFI and Trakindo must find ways to bring Trakindo employment and Papuan development standards into conformity with PTFI's stated commitments to employees and the Papuan community. This would include bringing their use of temporary, contract labor into conformity with Indonesian labor law, including reasonable and proper compensation for temporary contract workers who have worked with Trakindo for more than three years and a comprehensive plan to transfer other workers when they have worked for the maximum time permitted through contract labor suppliers.

Trakindo should also establish, with PTFI and on their own, comprehensive education, recruitment and training programs for Papuans—and especially those who are from the seven suku. Trakindo should use these programs to fulfill a public commitment to hire greater numbers of Papuans in their workforce. Trakindo should report to PTFI's management the commitment to education, training and employment of Papuans and the success of this commitment and the supporting programs should be independently audited.

Finally, Trakindo should fully implement the training of Trakindo employees in PTFI's Social, Employment and Human Rights policy (SEHR) and report publicly about the training, the number of employees trained, any human rights violations reported and the outcome of the investigations.

APPENDIX

HISWARA BUNJAMIN & TANDJUNG

MEMORANDUM

TO : International Center for Corporate Accountability, Inc.
Attn.: Mr. S. Prakash Sethi

FROM : David Dawborn/Santi Darmawan

DATE : **insert date of the original**

SUBJECT : **Freeport Indonesia – Temporary Worker Issues**

Dear Mr. Sethi,

We refer to your email dated 9 April 2007 attaching a note on Indonesian legal issues arising from the use of temporary workers employed by PT Freeport Indonesia (“**PTFI**”) and some of its affiliated privatised companies (the “**Attachment**”). We set out below our advice on the issues you have raised:

A. Description # 1 - Temporary Contractor - Supplied Workers

1. *PT Freeport Indonesia (“**PTFI**”) employs two kinds of workers. The first group consists of regular employees who are directly employed by PTFI. The second group consists of “temporary” contracted employees provided to PTFI by outside labor suppliers.*

Article 66 (2) (b) of Law 13 of 2003 concerning Manpower (“**Law 13**”) states that the employment relationship between a company which provides outsourced workers (Perusahaan Penyedia Jasa Pekerja/Buruh - the “**Outsourcing Company**”) and “temporary” contracted employees (the “**Outsourced Workers**”) may be in the form of (i) indefinite period employment (“**Permanent Workers**”) or (ii) definite period employment (Pekerja Untuk Waktu Tertentu - “**Contract Workers**”). A contract for both Permanent Workers and Contract Workers must be made in writing between each the Outsourced Worker and the Outsourcing Company.

Employment for a definite period must be of the nature described in Article 59 paragraphs (1) of Law 13 which state that:

- a. The work is expected to be completed within a short time frame and must take no longer than 3 (three) years;
- b. The work to be performed is a “one-off” task or the nature of the work is temporary;
- c. The work is seasonal; or
- d. The work relates to a new product or activity or to an existing product that is still in the experimental stage or phase.

Article 66 (2) (d) states that the agreement between the Outsourcing Company and the principal company providing the work to be performed (Perusahaan Pemberi Pekerjaan – the “**Principal Company**”) must be in writing (the “**Outsourcing Agreement**”) and must contain the provisions stated in Law 13. There is no employment relationship between the Outsourced Workers and the Principal Company (PTFI).

The question of temporary or permanent employment is between the Outsourcing Company and the Outsourced Workers. Therefore, in general, in implementing the outsourcing arrangement PTFI must comply with all provisions regarding outsourcing including Articles 59 (above), 65 and 66 of Law 13 (described below).

2. *These temporary contractor-supplied workers constitute approximately 15% - 20% of PTFI's total workforce. They are employed in virtually all departments and operations of PTFI. Moreover, the proportion of temporary contractor-supplied workers has remained relatively stable over the last 10+ years. In other words, these employees do not fill seasonal jobs whose continuity is unpredictable. A similar situation exists in many of the privatized companies affiliated with PTFI.*

Law 13 and the Decree of the Minister of Manpower and Transmigration No.KEP.220/MEN/X/2004 regarding the Requirements for Hand over of Works to other Companies dated 19 October 2004 (“**DC 220**”) are silent on the permitted number or percentage of Outsourced Workers in a Principal Company seeking to engage such services. We assume that there are one or more outsourcing agreements in place between PTFI and the Outsourcing Company. Law 13 and DC 220 do not provide any restrictions on the permitted period of an outsourcing agreement. However, PTFI must observe and comply with the requirements of Article 65 (2) of Law 13 and Article 6 (1) of DC 220 which require that the Outsourced Workers can only perform the following types of work:

- a. The work must be performed separately from the main activities of the principal company, whether in management or operational activities;
- b. The work must be undertaken under direct or indirect orders from the principal company explaining how the work is to be done in order to comply with the standards of the principal company;

- c. The work must be a supporting activity to the principal company's activities as a whole in order to enable smooth operation of the principal company;
- d. The work must not obstruct the production operation of the principal company – only supporting activities can be undertaken.

Article 65 (3) of Law 13 further stated that the Outsourcing Company must be a legal entity.

Article 6 (2) and (3) of DC 220 further state that the Principal Company which will outsource part of its operational activities to the Outsourcing Company must prepare a flow chart on relevant process activities. Based on that flow chart, the Principal Company will determine which types of works are considered as principal functions and which are supporting works and this must be reported to the relevant manpower authority. In practice, it is very difficult in many cases to distinguish between what is a principal function and which is supporting activities. The manpower authorities themselves are often unclear on applying this distinction and rarely enforce it actively.

From the above, you will see, however that at least in theory if the Outsourced Workers work in all departments and operations of PTFI, PTFI should not use the Outsourced Workers to conduct its main activities or activities related to its main production processes. They should only work in supporting activities.

If the Outsourced Workers do not perform seasonal jobs, PTFI must have regard to the type of employment relationship between the relevant Outsourced Workers and the Outsourcing Company. As mentioned above, a Contract Worker can not conduct permanent/regular work and the period of the contract can not exceed 3 years.

3. *The tasks performed by temporary contractor-supplied workers are not "unique" either as to activity or project that are time or task constrained. With few exceptions, these workers operate side-by-side with PTFI's regular employees, perform similar tasks and are indistinguishable from PTFI's own employees in any aspect except that they are hired by a contractor and then sent to PTFI.*

Who gives the contracts to the Outsourced Workers? There should not be any contract between PTFI and the Outsourced Workers (who, as described above, are employees of the Outsourcing Company).

There is no prohibition on the Outsourced Workers working side by side with PTFI's regular employees, provided the requirements on the use of Outsourced Workers referred to above are fulfilled. The duties should be 'supporting' activities. It is a concern therefore that the tasks are indistinguishable from those performed by PTFI's own employees and that this has been continuing for many years.

4. *These temporary contractor-supplied workers are given contracts of various durations. These contracts are invariably renewed and rolled over from one period to another with the result that many contracted workers have been doing similar jobs for over three years and even longer.*

See our advice in point 1 above.

As to duration of the contract between the Outsourcing Company and the Outsourced Workers, Article 59 further states that the contract for a Contract Employee may be extended. Normally, the initial period of the contract is for 2 years and may be extended once up to 1 year. The Outsourcing Company is required to notify the Outsourced Worker no later than 7 days prior to the date of expiry of the contract if it wishes to extend the contract. The total term of the contract with the Outsourced Workers cannot exceed 3 years. The contract can only be renewed 30 days after the expiry date of the previous contract has lapsed and can be renewed once for a maximum of 2 years. Therefore, to the extent that the type of work (see our advice above) and the extension/renewal of the contract between the Outsourced Workers and the Outsourcing Company are in accordance with Article 59, we are of the view there should be no legal implications for PTFI as it has no direct employment relationship with the Outsourced Workers (who remain employees of the Outsourcing Company). As we mentioned above, any failure to comply with such requirements may result in the relevant Outsourced Employee being deemed, by law, to be an employee of PTFI.

5. *Temporary contractor-supplied workers are paid approximately 60 – 65% of the wage paid to PTFI's regular employees. This wage gap persists regardless of these workers' skill, experience, and job tenure when compared with PTFI's own employees.*

Article 65 of Law 13 provides that Outsourced Workers shall receive the same working protection and terms and conditions as employees of the Principal Company (of equivalent position). However Article 65 does not further clarify whether they must receive the same terms and conditions regarding their salary/wage. Article 66 (2) c of Law 13 further states that wage and welfare protection, terms and conditions, and any employment disputes raised are the responsibility of the Outsourcing Company, not PTFI. The Outsourcing Agreement must make this clear.

6. *In a number of cases, PTFI transfers these temporary contractor-supplied workers to its own payroll as regular employees. These temporary workers, when transferred to PTFI's payroll receive wages and benefits, including job security that is comparable to PTFI's regular employees.*

The fact that PTFI transfers the Outsourced Workers to its own payroll as its regular employees may be used by the Outsourced Workers in the future to argue that they have actually always been an employee of PTFI. We understand that PTFI only pays the outsourcing fee to the Outsourcing Company pursuant to the terms of the Outsourcing Agreement. The funds used to pay wages of the Outsourced Workers must be paid directly by the Outsourcing Company (as employer) to the Outsourced Workers. If PTFI pays the wages directly, it is likely that there would be a deemed employment relationship with PTFI created.

7. *There is, however, no transparent system or objective criteria that would indicate how these temporary contractor-supplied workers would become eligible to be employed by PTFI as regular employees. In other words, it is not possible for an independent reviewer to examine a worker's personnel file and*

work history and predict as to when and under what conditions this worker would be likely to become a PTFI employee.

Legally speaking, the Outsourced Workers remain employees of the Outsourcing Company when that relationship is terminated whereas the transferred workers move over to become direct employees of PTFI. In an ordinary case, Outsourced Workers return to the Outsourcing Company upon termination of the Outsourcing Agreement. In practice, however, if the principal company is willing to employ the Outsourced Workers directly, they must first terminate their employment with the Outsourcing Company. It is a question for negotiation in each case whether PTFI recognises post services provided or whether it regards the transferred workers as fresh recruits when they become direct employees. A problem could arise if the transferring employee does not agree to any employment history being provided by the Outsourcing Company. However, in any event the details of any employment history transferred must also be agreed by the transferring workers.

8. *PTFI has asserted that temporary workers are akin to probationary workers whose employment status is regularized once they have meet certain qualifications and that there are available vacancies within the company's overall staffing patterns. However, as stated above, the current employment practices of temporary contractor-supplied workers do not seem to fit the normal conditions applied to workers during their probationary status.*

Temporary workers engaged by PTFI directly have some similarities in practice with probationary workers but the latter have far less protection. Legally speaking, however, temporary workers provided by an Outsourced Company are totally different from probationary workers for the reasons described above. Outsourced Workers from Outsourcing Companies are not employees of PTFI. It is correct that PTFI could require Outsourced Workers to be removed by the Outsourcing Company (in the same way that probationary employees of PTFI could be terminated immediately during the probation period). However, no probation period applies either for the Outsourced Workers or the Contract Workers from PTFI's perspective. From PTFI's perspective, probation will only apply to its own Permanent Employees. As we advised in point 7 above, if PTFI wishes to employ directly the Outsourced Workers as its permanent employees or under a contract arrangement, the Outsourced Workers must first terminate his/her employment relationship with the Outsourcing Company.

A.1. Legal Questions

1. *It is our understanding that employment of temporary workers by PTFI falls within the purview of Law Number 13 Year 2003 re: Employment ("Law 13/2003"), Decree of Minister of Manpower and Transmigration Number KEP.101/Men/VI/2004 re Prerequisites of Hand-Over of Some of Implementation Works to Other Company ("Decree 220/2004").*

Your understanding is correct. The basic principles of "temporary" contracted workers provided by outside labour suppliers (or the Outsourced Workers) are governed by:

- a. Law No.13 of 2003 dated 25 March 2003 regarding Manpower;

- b. Decree of the Minister of Manpower and Transmigration No.KEP.220/MEN/X/2004 regarding the Requirements for Handover of Works to another Company dated 19 October 2004 (not KEP. 101/Men/VI/2204 as mentioned in your Attachment).
2. *Please provide your legal opinion separately for each and every operating condition described above in the section "Situation Description # 1 and the extent to which these practices fall within the "acceptable" category of applicable laws.*

Please see our analysis above. As a general comment, it seems to us from your description there may be some major misperceptions about the position and rights of certain Outsourced Workers working at PTFI's operations. It seems that PTFI may regard them as effectively its own employees (which is legally not correct if they are provided by the Outsourcing Companies). Also, the length of such work and its nature may not, strictly speaking, comply with the rules, for outsourced workers under Law No. 13. Having said that, such approach is not that uncommon in Indonesia. One problem that arises is that the Outsourced Workers, after a period of time, will come to regard PTFI, the source of work, as their de facto employer.

A.2. Types of Remediation and Restitution Required under Applicable Laws

For each and every finding of non-compliance with the relevant laws by PTFI and its privatized companies, please indicate the relevant remedies prescribed under the applicable laws.

In principal PTFI (and the Outsourcing Companies) must comply with all requirements referred above.

Any failure to comply with Article 59 of Law 13 (see point A.1 above) may result in the employment status of the relevant Outsourced Workers (based on contract) being deemed by law to become that of an indefinite period employment (or permanent employee). As stated in point A.1 above in principle the employment relationship exists between the Outsourced Workers and the Outsourcing Company, not PTFI. However, as it is required by Article 66 (2) (d) that the Outsourcing Agreement must contain the provisions stated in Law 13, PTFI must ensure that the Outsourcing Agreements and their implementation comply with Article 59 of Law 13. Law 13, however, is silent as to penalties or administrative sanctions for failure to comply with Article 59 above.

Article 65 of Law 13 states that any failure to comply with Article 65 (2) and (3) (see point A.2 above) may result in the Outsourced Workers being deemed by law to become employees of the Principal Company.

As with Article 66 of Law 13, any failure to comply with Article 66 (1), (2) (a), (b), (d) and (3), may result in the Outsourced Workers being deemed by law to become employees of the Principal Company. The following are the relevant provisions:

Article 66

- (1) The Principal Company shall not use Outsourced Workers to perform main activities of the Principal Company or activities related to direct production processes - only for supporting activities (as explained above).
- (2)
 - (a) There must be a working relationship between the Outsourced Workers and the Outsourcing Company.
 - (b) The working contract between the Outsourcing Company and the Outsourced Workers referred to in a above is in the form of indefinite period employment and/or definite period employment which comply with Article 59 of Law 13 - both must be made in writing (as explained above).
 - (d) The Outsourcing Agreement must be in writing and must contain provisions stated in Law 13 (as explained above).
- (3) The Outsourcing Company must be a legal entity and posses a licence to operate as such from the relevant manpower authority (as explained above).

Law 13, however, is silent as to penalties or administrative sanctions for failure to comply with Articles 65 and 66 above.

We have made further informal discussions (on a no names basis) with the Department of Manpower. As mentioned above, in practice it is difficult for the Department of Manpower to distinguish which are the main functions and which are the supporting activities of the Principal Company. Obviously the deeming of Outsourced Workers to become employees of PTFI would create many difficulties in practice and the regulations do not resolve these. It would be necessary to look at the terms of the relevant Outsourcing Agreement and employment contracts between the Outsourcing Company and the workers. However, the Department of Manpower informed that if there is no provision in the Outsourcing Agreement in respect of settlement of dispute on these matters, theoretically if the Principal Company fails to comply with Articles 65 and 66 above this may result in the Outsourced Workers being deemed by law to be employees of the Principal Company as permanent employees.

B. Description # 2 F - Unequal Benefits for Different Classes of Workers

1. *PTFI provides extra travel allowances for travel back home during holidays and vacations to workers who originate from locations outside PTFI's work site. The rationale of this practice is based on these facts that these workers migrate from different parts of the country and cannot afford the transportation costs to return home to their families during the time of their annual vacation or national holidays.*

Normally, the amount of an allowance will be agreed between the employer and each employee in advance of commencing employment. It is common for certain employees to be given a different amount of travel allowance according to where they were hired from. For your information, Law 13 also states that one component of the Compensation Payment (in the case of employment termination) covers expenses or costs of the relevant employee/worker and their families returning to the place from where they were hired (if applicable).

If, however, there are generally applicable benefits, those benefits must be provided to each qualifying member of the relevant class of employee. It may be agreed in the outsourcing agreement that PTFI will pay an amount to the Outsourcing Company to cover holiday travel expenses of the Outsourced Workers. The Outsourcing Company would pay this to the Outsourced Workers.

2. *In practice, all Non-Papuan workers are assumed to qualify for this benefit. This is regardless of the fact as to whether or not these workers currently reside permanently in near PTFI's job site.*

Articles 5 and 6 of Law 13 provide that:

“Any manpower has equal opportunity to obtain a job without discrimination.....”

“Any worker/labour is entitled to obtain equal treatment without discrimination from the employer.....”

The elucidation of Law 13 relating to Articles 5 and 6 above states:

“Any employee has equal right and opportunity to obtain proper job and without distinguishing based on gender, ethnic group, race, religion and political ideology in accordance with their interest and capability

“The employer must give rights and obligations to the labor/worker without distinguishing based on gender, ethnic group, race, religion, color and political ideology”.

Based on the above provisions and our informal discussions, on a no names basis, with the Department of Manpower those employees who have the same position and capability should receive the same benefits regardless of their ethnic group.

However, as noted in paragraph B1 above, it is typical in Indonesia that annual holiday travel allowance is only paid to those workers who are hired in a location away from PTFI's operations. We do not believe it would be discriminating to not pay such travel allowance to employees who were hired in the area of PTFI's operations.

3. *An opposite situation exists in the case of Papuan workers who are assumed to reside in the local areas. PTFI has recognized that for a great many Papuan workers it is equally necessary to travel long distances, and at considerable cost, to visit their families in their distantly located villages. The fact of their being Papuan workers, ipso facto makes them ineligible for this benefit.*

Please see the principles described in our advice in points B.1 above. The same principles apply to this opposite situation.

B.1 Legal Questions and Remedies

1. *Although not in original intent, the current practice has the practical impact of “ethnicity based discrimination”. Is this assertion correct? If so, which provisions of the relevant Indonesian Labor and Employment Law would apply?*

In addition to Articles 5 and 6 of Law 13, Indonesia, by Law No.21 of 1999, has ratified Convention No.111 of the International Labour Organisation concerning Discrimination in respect of Employment and Occupation (“**ILO Convention 111**”).

Under Article 1 of ILO Convention 111 the term “discrimination” includes:

- (a) any distinction, exclusion or preference made on the basis of race, color, gender, religion, political opinion, nationality or social origin, which has the effect of nullifying or impairing equality of opportunity or treatment in employment or occupation;
- (b) such other distinction, exclusion or preference which has the effect of nullifying or impairing equality of opportunity or treatment in employment or occupation as may be determined by the Member concerned after consultation with representative employers and workers organizations, if applicable, and with other appropriate bodies;

Articles 2 and 3 of ILO Convention 111 further state that any distinction, exclusion or preference in respect of a particular job based on the inherent requirements of that job shall not be deemed to be discrimination. The terms of “employment” and “occupation” include the opportunity to participate in training, to obtain a job or occupation *and the terms and condition of employment*.

Subject to our comments above, in our view, if PTFI provides different benefits to employees occupying the same positions on the basis of their ethnic group (Non-Papuan and Papuan workers) or for other reasons referred to above, PTFI may be in breach of Articles 5 and 6 of Law 13 and will not have acted in line with the spirit of ILO Convention 111.

Under Article 190 of Law 13, the following administrative sanctions (of increasing severity) may be imposed on parties which breach Articles 5 and 6:

- a. reminder;
- b. written warning;
- c. restriction on business activity;
- d. freezing of business activity;
- e. revocation of approval;
- f. revocation of registration;
- g. suspension of part or whole of production equipment;
- h. revocation of licences.

Law 13 also states that details of the administrative sanctions mentioned above will be further regulated by the Minister. In our experience, however, the Minister is unlikely to impose such administrative sanctions in this kind of case.

The ILO Convention 111 is silent on the sanctions applicable for breach of these principles, however, it is stated in the opening of the Convention that discrimination constitutes a violation of rights enunciated by the Universal Declaration on Human Rights.

As noted above however, where travel benefits are expressly paid to a particular worker based on criteria such as place of hiring (and therefore the need of the relevant employee to undertake particular travel for annual home leave, etc) and not just because of their ethnic or racial status, we would not view this as 'constituting ethnically based discrimination'. On the other hand, if all workers were given a travel allowance as a matter of courtesy (without regard to the place of hire) but Papuan workers were excluded, that might amount to discrimination.

2. *What remedies should be required for PTFI to comply with the law. It should also be noted that PTFI's own Human Rights and Employment Policy bars the company for any kind of discriminatory work-place practices based on ethnicity, gender and other similar criteria.*

Please see our advice in point 1 above.

The above views and opinions are based on the information you have provided and not actual information regarding the actual relevant manpower practices of and at PTFI. We should point out that in practice the manpower authorities in Indonesia have not actively enforced many of these principles and deviation from the regulatory requirements is common (as we expect has happened at PTFI). We expect that there will be stricter enforcement of the rules going forward as the manpower authorities become more aware of outsourcing practices and issues arising.

We hope the above will be of assistance. Please let us know if you have any further questions.

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