Minimizing the Natural Resource Curse “Innovation of Extractive Industry Governance Policy in Bojonegoro Regency”

Ahmad Sholikin[1], Poppy Sulistyaning Winanti[2], Mada Sukmajati[3]
{ahmad.sholikin@unisda.ac.id[1], poppysw@ugm.ac.id[2], madasukmajati@yahoo.com[3]}

Universitas Gadjah Mada, Yogyakarta, Indonesia

Abstract. This research aimed at describing the various efforts to minimize the natural resource curse initiated and developed by the government of Bojonegoro Regency in ensuring that extractive industry activities will bring social benefits to all communities and minimize social costs. This research used the library research method to elaborate various kinds of literature in the form of books, journals and literature relevant to the theme. This method aimed at verifying previous researches, as well as finding novelty in this research.

Keywords: Policy Innovation; Minimizing the Natural Resource Curse; Bojonegoro

1 Introduction

This research aimed at describing the various extractive industry governance policy innovations in order to minimize the natural resource curse in Bojonegoro Regency. The Bojonegoro Regency was radically transformed before and after 2008. Prior to 2008, the government of Bojonegoro was considered one of the worst regencies in Indonesia. In 2011, McCulloch analyzed the economic characteristics and performance of regencies in Indonesia between 2001 and 2007. His research indicated that the governance index in Bojonegoro was among the worst in Indonesia [1]. In addition, H.M Santoso, a former Regent of Bojonegoro, was caught in two corruption cases. The two corruption cases involved corruption in Cepu Block socialization fund amounting to IDR 3.8 billion and corruption in the Regional Revenues and Expenditures Budget (Anggaran Pendapatan dan Belanja Daerah (APBD)) of Bojonegoro of 2007 in the amount of IDR 6 billion.

The management of Indonesia's natural resources in the era of decentralization poses many problems. The hypothesis of the natural resource curse in the era of regional autonomy is proven true because the central government grants greater power to regions to utilize their natural resources. Not only the central government but also the local government (Pemda) enjoys the outcome of natural resource exploration through the arrangement of natural resource revenue-sharing funds. The redistribution of revenue sharing from natural resource management among different levels of government is complicated by political elements, problems of macroeconomic stabilization, and efficiency [2]. This is marked by a decline in investment and low economic growth in natural resource-rich regions. The central government is considered to be a predatory state that exploits the region on a large scale, especially oil and gas-rich regions such as Nangroe Aceh Darussalam, East Java, Papua, Riau, and East Kalimantan. The stipulation of the Decree of the Minister of Finance No. 24/KM.66/2002 concerning oil and gas

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revenue sharing is considered not transparent because it only provides 1-2% of the actual figure for oil and gas extraction in each region.

However, the above hypothesis does not apply to Bojonegoro Regency. Instead of being a failure, Bojonegoro's economic growth rate was growing rapidly as seen from the Regional Gross Domestic Product (GDP), in 2009 reaching IDR 16,819 trillion. It increased to IDR 22.205 trillion in 2010 and further increased to IDR 27.615 trillion in 2011 and continued to increase until 2015. This data shows that empirically, it is essential to see how Bojonegoro successfully made policies to minimize the natural resource curse. Amid the pessimism of researchers, states that politicians in the midst of the abundant natural resources will try to gain political advantage and stay in power. Many politicians in resource-rich regions distribute public work in exchange for electoral support because they believe that these activities influence voting behavior [3]. The natural resource boom can increase incentives for politicians to engage in rent seeking activities. These incentives lead to a lower number of productive activities in the economy. There are two important literatures that attempt to summarize and evaluate this growing natural resource curse literature. The first is the Working Paper Series by Jeffrey A. Frankel [4] and another is a survey in the Journal of Economic Literature by Frederick Van der Ploeg [5]. A survey by Jeffrey A. Frankel diagnoses the resource curse and summarizes the potential mechanisms in the pattern of inverse relationships between natural resource dependence and economic growth.

Indonesia is one of the countries endowed with abundant natural resources, so there are a lot of researches discussing the hypothesis of natural resource curse in Indonesia as conducted by Rosser [6], Komarulzaman & Alisjahbana [7] and Feryawan [8]. Rosser [9] argues that Indonesia is an example of a country that has succeeded in avoiding the natural resource curse. This is indicated by the good performance of the Indonesian economy for 3 decades prior to the 1997/1998 economic crisis. Countries with rich natural resources, especially oil and gas, do not have any positive correlation with the quality of democracy, even from an economic perspective they tend to be unstable. In African countries, for example, the presence of oil and gas actually triggers the emergence of civil war [10]. Regions with high natural resource wealth tend to have high income levels. Therefore, the low growth in natural resource-rich regions is due to low initial income, not dependence on natural resources. However, Sebastian and Raveh's research [11] shows that countries with a high degree of fiscal decentralization (part of regional autonomy) are relatively more vulnerable to the natural resource curse phenomenon than countries with centralized fiscal policies. Regional autonomy and fiscal decentralization increase the rent (revenue sharing) of natural resources received by regions that possess natural resources. According to the large rental revenue of natural resources, it increases the possibility of the emergence of rent seeking behavior and corruption that hinders economic development [12]. Brazil is an example of a country with decentralized fiscal policies which shows that regions with large natural resource rents tend to be more corrupt, which is indicated by poor public service performance [13].

The common thread that can be drawn from the above explanation is that countries with abundant oil and gas revenues tend to have lower economic growth, underdeveloped democracies, greater social unrest, and poor institutions. The literature on the natural resource curse describes the economic and political outcomes that result from an abundance of natural resources, but little literature offers policy advice. One of the policies produced by politicians and bureaucrats in oil producing countries is attempting to find policy solutions and institutional designs to deal with the dire consequences of petroleum revenues. The situation in Bojonegoro is in stark contrast to the existing literature. Several researches explain that natural resources-rich countries tend to worsen transparency and accountability. Even in another extreme, the elites can be involved in rent-seeking activities [14]. Thus, this research attempts to fix this problem by investigating why various policy innovations to minimize the natural resource curse emerged in Bojonegoro. Meanwhile, there are few researches that focus on good governance in resource-rich countries such as Norway, Canada, and Australia. Thus, this is the first research to discuss the emergence of various policy innovations to minimize the natural resource curse in natural resource-rich regions at the regional level. This research, therefore, provides an important opportunity to advance the understanding of the resource curse.

2 Extractive Industry Governance Innovation in Bojonegoro Regency

Bojonegoro Regency is one of 514 regencies in Indonesia and one of 38 regencies in East Java Province. Located on the border of East Java Province and Central Java Province, Bojonegoro is regency located in the western part. The implementation of decentralization in 1999 to elect a local leader and distribute welfare to local communities failed to take Bojonegoro out of poverty. During the early 2000s, Bojonegoro was still underdeveloped and ranked the lowest in the human development index, 30 out of 37 regencies in East Java province and ranked at the highest in poverty. Oil mining in Bojonegoro began when Mobil Cepu Ltd discovered huge oil and gas reserves in Banyu Urip. In 2001, Banyu Urip, a newly discovered oil field, was estimated to have reserves of 445 billion barrels of oil, and 8.1 billion of gas. As a discourse, Santoso, the Regent of Bojonegoro previously started, through the media, to introduce what oil can be brought and why building facilities to support its production is essential. He is also involved and engaged in discussions between the community, the central government, and the company, but unfortunately the Cepu Block and the future of Bojonegoro are under the planning stages. Bojonegoro did not receive any revenue from this sector until 2010. Suyoto, the current Regent and Santoso's successor, introduced extractivism, during his first term of office between 2007-2013. Since then, his narrative of how the oil mining industry generates wealth and how this prosperity benefits Bojonegoro has neatly stitched together the realities of extractive industries and prosperity in the region.

Bojonegoro is a new resource-rich region in Indonesia for less than a decade. In the beginning of the period, there were several challenges and barriers that the local government in Bojonegoro had to respond to in order to prevent the resource curse. These barriers and challenges are related to fiscal management, social-environmental impacts and costs of extraction activities and corporate social responsibility. Bojonegoro needs to manage the volatility of its revenue which may affect poor planning and spending on regional budgets because the Revenue Sharing Fund (Dana Bagi Hasil) is unstable and fluctuates every year. To overcome these challenges and barriers, the local government of Bojonegoro, supported by an alliance of national and local civil society organizations, initiated and developed several efforts and innovations. The Bojonegoro Regency Government took the initiative to issue various policies, including Regional Regulation No. 11 of 2011 concerning Equity Participation in Bojonegoro Regency; Regional Regulation Number 23 of 2011 concerning Acceleration of Regional Economic Growth in the Implementation of Exploration and Exploitation as well as Oil and Gas Processing in Bojonegoro Regency; Regional Regulation number 6 of 2012 concerning Transparency of Revenue Management, Environment, and Corporate Social Responsibility in Oil and Gas Business Activities; and number 5 of 2015 concerning Corporate Social Responsibility; and the Regional Regulation Draft on the Perpetual Fund.

2.1 Transparency in Oil and Gas Revenue

The implementation of transparency and accountability in Bojonegoro Regency includes the policy planning to reporting stages. The accounting mechanism that has been included in the Regional Regulation no. 28/2012 is considered the first innovation in Indonesia and even in the world. The key aspects of this mechanism are as follows: a) Establish an Oil and Gas Transparency Committee at the regency level, with various stakeholders including government, companies and civil society. b) Set an annual work agenda that coordinates extractive industry transparency management and is approved by various stakeholders. c) Promote inclusive access to information related to the transparency of the oil and gas extractive industry. d) Socialize and publicize information related to oil and gas extraction, particularly oil and gas revenues (Revenue Sharing Fund and Participating Interests), social and environmental information - including job opportunities, emergency response plans, AMDAL, as well as information on CSR programs. An interesting fact is that the process of increasing transparency at the local level is carried out in parallel with similar initiatives at the central level, such as the Extractive Industries Transparency Initiative (EITI) - although the transparency report did not include sub-national. However, the implementation of the Regional Regulation on transparency was held back at the provincial level and the Ministry of Home Affairs because it was under review for more than a year. Currently, the ongoing transparency mechanism is the disclosure of APBD data and the Dialog Jumat with the Regent. In addition, dialogue also acts as a mediator for conflicts related to oil and gas operations.

2.2 Innovation in Participatory and Sustainable Planning

Oil and Gas revenue management in Bojonegoro is directed at Medium-Term Regional Development Plan (RPJMD). The RPJMD of Bojonegoro Regency focuses on the vision to make Bojonegoro a source of people's economy, and local socio-culture for the realization of a faithful, prosperous, and competitive society; the vision of which is divided into 7 development visions: (1) Realizing a social life system based on religious values and local wisdom; (2) Realizing clean, transparent and responsible governance, (3) Realizing the continuous improvement of the quality of human resources; (4) Creating a sense of security and alignment for women, children, the disabled, and the poor; (5) Realizing an increase in welfare based on the people's economy and the creative economy; (6) Realizing regional economic competitiveness based on local potential; and (7) Realizing equitable and environmentally friendly infrastructure development. Bojonegoro invites stakeholders to get involved in Participatory and Sustainable Planning. This scheme is actually not unique to Bojonegoro but works more meaningfully in the district. Local Social and Economic Development (LSED) Planning was used for this planning. The result of the LSED is the Sustainable Regional Development Plan *(Rencana Pembangunan Daerah Berkelanjutan (RPDB))* document, which involves: 1) Priority to development. In Bojonegoro for example, there are 2 main priorities in the RPBD, namely (a) improving education and health standards for human resource development, (b) increasing the economic sector base in agriculture and MSMEs. The local government arranges to reinvest oil and gas revenues in the two basic economic sectors to support the community's economy, 2) List of programs and activities available for a five-year period, and 3) Budget accounting available. Ironically, multi-stakeholder forums for oil and gas exclude local communities and vertical government agencies yet.

2.3 Innovation in Distribution of Oil and Gas Funds to Rural Areas

The local government of Bojonegoro strives to maintain regional balance and equality within the regency by implementing the Distribution of Oil and Gas Funds to Rural Areas. In fact, the Indonesian government has designed an instrument for the Village Fund Allocation (ADD). This instrument is regulated in the Regional Regulation through Domestic Regulation no. 37/2007 on Guidelines for Rural Financial Management. The guidelines state the mandatory regulation on the minimum Village Fund Allocation *(Alokasi Dana Desa (ADD))* to be 10 percent of the total APBD budget. Village Fund Allocation is implemented to minimize the risks of mining extraction activities borne by the villages around the site, including damage to infrastructure (roads, etc.), environmental damage, extraction-related disasters, and social conflicts. Thus, local governments strictly regulate DBH for regencies and villages through Regulation of Regent no. 31/2009 concerning Guidelines for Rural Proportional Budget Allocation based on Variable Coefficients in the region. The Regulation of Regent has two objectives, including (a) increasing the ADD allocation from the total regular ADD. Notwithstanding the regular ADD allocations from the APBD, an additional 12.5% of the total annual DBH for oil and gas ADD is received by the Local Government of Bojonegoro, (b) prioritizing budget allocation for villages adjacent to oil extraction sites. 12.5 percent of the ADD budget is allocated as follows: producing villages (12.5 %), ring I villages (10 %), ring II villages (7.5 %), other villages (70%). Therefore, each village in Bojonegoro receives a much higher budget than the regular ADD budget allocation prior to the implementation of oil and gas ADD. However, the following challenges also occur due to the poor capacity of the village government to manage and regulate budget allocations and expenditures. There are institutional capacity issues at the village level which may result in new corruption or misuse of budget allocations.

2.4 Local Content

The mix of literature suggests that the idea of local content is actually defined in a variety of ways. In a common and simple definition, local content refers to policies or programs that aim at maximizing the procurement of goods, services and other benefits from extractive economic activities, such as sustainable jobs and infrastructure. Hence, the idea of local content can be interpreted from any practice. For example, it can be construed, in relation to local procurement, by the business activities of a company. Meanwhile, in another extreme, it is sometimes used simply to describe any business with a permanent operational office in a certain area. Local content is also defined as the added value brought to the host country (or region or locality) through workforce development (local workforce employment and training), and investment in supplier development (local development and procurement of supplies and services).

In short, the idea of local content arose because extractive industries often create a lot of problems but are enjoyed by few people only. Local content policies seek to solve the problem by emphasizing the advantages of "localization": broadening or extending the benefits of oil, gas and mining activities to the local or national economy. The local content policy aims at ensuring the accessibility of all local stakeholders to any economic opportunity in the extractive industry value chain, such as any employment or support services. The local government of Bojonegoro supports the Local Content initiative to ensure that the benefits from extraction activities are brought to local communities and local entrepreneurs. Through Regional Regulation No. 23/2011 concerning Optimization of Local Content, local governments aim at involving and empowering all local potentials in mining operations such as local labor, equipment, and materials. The premise of local content innovation is to generate higher benefits and job creation for local communities in Bojonegoro.

3 Conclusion

Various extractive industry governance policy innovations in Bojonegoro Regency provide several things to learn. First of all, decentralization paved the way for innovation at the local level. In addition, the role of committed agents, both regents and local bureaucracies and strong civil society organizations, is critical. The Regent of Bojonegoro is relatively open-minded to innovation. Good innovations and reforms will also contribute to strengthening the public legitimacy and political support needed because the majority parties and Islamic social organizations in his early days opposed him for elections. The presence of national CSOs also greatly contributed to covering the absence of strong local civil society organizations in the early period. Not only have they, CSOs, supported governance reform but they also have successfully increased the capacity of local CSOs.

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