

# The Extractive Industries Transparency Initiatives Challenges of Transparency in the Extractive Industry Sector

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**Abstract:** Transparency is a solution to various problems in the extractive industry and also perceived as the main prerequisite to achieving good governance. Transparency in the extractive industry can encourage the quality of natural resource management so that natural resources owned by Indonesia are expected to have a significant effect on people's welfare and development. EITI (*Extractive Industries Transparency Initiatives*) is a global standard for transparency in the extractive industry sector. The advantage of Indonesia to implement transparency according to the EITI Standards from the perspective of the government is that transparency will facilitate the process of communication and information to the public. Through published information, the public can find out how far the government records and manages extractive industry sector utilization. From a business standpoint, transparency will provide equal information to all parties. With the same information, business people will compete healthily to provide optimal benefits for the country. From the perspective of the community, transparency can provide information to the public about the natural resources extracted from the region. Communities can monitor whether management is appropriate and provide fair benefits.

## 1 INTRODUCTION

The industrial sector always plays an important role in the country's economy, especially as a driver of economic growth. One industry that holds an important role in the extractive industry sector. Extractive industries are one of the biggest contributors to state revenue in Indonesia. The data of the *Extractive Industries Transparency Initiative* (EITI) stated that 25% of total state revenue comes from extractive industries. The Data from the Ministry of Energy and Mineral Resources states that in 2017, minerals and coal contributed 40.6 trillion Non-Tax State Revenues (PNBP) or an increase of 48.3 percent from 2016.

Seeing the strategic position of the extractive industry towards state revenue, poverty in Indonesia is still very high. An industry with such great potential should be able to become an engine to improve people's welfare and reduce poverty. Unfortunately, extractive industries have not been able to do much to improve the people's economy due to the poor and weak governance of extractive industries, which also has an impact on the high potential for corruption in this sector. The weak

transparency in all extractive industry lines has an impact on the ease of political actors to commit corruption without being examined. Environmental damage is still largely due to mining techniques and waste that has an impact on society. This happens because many mining companies do not pay for reclamation and post-mining guarantees. Even though the obligation is regulated by Law No. 4/2009 concerning Minerals and Coal. In China, most cement factories are closed because they are believed to pollute the environment, which causes factory workers and the surrounding community to get acute respiratory disorders. Similar conditions also occur in India, where the government began to think about reorganizing the mining sector because it has taken many lives. According to the Antara News portal in 2017, as many as 16 miners died due to an ecological disaster (landslide) at the Jharkhand coal mine in January 2017.

Besides, countries with abundant natural resources tend to be in an unfavorable economic condition when compared to countries without natural resources. This condition happens because of the countries with high natural wealth are vulnerable to changes in commodity prices, especially if the financial system is not well developed (Ploeg, 2011).

Therefore, various international civil society organizations jointly campaigned for *Publish What You Pay* in 2002 to invite extractive industry companies to inform government payments to encourage transparency in this sector while also protecting the government and companies from the game of changing commodity prices.

For this purpose and to be a solution to the problems faced by extractive industries, increasing transparency in the management of extractive industries is important. Transparency means that people understand the whole decision-making process carried out by the government. Thus, transparency means that it is open, easy, and accessible to all parties who need it and is provided adequately and easily understood. Transparency requires that the public service implementers have knowledge of the problems and relevant information to those of service activities. Transparency is built in an atmosphere of the free flow of information. In this atmosphere, processes, institutions, and information can be directly accessed by those who are interested. In addition, enough information is also available to understand and monitor these three things.

In the process, the *Extractive Industries Transparency Initiative* (EITI) was formed. EITI is expected to be a tool for the Indonesian government to eradicate corruption and increase transparency in the extractive industry sector.

## 2 METHODOLOGY

Through a qualitative approach with a descriptive method, this study aims to obtain a picture of how the practices of transparency in the management of extractive industries in Indonesia are encouraged by EITI Indonesia. There are two sources of data in this study, namely primary data and secondary data.

### a. Primary Data

The main data obtained from respondents or research subjects. In this study, the authors get primary data through the process of interviews, observation, and document search. This primary data was obtained through EITI Indonesia and Publish What You Pay (PWYP) Indonesia.

### b. Secondary Data

Data is obtained from secondary sources (other than primary data), which are intended to supplement information and strengthen the findings of primary data. Secondary data in this study were obtained

through news or articles that are relevant to the research.

## 3 EXTRACTIVE INDUSTRIES TRANSPARENCY INITIATIVE (EITI)

Increasing transparency is a solution to various problems in the extractive industry (Richard, 1994). Transparency in this extractive industry can encourage the quality of natural resource management so that natural resources owned by Indonesia are expected to have a significant effect on people's welfare and development. The experience of several countries in the extractive industry sector shows that transparency and accountability will contribute positively to economic growth, and reduce the risk of corruption and conflict (Evi, Francisia and Yesi, 2014). Besides, transparency in extractive industries is also a consensus for good governance.

History says that the idea of transparency in the extractive industry did not come suddenly. The idea has been campaigned globally by involving a coalition of international organizations that are transmitted to domestic actors to be accepted and adopted by the state. That is, there is intellectual hegemony that helps to make transparency in the extractive industries possible. There is a political process involved until this idea can be accepted, regardless of whether there is another agenda behind the global campaign of extractive industry sector transparency, both in the global political perspective and in the ideological perspective that rides this idea.

Transparency is a collective spirit of striving to improve the governance of extractive resources in Indonesia. In addition to data disclosure, transparency requires political will and incentives to be able to apply evenly throughout the extractive industry decision chain. Transparency in this extractive industry is globally institutionalized in the *Extractive Industries Transparency Initiative* (EITI).

EITI (*Extractive Industries Transparency Initiatives*) is a global standard for transparency in the extractive industry sector. British Prime Minister Tony Blair is getting the initiative of transparency in the extractive industries (*Extractive Industries Transparency Initiative*), or EITI, in the forum of *the World Summit for Sustainable Development*, Johannesburg, 2002 (Clayton and Sadler, 2014). The following year, the G-8 published a declaration entitled "*Fighting Corruption and Improving Transparency*," which prioritizes transparency in the extractive industry (World Bank, 2010). A wave of transparency ultimately creates a global coalition of

elements from governments, corporations, civil society organizations, investors, and international financial institutions.

The main objective of EITI is to strengthen government and company systems by encouraging public discussion and community participation in the management of Extractive Industries. In each implementing country, EITI is supported by a coalition between government, companies, and civil society (CSO). In its implementation, the EITI standard was established as a working guide for implementing countries. The 2016 Standard is now in force, which requires EITI to implement member countries to submit an Annual Report.

EITI standards have been implemented in 51 countries in the world. Initially, the concentration of EITI was in countries that have a dependency on extractive industries and weak governance of these natural resources (*governance*). In the early 2000s, the countries implementing EITI were only from energy-rich developing countries, especially African and South American countries. At present, several developed countries or G8 are also implementing countries of EITI, namely: the United States, the United Kingdom, and Germany.

The main part of this standard is the process by which a comparison is made between payments to the government by companies in this sector and government revenue (Interview with Edi Effendi Tedjakusuma, Ph.D.). The results of this process called reconciliation to become a report and published to the public. The process that uses an Independent Administrator is carried out under the supervision of a multi-stakeholder group or so-called *-multi-stakeholder working group* (MSWG).

#### 4 EXTRACTIVE INDUSTRIES TRANSPARENCY INITIATIVE (EITI) INDONESIA

In Indonesia, the transparency initiative of state revenue from extractive industries began in 2007 when the Minister of Finance, Sri Mulyani, expressed support for EITI to representatives of *Transparency International* Indonesia. The Deputy Chair of the KPK at the time, Erry Riyana Hardjapamekas and the Deputy of the KPK for Prevention Waluyo, reviewed the legal basis for its implementation. The Presidential Regulation on EITI was then discussed by the Ministry of Energy and Mineral Resources (ESDM). The following year the Coordinating Minister for the Economy at the time, Boediono, chaired a coordination meeting for EITI. In 2010, Indonesian President Susilo Bambang Yudhoyono

signed Presidential Regulation no. 26 of 2010 concerning Transparency of State Revenues and Regional Revenues obtained from Extractive Industries.

The State of Indonesia was formally accepted as an EITI implementing country candidate in October 2010 in Dar-Es-Salaam, Tanzania, at the EITI Board Meeting (EITI Organization, "Southeast Asia Warming Up to EITI," accessed 24 June 2019, <https://eiti.org/blog/southeast-asia-warming-up-to-eiti>). The criteria *compliance* EITI must be achieved by Indonesia within two and a half years. In implementing the EITI, the Government of Indonesia is committed to disclosing all taxes, royalties, and fees received from the oil, gas, and mining sectors.

The Indonesian EITI implementation activities are currently coordinated under the office of the Deputy for the Coordination of Energy, Natural Resources, and the Environment, the Coordinating Ministry for Economic Affairs. To assist with the implementation of EITI in Indonesia, an EITI Indonesia Secretariat office has been formed under the agency.

The legal basis for EITI in Indonesia is Presidential Regulation (*PerPres*) No. 26/2010 concerning Transparency of State Revenues and Regional Revenues Obtained from Extractive Industries signed by President Susilo Bambang Yudhoyono on April 23, 2010. Presidential Regulation No. 26/2010 prioritizes the principles of improving public welfare, good governance, transparency, sustainable development *as well as* the involvement of various stakeholders such as government agencies, NGOs, CSOs, and the business community following the principles and criteria of the EITI (EITI Organization, "Prinsip-Prinsip EITI", accessed 24 June 2019, <https://eiti.org/document/eiti-principles>).

The multi-stakeholder group in Indonesia is embodied in a team organized under *PerPres* No. 26/2010, namely the Transparency Team. The Transparency Team consists of a Steering Team and an Implementation Team chaired by the Coordinating Minister for the Economy. The team members consisted of the Minister of Energy and Mineral Resources, the Minister of Finance, the Minister of the Interior, the Head of the BPKP, and Prof. Dr. Emil Salim, the Minister of Environment and Forestry at that time who had a big part in the idea of transparency in the extractive industry by the Indonesian government (EITI Indonesia, "Perpres No 26 Tahun 2010", accessed 25 June 2019, [eiti.ekon.go.id/perpres-26-2010/?aid=262&sa=1](http://eiti.ekon.go.id/perpres-26-2010/?aid=262&sa=1)).

The development of EITI in Indonesia cannot be separated from the history of the entry of a Non-Governmental Organization (NGO) called Publish What You Pay (PWYP) in 2007. PWYP Indonesia is

affiliated with PWYP International, which aims to encourage mining companies to open their payment data to the government. PWYP was initiated by George Soros by combining five previous NGOs that had already been established, namely *Global Witness*, CAFOD, Oxfam, *Save the Children* UK, and *Transparency International* UK (Oranje and Parham, 2009). PWYP was also formed in the *World Summit for Sustainable Development* Together with EITI's founding initiatives to accompany the spread of EITI in various countries. PWYP Indonesia itself was given the right to elect three members in the EITI Indonesia implementation team.

The IMF advised the Indonesian government to adopt EITI to strengthen the government's fiscal policy and in August 2008 finally, on December 2008 the Indonesian government stated its commitment to carry out the stages of becoming an EITI candidate country (EITI Organization, "Southeast Asia Warming Up to EITI", accessed 23 February 2017, <https://eiti.org/blog/southeast-asia-warming-up-to-eiti>). The World Bank then played its role in implementing EITI in Indonesia since then. The World Bank facilitates and prepares all the necessary costs needed in the process of implementing EITI in Indonesia through the mechanism *Multi-Donor Trust Fund* (MDTF) (Susan, 2011).

Presidential Instruction No. 5/2008, which places the transparency points of the oil and mining industry revenues in 2008 as well. Boediono, who at the time was leading the Coordinating Ministry for Economic Affairs, encouraged the Presidential Instruction to leave. This Presidential Instruction then led to the birth of Presidential Regulation No. 26 of 2010, which started the implementation of EITI in Indonesia.

EITI Indonesia began to publish reports so that the requirements to get the title was *candidate country* fulfilled. In addition to EITI, the Report is also a measure of *best practice* for extractive industry companies. Timely reporting and the absence of discrepancies between reports reported and actual conditions are at least an indicator of the *best practices* of an extractive industry company and EITI itself (Interview with Edi Effendi Tedjakusuma, Ph.D.). Every year, Indonesia must publish a report containing information about state revenues from extractive industries. EITI Indonesia has published five reports starting from 2009, 2010-2011 reports, 2012-2013 reports, 2014-2015 reports published on 28 February 2017. And 2016-2017 reports published on 27 December 2018. EITI reports can be downloaded at [www.eiti.ekon.go.id](http://www.eiti.ekon.go.id), which can be accessed by all levels of society according to the principle of transparency.

The publication of the EITI Report is quite long with the current year because the EITI standard

stipulates that the publication of the EITI Report is a maximum of two years from the current year. Data reconciled in the EITI Report is data that has been audited and published in the Central Government Financial Report (LKPP). LKPP publications are carried out in the following year from the audited calendar year. After being published, LKPP can only be used as data for the EITI Report.

Reports that are open to the public contain Contextual reports and reconciliation reports. An open report, subjectively, is also a measure in *best practice* EITI as well as extractive industry companies (Interview with Edi Effendi Tedjakusuma, Ph.D.). Contextual Report is a report that contains an overview of extractive industry governance in Indonesia which can be an important reference for the community, namely, extractive industry governance, processes licensing and stipulation of oil and gas working areas and mining areas, management of extractive industries in Indonesia, management of state revenue from extractive industries, State-Owned Enterprises (SOEs), and environmental and social responsibilities. The Reconciliation Report is a report that shows reconciliation information from the company that reports payments to the government in the form of taxes, royalties, and *in-kind*, while government agencies report state revenues obtained from extractive companies. The two reports were reconciled (compared) by independent administrators, in a process overseen by representatives from government, industry, and civil society organizations.

In the report, there is a scope of the report. The scope of the report is also a measure in the *best practices* of EITI and extractive industry companies because it will increasingly show the transparency of EITI and the extractive industry companies. One of the important things in the scope of the report is the determination of materiality for the EITI Reconciliation Report. Materiality is the basis for determining whether a production unit can be categorized as a reporting entity or not. Materiality for the EITI report uses a certain value limit based on a type of revenue that is considered sufficient to represent the contribution to the country. For oil and gas, the limit of materiality value is if the contractor and its partners deposit the government's oil and gas share above zero, which means 100% of contractors and partners who contribute to state revenue for oil and gas will submit a report. While for the mineral and coal sector, the materiality is based on each mining production unit that deposits royalties to the state during the year determined by the materiality limit by the decision of the Implementation Team Meeting.

Within the scope of the 2016 EITI Report, for example, it was determined that the materiality limits

of the EITI reporting companies are the largest companies that contributed 94% of the total cumulative National Non-Tax State Revenue (PNBP) in 2016. There are 112 largest mineral and coal companies that contributed 94% to total National PNBP that will become reporting entities for the 2016 EITI Report. In the 2015 EITI Report, 123 mining companies are EITI reporting entities contributing to 93.6% of the total National PNBP. Of the 123 companies, 85 companies reported, and 38 companies did not report. The limited database in the mining sector is the most hindering the process of collecting company reports. Determination of 112 reporting companies for the 2016 EITI Report, it is expected that the level of difficulty in data collection can be minimized, and the reconciliation process can be optimized.

The scope for the Contextual Report contains references to the latest information in the extractive industry sector and is not only limited to information in 2016. Some things that must be discussed in the 2016 EITI Report include the latest issues regarding licensing simplification, *Beneficial Ownership*, implementation of Law No. 23 of 2014 concerning Regional Government, and the latest development of regulations concerning Revenue Sharing Funds (DBH). In accordance with the scope, the 2016 EITI Report must also discuss current challenges and issues related to governance in the extractive industry, such as: the implementation of the gross split scheme, the current status of the revision of the Oil and Gas Law and the Mining Law, the *Domestic Market Obligation* (DMO) of coal, the progress of the planned stock divestment mining companies, BUMN Mining Holdings, and other recent extractive industry issues.

The advantage of Indonesia to implement transparency according to the EITI Standards from the perspective of the government is that transparency will facilitate the process of communication and information to the public. Through published information, the public can find out how far the government records and manages extractive industry sector utilization. From a business standpoint, transparency will provide equal information to all parties. With the same information, business people will compete healthily to provide optimal benefits for the country. From the perspective of the community, transparency can provide information to the public about the natural resources extracted from the region. Communities can monitor whether management is appropriate and provide fair benefits.

EITI can prevent corruption because it is one of the initiatives that support the Presidential Instruction on Corruption Prevention and Eradication Action (PPK) together with other agencies, namely the Corruption Eradication Commission (KPK), the

Presidential Staff Office, (KSP), and other agencies. EITI ensures transparency occurs. With transparency through the issuance of the EITI report, it can be seen whether there is a difference between the amount that companies pay to the government and the amount that the government receives from companies. The public is also given a tool to help control state revenues from extractive industries.

EITI can improve the Extractive Industry Governance in Indonesia, because, in the report, EITI presents several findings and recommendations for improving extractive industry governance in Indonesia. The recommendations contained in the report are determined based on observations of several obstacles encountered during the preparation of the report. The recommendation is expected to be a reference for all stakeholders who are in direct contact with oil and gas and mining management. One example of the 2012-2013 EITI Report recommendations is the use of an integrated payment and reporting system because there is still an error in recording the account in the General Accounting System (SAU) at the Ministry of Finance. The error is caused by the taxpayer not depositing the Non-Tax State Revenue (PNBP) properly, such as the use of bank deposit slips that are no longer *applicable*, resulting in incorrect input. This causes a difference between the amount of state revenue at the SAU and the Institutional Accounting System (SAI) at the Directorate General of Mineral and Coal. The government then published the Simponi application in response to EITI recommendations for the use of an integrated payment and reporting system so that there is no mistake in recording state revenues.

Reporting entities for the EITI Report are the Central Government, Local Governments, and extractive companies. In the 2014 EITI Report, companies that were required to report were 71 oil and gas sector companies and 120 mineral and coal sector companies. For government agencies that must report are seven agencies namely the Directorate General of Oil and Gas and the Directorate General of Mineral and Coal (Ministry of Energy and Mineral Resources), the Directorate General of Budgeting, the Directorate General of Taxation, the Directorate General of Treasury, and the Directorate General of Fiscal Balance (Ministry of Finance), and SKK Migas. Local governments must provide reports on Revenue Sharing Funds (DBH), namely the Provinces of Riau, East Kalimantan and East Java as representations of energy-rich regions in Indonesia.

## 5 THE CHALLENGES OF THE EXTRACTIVE INDUSTRIES TRANSPARENCY IN INDONESIA

The challenges that Indonesia needs to pay close attention to in managing extractive industries are related to the consistent implementation of policies. In various forums, it was revealed that legal certainty and business certainty in Indonesia are often questioned so that investors must take these risks into account in their investment decisions. One form of policy inconsistency is the issue of licensing and overlapping land. This is still happening today with all the problems. Uncertainty about this policy is the weakest thing done by the government, so the practice of transparency and integrity in this aspect is impossible to do.

The potential for corruption in this aspect is quite large, both by the government and companies. From the company side, the weakness of this aspect requires the company, indirectly, to prepare more budget to maintain the permits and land. For companies, certainty in doing business, including consistent implementation of regulations and policies, is necessary to make long-term business planning. Uncertainty about this policy presents a subjective domain in the extractive industry (the objective domain is a report) and increases risk, thereby reducing investment interest, which ultimately impedes economic growth.

Besides, the role of state enterprises in managing extractive industries is too high. Government control over the management of natural resources is often exercised by state-owned companies. This causes inequality in many aspects. The government should provide *equal treatment* for players in the extractive industry to create a conducive business environment. Just as before, in this context, transparency and integrity are also impossible to do. This condition, by companies, is considered a condition that is "maintained" so that the profits for the government and companies that are close to the government are greater than other private companies. This aspect also becomes the ground for the emergence of great corruption, especially when it is supported by policy uncertainty by the government. Both of these challenges are still the homework of the government and CSOs in monitoring so that transparency and integrity in the extractive industry sector are no longer impossible to do.

EITI Indonesia did not touch this realm because EITI only worked on the objective aspect (report). In an objective context, the government and companies can be said to have carried out transparency and

integrity in this sector, because they have provided all information requested by EITI. The biggest problem of extractive industries is not finished in the report alone, because the main problem is in the field not in the report.

## 6 CONCLUSIONS

Indonesia is a country that has abundant oil and gas and mineral resources, but Indonesia needs to increase transparency and accountability in managing these resources. This is important to be done so that the utilization of these resources can be optimized for the interests of the people and can also support more sustainable development. For this reason, the government needs to continue to improve the existing extractive industry policies and management.

EITI can be said to be quite successful in the objective aspects so that transparency and integrity in the extractive industry sector are created, but EITI's authority in Indonesia may also need to be added because the biggest problems of extractive industries are in the field not in the report. The subjective side of the extractive industry sector is still a big homework for the government, companies, and society because, on this subjective side, transparency in the extractive industry sector is still an impossible part to realize.

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