

Governance and the problem of Corruption

by

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In the earlier sessions we have extensively covered the economic issues that are traditionally discussed at this meeting. This afternoon, I would like to address a topic that has seldom been discussed in depth in this forum; that is Governance and the Problem of Corruption. But certainly, this is not a new topic. The international community has been raising it for years and it has been a subject of many debates by many Indonesians for even longer. In fact, only last week with the support of the Asian Development Bank we organized a High Level Workshop on Good Governance and Anti-Corruption Efforts, participated by representatives of the government, academia, business and civil society. I am sure the representative of the ADB will further enlighten us on their proposed action plan, which was presented in the workshop. With the current emphasis on *reformasi*, the issue of governance has now fully entered public discourse and we are beginning to see the fruits of the new openness in debate in this area.

The issue of governance is important for many reasons. For my purposes today, it is sufficient to highlight two. First, good governance is necessary to ensure the legitimacy of governmental authority. Without good governance, the government can become ever more estranged from its people and lose their confidence. Second, good governance is required for the long-term health of the economy. For instance, there is now little doubt among most observers that a number of illegal and unethical business practices commonly practiced in the region at least contributed to the magnitude of the impact of the crisis. I hope I do not sound defensive in highlighting that none of these practices can be described as uniquely Asian – they can be found in the capitals and hinterlands of most developed countries, as well. Indeed, many of the most egregious forms of corruption in Indonesia included willing foreign partners who profited greatly from these arrangements.

That having been said, it is incumbent upon us, as Indonesians, to ask whether the structure of our legal system and, perhaps, even of our society have made it easier for corruption to flourish. This is where the issue of good governance is so important. Fortunately, I believe that the events of the past two years have begun to force us to address these issues.

The most obvious step in this direction has been the recent elections. For the first time in over forty years we have held a really free and fair democratic elections. These elections, and the new election laws that supported them, put us on the path toward increased democracy that must lie at the heart of good governance. But there is also a need for other reforms. Democracy creates a level of accountability for the government at a political level, but there also needs to be greater accountability between elections as well. This requires both greater use of consultation by the government, and a degree of legal accountability to the people to ensure that the Government is executing the laws and policies properly. Fundamentally, this requires a strong and autonomous judiciary that will ensure that the laws are enforced fairly. While steps have been taken toward this goal, the needed radical transformation may take much more time.

The rule of law and accountability will not be sufficient without the third element of governance, that is transparency. Through the reforms in political, economic and administrative field, we are opening up our society and the way of doing things. People have the right to know not only the background but also how policies and procedures are being carried out. Establishing fair and equal treatment and level playing field is very much a problem of transparency. And through transparency we can prevent opportunity for corrupt practices. Full control not only by political machinery of the state, but the people on the conduct of government is a necessity in a modern and democratic society. Freedom of the press and the active role of the civil society can ensure the people will not be manipulated of its rights and of its wellbeing by wrong and bad governance. For instance, the controversy surrounding the social safety net program prompted us to make improvements in its planning, execution and supervision.

As we say in Indonesia, it needs two hands to clap. Improving governance should not only be limited to the public sector but also to the private sector. Good corporate governance is as important as public governance for the economy. Improving corporate governance should include measures to rationalize the regulatory framework, emphasize transparency of business practices, increase the accountability of corporate insiders to shareholders and regulators, and increase the effectiveness of enforcement by regulatory agencies. These measures are crucial to strengthening market discipline, reducing the scope for corruption, and preparing for private sector-led growth. We will establish a high level committee on corporate governance to develop the strategy and oversee its implementation, with members from the private and public sector.

We have to give particular attention to public enterprises that still play an important role in our economy. One strategy to improve the performance and profitability of our public enterprises is through privatization. To improve efficiency and governance we subjected key public companies to special audit by international auditors. The audits of three public entities—BULOG, Pertamina and PLN—were completed in June 1999. Their reports are currently being reviewed by the government and the findings will be published no later than next month. The Reforestation Fund audit will be completed in August 1999; after its review by the government, the findings will also be immediately published. In each case, corrective actions will be taken as necessary. A second round of special audits for enterprises with strategic significance and public exposure has been drawn up. The list includes the principal national airline, the port corporations, the domestic telecommunication company, and the toll road operators.

In fact it is important for us to improve our control and supervisory mechanism, to prevent the occurrence of corruption and other misconduct, and promptly detect them when they happen. We actually have a functioning internal and external auditing system but we realize that it needs to be improved and to be made more effective.

I felt it important to discuss the governance issues first, because the current drive to eliminate corruption will ultimately fail to change long-standing practices without a change in governance. It is one thing to identify current cases of corruption and to eliminate them. It is another to establish a culture of incorruptibility that will keep the problems of the past from reappearing in the future.

Let me now turn directly to the issue of corruption. It is becoming more evident that in the years leading up to the crisis, the Indonesian economy had become particularly ensnared in a system of special costs and privileges.

I do not think it necessary to go into the details of any specific cases. As in other countries, Indonesia's judicial system must ultimately decide which practices can legally be defined as corruption, and I do not wish to prejudice this normal albeit often frustratingly slow process of determination. But I think it is important that we all have the same understanding of what we are

talking about when we speak of corruption and the Government of Indonesia's efforts to eradicate it.

In the midst of the economic crisis, it was imperative for us to aggressively pursue the most damaging form of corruption, that is the granting of special privileges to specific businesses. This was particularly true since the system of granting special privileges in Indonesia was widely seen as the source of poor decisions that eroded our economic competitiveness. Addressing the distortions created by these privileges was and is critical to moving the economy forward in the medium-term. The scope of activities it covers are broad and reach into the most important economic activities of the Government. Included under our new anti-corruption activities are infrastructure construction and management, the swap and sale of state assets, the privatization of public entities, the granting of tax facilities, the procurement process for government goods and services, and the processes by which contracts, credit and licenses are granted. Thorough and effective reform in these key activities will obviously reflect a radical change in the way government works in Indonesia.

Let me now spend a few more minutes explaining our approach to address this problem.

First, while the Government of Indonesia has been active in discussing and enacting new laws, everyone must recognize that many of the corrupt practices of the past often contravened even the laws of that time. It is not enough to change the laws, they must be enforceable. As I noted earlier, this requires strong and independent legal institutions that can limit the reach of the government. Such accountability is a critical part of the regime of good governance that we are seeking to create. In this regard, the World Bank's paper has a particularly succinct and useful discussion of the problems that we face in this area.

At the same time, our legislature has been busy developing and passing new legislations to define and criminalize corrupt practices. In May this year, Indonesia's Parliament passed Law number 28 on Clean Government. This law includes provisions requiring fair and equal treatment from government officials for all people, as well as the right of the public to seek information about policy-related matters and to express views on those issues in a responsible manner. Another provision of this law requires that state administrators should report their wealth, subject to investigation by a special commission to ensure that government officials cannot enrich themselves improperly. In addition to this law, the Government has also submitted a number of other laws, including one on the Eradication of Corrupt Practices which has recently been passed by the Parliament. The new law on competition will also prevent corrupt practices through the granting of licenses, special treatment and monopolies to certain group of people. The recent law on the Central Bank will reduce the danger of moral hazard and prohibit government interference in the banking and monetary policies. Taken together, the list of new regulations and legislations of the past year provides compelling testimony regarding our commitment to improving governance and eliminating corruption.

The second part of our strategy for eliminating corruption is the termination of any unusual privileges of the past. Again, any close observer of recent events in Indonesia is fully aware of the enormous progress that has been made on this score. In virtually every sector of the economy, unusual privileges were found, and many have already been withdrawn. Tariff exemptions have been repealed, special loan arrangements have been undone, dubious contracts with public enterprises have been cancelled, excessive forest and land concessions have been revoked, and monopoly control over many markets has been dissipated. Special trade arrangements on food and other commodities have been eliminated. There is ample evidence that such reforms have generated significantly new opportunities in many parts of the country. Of course, even as we celebrate the achievements to date, let me acknowledge that there still remains more to do. The achievements, however, serve as a telling sign of our commitment to the process.

The third aspect of our anti-corruption strategy entails the prosecution of those responsible for corrupt practices. Obviously, as in any other situation where criminal activities are suspected, the collection of information against those suspected of having engaged in illegal activities must come first, but this means an inevitable delay before action can be taken, often even in cases where everyone believes that corruption occurred. In cases where foreign companies are involved we hope that we can count on the support of their governments to help us in gathering evidence and in upholding justice.

This part of the anti-corruption effort often evokes the most frustration and disappointment from those outside the justice system, as the legal process never moves quickly enough for those who have been wronged or outraged by the alleged violations. Let me be clear – we will pursue these cases as aggressively as possible to ensure that criminals will be punished and that future acts of corruption will be deterred. But we can not subvert our justice system simply to hasten the process. Especially in an era of reform, the judicial system must be above any suggestion that prosecution is politically motivated. Indeed, we have to demonstrate that the practices of the past will no longer be tolerated, and that means allowing the judicial system to operate without intervention from the government which might prejudice the outcome. We should also not undermine the need to recover the losses incurred by the government in cases where there is suspicion of corruption and other forms of abuses. The efforts of pursuing the prosecution and maximizing the returns of asset should go hand in hand.

We recognize that reforming the legal and judicial system is a gigantic undertaking. Aside from establishing the right norms and rules, the quality of the human resources is also crucial. In this regard we would seek the support and the assistance of the international community to help us in the upgrading of the quality of people that run the system. Indeed, in comparison with other professions, we feel that the legal professions are left somewhat behind in terms of taking advantage of the education and training facilities available in the developed world. It should also include enhancement of the quality and knowledge of our auditors.

Of course, if enforcement is the stick by which we threaten those who are in a position to engage in corruption, we understand that a carrot must be extended, as well, that represents appropriate incentives to reward honest and clean behavior. Improving governance can form a strong pedestal upon which to build a new Indonesia, but they will not be achieved without significant reform in the civil services. At the same time, low salaries mean that we have very low expectations of civil servant performance. Our civil service structure for remuneration is woefully inadequate. Even with wages that are often supplemented by non-cash benefits, including housing for many and rice provisions for almost all, civil servants are simply not adequately compensated for their work. This does not excuse corruption, but it does help explain how corruption became so endemic to our bureaucracy. Only when the civil service is efficient and honest will we attain the level of consistency and transparency in government operations that are required to restore the faith of the people in the government.

Unfortunately, the economic crisis has significantly reduced our fiscal resources, thereby making it much more difficult to improve welfare levels among the civil servants, the military and the police. Our national anti-corruption strategy, however, includes provision for increasing our tax revenues – our ratio of tax revenues to GDP of 11 percent is almost one-third lower than in the Philippines (16%) and less than half of Thailand (28%) and Malaysia (32%) – and we anticipate that these revenues will not only help us reduce foreign indebtedness but also increase salaries for public servants. It is important to make this commitment because we want our bureaucracy to be a participant, rather than a target, of our anti-corruption efforts.

In closing, I would like to remark that the generous support of the donor community over the past three decades has helped fuel an economic expansion that was real. Living standards by any

measure improved appreciably, and the returns to the investments of the donors, including not only better homes and more material belongings, but also remarkably higher health and education standards for the vast majority of the population, were not destroyed by the events of the past year. Let me assure you that your assistance has had a tremendous impact on my country, and let me express our deep appreciation for this past assistance. But with the economy suffering from so many distortions, efficiency losses and misdirection of funds almost certainly occurred.

Our acknowledgement of the problems ushered in what Indonesians call the Reform Era that began roughly one year ago. In that very brief time, even as the Government of Indonesia has fought to stabilize the economy, considerable administrative and legislative efforts were directed expressively at the issue of good governance and corruption. We are still some distance away from entrenching the principles of good governance and eliminating corruption, but we have made a start and are committed to seeing the process completed. We appreciate your concern and welcome your offer to help to achieve those ideals.

Thank you.