

POLICY REFORMS IN ENERGY SECTOR RETHINKING NEOLIBERALISM IN A WELFARE STATE

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ABSTRACT

This paper is intended on searching of liberalization development process particularly in the energy sector reflected by policy changes in Indonesia. It examines and investigates to what extend policy changes in Indonesia coherent with neo-liberalism characters particularly after Asian Crisis in 1997 which followed by Suharto's regime resignation, when liberalization process was heavily accelerated by reformed government. The problem that rose next was how neoliberalism thoughts may convergence into welfare state ideology as the founding fathers ideas accordingly. The conclusion part clearly discusses about the pros and cons of neo-liberalism characters in policy changes in Indonesia.

Keywords

Neo-liberalism, policy, regulation, reformation

Introduction

Constitutional Court finally annulled some portion from articles no 1, 4, 41, 44, 45, 48, 59, 61, and 63 of the 2001 Law on Oil and Gas on November 13, 2012. As a consequence of this cancellation, the existence of BP Migas as upstream oil and gas regulator is then violated the 1945 Constitution particularly as stipulated in article no. 33.

Article no. 33 paragraph 2 of Indonesia's Constitution obliges the state to control natural resources and important branches of production. However, to what extent the state has to take control has been a crucial discourse since the independence of Indonesia. Does it require a direct management of the state or regulation only is sufficient.

Liberalism and Welfare state

Neo-liberalism is a term that simply defined to the free and open market driven approach. Open market means less or no government intervention and therefore maximizes the function of private enterprise. State intervention is limited only as a policy

maker and supervises the regulation to keep on track.

Neo-liberalism, as the name implies is a new form of liberal market economy concept. As one variant of capitalism which consists of Keynesianism, neo-Keynesianism, mercantilism, liberalism and neo-liberalism and, neo-liberalism is an attempt to correct the weaknesses found in liberalism.

Market economy according to liberal thought is believed has the ability to take care of itself particularly in the event of failure. Therefore state intervention is not needed at all because the market can take care of itself. But confidence in the concept of liberal market economy slumped drastically after the world economy fell into a large depression in the 1930s. Apparently there is always market failure. As recently happened in the US subprime mortgage crisis, in the case of market failure, the market was not only unable to take care of itself, but can be a source of catastrophe for humanity.

Furthermore, liberalism that was embedded in the development concept could not overcome inequalities problem. Kuznets (1952) introduced 'inverted U-curve' that

showed a tradeoff between economic growth and inequality (Alastair Greg, 2007).

However, neoliberalism as a correction for the weaknesses found in liberalism also raised main criticism concerning inequality along with economic growth. This criticism has contended by neoliberals that the growth should alter the poor as well as the rich (Alastair Greg, 2007)

Neo-liberalism itself has many dimension and concept such as neo-liberalism concept in the realm of democracy, politic, religion and economy. It should also be understood that there are differences in terms of neo-liberalism in the realm of politics and social economics, although both affect each other. Therefore, considering those facts, this paper focuses the analysis limited to neo-liberalism in term of market economic concept instead of political concept.

A welfare state is a concept literally means to the state role to impose welfare development. According to basic ideology of Pancasila and State Constitution article 27, 31, 33 and 34, it can be concluded that Indonesia is the country with the welfare state concept. The concept implies that the state has to manage and control public utilities, public goods, land, water and natural resources and used for the maximum amount of people's prosperity.

In accordance with 1945 Constitution article 33 paragraphs 1, Indonesia's economy is based on the kinship principle locally known as pro-people economy (*ekonomi kerakyatan*). With kinship principle, common interests should be protected to give satisfaction to the individual needs.

Contrary with liberalism, which achieved prosperity by individuals who will transforms to community prosperity. (Levi-Faur, 1997) (Adamson) Thus, individualism becomes a key point that must be protected.

Therefore, the main objective of this paper is to investigate to what extent neo-liberalism

may fit into welfare state concept as founded in state constitution.

Liberalization in Indonesia

During Dutch Colonial regime in Indonesia, economy activity was dominated by Dutch big company. The main economic activity was from plantation sector. The entire plantation product was mainly for export and managed by big company (*onderneming*). Profit from this activity became financial capital for the Dutch Kingdom while people of Indonesian exploited and squeezed. This economic activity which is full of exploitation already saw and perceived as liberalism. Eventually liberalism had become a dirty word that has to be avoided. The word liberalism had become avoided later and refined by the use of word like deregulation, reformation and restructuring.

Further understanding of neo-liberalism is often associated with the term of liberal life style, so that the neo-liberal conception despite of its context is always resisted by some religious groups. Some nationalist groups also perceived neo-liberalism as the absence of state control in energy sector eventually raising concern about foreign company domination in energy sector.

Liberalization process in Indonesia itself has been started since mid-1980. This was primarily spearheaded by the economist who later called the Berkeley Mafia (Indonesian economists who graduated from University of California Berkeley). This liberalization process was mainly done triggered by falling world oil prices at that period which caused by declined state revenues. This is due to the fact that the revenues were largely derived from oil.

During that time liberalization process was characterized by changing the status of state enterprises into limited company, divestment, privatization, simplify regulations permit the establishment of banks and capital markets.

The process of liberalization in the early decades of the 1990s was indicated by privatization and divestment of state-owned enterprises in the capital market. President Suharto through the instruction of the president in 1989 ordered 50 state-owned enterprises to bid for shares or an Initial Public Offering (IPO) in the capital market within three years.

PT Semen Gresik in 1992 was made an initial public offering on the Indonesian stock exchange that followed by PT Telkom Indonesia, PT Indosat and PT Tambang Timah in 1996. Furthermore PT Telkom Indonesia and PT Indosat did a dual listing on the Jakarta Stock Exchange and the New York Stock Exchange. PT Telkom Indonesia is the largest telecommunications company owned by the Indonesian government. Go public or Initial Public Offering is the strategy of privatization carried out by selling some companies shares to public on the exchange floor. This privatization strategy is a partial privatization because private share ownership restriction is limited to a maximum of 5% (Pangestu, 1996).

Financial crisis in Asia in 1997 which was followed out by the fall of the Suharto regime in 1998 became a crucial entry point to accelerate reformation in every sector. The entrance to the liberalization process at the time started with amended a portion of state constitution. IMF (International Monetary Fund) has a big influence in term of giving advice and pressure in this process considering that amendment of 1945 Constitution is a sacred thing which seems impossible to amend during Suharto regime.

After the fall of the Suharto regime, the new administration named the reform government, privatization strategy was carried out by a block sale of state enterprise share and inviting strategic partners. Privatization strategy by inviting strategic partner has opened opportunities for foreign companies to dominated state-owned company which particularly controls public

services and goods. At this moment the issue of nationalism became a public debate which was caused by the too low asset valuation led to lower initial stock price than its true value.

The IMF's involvement in the process of liberalization was a prerequisite for the disbursement of IMF funds that are part of the financial debt restructuring that is needed by the Indonesian government to rescue its economy due to spiralling government debt. Government debt denominated in foreign currencies soared when the government changed its exchange rate policy became a floating currency, the exchange rate of IDR against the USD declined from 2000 IDR to 15,000 IDR per USD.

Thus the emergence of liberal policies in Indonesia cannot be separated from foreign interference by government, NGOs / multilateral agencies, and multinational corporations (MNCs) which have symbiotic relationship with the Indonesian politicians and state officials.

Legislation in energy sector that reflects the spirit of neo-liberalism

Oil and Gas law no. 22/2001

Oil and gas Law no. 22 of 2001 contains the spirit of neo-liberalism is reflected in the regulation of the key points as follows:

1. Repeal subsidies to fuel oil prices following the market mechanism.
2. Establish an independent regulatory body BP Migas for upstream and BPH Migas for downstream business.
3. Shifting roles and functions of Pertamina as a state enterprise into a limited liability company whose status is similar to the other PSC.
4. Privatization and unbundling of Pertamina's upstream and downstream business.

Prior to the mid of 2001, Pertamina was a state owned company that had a monopoly for oil and gas business both upstream and downstream. The role of Pertamina as the monopolist has been dismantled as enactment of Oil and Gas law no.22/2001. The law has diminished the power and control of Pertamina to the exploration and exploitation of crude oil reserves in Indonesia since it put into effect.

However shifting role and functions of Pertamina as the monopolist may cause loss of sovereignty and control over sources of natural resources particularly in the upstream business. In the current geopolitical map, the oil becomes a tool of political power rather than a common commodity. In that frame of thought, the loss of control over oil resources may result weakening government bargaining position the geopolitical map.

In the downstream business, the new Oil and Gas law no.22/2001 article 28 paragraphs 2,

	2003	2004	2005	2006	2007	2008	2009
1.Electricity Subsidy	3.36	3.31	10.65	33.9	37.48	78.58	53.72
2.Electricity Subsidy from fossil energy	2.92	2.86	9.2	29.75	32.63	68.16	46.14
3.Fuel Subsidy	30.04	59.18	103.35	64.21	83.79	139.03	45.04
Total Subsidy for fossil Energy	32.96	62.04	112.55	93.96	116.42	207.19	91.18

Table 1. Electricity and Fuel subsidy in Trillion IDR.(Source : Ministry of Energy and Mineral Resources 2009)

Table 1 shows that increased fuel price in 2005 resulted to reduced subsidy by 16.5 % in 2006 (from year 2005) and significantly by 56% in 2009 (from 2008). Due to the fact that fuel price was determined as a fixed price rather than fluctuated word oil price, it can be seen from table 1 that fuel subsidy was decreased (let say in year 2005-2006) but oil price and fuel consumption increased

mandate to repeal oil and gas subsidy price. The oil and gas price should be determined by market competition mechanism. This regulation has become a legal standing for Government of Indonesia to implement increasing price and furthermore to remove fuel subsidy in the future.

Fuel and electricity price in Indonesia are determined as a fixed price rather than adhere to fluctuated world oil price, so increased world oil price resulted to increased fuel subsidy due to Indonesia has become a net oil importer country since year 2004 (Pallone, 2009).

In January 2002 Government of Indonesia increased fuel price by 30% averagely and resulted with subsidy reduced become 1.9% from 4.6% of GDP. In 2005 Government of Indonesia was increasing fuel price by 126% and 28.7 % averagely in May 2008. (Syeirazi, 2009)

steadily so the fuel subsidy increased. Furthermore, it should be noted that increasing domestic fuel price in year 2005 mostly influenced by the hike of oil price in that year.

In 2008 in accordance to increasing domestic fuel price policy, Government of Indonesia also introduced shifting from

kerosene to LPG program that eventually reduced kerosene subsidy. Both programs which were followed by significance decline in oil price resulted to significance subsidy budget decline in 2009.

Increasing domestic fuel price policy in 2009 also mostly influenced by the hike in oil price that reached the world record high in 2008 as can be seen on table 2. (Fajrian, 2011). So the decision to raise domestic fuel price is heavily influenced by the needs to reduce fiscal burden, despite it may gain exposure to political risk and riots.

However after the judicial review sought by several noted Muslim figure, Constitutional Court finally annulled some portion from articles no 1, 4, 41, 44, 45, 48, 59, 61, and 63 of the 2001 Law on Oil and Gas on November 13, 2012.

Electricity Law no. 20/2002

The electricity generation, transmission and distribution in Indonesia is dominated by PLN, an electricity company owned by the government of Indonesia. The nature as monopolist is justified in the article no. 33 of Indonesia's constitution. As the constitution states that all the important branches of production must be controlled by the state, furthermore electricity system is considered as one of "important branches of production".

After the fall of Suharto In 1998, GoI sought to dismantle PLN monopoly by issuing electricity law no.20/2002. The spirit of the law was to break down PLN monopoly and attracted private enterprises participation. Article no. 16 governs unbundling in generation, transmission and distribution and article no. 17 regulates competition and market domination prohibition.

The Electricity sector no.20/2002 was a legislation product that came after the signing of an agreement between the Government and the IMF in the form of a Letter of Intent (LOI) by President Soeharto at the dawn of his governance. LOI will

involve a commitment of the Government of Indonesia to liberalize the Electricity Sector as a prerequisite for the structural loan granted \$ 900 million in 1999, most of which comes from ADB, JEXIM (JAPAN) and USAID (United States). (Tumiwa)

Electricity Law no. 20/2002 contains several points that reflect the spirit of neo-liberal:

1. Vertical unbundling
2. Horizontal unbundling
3. Privatization of PLN (state owned electricity company)
4. The basic electricity tariff adjustments to market mechanisms

The concept of vertical unbundling is to dismantle the electricity business vertically into separate business units among the Generation, Transmission, Distribution and Retail, which then competed to follow free market mechanism.

The Electricity law no. 20/2002 contained restructuring program to vertically unbundling power generation business in Java-Bali which is more developed, the business of electrical power supply will also be broken down (unbundling) to attempt the generation, transmission and distribution, competition will be introduced and an independent regulatory body will be established.

However a judicial review to the Constitutional Court filed by the PLN's worker union in 2004 had revoked the law and the old law no.15/1985 is up held. The court has decided that the term "control" of article no.33 should be interpreted as "direct management" of the state instead of "government as regulator only" interpreted implicitly in the law. In order to avoid uncertainty in electricity business then GoI and the House of Representatives issued the new law no. 30/2009.

The new electricity law no. 30/2009 has the same spirit of electricity market liberalization. The law has enacted decentralization of responsibility and

authority. To this end, the law allows Cooperatives, State Owned Companies, Regional Government Owned Companies, Private Companies and Non-Governmental Enterprises to participate in Electricity Supply Business (Article 4 paragraph 1 and 2).

As stated in article 10 paragraphs 1, electricity supply for public needs includes power generation, transmission, distribution, and electricity sales. Furthermore, article no.

21 and 34 allows province, regency and municipality government to issue Electricity Supply Business License and regional tariffs determination with consent to the regional House of Representatives.

Therefore as the law stated that the first priority is given to State Owned Company, it is interpreted that PLN has a first priority to be the electricity supplier for the public needs due to PLN still the only Electricity Supply Business License (IUPTL) holder.

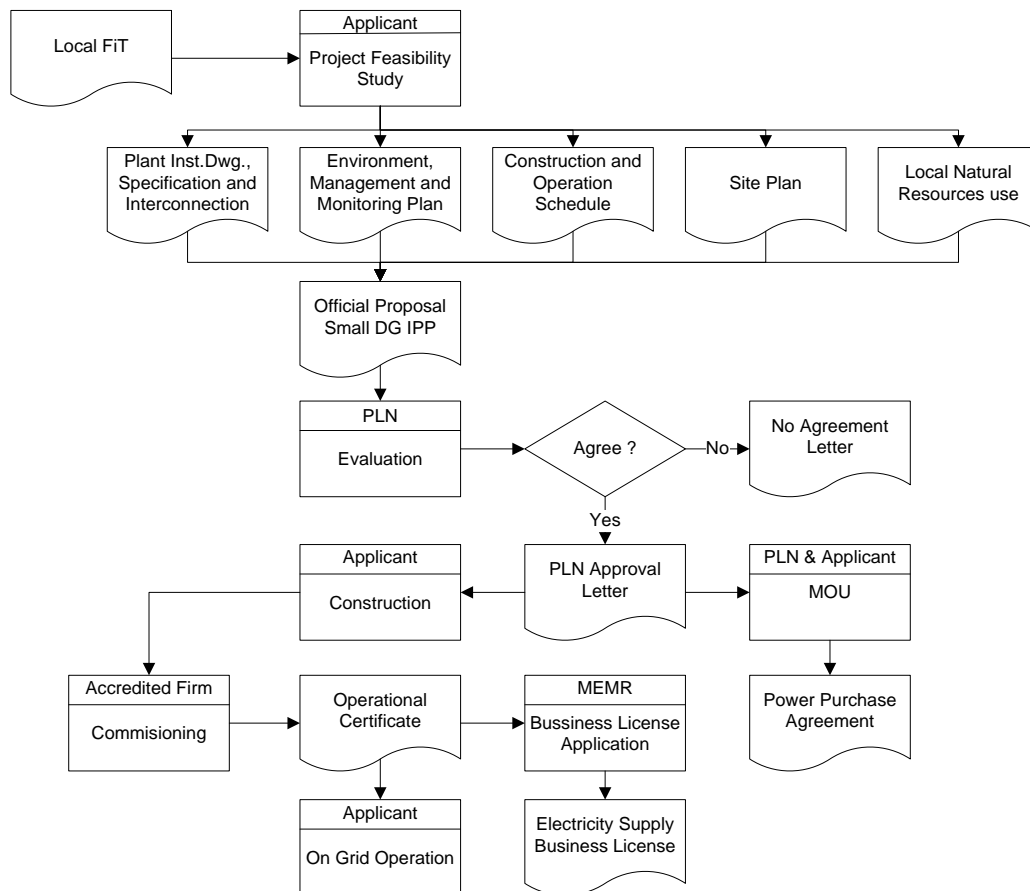


Figure 1. Schematic PPA process of Ministerial Decree 1122K/30/2002 adopted for PV technology (PT Chazaro Gerbang Internasional (CGI), 2012)

State Control on mineral resources, a Freeport case

As mentioned before, Republic of Indonesia was founded with the concept of the welfare state, in accordance with the Constitution 1945 article 27, 31, 33 and 34 (Asian Human Rights Commission - Indonesia). Furthermore Indonesia's Constitution has a

strong intention in resource nationalism ownership as mentioned in article 33 paragraphs 3 of 1945 Constitution: "The land, the waters and the natural resources of Indonesia shall be under control of the state and shall be used to the greatest prosperity of the people"

It is clearly stated explicitly that the State controls the resources and shall be used to the greatest benefit of the people but government's ability to control becomes brittle if the government is a minority shareholding.

Freeport Mc. Moran is one of the biggest gold and copper mining in Indonesia. Operated since 44 years ago, Freeport Mc. Moran has ownership as 81.28% (Freeport-Mc Moran Copper and Gold Official Website) as can be seen on table 2.

Company Tax	7.3
Employee Tax, Regional tax, and others	2.3
Royalty	1.2
Dividend	1.2
Shares Ownership	
Government of Indonesia	9.36%
PT. Indocopper Investama	9.36%
Freeport Mc Moran (Copper and Gold)	81.28%

Table 3. Financial Liability of PT Freeport Indonesia according to KK II/1991 (in Billion USD) during the period 1992-March 2011. (Source: PT Freeport Indonesia 2010)

Based on the financial statements of PT Freeport Indonesia during the period 2004-2008 as can be seen on table 4, with total revenue of 17,893 billion USD and gross

profits amounting to 10,762 billion USD, the Indonesian government only gets revenue from taxes and royalties amounting to 4,411 million USD or equal 40% of the profit.

Year	Gold (thousand ounces)	Copper (million pounds)	Revenues (M USD)	Gross Profit (M USD)	Tax (M USD)	Royalty (M USD)
2004	1,456	997	1,980	804	266.4	43.5
2005	2,789	1,456	4,012	2,380	781	103.7
2006	1,732	1,201	4,883	2,929	950	126
2007	2,198	1,151	5,315	3,234	1,326	133
2008	1,163	1,094	3,703	1,415	612	113
Total	7,281		17,893	10,762	3,935	475.7

Table 4. Production and Revenue of PT Freeport Indonesia during the period 2004-2008. (Source: PT Freeport Indonesia 2010)

Freeport is one example that brings neo-liberalism to public discourse in the media. Such high Freeport Mc Moran ownership, make Government of Indonesia does not have voting right and built perception that neo-liberalism is the new form of neo-colonialism.

High foreign ownership portion on Freeport Mc Moran, nevertheless makes the gold company takes control and power. Eventually, Government of Indonesia has merely less power and ability to do

correction for the environment destruction, labor issues and etc.

Conclusion and Discussion

Neo-liberalism in Indonesia in the post Suharto regime has an important momentum with the enforcement from IMF in giving pressure and advice in exchange with debt restructuring of Indonesia followed by Asian financial crisis.

However, pressure from IMF raised reluctance to policy changes which obviously have neo-liberalism character. Thus, reluctance to neo-liberalism policies affecting implementation in some region of Indonesia which make it became not effective. (Wie, 2011)

The pro nationalism fostering anti foreign ownership, usually this is due to election campaign for parliament members or head of region candidate. This is also partly due to concern regarding to state sovereignty over natural resources brought into campaign materials for the politicians who fought in local elections or parliamentary elections (Boyd, Devero, Frias, & Jeff Meyer, 2010).

In the case of Indonesia and other developing countries, neo-liberalism which allows foreign ownership until 99% and not pro domestic entrepreneur has become a new form of colonialism more or less. The power of foreign cartel is believed become a power that dictates the market and against democracy and neo-liberalism itself. Nevertheless imposing less state intervention paves the way for multinational companies and transnational company to invest in Indonesia and eventually dominates minerals and other natural resources.

As noted earlier, the concept of neo-liberal elements contain elements of fairness and equality for every individual in all aspects. But what happens in Indonesia is the fact that imposing of neoliberal concept has become very massive as reflected in the policy regime after Suharto resignation.

The concept of neo-liberalism then becomes absurd when it is imposed on undeveloped market. Principles of equality should be interpreted as levelling playing field for each actor, rather than giving so many privileges to multinational companies. Therefore, it is

the role of government to create a balanced market and create a levelling playing field for the players.

Nevertheless due to the fact that there is no perfect market, state control and intervention has to be needed in the time of market failure. Even though in developed country, state control always been there to protect and balancing the market.

In the case of Indonesia, dismantling the monopoly of state enterprises and invited foreign investment led to domination on minerals and other natural resources by foreign companies. Either it is contrary to the Republic of Indonesia concept as a welfare state, also makes the neo-liberalism more or less as another form of colonialism.

As the final conclusion it can be stated that neo-liberalism cannot be fully implemented in Indonesia because it perceived as contradicts with the Indonesia ideology as a welfare state. Eventually neoliberalism has become a dirty word that must be avoided.

However, neoliberalism thoughts should not be contradict with the welfare state ideology. This is due to the fact that neoliberalism is actually a correction for the weaknesses found in liberalism. It is also raised main criticism concerning inequality along with economic growth. This criticism has contended by neoliberals that the growth should alter the poor as well as the rich.

To this end, neoliberals still need state intervention in controlling natural resources. The problem rose next was, to what extend the intervention was not determined by stake holders. It was imposed by donor countries which are represented primarily by the IMF and World Bank. Under the guise of globalization and free trade, this imposition has succeed to some extent by riding the bureaucrats, politicians and rent-seeking hunters eventually bring bad perception to neoliberalism ideas.

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