

# Decentralization in Indonesia's forestry sector – Is it over? What comes next?<sup>1</sup>

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## Abstract

*This paper analyzes the dynamics of the decentralization process in relation to Indonesia's forestry sector since its emergence in the late 1990s. Under decentralization, district governments were to be given greater authority for the management of Indonesia's extensive timber resources. The transfer of authority and new revenue sharing mechanisms were laid out in government policies issued in 1999. These marked a radical break with the centralized forest management of the past, and provided a promising new framework for managing the country's forest resources and distributing the benefits. During the decentralization period, regional and central governments became involved in a long and often emotional tug-of-war over the division of authority and benefits from the forestry sector. Citing problems with, among other things, the implementation of decentralization, central government has gradually withdrawn the districts' authority for forest management.*

*As central government has now issued a raft of policies reclaiming many of the decentralized forestry administration functions, this paper's key argument is that the era of forestry sector decentralization has now effectively ended, and it remains to be seen what if any effective decentralized forest policies will materialize.*

*Drawing on CIFOR research on decentralization and forestry conducted in the last six years in various districts, the paper highlights the prospects for and challenges of decentralizing the forestry sector in Indonesia. Research indicates that efforts to set the agenda and develop a legal framework for forestry sector management by both central and regional governments may be counterproductive. Our argument is that these efforts overlook the potential lessons to be learned from the decentralization process and that they fail to make best use of the social capital and skills that local stakeholders have developed as a result of the decentralized policies. This demonstrates that the current policymaking processes are failing to build on local people's enhanced capacities for sustainable and equitable forest management and to distribute benefits equitably to them.*

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## **1. Introduction**

After half a decade since the initial attempt to decentralize the forest sector in Indonesia in 1957, and more than five years since the second attempt to implement decentralization, in 2001, sufficient time has elapsed for a comprehensive analysis of the impacts of decentralization to be made. In line with the focus of research undertaken by the Center for International Forestry Research (CIFOR) and its regional partners over the last six years, this paper concentrates on the impacts of decentralization on forest-dependent people, who were intended to be the ultimate beneficiaries of the new decentralized policy framework. We hope that this analysis will provide insights and new perspectives on how decentralization in Indonesia's forestry sector could move forward, drawing lessons from the successes and the failures of decentralized forestry policies.

Studies have been made in various parts of the world that aimed, in particular, to document the decentralization process in the forestry sector at various levels. These studies have not yielded uniform conclusions on the extent of the impacts of decentralization on forests and the people's wellbeing. However, there are conditions, which are locally very specific, under which decentralization policies have been shown to succeed in improving forest resource management while at the same time delivering livelihoods benefits for local communities.

There is strong support amongst international research institutes, donors and some national governments for decentralizing forest administration to the local level. The logic is that decentralized management will be more responsive to specific local socio-economic and ecological conditions and to local people's needs. Decentralization is seen by many as a way of bringing government closer to local people, at least geographically. This gives a clear opportunity to improve accountability for forest management and, more critically, for the exploitation and distribution of benefits (e.g. Agrawal and Ostrom 2001; Ribot 2002). On the other hand, although many members of the international development community and local governments see decentralization as an opportunity to deliver better standards of governance, there is evidence that the incentive mechanisms set up for local government under decentralization can be vulnerable to abuse. In these cases, local elites and powerful external actors are able to capture the lion's share of any new benefits for themselves. Likewise, decentralized policy frameworks have failed to create incentives for local governments to improve public service delivery. These factors have hindered the success of decentralization (e.g. Davoodi and Zou 1998; Johnson 2001; Tanzi 2001; Djogo and Syaf 2003).

The paper outlines Indonesia's forestry decentralization process and analyzes the various dynamics that have affected its implementation. We present key lessons from the process and, to the extent possible, identify recommendations for future policy development. Section 2 discusses the regulatory legal and policy framework for decentralization in the forestry sector. Section 3 discusses the impacts of this framework on forest concessions and the timber industry. Section 4 discusses the fiscal balancing of forest revenues and district finance. Section 5 considers the impacts of the policy framework governing the division of responsibility for forest administration and benefit sharing at the community level. Section 6 presents some examples of the district governments' agenda for better forest management, challenging the arguments of proponents of (re)centralization. Finally, Section 7 provides a summary of our conclusions and new perspectives on forestry sector decentralization in Indonesia.

## 2. The legal and policy framework for decentralization in Indonesia

The implementation of decentralization in the forestry sector in Indonesia has swung like a pendulum between decentralized and highly centralized control. In 1957, the government transferred broad rights to regional governments. District governments were empowered to issue permits for timber and non-timber forest product extraction, to levy a tax or taxes on concession permit holders, and to regulate and implement forest conservation measures and manage the transportation of forest products.

This period of local control was brought to an end by the basic forestry law of 1967. The New Order (*Orde Baru*) government under President Suharto swung the pendulum back toward central government. The central government classified almost all areas of forest on the outlying islands as *kawasan hutan* or “state forest estate”, legally owned by the government. The New Order government gave itself absolute authority for virtually all aspects of forest management, from planning, administration and exploitation to forest conservation. Almost all decisions about forest management were taken in Jakarta, often at the expense of the forest-dependent indigenous communities who had been living in or around the forests for centuries (Kartasubrata 1993; Resosudarmo and Dermawan 2002).

The issuance of Law 5/1974 on the principles of local administration, which put the emphasis on greater authority at district level, did not greatly change the balance of power over forest management. Five years later, the government issued Law 5/1979 on village administration. The objective of this legislation was to implement a uniform structure for village administration for all villages across the country. The new structure was modelled on traditional Javanese village governance systems, which bore no relation to indigenous governance systems on the outer islands. This inevitably strengthened the power of central government by imposing centralized governance structures on local people with no reference to social and cultural diversity or local wisdom and forest management practices. The new statutory system usurped traditional governance at the local level, a step very far from the spirit of decentralization. For almost 30 years decisions regarding forest management and profits from forest exploitation were concentrated in the hands of an elite minority based in Jakarta and with close ties to Suharto’s New Order administration.

To sum up, forest management under the New Order government was characterized by strong control by central government of almost all aspects of forest management. Little, if any, power was transferred to the regions. Coinciding with the end of Suharto’s presidency, the government issued regulation No. 62/1998, granting authority for a number of forestry affairs to the district heads (*bupati*). Some read this as a signal that central government was prepared to support decentralization in the forestry sector. However, others criticized what they saw as an empty gesture: the first delegated powers gave very little real control or incentive to districts.

Law 22/1999 on regional administration, issued a year after the fall of Suharto, gave a stronger signal that the pendulum was swinging back in favour of the districts. This law gave district governments greater autonomy to formulate their own policies. Law 25/1999, on fiscal balancing between central government and the regions, was issued to complement Law 22. It allocated a larger share of forest revenues to the districts and provinces by altering the share of revenues from the Reforestation Funds (*Dana Reboisasi*, DR) and the Forest Resource Rent Provision (*Provisi Sumber Daya Hutan*, PSDH). The People’s Consultative

Assembly issued a decree in the following year<sup>5</sup> recommending that decentralization should be officially implemented as of 1 January 2001.

Forest decentralization was strengthened when national regulations and ministerial decrees devolved forestry functions to district governments. In January 1999, central government transferred the authority to issue forest concessions to district governments<sup>6</sup>. Whilst the central administration retained authority to issue permits for large-scale concessions, districts were empowered to issue permits for small-scale forest concessions for an area of up to 100 ha to communities or cooperatives, valid for one year. The Ministry of Forestry and Estate Crops (MoFEC) followed up with implementing regulations in May 1999<sup>7</sup>. From this point, there was a rush in the districts to enact their new powers. (This continued until 2003 in some districts, despite the MoFEC's decree postponing the implementation of the districts' authority to issue small-scale concessions in early 2000<sup>8</sup>.)

At the end of 2000, legislation moved still further in favour of the regions when the Ministry of Forestry (MoF) issued a decree<sup>9</sup> (re)establishing the district heads' authority to issue small-scale concession permits. When decentralization came into effect in January 2001, the districts raced to issue as many small-scale concession permits as possible, and started to impose charges on existing companies. They began to levy fees on all manner of forestry sector activities, collecting timber fees, log export taxes and timber transportation fees, amongst others (McCarthy 2001a; Dermawan 2004; Sudirman *et al.* 2005). The private sector complained that the new framework had created double taxation. The chaos was compounded by frequent overlaps between 100-ha concessions and existing large concessions (Suparna 2002). Weak legal provisions for re-forestation or rehabilitating small-scale concession areas were subject to heavy exploitation, leading to environmental degradation.

In response to these problems and concerns about sustaining resources, the MoF issued yet another decree<sup>10</sup> in February 2002, withdrawing the district heads' authority to issue small-scale concession permits. In June 2002, central government effectively took back the district heads' authority to grant forest concessions, through a governmental regulation<sup>11</sup>. The regulation limited the districts' authority to issuing small-scale timber concession permits of up to 20 m<sup>3</sup> of timber a year only, a very small amount compared to that potentially to be

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<sup>5</sup> Decree of People's Consultative Assembly No. IV/MPR/2000 on policy recommendations in the implementation of regional autonomy (*rekomendasi kebijakan dalam penyelenggaraan otonomi daerah*).

<sup>6</sup> Government Regulation 6/1999 on forest utilization and forest product harvesting in production forest (*pengusahaan hutan dan pemungutan hasil hutan pada hutan produksi*).

<sup>7</sup> MoFEC Decrees No. 310/1999 to No. 317/1999. The widely recognized decree was No. 310 on the guidelines for granting forest product harvesting rights (*pedoman pemberian hak pemungutan hasil hutan*).

<sup>8</sup> MoFEC Decree No. 084/2000 on postponing the implementation of decree 310/1999 (*penangguhan pemberlakuan Keputusan Menteri Kehutanan dan Perkebunan Nomor 310/1999 tentang pedoman pemberian hak pemungutan hasil hutan*).

<sup>9</sup> MoF Decree No. 05.1/2000 on criteria and standards of licensing of forest product utilization and harvesting in natural production forests (*kriteria dan standar perijinan usaha pemanfaatan hasil hutan dan perijinan pemungutan hasil hutan pada hutan produksi alam*).

<sup>10</sup> MoF Decree No. 541/2002 on abolishing MoF Decree 05.1/2000 on issuance of permits for small-scale concessions (*pencabutan Keputusan Menteri Kehutanan No. 05.1/Kpts-II/2000 tentang kriteria dan standar perizinan usaha pemanfaatan hasil hutan dan perizinan pemungutan hasil hutan pada hutan produksi*).

<sup>11</sup> Government Regulation No. 34/2002 on the forest and the formulation of forest management plans, forest utilization and the use of the forest estate (*tata hutan dan penyusunan rencana pengelolaan hutan, pemanfaatan hutan dan penggunaan kawasan hutan*).

harvested from 100 ha<sup>12</sup>. Subsequent regulations issued by central government effectively confirmed its authority to issue logging permits<sup>13</sup>.

Table 1 summarizes key forestry decentralization regulations. Regulations issued in early 1999 were aimed at decentralized forest management. However, by the end of 1999 and early 2000, central government had already begun to try to recentralize forest administration<sup>14</sup>. The problem with these recentralization measures was that they did not clearly revoke decentralized powers; instead they “postponed” them. This led to a legally ambiguous position whereby district governments were able to argue that the earlier decrees and policies giving them authority were still in force<sup>15</sup>. They also appealed to Law 22 on regional administration, arguing that this law was higher in the legal hierarchy and therefore trumped any attempts by the MoF to take back authority. When the MoF finally succeed in abolishing the earlier decrees on decentralization<sup>16</sup>, in July 2002, the districts lost the most tangible manifestation of decentralized power: they no longer had the legal authority to obtain direct benefits from forestry by taking control of commercial forest management (Dermawan 2004), although, according to Siswanto and Wardoyo (2005), a technical recommendation from the district forestry office was still required before a permit could be issued by the central authority.

Table 1. List of key regulations issued since 1999 that have implications for (de)centralization in forest management

No.	Regulation Number and Year Issued	Hierarchy of Laws			Decentralize (D) or Recentralize (R)
		Law	Government Regulation	Ministry of Forestry Decree	
1	6/1999		*		D
2	310-317/1999			*	D
3	22/1999	*			D
4	41/1999	*			R
5	084/2000			*	R
6	05.1/2000			*	D
7	541/2002			*	R
8	34/2002		*		R
9	6886/2002			*	R
10	32/2004	*			R

Source: Compiled by the authors

<sup>12</sup> For example, according to 2002 data from Kapuas Hulu, a permit of 100 ha translates potentially as 3,600 m<sup>3</sup> of timber on average (Dermawan 2004). Interviews with numerous parties revealed that the new administrative authority granted to the district heads to issue this permit was not particularly welcomed by the districts because harvested timber was to be for personal use only and was not for commercial purposes, and there were limits on the amount of timber that could be felled.

<sup>13</sup> For example, MoF Decree No. 6886/2002 on guidelines and procedures on the issuance of forest product harvesting permits (*pedoman dan tata cara pemberian izin pemungutan hasil hutan (IPHH) pada hutan produksi*), MoF Regulation (*Peraturan Menteri Kehutanan*) No. P.03/Menhut-II/2005 on guidelines for verification of forest concessions or timber plantation permits issued by Governors or District Heads/Mayors (*pedoman verifikasi ijin usaha pemanfaatan hasil hutan kayu pada hutan alam atau pada hutan tanaman yang diterbitkan oleh gubernur atau bupati/walikota*), and MoF Regulation No. P.07/Menhut-II/2005 on the abolition of MoFEC Decree 317/1999 (*pencabutan Keputusan Menteri Kehutanan dan Perkebunan nomor 317/Kpts-II/1999 tentang hak pemungutan hasil hutan masyarakat hukum adat pada areal hutan produksi*).

<sup>14</sup> Law 41/1999 and MoFEC Decree 084/2000 brought power back to the centre.

<sup>15</sup> MoFEC Decree 084/2000 did not explicitly state that MoFEC Decree 310/1999 was abolished, rather it stated that the implementation of MoF Decree 310/1999 was postponed, which led to legal ambiguity.

<sup>16</sup> MoFEC Decree 310/1999 itself was finally annulled in 2002 by MoF Decree 6886/2002.

Indication on (re)centralization could also be seen from the changes in the priority areas for forestry development in the MoF. Strengthening decentralization was explicitly mentioned as one of the five key priority areas of the MoF in its strategic plan issued in 2001. Other priorities included combating illegal logging, controlling land and forest fires, restructuring the forestry sector and carrying out rehabilitation and conservation of natural resources<sup>17</sup>. Although decentralization was included as one of the five priorities, Samsu *et al.* (2005) found that district officials and other stakeholders felt that the Strategic Forestry Plan had no clear objectives or achievement indicators. Some district officials knew no basic facts about the plan at all, far less the extent to which it involved local stakeholders or whether it was providing solutions to the basic problem of unclear administrative authority for forestry.

However, by mid-2004 decentralization had been dropped as a high-level priority. It was reformulated as a ‘cross-cutting issue’ related to the remaining three priority areas. Social forestry was dropped altogether. By the end of 2004, the MoF had issued its strategic plan for 2004–2009. This time, the five priority programmes included combating timber theft and the illegal timber trade, revitalizing the forestry sector and forest industry, carrying out rehabilitation and conservation of forest resources, empowering the economy of communities in and around forests, and gazettelement of the forest estate. Decentralization was dropped altogether, and social forestry priorities were reformulated in abstract and unclear terms<sup>18</sup>.

In the face of fierce criticism, the MoF has argued that the district governments had no capacity and were not ready to assume authority for forest management. It felt that this was sufficient reason to retract their authority. Article 42<sup>19</sup> of Government Regulation 34/2002 explains that the minister would “gradually and selectively” delegate administrative authority for forest concessions to district governments in the future, depending on their “institutional capacity, vision and mission”. No guidelines on how their capacity, vision and mission would be assessed and evaluated are given. Furthermore, as Samsu *et al.* (2005) have pointed out, no clear or concrete measures were ever taken to support the development of the district governments’ capacity. Central government also seemed to fail to issue any regulation governing the implementation of its supposed commitment to decentralize authority “gradually and selectively” in the future. This commitment has been seen by many as another empty gesture.

From this analysis of the development of the regulatory framework since 1998, we conclude that the policies supporting decentralized forest governance has been ended, following repeated attempts by the MoF to take back power from the districts. However, *de facto* decentralization, as Rhee (2000) called it, has continued to take place. There are a lot of strategic actions by stakeholders based on their understanding of what decentralization means.

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<sup>17</sup> MoF Decree No. 342/Kpts-VII/2003 on changes to MoFEC Decree No. 213/Kpts-VII/2000 on the Strategic Plan of the Ministry of Forestry and Estate Crops 2001–2005 (*Perubahan SK Menteri Kehutanan dan Perkebunan No. 213/Kpts-VII/2000 tentang Rencana Strategik Dephutbun 2001–2005 [Penyempurnaan]*).

<sup>18</sup> MoF Decree No. P.04/Menhut-II/2005 on the Strategic Plan of the MoF 2004–2009 (*Rencana Strategis Kementerian Negara/Lembaga [Renstra KL] Departemen Kehutanan Tahun 2004–2009*).

<sup>19</sup> We observed that most stakeholders paid little attention to this crucial article, which has been used by central government to justify its attempt to annul decentralized authority. In terms of hierarchy, this regulation is lower than Law 22/1999, and some consider it to embody the MoF’s strong antipathy to the spirit of decentralization.

### 3. Decentralization and Indonesia's forestry industry<sup>20</sup>

This section considers the impacts of the legal tug-of-war over authority for forestry in Indonesia since the move towards decentralization began in 1998. In response to the initial transfer of authority for issuing concession permits, the districts issued many small-scale concession permits<sup>21</sup>. In Kutai Barat, East Kalimantan, for example, 223 small-scale concessions had been established by August 2000. Bulungan, another district in East Kalimantan, issued 585 permits in 2000 – about 15 times more than the number of permits issued in 1999. Some districts, for example Kapuas Hulu and Tanjung Jabung Barat, tended to be more cautious, issuing a smaller number of permits during the transition period and accelerating the issuance of permits only once decentralization was officially implemented with the enactment of Law 22 in 2001 (Table 2).

Table 2. Numbers of small-scale forest concessions permits issued in various districts in Indonesia, 1999–2004

No.	District	Small-scale Forest Concession Permits					
		1999	2000	2001	2002	2003	2004
1	Kutai Barat <sup>a</sup>	-	223	-	-	-	-
2	Berau <sup>b</sup>	16	17	-	-	-	-
3	Barito Selatan <sup>c</sup>	5	-	-	-	-	-
4	Kapuas <sup>d</sup>	25	60	-	-	-	-
5	Kapuas Hulu <sup>e</sup>	-	11	168	235	-	-
6	Sintang <sup>f</sup>	-	110	320	159	13	-
7	Tanjung Jabung Barat <sup>g</sup>	-	-	17	55	13	6
8	Bulungan <sup>h</sup>	39	585	618	188	189	-
9	Malinau <sup>i</sup>	-	30	9	-	-	-
10	Luwu Utara <sup>j</sup>	-	-	24	-	-	-
11	Manokwari <sup>k</sup>	-	-	-	3	3	-

Source: CIFOR reports (<sup>a</sup>Casson (2001), <sup>b</sup>Obidzinski and Barr (2003), <sup>c</sup>McCarthy (2001a), <sup>d</sup>McCarthy (2001b), <sup>e</sup>Budiarto *et al.* (2003), <sup>f</sup>Yasmi *et al.* (2005), <sup>g</sup>Sudirman *et al.* (2005), <sup>h</sup>Samsu *et al.* (2005), <sup>i</sup>Barr *et al.* (2001), <sup>j</sup>Ngakan *et al.* (2005), and <sup>k</sup>Tokede *et al.* (2005))

Note: - indicates that the data were either not available or not collected

Although small-scale concession permits were intended to benefit the community, they were found to be controlled by private investors and external companies and not by community cooperatives. Local people's lack of capital and capacity for forest exploitation put them in a weak position. They were pushed to enter into partnerships with more experienced forestry companies and investors. CIFOR and its partners' research on the impacts of decentralization in five districts across Indonesia clearly demonstrate that external investors, local elites and existing timber companies have controlled decentralized timber operations and reaped the benefits. Although local communities have received comparatively little, they believe that the decentralized timber operations have nevertheless given them more access to benefits than they had under the New Order<sup>22</sup>.

<sup>20</sup> The term 'forestry industries' in this paper refers to forest concessions and timber processing industries.

<sup>21</sup> The small-scale concessions have many different names, including *Hak Pemungutan Hasil Hutan* (HPHH), *Ijin Pemanfaatan dan Pemungutan Kayu* (IPPK) and *Ijin Pemanfaatan Kayu Rakyat* (IPKR). They share similar characteristics, such as small size of operation (around 100 ha), ownership by cooperatives, farmer groups or indigenous communities, and limitations in terms of capital.

<sup>22</sup> Ngakan *et al.* (2005), Samsu *et al.* (2005), Sudirman *et al.* (2005), Tokede *et al.* (2005) and Yasmi *et al.* (2005).

The large timber industries continue to burden the Indonesian economy despite maintaining its ability to earn foreign exchange. First, the timber industries contribute to central government's growing fiscal deficit, since the Indonesian Bank Restructuring Agency (IBRA) has failed to collect the US\$ 3 billion in debts that they owe. As a consequence, the debts and accumulated interest have become the responsibility of the government, reducing the amount of funding that would otherwise be available for the poor and/or to maintain forests, and contributing to the country's fiscal deficit. Second, the timber industries have continued to report losses despite earning significant amounts of financial subsidy in the form of debt write-offs. By reporting losses, they did not need to pay the corresponding corporate tax to the government, and this could be used as a basis for arguing with their creditors and to justify to the MoF their not fulfilling their financial obligations, such as paying Reforestation Funds and Forest Resource Rent Provision. Third, despite continuing to earn cash from forestry operations, the timber industries are not interested in re-investing in the forests to maintain their role in the Indonesian economy. Instead, timber barons are far more interested in finding new investment opportunities in the growing Chinese economy and in accumulating personal wealth (Setiono 2004).

According to Barr *et al.* (in prep), under decentralization structural problems faced by the timber industries continue despite efforts by the MoF to cope with them. Instead of resolving or reducing an issue, the decentralization framework creates more problems. In addition to the problem of overcapacity in the timber industry, where the industry's demands far exceed the amount of timber that could be supplied in a legal and sustainable manner (Barr 2001), the forestry sector is now facing the problem of a growing illegal timber industry. By the end of 2001, there were 144 illegal sawmills in Jambi Province alone, whereas only 28 had been documented in September 2000. This province also saw timber companies processing logs without the necessary permits, thereby abusing the terms of their licences (WARSI 2001; Nurdin 2002). These abuses occurred not only in Jambi Province but also in other parts of Indonesia (see, e.g. Budiarto *et al.* 2003).

Although some districts have continued to issue both large and small-scale concession permits since the enactment of Government Regulation 34/2002, which revoked their authority to do so, the number of permits issued is gradually declining. For instance, by mid-2003 no new licences were being issued by Kapuas Hulu District Government (Kartodihardjo and Putro 2004). In the case of Tanjung Jabung Barat, however, the district government continued to issue a few small-scale concession permits a full two years after it no longer had the authority to do so. This is probably a manifestation of Tanjung Jabung Barat District Government's unwillingness to accede to central government's attempt to revoke the districts' authority (Sudirman *et al.* 2005).

Further, in January 2005, the MoF formed a team to verify permits that had been issued by the districts and provinces. The team members are drawn from the Directorate General of Forest Production, MoF Planning Agency and the Bureau of Legal Affairs at the Secretariat General of the MoF; none of the team comes from the districts or provinces. If a concessionaire is shown to have fulfilled the administrative requirements, the MoF may confirm the permit and allow the concession to continue operating<sup>23</sup>. For example, the team has verified a district-licensed forest concession in Bengkulu Utara for areas comprising

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<sup>23</sup> MoF Regulation (*Peraturan Menteri Kehutanan*) No. P.03/Menhut-II/2005 on guidelines for verification of forest concessions or timber plantation permits issued by Governors or District Heads/Mayors (*pedoman verifikasi ijin usaha pemanfaatan hasil hutan kayu pada hutan alam atau pada hutan tanaman yang diterbitkan oleh gubernur atau bupati/walikota*).



about 23,000 ha. By mid-2005, about 17 companies were undergoing similar investigations<sup>24</sup>. These steps taken by central government indicate that it is making an attempt to recentralize forest concession licensing, which was previously under regional government authority. The lack of involvement of regional representatives in the process has prevented them from sharing and learning from past experiences and from building social capital among the forestry actors, i.e. trust and networks.

#### **4. Decentralization, fiscal balancing of forest revenues and district finance**

Indonesia's fiscal decentralization has had a large impact on both the districts' finances and their administration, particularly for natural-resource-rich districts. The districts' budgets have increased substantially since the pre-decentralization period, mainly through central government transfers of shared revenues and general allocation funds (*Dana Alokasi Umum*, DAU). In the first two years of implementation, at least, decentralization provided greater opportunities for districts to raise their own-source revenue (*Pendapatan Asli Daerah*, PAD). In addition, the fact that these funds can be used at the districts' discretion makes them very attractive. Even Reforestation Funds, which are highly restrictive with respect to their uses, are quite flexible to a certain extent. Once these funds are transferred into the districts' accounts, the districts have sole control over their use.

Forestry-related shared revenues have been among the most important sources of income for the districts. Although they may not comprise a very large portion of the districts' budgets, they are still significant. Apparently, incomes from forestry were significant in terms of the contribution to own-source revenue, mostly due to the ability of districts to issue logging permits and collect fees for forest products. For example, forestry-related revenues accounted for 89.9% of the Kapuas Hulu District's own-source revenue in 2001 and 92.5% in 2002, and in 2001 the total contribution from small-scale concessions constituted 74% of Bulungan District's own-source revenue (Dermawan 2004; Samsu *et al.* 2005).

From a seminar on forestry fiscal balancing organized by the MoF's Research and Development Agency in 2004, it became clear that the redistribution of forest revenues has not been without problems. The process is complex, involving the crucial and meticulous calculation of how much of the payment originates from a particular district before a portion is redistributed to each region. It also engages intersectoral and multilevel government actors, including the MoF and forestry offices at the provincial level, and the Ministry of Finance and its provincial offices. Consequently, district governments perceive that how and when the funds are distributed is not transparent, and there were often inconsistencies between the amount of money that should have been redistributed to the regions and the actual receipts, leading to dissatisfaction.

This situation has led some district governments, in West Kalimantan for example, to suspend the transfer of the Forest Resource Rent Provision and Reforestation Funds payments to central government (Dermawan 2004; Yasmi *et al.* 2005). Studies on fiscal balancing in the forestry sector emphasize the need for a more transparent and clearer system (Dermawan 2004; Ngakan *et al.* 2005; Subarudi in prep.). In particular, Ngakan *et al.* (2005) called for more equitable distribution of shared revenues to producing and non-producing districts, as the existing mechanism provides no incentive for the sustainable management of resources.

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<sup>24</sup> Personal communication with officer at Directorate General of Forestry Production, MoF, 21 June 2005.

Central government policies employed to take back the districts' authority to issue logging permits have in fact affected the districts' ability to raise own-source revenue from activities associated with forest extraction. The district governments lost the 'golden moments' in terms of higher own-source income that they enjoyed during the first two years of decentralization. This is demonstrated by the fact that the contribution of forestry-related fees to the districts' own-source revenue was initially very high, but decreased sharply after the enactment of these central government policies.

It is interesting to note that although central government had suspended the district heads' authority to issue small-scale concession permits, and any permits subsequently issued were considered illegal, some forestry fees continued to be transferred to central government. Samsu *et al.* (2005), for example, found that the total Reforestation Funds and Forest Rent Resources Provision deposited with central government by small-scale concession holders in Bulungan District in 2002 and 2003 were relatively high, at US\$ 4.2 million and US\$ 8.9 million respectively.

"Budgets often seem like boring things, but they do quantify an administration's priorities"<sup>25</sup>. The quote is relevant when we look at the expenditure side of some of the district budgets. It appears that many districts put less priority on increasing development expenditures in the agricultural and forestry sectors; instead, they tend to try to increase revenues from forests. Districts see it as being more urgent to build the infrastructure and transportation sectors than develop forestry, in spite of the fact that forestry has been one of the key cash cows.

At district level, decentralization has not been good for conservation – at least, not yet. First, the incentives on the ground are all about raising district revenues by felling trees, possibly because of the need for revenge for the government's actions during the New Order period, and also because of the need to raise own-source revenue for local fiscal and political purposes. Second, districts feel that the responsibility for managing conservation areas lies with central government. The late disbursement of Reforestation Funds creates yet another obstacle for forest conservation and rehabilitation. The implication is that districts could re-prioritize their development to balance the economy–environment interface. The existing initiatives taken by Kapuas Hulu District to establish a conservation district and the issuance of a district regulation (*Peraturan Daerah*, Perda) on saving the forests (*penyelamatan hutan*) in Luwu Utara are examples of steps taken toward meeting this balance, therefore any support from external parties is welcomed. Nevertheless, mechanisms that comply with existing legislation are required to support these initiatives.

## **5. Community benefits and elite capture**

Decentralization of the forestry sector was expected to give communities greater access to forest resources, in terms of both tangible and intangible benefits. Small-scale concession permits issued by district heads may be granted to communities, individuals or a registered company. In reality, because of the rigid procedures and requirements of the application process, and the capital outlay and experience required to manage a concession, most local communities had no choice but to hand over responsibility for the permit application process and concession management to wealthy companies or contractors.

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<sup>25</sup> Quoted from speech by Janet Yellen, currently the President and CEO, Federal Reserve Bank of San Francisco on 2 April 2003. From [http://www.berkeley.edu/news/media/releases/2003/04/02\\_forum\\_yellen.shtml](http://www.berkeley.edu/news/media/releases/2003/04/02_forum_yellen.shtml)

In agreements made with village authorities, business people or contractors would give the village communities a share of timber profits by paying cash fees<sup>26</sup> and providing social benefits such as village development, livelihoods opportunities and physical assistance. Weaknesses in the initial national regulations governing small-scale concessions meant that mechanisms to control the distribution of benefits were drawn up in an ad hoc manner<sup>27</sup>. Fee distribution patterns varied among districts and even among villages within a district. As Samsu *et al.* (2005) found in some villages in East Kalimantan, fees were divided equally among individuals, with equal allocation given even to babies. In other villages fees were divided among households and further divided for main families, new families, widow(er)s and youths. Our research network also found instances where fees were reserved solely for village heads and other members of the local elite (Yasmi *et al.* 2005).

CIFOR and its partners also discovered that benefits were not always distributed in accordance with the agreements made in signed contracts. There were several discrepancies and conflicts, both between communities and investor partners and communities and their own representatives (village officials, *adat* (customary) leaders). A common problem was that investors were not open about actual timber production volumes. Reporting lower volumes than their actual harvest resulted in disputes, as payments were based on volume. One cause of this exploitation was the fact that communities had very little capacity for monitoring and measuring production volumes. Another problem was that even where communities sent representatives to the felling locations to monitor activities, it did not guarantee that the communities' fees matched the volume harvested (Samsu *et al.* 2005; Tokede *et al.* 2005; Yasmi *et al.* 2005, McGrath *et al.* in prep).

Our research showed that although decentralization has provided local communities with much greater access to resources than they had enjoyed before, the nature of the benefits tended to be short-lived and unsustainable (McGrath *et al.* in prep). Despite the new policy's stated objectives of improving forest-dependent communities' livelihoods opportunities, it was other actors such as village elites, investors and timber brokers with links to district officials who captured most of the benefits. Control over small-scale logging concessions was in the hands of high-ranking officials who were connected to *cukong kayu* (local timber barons) and other opportunistic characters who took it upon themselves to broker deals with local communities to take advantage of the new concession system. As shown by research in East Kalimantan (Palmer 2004; Samsu *et al.* 2005; Yasmi *et al.* 2005) and in Papua (Tokede *et al.* 2005), certain village elites received disproportionate benefits from timber extracted from communal customary forests.

## **6. Lessons overlooked**

Forestry decentralization in Indonesia has clear limitations, but it has delivered valuable lessons about how the regulatory framework could be improved to deliver sustainable and equitable forest management processes to support the development of livelihoods for the

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<sup>26</sup> Cash fees were calculated according to the volume of timber extracted, the amount depending on negotiations between community representatives and businessmen or contractors, hence the fees vary from village to village. Samsu *et al.* (2005) reported that average cash fees in study locations varied between US\$ 2.6/m<sup>3</sup> and US\$ 3.7/m<sup>3</sup>. Contractors paid fees to communities after logs had been shipped; they made the payments through village officials or people representing communities in the partnership, usually people having connections with businessmen or village customary figures.

<sup>27</sup> Despite the fact that the objective of decentralization was to give communities access to benefits, no mechanisms for distributing the benefits or supporting communities to develop their capacity to negotiate deals or manage concessions were laid out in the regulations, far less were budgets allocated to support capacity building or monitoring benefit distribution.

country's 20 million forest-dependent people (Sunderlin *et al.* 2000). The district governments' agenda for forest management has not always been weak, whatever many proponents of (re)centralization have tried to argue. CIFOR's research network has documented some clear examples of policy learning and capacity building at the district level. Local governments have begun to introduce clear measures to rectify early policies that had negative impacts (McGrath *et al.* in prep). For example, Samsu *et al.* (2005) found that Bulungan District Government moved the location of small-scale concessions to ensure compliance with prevailing national regulations. Researchers also documented instances where district governments did not issue any small-scale concessions; instead they tried to develop development-oriented conservation and forest product harvesting regimes (Ngakan *et al.* 2005). Other district governments halted the issuance of small-scale concession permits once the district head learned that the concessions did not benefit the local communities as intended. There have also been some collective actions among the community groups, where people learned about achieving common goals together and shared responsibilities (Palmer 2004).

Other positive policy learning includes a district government initiative in Jambi to invite multi-stakeholder input into revising policies (Sudirman *et al.* 2005), attempts to establish traditional *adat* forest management policies in South Sulawesi (Ngakan *et al.* 2005), and an initiative by the local authority to introduce a conservation-oriented policy in Papua with very clear guidelines for reforestation, conservation and community development support mechanisms (Tokede *et al.* 2005).

In the light of these clear examples of stakeholder involvement in policy development, capacity building and policy-learning at the district level, central government's attempts to take back devolved authority seem to be counterproductive. New regulations issued by the MoF have had the objective of recentralizing authority, without including the necessary guidance on the sustainable management of forests, local capacity building or mechanisms for ensuring that the forest-dependent poor are involved in local decisions and benefit from the outcomes. The MoF's introduction of a team to evaluate small as well as large-scale concessions without involving local governments, far less local stakeholders, in any meaningful way also seems to be counterproductive.

The MoF's new priorities for strategic plans for forestry sector development and management are highly unlikely build the capacity of local governments and local stakeholders. Depending solely on centrally based officials to administrate and regulate the forestry sector will put a serious strain on central resources. The new strategy misses a valuable opportunity to exploit local resources and capacity for forest management. This opportunity could be harnessed by building partnerships with local government and local actors, based on trust, confidence and effective multi-stakeholder governance networks (Perkin and Court 2005). Instead, the gains achieved at the local level will diminish (McCarthy 2004).

## **7. Conclusions and perspectives**

This section provides several key lessons from the discussion in the previous sections. Indonesia's experiment with decentralization is still young; at this stage only the short-term effects can be evaluated. We conclude that the long-term prospects for sustaining the country's forestry sector and improving local people's livelihoods by adapting and implementing decentralized forestry policies are far from dismal. There is even cause for optimism.

In relation to the key challenges identified in this paper, the unclear division of authority for forest management and the ad hoc development of a contested legal framework by the MoF, the key lesson is that *powers that are given by means of regulations can be taken away*. As Larson (2005) states, three arguments are commonly used by central governments for retaining authority for forest management: these are that forests, by their nature, are a national public good; that there is lack of capacity in local government; and that local government agendas are ‘too political’, which will limit their use of technical knowledge in decision-making.

However, these three arguments do not justify the recentralization of authority. If the nature of forest as a national public good genuinely justified its control by central government, time has shown that centralized management in Indonesia has failed. If lack of capacity at the district level is the problem, the most sensible solution is not to re-centralize control and put additional strain on limited central resources (finance, manpower and local knowledge). Rather, the sensible approach would be to increase the capacity of districts and local stakeholders to manage forests sustainably and equitably. This would increase the resources available for an effective forest governance network, involving local and national actors working in partnership. Finally, if district governments’ agendas are thought to be ‘too political’, exactly the same problem exists at the centre (Barr 1998; Setiono 2004). Money politics in forestry is not a new phenomenon in Indonesia.

In relation to the continued operations of small-scale concessions, *the contested legal framework has blurred the concept of legality*. On the one hand, forest concessions issued by districts and provinces might be considered illegal according to Government Regulation 34/2002 and its implementing regulations. On the other hand, central government has continued to accept revenue payments from the very concessions that it has tried to outlaw. Governments have also received non-statutory payments from illegal forestry operations and other sources<sup>28</sup>. This lack of clarity about what constitutes legal and illegal concessions and the lack of transparency about how key decisions are made stem from the unclear and contested regulatory framework and its weak provisions governing accountability. This is another area that decision-makers should address urgently.

The role of the private sector during the decentralization-recentralization era of policy-making has been blurred in the sense that *there are several other factors that influence the outcome that may not be attributable to decentralization alone*. However, the big picture is emerging. The quest for local revenue generation, conflicts of authority, the overcapacity problem, illegal forestry activities, the increased costs of doing business in the sector, and the lack of government incentives to encourage the major timber companies to behave like good corporate citizens have all contributed to a negative investment environment in the forestry sector.

*The legal framework must be revised to establish better transparency at every level of government*. Information about the total value forestry-related revenues, what proportion of them has been transferred to whom and when this happened, must be recorded accurately and placed in the public domain. The current system of decision-making by attrition over revenue sharing mechanisms must be replaced with a decision-making process that facilitates officers at central and district levels to be open and able to listen to each other during discussions

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<sup>28</sup> Statement by Head of District Forestry Office, 6 September 2005, and others (McCarthy 2004; McGrath *et al.*, in prep.)

about the best mechanisms for allocating and disbursing forest revenues. Better transparency will result in better governance in Indonesia, as the country races against time to save its forests from disappearing.

In relation to community empowerment, the government should ensure *that decentralized policies take local capacities and skills-requirements into account and introduce clear regulations on the distribution of benefits to stamp out elite capture at the expense of the forest-dependent poor*. All levels of governments have an important role to play in providing advice and guidance on how local people may be able to sustain their income-generating activities and manage their resources sustainably.

To conclude, let us reflect on what Doris Capistrano, the Director of CIFOR's Forest and Governance Programme, said in a National Workshop on Decentralization and Forestry in September 2004, "*...decentralization does not mean weakening the center. Rather, decentralization requires a strong central government that behaves in a different way – different from what it used to do in the past. At the same time, for effective decentralization, provincial and district governments need to be equally strong.*"

The key message from our research on the impacts of decentralization over the last six years is not that decentralization has failed. The message is that the government has failed to implement decentralization.

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