Over four-fifths of the timber harvested in Indonesia comes from illegal sources. Here, timber is extracted from a forest in Riau, Sumatra. (Photo by Romain Pirard)

Cracking down on the money launderers

If you are in the business of drug smuggling, kidnapping for ransom, prostitution, illegal arms trading or illegal logging, you don't stuff the profits from your nefarious activities into a cardboard box under your bed. You launder them through the banking system. If you're going to do that without getting into trouble, you need banks which don't ask too many questions about where and how you made your money.

'Getting banks and other financial institutions to clamp down on money laundering is essential if these illegal activities are to be curbed,' explains CIFOR financial analyst Bambang Setiono. During 2003, Setiono, a former Indonesian government official, worked with the government's Reporting and Financial Transaction Analysis Centre (PPATK) to get illegal logging listed as a money-laundering crime. At present, around 80-90 per cent of the timber harvested in Indonesia comes from illegal sources. The trade in illegal timber damages the environment, deprives the government of billions of dollars in lost revenues and encourages corruption.

In 2000, Indonesia was placed on the list of non-cooperative countries and territories by the G-7's Financial Action Task Force on Money Laundering (FATF). This was a serious situation, as it meant that Indonesian banks could be subject to sanctions which could halt transactions with foreign banks. Two years later, the government published a new anti-money-laundering law, but it was still considered unsatisfactory by FATF. 'It was around that time that I got involved,' explains Setiono. 'I had been working on forest finance, and I offered to provide input on the money-laundering issue.'

Setiono was invited to workshops and seminars organised by PPATK. 'I argued that you couldn't tackle illegal logging – something the government has pledged to do – simply through forestry laws,' he explains. 'Illegal loggers have to put their money somewhere. That means we need to make banks responsible for checking where large sums of money come from.'

Thanks in part to Setiono's efforts, the government introduced a new law in September 2003 which classified forestry and environmental crimes as 'predicate offences' for money laundering. The penalties are harsh: up to 15 years' imprisonment and a maximum fine of 15 billion rupiah (US$1.7 billion). Indonesia is the first country in the world to have done this, and it represents a major step in the fight against illegal logging. The law now requires banks to inform the government of any suspicious transactions, and if they fail to do so they can be prosecuted.

Setiono believes that the new anti-money-laundering law is a significant move in the right direction, but it can only be one element in a multi-pronged strategy. 'Whatever attempts are made to clamp down on the laundering of money derived from illegal exploitation of natural resources, it will be to no avail unless there is a significant improvement in law enforcement,' he says.

Tracking debt

Despite being heavily in debt, many Indonesian forestry companies are still in business and they continue to consume large volumes of timber. (Photo by Christian Cossalter)

Many key decisions about Indonesia's forests are made not by the Ministry of Forestry, but by the various agencies under the Ministry of Finance. One of these is the Indonesian Bank Restructuring Agency (IBRA), which was set up in 1999 to help sort out the country's banking crisis. In return for an injection of cash, bankrupt banks selected for recapitalisation handed over their bad loans to IBRA, whose task it has been to get defaulting companies to settle their debts. Forestry-related assets pledged to IBRA amounted to some US$3 billion in outstanding loans and over US$8 billion in shares and physical assets.

In February 2000, at a meeting of the Consultative Group on Indonesia (CGI), whose 33 members had been providing over US$3 billion in loans each year to keep the Indonesian economy afloat, donors persuaded the government to close the heavily indebted forest industries under IBRA. The aim was to downsize Indonesia's processing capacity, thus reducing pressure on the forests. By closing these companies down, IBRA would also save Indonesian taxpayers considerable sums of money.

Unfortunately, little has been done to meet these commitments. 'What is happening is that bankrupt timber companies have been buying back their debts at sharply discounted prices and the government is writing off the rest,' explains CIFOR policy scientist Chris Barr. This is enabling the companies to continue consuming large volumes of timber.

Even more worrying is the fact that in 2003 IBRA sold US$1.3 billion of forestry debt to Bank Mandiri, a government-owned bank which was soon to be privatised. This meant that the government's net revenue from the sale was zero, as opposed to the 20-30 cents a dollar it was getting for sales to external buyers.

CIFOR raised this issue prior to a meeting of the CGI in June 2003. It urged members of the CGI to insist that Bank Mandiri call in the forest-sector debts on its books before offering shares to the public prior to privatisation. It argued that companies which failed to repay their debts should be closed, as the Minister of Forestry had suggested. CIFOR's efforts to raise this issue received widespread coverage in both the national and international press.