

Mandatory CSR Law in Indonesia ; New Emerging Policy

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ABSTRACT

The changing CSR policy in Indonesia has yet to bring significantly social prosperity to its main beneficiaries. Article 74 of the Limited Company Liability Act has been passed since 6 years ago but unfortunately the provision is not well implemented until now. A lot of sectoral acts were related to the mandatory CSR provision. Some of the Acts are Environmental Management and Protection Act, Coal and Mineral Mining Act, Forestry Act, State Owned Company Act and Social Prosperity Act. Interconnected acts make the situation become worse because there are a lot of “players” on mandatory CSR itself. The aim of this papers is to examine mandatory CSR law in Indonesia (new emerging policy). This a concept paper to elaborate CSR implementation strategy framework from traditional to more responsive one.

Not surprisingly if the provision cannot be well implemented, even though the government regulation has passed the Act in April, 2012 but there are some problems with its implementation and detail mechanism of implementation is required for the fulfilment of mandatory CSR provision.

Theory of legal system will be the tool of analysis in order to describe any constraint in the term of implementation. There are three key elements of the theory such as legal substance, legal structure and legal culture. Those elements would be analysed scientifically against related laws and regulations both national and sub-national level and law is as a tool of social engineering will be also additional tool of analysis for the research.

Mandatory CSR is a concept in which it comes from the perspective of beneficiaries because in some cases corporations are more powerful than the country itself. In other words we can say that Mandatory CSR is a concept of Eastern society. Furthermore, in western society, they recognized CSR as a voluntary action. It can be well implemented there because their level of compliance to the law and other regulations are better than others society. The lives of human being is just like a cyclus of life, different age and place has different way of life or culture. Finally, mandatory CSR as an emerging policy will appear to be solution of new relationship standard between the government, coporation and society.

Keywords: Mandatory, Corporate Social Responsibility, Law, Policy

Sectoral CSR Laws in Indonesia

Introduction

Indonesia as one of emerging developing countries has been at a top list of direct foreign investment. The situation will attract more companies to invest their capital to Indonesia. among factors considered by the companies in making decision to invest are infrastructures, raw materials, cheap labour cost, political and security stability and economic incentives offered by host government. For many years Indonesia has been practising Corporate Social Responsibility (CSR) on a voluntary basis since the Limited Company Liability Act Number 1/1995 come into force on 7 March 1995.¹The Act was silent about CSR, but how the companies were disbursing their funds to finance some social project within their areas of business operations from time to time. But after the enactment of Limited

¹Act Number 1/1995 on Indonesia Company Liability

Company Liability Act No 40/2007, there were two types of CSR implementation in Indonesia which is voluntary and mandatory. Voluntary one has been implemented by non-natural resources based companies and mandatory was implemented by natural resources based companies. Unfortunately, until now specific guidance on mandatory CSR is not yet available therefore each company in Indonesia has been fulfilling its CSR programs based on voluntary basis. Moreover, they interpret CSR in multi definitions and types of program. Some of them considered CSR as a charity and some of them considered CSR as philanthropy. There is no specific and technical guidance on CSR project's implementation released by the government. As a result, the companies conducting the programs based on self-regulatory framework and its own discretion. Additionally, there were a number of companies were voluntarily be part of international standards of CSR framework, such as ISO 26000 on Social Responsibility,² OECD guidelines for multinational enterprises³ or Roundtable Sustainable Palm Oil (RSPO) manual for palm oil plantation companies.⁴

After some time, local communities extractive industries demanded that the companies should be socially responsible to the social and environmental condition of the society around them. In some areas where extractive industries operating their businesses, incidents may happened for example environmental disasters caused by the industries i.e. waste leakage, mud volcanoes, forest destruction, or animals mass killing as well as social disharmony between the companies and local communities. The environmental cases and social disharmony were increasingly occurs and some of NGOs also supported the people's demand by providing advocacy and legal advise or negotiation to the decision makers. Therefore, the government of Indonesia had revised the Limited Company Liability Act, and mandatory CSR legal provision was included as a way out to mantain good relationship between the local communities and the companies.

Although, the government did not provide any standards, guidelines, principles or guidance to implement mandatory CSR but there are some international organizations offer guidance or guidelines to implement CSR. One of them is a CSR mechanism reporting which is organized by Global Reporting Initiative.⁵ The voluntary initiative is intended to assist companies to draft its annual CSR reproting to be recognized by international reproting standards. They also regularly organize Indonesia Sustainability Reporting Awards to be granted for Indonesian companies which of the sustainability report has met global standard.

Currently, there are three leading ministries that are directly initiating, managing and mobilizing CSR funds from companies throughout Indonesia. There are The Ministry of Environmental Republic of Indonesia⁶, Ministry of State-Owned Companies Republic of Indonesia⁷ and Ministry of Social Republic of Indonesia.⁸ each of them had released their policies based on their sectoral laws.

²International Organization of Certification (ISO), http://www.iso.org/iso/iso_catalogue/management_and_leadership_standards/social_responsibility (Accessed 20 July 2013).

³Organization for Economic Cooperation and Development (OECD), <http://www.oecd.org/daf/inv/mne/>, (Accessed 20 July 2013)

⁴Roundtable for Sustainable Palm Oil (RSPO) <http://www.rspo.org/>, (Accessed 20 July 2013).

⁵Global Reporting Initiatives (GRI), <https://www.globalreporting.org/Pages/default.aspx>, (Accessed 20 July 2013).

⁶ Act Number 23/2007 on Environmental Management then it was revised by Act Number 32/2009 on Environmental Management and Protection.

⁷ Act Number 19/2003 on State-Owned Companies. The terminology is also known as Government Linked Companies in Malaysia context.

⁸ Act Number 11/2009 on Social Prosperity.

Further, neither Act Number 1/1995 on Company Liability Act nor its newest version Act Number 40/2007 on Limited Company Liability Act has appointed specific ministries to take responsibility to lead CSR policies and implementation strategies in Indonesia. It disrupts the situation because each of them is competing with each other to issue CSR related policies and as a result there was lack of coordination and communication among them. This scenario can be seen as a challenging situation. This is because CSR standardization on environmental aspect that was issued by the Ministry of Environmental has a minimum communication and coordination with other stakeholders such as other governmental institutions or CSOs. Additionally, in some cases the companies and beneficiaries would confuse because of overlapping policies and CSR standards.

The writer is of opinion that the government of Indonesia is encouraged to produce more comprehensive CSR related policies to be implemented. This is to establish transparent and accountable CSR programs in Indonesia.

CSR Standardization in Indonesia

To date, generally Indonesia does not have a mandatory CSR manual. Even though mandatory CSR has been enshrined into national law system since 2007. After the enactment of the Bill until now, companies in Indonesia are carrying out their CSR programs based on their own initiatives. Most of them developed the programs based on their own discretion and others are hiring CSR consultant either from consultant companies or universities. It was very difficult to measure the degree of successfulness of the implemented CSR programs.

Additionally, lots of sub-national government either provincial or districts government competing each other to set CSR rules and take CSR fund as its domestic revenue. Based on this, it needs a standard of policies on the guidance and its implementation. Until now, there are some voluntary standards have been released by international and national organizations either governmental and non-governmental institution. As examples CSR guidelines on environmental aspect,⁹ Corporate Social Responsibility Empowerment Manual in Social Prosperity,¹⁰ United Nations Global Compact,¹¹ United Nations Guiding Principles on Business and Human Rights,¹² International Standard ISO 26000 on Social Responsibility, International Finance Corporation (IFC) Policy and Performance Standards on Social and Environmental Sustainability,¹³ European Union Policy on CSR¹⁴ and OECD Guidelines for Multinational Enterprises.¹⁵

Most of these standards are internationally recognised and some instruments have been developed by international organizations. Apparently, Indonesia has a different paradigm where Indonesia introduced mandatory CSR rather than voluntary one.

⁹ Ministry of Environmental Republic of Indonesia, *Corporate Social Responsibility Guidelines in Environmental Aspect*, <http://www.menlh.go.id/proper/> (Accessed on 21 July 2013).

¹⁰ This guidelines was made Ministry of Social Republic of Indonesia.

¹¹ United Nations Global Compact, <http://www.unglobalcompact.org/> (accessed on 21 July 2013).

¹² Business-Human Rights, <http://www.business-humanrights.org/SpecialRepPortal/Home/Protect-Respect-Remedy-Framework/GuidingPrinciples> (accessed on 21 July 2013).

¹³ International Finance Cooperation (IFC), http://www.ifc.org/wps/wcm/connect/topics_ext_content/ifc_external_corporate_site/ifc+sustainability/publications/publications_handbook_pps (accessed on 21 July 2013).

¹⁴ European Union (EU), http://ec.europa.eu/enterprise/policies/sustainable-business/corporate-social-responsibility/index_en.htm (accessed on 21 July 2013).

¹⁵ Organization for Economic Cooperation and Development (OECD), <http://www.oecd.org/daf/inv/mne/> (accessed on 21 July 2013).

The article 74 of Limited Company Liability Act No. 40/2007 is the legal basis for mandatory CSR implementation in Indonesia. but however, It was only implemented by the government in April 2012. Even though there is nearly 5 years interval time between the executing regulation and Limited Company Liability Act No 40/2007 but it is still incomplete towards the implementation of mandatory CSR legal provision in Indonesia. Based on this provision the company as a legal subject has an obligation to fulfill its social and environmental responsibility.¹⁶

Mandatory CSR Legal Norms

Mandatory term means that it is absolutely demanded or required.¹⁷ It is a legal term to require other parties to do as prescribed on an Act. The term is in contrast with voluntary¹⁸. The notion of mandatory CSR has been enshrined into the Company Liability Act due to adverse impact of mining industries to the environmentsurrounding the company operation.¹⁹ It brings rejection and protest from the local communities.²⁰the Non-Governmental Organizations together with the affected communities organized advocacy effort by demonstration, public pressure and any other protest to the decision makers. It has been about nearly 5 years since its enactment, mandatory CSR legal provision does not work well in Indonesia because there is no further executing regulation as mentioned in the Bill. The government should execute a government regulation in order to implement the new policy. Although, the new CSR policy has been legally challenged by some business associations in Indonesia such the Indonesian Chamber and Commerce (*Kamar Dagang Indonesia*), the Indonesian Businesswomen Associations (*Ikatan Wanita Pengusaha Indonesia*) and the Indonesian Young Businessmen Association (*Himpunan Pengusaha Muda Indonesia*). but the provision is still prevail.

Mandatory CSR legal norm is a new emerging policy in dealing with CSR issue. Most of countries especially European Countries are more familiar with the norm of voluntary CSR. Moreover, in its CSR policy document, European Union says obviously that “*Corporate Social Responsibility is defined as a concept whereby companies integrate social and environmental concerns in their business practices and in their interaction with their stakeholders on a voluntary basis*”²¹. Furthermore the World Business Council for Sustainable Development defined CSR as “*a continuing commitment of the business to behave ethically and contribute to the economic development while improving the live of the workforce as well as of the local community and society at large*”.²²

In the Organization for Economic Cooperation and Development (OECD) guidelines also define CSR as a voluntary basis and not legally enforceable.²³ But the guidelines will not substitute the domestic law of any state. Even though, multinational enterprises has adhered to the guidelines but still they should obey the national law of any respective country. However the writer has off-opinion that mandatory CSR intriduced by Indonesian Government is not contradicting with legal document that has been released by OECD on its Guidelines for Multinational Enterprises.

Civil Society Organizations Participation

¹⁶ Article 2 of Government Regulation Number 47/2007 on Corporate Social and Environmental Responsibility “Each company as legal subject has social and environmental responsibility”.

¹⁷ <http://dictionary.law.com/Default.aspx?typed=mandatory&type=1> (accessed on 22 July 2013).

¹⁸ Voluntary means; without intent, will or choice. <http://dictionary.law.com/Default.aspx?selected=1026> (accessed on 22 July 2013).

¹⁹ Academic papers of the Limited Company Liability Act Number 40/2007

²⁰ Mud Volcanoes in Porong Sidoarjo, East Java, http://id.wikipedia.org/wiki/Banjir_lumpur_panas_Sidoarjo (accessed 25th August 2012).

²¹ European Union Policy Papers on Corporate Social Responsibility,

²² World Business Council for Sustainable Development

²³ OECD Guidelines for Multinational Enterprises, p.17.

In today's world Civil Society Organizations (CSOs) role is very significant to encourage transparency and accountability of particular projects. A partnership with local CSOs is a must to enhance strategy implementation of CSR projects. There were some previous academic studies demonstrated that CSOs involvement may strengthen transparency and good governance in many countries.²⁴ Furthermore, CSOs may play a significant role in raising awareness on public procurement and other areas of public financial management (PFM).²⁵ Subsequently, CSOs mobilize people and resources through strong commitment among them to social values and missions that strengthen public good.²⁶ There were some academic examples on how CSOs involvement is very important in the execution of CSR projects in Indonesia which are very significant to enhance good CSR governance.

According to Article 74 of Limited Company Liability Act Number 40/2007, CSOs involvement was not obviously mentioned by the Bill. No single word of the article was saying about the involvement of CSOs. Furthermore, on the Government Regulation Number 47/2012 on CSR was not clearly stated any CSOs role. Notwithstanding, in some international recognised guidelines such as European Union Policy on CSR and OECD Guidelines for Multinational Enterprises encouraged any close interaction with the company's stakeholders. It can be translated as CSOs involvement in the process of CSR implementation. Indonesia has enacted its own policy for CSR which is called mandatory CSR legal provision, this is a new policy that can encourage the involvement of CSOs as part of the CSR long-term strategic planning in strengthening accountability and transparency of CSR projects in Indonesia.

According to Government Regulation Number 93/2010 on Charity for National Disaster, Research & Development, Educational Infrastructures, Sports Development and Social Infrastructures which can be deducted from the Companies' Bruto Revenue, it clearly says that CSOs may closely involve to the some activities as mentioned by the regulation. Indeed, CSOs may receive the financial assistance from the companies then they can distribute to the recipient either natural disaster victims or research and development activities.²⁷

Tax Reduction Law System

As stated on the government regulation No 93/2010, companies can disburse for charity for maximum 5% of its net to revenue based on its previous fiscal tax year. Indeed, the government has released a tax-holiday or tax reduction scheme as demanded by companies in Indonesia related to the implementation of mandatory CSR policy. Although, the regulation has come into force earlier than the government regulation on CSR itself. The regulation on charity which is contained tax reduction policy has been passed on 2010 but the regulation on CSR has passed in April 2012.

In practice, the companies participated in social activities in CSR projects can claim tax reduction to the Tax Directorate General. Some of the local communities or CSOs lack of knowledge on how the

²⁴ Ngozi Okonzo-Iweala and Philip Osafo-Kwaako, The Role of Civil Society Organizations in Supporting Fiscal Transparency in African Countries, http://www.resultsfordevelopment.org/sites/resultsfordevelopment.org/files/resources/Ngozi-CSO_Paper_Revise_Version.pdf (accessed on 25th August 2013).

²⁵ Procurement Capacity Development Centre United Nations Development Program (PCDC UNDP), Accountability in Public Procurement, Transparency and the Role of Civil Society, <http://www.unpcdc.org/media/142496/story%20of%20an%20institution%20-%20accountability.pdf>, (accessed on 25th August 2013).

²⁶ L. David Brown & Jagadananda, Civil Society Legitimacy and Accountability, http://www.civicus.org/new/media/LTA_ScopingPaper.pdf, (accessed on 25th August 2013).

²⁷ Article 1 point a and b of government regulation number 93/2010.

mechanism being used by the companies to identify their CSR beneficiaries. The companies increasingly demanded tax holiday from the government if they implement mandatory CSR programs. But the government is reluctant to give the real tax reduction for CSR implementation by the companies within the mandatory CSR framework. It is suggested that the government provides a CSR clear and transparent measures regarding the implementation of CSR programs. This is to enable the companies to enjoy the benefits of tax reduction based on their performance.

Article 74 of Limited Company Liability Act stated that CSR fund will be calculated as a cost production of the company.²⁸ It means that the company has a flexibility to allocate number of CSR fund to be disbursed for a particular budget year. Furthermore, the Article said that the implementation of CSR program shall be performed based on decency and fairness principles.²⁹ Decency and fairness principles will define financial capacity and human resources ability of a particular company to implement its CSR program. Therefore, according to the Article 74 the execution of CSR program within mandatory CSR framework is in immediate effect.

Furthermore, article 5 clause (2)³⁰ re-affirm that CSR fund that will be disbursed by the company calculated as the company's cost. In this instances the company should not hesitate to implement CSR programs because the tax system is guarantee where the company will be able to obtain tax deduction. As an example, Pertamina, a national oil and gas company of Indonesia is committed to implement CSR programs within mandatory CSR framework if it is not exceed 5% of its total profit.³¹ Pertamina is still able to finance for some CSR projects when it is below 5% or at 5% in total.

The Overlapping CSR related Law

There were some Acts at the national level is governing CSR issue. Most of them use CSR fund a source of funding to finance some projects either physical or non-physical project. Then, the project is owned by governmental institution or based on proposal submitted by private person, groups of business and small and medium sized enterprises. The bills were handled by some different ministries so that based on those Bills, each ministry has a legal right to mobilize and to manage CSR fund based on its ministry scope of work.

As a result, these ministries starting to initiate and execute their rules and regulations, technical guidance, manual, guidelines or even facilitating some meetings such as seminar, workshops, training or giving awards to some of most outstanding companies that has implemented CSR program in a very well manners according to their own appraisal. As example there are specific laws that is related to CSR issues, Law Number 19/2003 on State-Owned Company, Law Number 32/2009 on Natural Management and Protection, Law Number 11/2009 on Social Prosperity, Law Number 22/2001 on Oil and Gas, Law Number 19/2004 on Forestry, Law Number 25/2007 on Investment and Law Number 40/2007 on Limited Company Liability. Therefore, the existing sectoral implementation strategy leads to confusion, redundant and overlapping measurements on CSR projects in Indonesia. The companies should be given autonomy power to determine their own CSR projects and they are also has equal rights to get fund from the CSR projects.

²⁸ Article 74 Limited Company Liability Act Clause (2) "*Social and environmental responsibility constitutes an obligation of the company which shall be budgeted for and calculated as a cost of the company performance of which shall be with due attention to decency and fairness*"

²⁹ *Ibid*

³⁰ Government Regulation Number 47/2012 on Social and Environmental Responsibility

³¹ Detik Finance, Enterprises request CSR fund is maximum 5% of its total profit, <http://finance.detik.com/index.php/detik.read/tahun/2007/bulan/07/tgl/21/time/143138/idnews/807730/idkanal/4> (accessed 26th August 2013).

Conclusion

Based on the discussion above, it shows that there are exist unresolved issues and problems in executing of mandatory CSR legal framework in Indonesia. the decision of consituitional court in Indonesia, clearly said that the mandatory CSR is in line with the spirit of constitution and article 74 is prevail. However, the main weaknesses is relation to implementation of mandatory CSR programs because they should have standardisation, standard guidelines and procedures for government organizations and private companies. Finally, it is suggested that Indonesia should have an authoritised CSR body that is able to issue policies, rules, regulations, standards or guidelines as well as to monitor and to evaluate CSR programs in Indonesia either CSR programs at national or sub-national level.

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