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**MANDATORY CORPORATE SOCIAL
RESPONSIBILITY: LAW AND POLICY IN INDONESIA**

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JULY 2016**

CERTIFICATION OF THESIS WORK

I hereby certify that this thesis is the result of my own research, except where otherwise stated. I also declare that it has not been previously or concurrently submitted as a whole for any other degrees at UUM or other higher education institutions.

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ABSTRAK

Kajian ini adalah berkaitan dengan Perlembagaan Kehakiman Bilangan 53/PUU-VI/2008 mengikut Semakan Kehakiman artikel 74 Undang-Undang Perseroan Terbatas Nombor 40/2007. Penghakiman tersebut secara rasmi dan sah mengukuhkan bahawa peruntukan undang-undang mandatori Tanggungjawab Sosial Korporat (CSR) adalah selaras dengan perlembagaan Indonesia. Oleh itu, peruntukan undang-undang mandatori CSR masih menjadi sebahagian daripada Undang-Undang Perseroan Terbatas Nombor Nombor 40 /2007. Penghakiman tersebut telah diluluskan pada 2008 tetapi mengambil masa yang agak lama untuk direalisasikan disebabkan Kementerian Keadilan dan Hak Asasi Manusia telah meluluskan Peraturan Nombor 47/2012 kepada Tanggungjawab Sosial dan Alam Sekitar. Peraturan ini hanya dilaksanakan selepas 4 (empat) tahun ianya diluluskan. Dalam tempoh tersebut terdapat perdebatan pro dan kontra dalam kalangan persatuan perniagaan, kerajaan, ahli akademik dan Pertubuhan Bukan Kerajaan berasaskan CSR berkaitan dengan enakmen peruntukan undang-undang mandatori CSR. Kajian ini memeriksa dan menganalisis beberapa isu utama seperti rasional falsafah di sebalik Enakmen undang-undang mandatori, tahap mandatori CSR yang digunakan sebagai garis panduan oleh syarikat pada masa kini dan fungsinya, serta liabiliti dan bidang kuasa badan pengawasan mandatori CSR di Indonesia. Kajian ini menggunakan kaedah penyelidikan kualitatif di mana analisis kandungan digunakan sebagai unit analisis. Beberapa data seperti artikel jurnal, buku, Rang Undang-Undang, dan fail peraturan yang berkaitan dikumpulkan. Selain itu, beberapa data lapangan turut dikumpul melalui temubual yang diperolehi daripada tiga puluh orang sumber utama CSR yang terdiri daripada ahli akademik, Pertubuhan Bukan Kerajaan berasaskan CSR, pegawai kerajaan, syarikat dan wakil-wakil persatuan perniagaan. Hasil kajian adalah seperti berikut: Kerajaan Indonesia perlu mengukuhkan pengawalaturan terhadap CSR dengan meluluskan Akta berkenaan CSR. Penubuhan badan pemantauan CSR juga perlu, manakala peraturan mandatori CSR, pengawalaturan, dan garis panduan juga perlu dikanunkan dan diluluskan oleh pihak kerajaan. Selain itu, Buku Panduan berkaitan CSR Mandatori bagi Indonesia disyor agar diluluskan oleh pihak kerajaan. Sehubungan dengan itu, kajian ini menyediakan beberapa hasil dapatan kajian bagi menyebarkan maklumat yang komprehensif mengenai Enakmen undang-undang mandatori CSR. Selanjutnya, kajian ini mencadangkan piawaian mandatori CSR yang sesuai dengan konteks Indonesia dan fungsi pengurusan yang lebih baik, liabiliti dan bidang kuasa badan pengawasan mandatori CSR di Indonesia. Kajian ini diharapkan dapat memberi manfaat kepada pengukuhan peruntukan undang-undang CSR dan pelaksanaannya bagi penderafan rangka kerja mandatori CSR yang lebih baik di Indonesia.

Kata Kunci : Tanggungjawab Sosial Korporat, Undang-Undang CSR, CSR Mandatori, Polisi CSR.

ABSTRACT

This research is related to Constitutional Court Verdict Number 53/PUU-VI/2008 on Judicial Review of Article 74 of Company Liability Act Number 40/2007. The verdict officially and legally stipulates that mandatory CSR legal provision be made consistent with the Indonesian constitution. Therefore, the mandatory CSR legal provision is still part of Act Number 40/2007 of Limited Company Liability. The verdict was passed in 2008 but its realization was delayed since the Ministry for Justice and Human Rights passed Regulation Number 47/2012 on Social and Environmental Responsibility. This regulation is only executed four years after the regulation was released. During that period there was pro and contra debates among business associations, the government, CSR academics, and CSR based NGOs on the enactment of mandatory CSR legal provision. This research examines and analyzes the following key issues: (1) the philosophical rationale behind the enactment of mandatory legal provision, (2) the mandatory CSR standard of guidelines currently used by corporations, and (3) the functions, liabilities and jurisdiction of the mandatory CSR surveillance body in Indonesia. Using a qualitative approach, this study applies a content analysis as an analysis tool. Relevant data from journal articles, relevant books, Bill, and rules and regulations were collected. Additionally, some field data were collected from the interviews with thirty key CSR resource persons. These respondents consisted of academics, CSR-based NGOs, government officials, corporations, and business association representatives. The findings are as follows; the government of Indonesia should strengthen regulation on CSR by passing an Act on CSR, the establishment of CSR surveillance body is necessary, mandatory CSR rules, regulations, and guidelines are also important to be codified and passed by the Government and Indonesia Manual on Mandatory CSR is encouraged to be passed by the Government. Accordingly, this research significantly provides some recommendations on a comprehensive information dissemination of the enactment of mandatory CSR. It also suggests a proper mandatory CSR standard be outlined to suit the Indonesian context and complexity, and that better management functions, liabilities, and jurisdictions of the mandatory CSR surveillance body be strengthened in Indonesia. It is hoped that the findings would benefit the implementation of mandatory CSR legal provision and the drafting of a better mandatory CSR legal framework in the country.

Keywords: Corporate Social Responsibility, CSR Law, Mandatory CSR, Policy CSR.

ACKNOWLEDGEMENTS

All praise is due to Allah SWT, peace and blessing be upon Prophet Muhammad SAW, his family and his companions. I would like to express my appreciation to the following person who always support and help me during this thesis- making.

I would like to acknowledge advice, guidance, support and kindness of my academic supervisor Prof. Dr. Asmah Laili Hj Yeon. Thank you for all the opportunities that you have showed me to which definitely will help me in my future career.

I acknowledge for scholarship is provided by *Aceh Scholarships Commission* who gave me an opportunity to pursue my PhD degree in Law at College of Law, Government and International Studies Universiti Utara Malaysia (UUM). Further, I highly appreciate the support and contribution of all people including all Aceh PhD students who encourage me to finish my thesis in time.

Moreover, my endless appreciation is directed to my wife, *Susanti* who always accompanying me and encouraging me in her passionate and also waiting for a long period of my study at UUM.

In addition, I would like to acknowledge my endless appreciation and perpetually grateful to my late mother *Rosdiana Dalimunthe* for what I have achieved today. she had taught me to be a tough person and she will remain in my heart forever. Allah Subhanahu Wata'ala grants her a jannah. Even though, you are not exist today but I believe that your soul are still standing by me. her spirit will be the greatest power for me to sustain my life ever.

My special thanks also come to my late step mother *Sri Mulyani* who has supported and helped me very much in the early stage of my study. Further, my great appreciation is also given to my late uncle *Ilham bin Tgk Ilyas Leube* for his support both spirit and financial. May Allah Subhanahu Wata'ala grants him a jannah too.

I would like also to thankful to my father *Muhammad Darsah* who never give up providing me advice, guidance and supports in whole my life, especially during my PhD study at UUM. Again, my highly appreciation come to my younger sister *Dia Aulia*, her husband *Tawarmiko* and my three nephews *Akbar Al-Hazhiem*, *Isagali* and *Sirhan Adli*. Your endless support to my study is really unforgettable.

At last but not least, I would like to thankful to anybody who support me during the completion of my thesis, their humble acceptance and valuable inputs and advice always be a spirit for me to finish my thesis.

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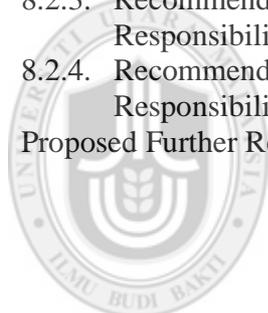
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List of Abbreviations

CSR	: Corporate Social Responsibility
KADIN	: Indonesia Chamber of Commerce and Industry
IWAPI	: Indonesian Business Women Association
HIPMI	: Indonesian Businessmen Association
BPK	: Supreme Auditor Agency
BPKP	: Financial and Development Auditor Agency
BKPM	: Indonesian Investment Coordination Board
TJSL	: <i>Tanggung Jawab Sosial dan Lingkungan</i> /Corporate Environmental and Social Responsibility
PKBL	: <i>Program Kemitraan dan Bina Lingkungan</i> (Partnership and Community Development Program)
FDI	: Foreign Direct Investment
PT	: <i>Perseroan Terbatas</i> /Limited Company
SOE	: State Owned Enterprise
BAPEPAM-LK	: <i>Badan Pengawas Pasar Modal dan Lembaga Keuangan</i> /Indonesia Financial Institution and Stock Exchange Supervisory Body
OECD	: Organization for Economic and Cooperation Development
ISO	: International Certification Organization
DPR	: Dewan Perwakilan Rakyat/The People's Representative Council
DPRD	: Dewan Perwakilan Rakyat Daerah/Regional Peoples's House of Representative
UDHR	: Universal Declaration of Human Rights
UNDRIP	: United Nations Declaration on the Rights of Indigenous Peoples
REDD	: Reducing Emission from Deforestation and Degradation

ICCPR	: International Covenant on Civil and Political Rights
ICESCR	: International Covenant on Economic, Social and Cultural Rights
MEAs	: Multilateral Economic Agreements
TNCs	: Trans National Corporations
AMAN	: <i>Aliansi Masyarakat Adat Nusantara</i> /Customary Community Alliance of Archipelago
FPIC	: Free and Prior Informed Consent
CSO	: Civil Society Organization
NGO	: Non-Governmental Organization
GLC	: Government Linked Companies
CSD	: Corporate Social Disclosure
MERA	: Malaysian Environmental Reporting Award
MESRA	: Malaysian Environmental and Social Reporting Award
APIP	: State Internal Supervisory Apparatus
EP	: Equator Principles
EPA	: Equator Principles Association
EPFIs	: Equator Principles Financial Institutions
IFC	: International Finance Corporation
EHS	: Environmental, Health and Safety
WBDID	: World Bank Development Indicators Database
WBPPAH	: World Bank Pollution Prevention and Abatement Handbook
PROPER	: Company's Performance Appraisal Programme in Environmental Management
UKL-UPL	: Environmental Management Tools-Environmental Protection
AMDAL	: Environmental Impact Assessment

PRIA	: Principles for Responsible Investment Association
PRI	: Principles for Responsible Investment
ESG	: Environmental, Social and Governance
UNEP	: United Nations Environmental Programme
UNGPBHR	: United Nations Guiding Principles on Business and Human Rights
TAC	: Technical Advisory Council
SC	: Stakeholder Committee
GAG	: Governmental Advisory Group
GRI	: Global Reporting Initiatives
PPSSES	: Policy and Performance Standard on Social and Environmental Sustainability
UNGC	: United Nations Global Compact
GCLN	: Global Compact Local Networks
LCG	: Local Community Group
CFCD	: Corporate Forum for Community Development
BPK	: Supreme Audit Agency
BPKP	: Development and Financial Auditor Agency
CPA	: Certified Public Accountant
BUMD	: Local Government Owned Enterprise
SKPD	: Province/District/City Implementation Unit
APBN	: National Annual Revenue and Expenditure Budget
APBD	: Province/District/City Annual Revenue and Expenditure Budget
APIP	: Government's Internal Inspector.
KPK	: Corruption Eradication Commission

DPR	: National House of Representative
DPD	: National Senate Council
SKK MIGAS	: Special Task Force for Upstream and Gas Business Activities Republic of Indonesia
WALHI	: Indonesian NGOs Forum for Conserving Environment
WUP	: Mining Area License
WPR	: Mining Community Are License
WPN	: Mining Province License
WIUP	: Mining Business Area License
IUP	: Mining Busines License
PAD	: Local Government Revenue
NPWP	: Taxpayer Identification Number
MK	: Constitutional Court
RUPS	: Annual General Meeting of Shareholders

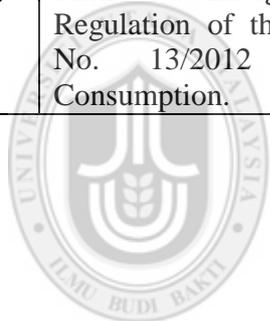
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CHAPTER ONE

INTRODUCTION

1.1 Background of the Study

The notion of modern corporate social responsibility (CSR) was first marked by a book on the social responsibility of businessmen.¹ The author establishes that a businessman should be socially responsive to the people living around his or her business operations.² Further, CSR is defined as “the social responsibility of business comprising of economic, legal, ethical, and discretionary expectations (which later referred as philanthropic) that a society has of organizations a given point in time.”³ The European Union defined CSR as “a concept whereby companies integrate social and environment concerns in their business operations and in their interaction with their stakeholders on a voluntary basis.”

Subsequently, the World Business Council for Sustainable Development (WBCSD) states that CSR is a continuing commitment by businesses to behave ethically and contribute to economic development. It is also a commitment to improve the quality of life of the workforce and their families as well as of the local community and society at large. CSR practitioners define CSR as the ways companies manage their business processes to produce an overall positive impact on society.

The mandatory CSR legal provision has been considered by legislative members to be included in the new Limited Company Liability Act due to

¹Howard B. Bowen, *Social Responsibilities of the Businessmen*, [New York, Harper & Row, 1953], 17.

²Ibid

³Archie B. Carroll, “A Three-Dimensional Conceptual Model of Corporate Social Performance,” [New York, Academy of Management Review, Vol. 4, 1979], 497.

environmental reasons. Environmental cases that occurred in many places throughout Indonesia, such as the mud volcano disaster in Porong Sidoarjo, are the reasons behind the enactment of Article 74 of Act No. 40/2007 in the Limited Company Liability Act.⁴ Another case is at Freeport-McMoran, a gold mining company in Papua.⁵

Environmental reasons were the main factors that led to the adoption of mandatory CSR legal provisions. At the international scene, there have been several negative examples of massive environmental and social impacts incurred by the business operations of several extractive industries. Examples include (1) the chemical leakage case in Bhopal India, (2) the negative environmental impact and unfair social treatment provided by Shell to the local groups in Nigeria, and (3) the child labour case of Nike in China.⁶

The Bhopal gas tragedy was a clear evidence that extractive industries must pay heed to their environmental management while they are operating in a certain place. Environmental destruction may cause suffering for the people living around the project sites. The Bhopal tragedy reportedly caused 3,787 deaths, over 16,000 inflicted with disability, and approximately 558,125 injured. The tragedy was caused by the leakage of a storage tank in the premise of Union Carbide India Limited. The casualty then triggered the Government of India to draft a guideline on environmental and social aspects for these industries. Eventually, India came up with National Voluntary Guidelines on Social, Environmental, and Economic Responsibilities of Business. The standardization was to guide

⁴ Maria Åkesson, "Mud Volcanoes-A Review." *Lund University*, [Stockholm, 2008], 2.

⁵ J. Perlez, and R. Bonner, "Below a Mountain of Wealth, a River of Waste," [New York, New York Times, 2005], 7.

⁶ Gunther Teubner, "The Anonymous Matrix: Human Rights Violations by 'Private' Transnational Actors", [United Kingdom, *The Modern Law Review* 69, No. 3, 2006], 328.

business entities to act socially, environmentally, and economically, and to be more responsible.⁷

In one case, an oil company, Shell, has caused an environmental devastation in Ogoni Lands in Niger Delta. The case was the flaring of gas that was contaminated with toxic compounds.⁸ Through precipitation, the toxic gas ended up in the nearby rivers, waterways, and fields. The toxic might have caused carcinogens, convulsions, chromosomal damage, and birth defects. Subsequently, the Government of Nigeria passed Associated Gas Reinjection Act in 1979 which required all oil and gas companies to submit a detailed business plan for exploring and utilizing gas in oil industries.⁹

Nike is one of the world's leading trademarks for shoes products. Nike products are currently produced in more 700 factories in over 50 countries.¹⁰ Most of Nike products are produced by third manufactures and suppliers. In fact, manufacturers, sub-contractors and suppliers provided salary below wage rates in country where they live and also workplace conditions are really sore.¹¹ It was a real example how a multinational company against an international labour standard.

All of the above violations have encouraged NGOs of the environment and human rights to advocate community's right in relation to the negative impacts of the mining industries. Social demand from the community and social pressure

⁷ National Voluntary Guidelines on Social, Environmental and Economic Responsibilities of Business, Ministry of Corporate Affairs, Government of India, 2011.

⁸ Center for Constitutional Rights, *Shell's Environmental Devastation in Nigeria*, New York: 2007.

⁹ Ibid

¹⁰ David F. Murphy and David Mathew, *Nike and Global Labour Practices; A case study prepared for the New Academy of Business Innovation Network for Socially Responsible Business*, London: 2001.

¹¹ Ibid

from the NGOs have changed the situation. In early 2007, the Government of Indonesia together with the Indonesia National House of Representative amended the Company Liability Act.¹²

CSR debates in Indonesia have been ongoing since the enactment of the new Limited Company Liability Act.¹³ This is due to the regulating of special legal provision that serves as the legal basis of mandatory CSR implementation in Indonesia. The legal provision stated as follows:

- (1) *Companies doing business in the field of and/or in relation to natural resources must put into practice environmental and social responsibility.*
- (2) *Environmental and social 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.*
- (3) *Companies who do not put their obligation into practice shall be liable to sanctions in accordance with the provisions of legislative regulations.*
- (4) *Further provisions regarding environmental and social responsibility shall be stipulated by government regulation.*¹⁴

The above is the latest amendment of the previous Limited Company Liability Act.¹⁵ The legal provision comprises only four (4) sub-articles and this is not sufficient to cover the many areas of the implementation of mandatory CSR. In fact, some information are not covered by the legal provision such as (1) types of CSR programmes, (2) the monitoring and evaluation mechanism, (3) the mandatory CSR manual and handbook, and (4) the monitoring and evaluation body or state institution that is in-charged of handling the mandatory CSR policies. These areas should be described in the provision's executing regulations, manuals and other kinds of policies.

¹²Act No. 40/2007 on Limited Company Liability.

¹³Ibid

¹⁴Article 74 of Act No. 40/2007 on Limited Company Liability.

¹⁵Act No. 1/1995 on Limited Company Liability.

In Act No. 40/2007 of Limited Company Liability, only five clauses discuss about mandatory CSR. They include four (4) clauses in Article 74 and another clause in the definition section of the act. According to the researcher, the existence of Article 74 is already justified through the discussions in a formal legislation process in which the acts and regulations were produced. Further, the article has also been constitutionally reviewed by the submission of constitutional review by three business associations, which are KADIN, HIPMI and IWAPI. The legal provisions are also constitutionally binding all citizens to be implemented.

In fact, CSR has become a very familiar term to multinational corporations and governmental institutions such as the *Badan Pelaksana Hulu Migas (BPMIGAS)*, whose annual CSR fund reaches 2 trillion rupiahs. Few social responsibility activities have been implemented by some companies in Indonesia. The activities included (1) supporting uniforms to youth associations; (2) providing small fund aids for worship activities, charity for orphans; and (3) providing funds for natural disaster victims.¹⁶

Based on the above information, the present research is carried out for the following reasons: Indonesia has passed a mandatory CSR legal provision since 2007 through Act No. 40/2007 of the Limited Company Liability. Nearly five years after the enactment of the act, the government passed a specific government regulation which clearly specifies the mandatory legal provision.¹⁷

Further, three business associations have submitted judicial reviews regarding

¹⁶Government Regulation No. 93/2010 on Donation for National Disaster, Research and Development, Educational Facilities, Sports Empowerment, and Social Infrastructure Development Costs Deductible from Gross Revenue.

¹⁷Article 74 of Act No. 40/2007 on Limited Company Liability.

Article 74 because according to them, the legal provision will jeopardize their company's cashflow and competitiveness.

It is also evident that even though mandatory CSR legal provision has been enshrined within the Indonesian legal system, there is still no specific and clear guidance or standard to implement it. One existing standard or guideline on environmental management which is available is PROPER.¹⁸ The guideline was developed by the Ministry of Environmental Republic of Indonesia to measure the environmental performances of companies in Indonesia. While the appraisal programme does not launch to implement mandatory legal provisions, it serves to implement Article 22 Act No. 23/1997 on Environmental.¹⁹

According to the data of the ministry from 2002 to 2012, there were approximately 235 companies certified as green companies, 1,681 companies as blue companies, 754 companies as red companies and 264 companies black certified companies. During the same period, 7 companies were certified as gold companies. Companies which received red certification are given warning letters while black certified companies will be recommended to the relevant ministry for revocation of business licenses.²⁰ Accordingly, it is necessary to understand the punishment and reward systems that have been developed by the relevant governmental institutions in Indonesia in terms of implementing the mandatory CSR legal provision.

Nevertheless, private companies, either foreign or domestic, have not found clear guidelines and directives to execute their CSR programme in the community. Hence, it is necessary to have an ideal format of CSR programme

¹⁸Corporates Ranking Appraisal Programme on Environmental Management/Programme Penilaian Peringkat Kinerja Perusahaan dalam Pengelolaan Lingkungan Hidup (PROPER).

¹⁹The Act has been revised by Act No. 32/2009 on Environmental Management and Protection.

²⁰Article 22 until 27 Act No. 23/1997 on Environmental Management.

implementation in Indonesia. The ideal format is based on a clear regulation and guidelines that are applicable in various core businesses of corporations in Indonesia.

Various terms of CSR have been adopted by the stakeholders in sectoral CSR management, which tend to have their own regulations, mechanism, guidance or standard in implementing their CSR programmes as demonstrated by particular ministries. However, such decisions will lead to misconduct and fraud that can be a source of corruption. This necessitates a clear mechanism, standard or guidelines on mandatory CSR in Indonesia that involve local communities and NGOs as part of the stakeholders. The guidelines may guide toward better, more transparent and more accountable CSR implementations.

Currently, there are at least three ministerial boards that have been implementing CSR projects such as the Ministry of Environmental Republic of Indonesia, the Ministry of Social Republic of Indonesia and the Ministry of State Owned Company (BUMN). In fact, the situation lead to dividing CSR programmes into two main streams. The first is the programmes implemented by state-owned companies within the Ministry of State-Owned Company.²¹ The programme is called Partnership and Environmental Empowerment Programmes (*Programme Kemitraan dan Bina Lingkungan or PKBL*).²²

State-owned companies are required to allocate at least one to five percent of their net profits to empower co-operatives and the small enterprise sectors.

Second is the CSR programmes implemented by private companies.²³ Finally, it

²¹Ministry of State Owned-Company Decree Republic Indonesia, “Kep-216/M-PBUMN/1999 on Partnership and Environmental Programme/*Programme Kemitraan Bina Lingkungan (PKBL)*.”

²²Ministry of Finance Decree Republic of Indonesia No.316/KMK.016/1994 on Cooperatives and Small Enterprises Empowerment through Profit Fund of the State Owned-Company.

²³The implementation will refer to Article 74 of Act No. 40/2007 Limited Company Liability.

urgently needs to come up with a clear picture of mandatory CSR legal provision in Indonesia by describing in more detail the philosophical rationale of the enactment of mandatory legal provision in addition to providing mandatory CSR guidelines and the functions, jurisdictions and liabilities of the mandatory CSR surveillance body in Indonesia.

1.2 Problem Statement

Basically, this study has three gaps to be filled such as (1) the philosophical reasons of the mandatory CSR provision in Indonesia, (2) the clarity of specific guidelines of mandatory CSR legal provision, and (3) the functions, jurisdictions and liabilities of CSR surveillance body in Indonesia.

Recently, CSR has become a major issue in relation to social and environment responsiveness of companies in Indonesia. Since the enactment of the Act,²⁴ CSR has become mandatory rather than voluntary. Before the enactment, CSR was a voluntary responsibility of private and state-owned companies in Indonesia to the community. The enactment received negative reactions from the Indonesia Chamber of Commerce, industries and several other business associations such as the Indonesian Businessmen Association, the Indonesian Business Women Association and the Indonesian Young Businessmen Association.

Except for the Indonesian Businessmen Association, the other organizations have submitted a legal appeal to the Constitutional Court of Indonesia. The main content of their claim was their disagreements with the

²⁴Act No. 40/2007 on Limited Company Liability.

content of article 74 of the Act.²⁵ The rejection of the legal provision was based on the fact that the mandatory CSR provision is implemented only for companies which operate in the natural resources business sectors.

Further, mandatory CSR would increase the company's production cost and affect the competitiveness of Indonesian companies since they must increase their products' selling price. Furthermore the legal provision will decrease foreign investment to Indonesia. Hence, these companies have submitted a judicial review application to the Constitutional Court to revoke the article. Unfortunately, their judicial review were unsuccessful as the court did not fulfil their legal claims.²⁶ Further, Philosophical rationale for the enactment of mandatory CSR legal provision will be discussed further in this research.

CSR has been implemented voluntarily by state-owned companies and private companies for years. Unfortunately, the CSR programme they have been implementing were not significantly beneficial for the communities. Moreover, the Government of Indonesia or respective ministries have yet to produce any basic standard or guidelines on the implementation of mandatory CSR programme. This resulted in companies, implementing their own CSR programme based on their own discretions. In fact, institutionally, at least three different ministries are attempting to be the leading institution/ministry to implement the CSR programme in Indonesia.

It seems like the "competition" among those ministries has led to the management and operational of CSR programme based on the objectives of respective ministries for example, environmental component of the CSR will be

²⁵Ibid.

²⁶ Constitutional Court, Verdict Number 53/PUU-VI/2008 on Judicial Review Article 74 of Act No. 40/2007 on Limited Company Liability.

developed by the Ministry of Environmental; societal component of the CSR will be developed by the Ministry of Social and economic empowerment component will be developed by the Ministry of Domestic Affairs and the Ministry of Cooperatives, Small and Medium Enterprise. Additionally, the Ministry of BUMN will be responsible for developing CSR mechanism for all state-owned companies.

Further, the Ministry for state-owned companies is also adopting CSR programmemes based on Article 74 of Act No. 40/2007 on Limited Company Liability. The above facts give some evidence that the CSR implementation policy in Indonesia, which is based on sectoral institution, is based on management or it has been institutionally separated to at least three different ministries which have been formulating policies and implementation strategies based on their own ministry's objectives without close co-ordinating and communicating with other related ministries.

Besides the institutional problems mentioned above, another constraint is about unclear functions, jurisdictions and liabilities of the mandatory CSR surveillence body in Indonesia. As mentioned above there are at least three different ministries that have been initiating CSR projects, mobilizing CSR funds and implementing CSR projects in Indonesia. Each of the three ministries are also drafting and producing their own manuals on implementing the CSR projects within the objectives of their respective ministries. Furthermore, several different Act have mentioned about CSR such as Social Prosperity Act Number 11/2009, the Investment Act Number 25/2007; the Coal and Mineral Mining Act Number 4/2009, the State-Owned Enterprise Act Number 19/2003; the Micro, Small and Middle-Sized Enterprise Act Number 20/2008; the Environmental

Management and Protection Act Number 32/2009; and the Law of Governing Aceh Number 16/2006.

The overlapping policies provide obscurity and ambiguity to the situation especially to the functions, jurisdictions and liabilities of the mandatory CSR surveillance body. Sometimes, the contents of the acts are contradictory with each other. Hence the research will discuss further the functions, jurisdictions and liabilities of mandatory CSR surveillance body in Indonesia in order to find out the best surveillance body that suits the Indonesian context.

Moreover, the former minister of Environmental Republic of Indonesia, according to WALHI data less than 50 percent of the companies that are based on registered natural resources have implemented CSR programme especially CSR in environmental aspect. This objectively shows that voluntary CSR initiatives may not encourage companies to conduct CSR programme significantly. Therefore, a mandatory CSR is the solution to impose the companies to implement CSR programme as prescribed by the law and as to the interest of the society.

1.3 Research Questions

Based on the previous discussion, the present research has posed three research questions:

1. Why does CSR in Indonesia become mandatory?
2. What are the guidelines of mandatory CSR in Indonesia?
3. What are the functions, jurisdictions and liabilities of the mandatory CSR surveillance body in Indonesia?

1.4 Research Objectives

The main aim of this study is to come up with an alternative model of implementing CSR. Prior to implementation, of the alternative model should be enhanced by policies, guidelines or a manual in advance. Further, the alternative model has been judicially reviewed to the Constitutional Court of Republic of Indonesia. Afterwards, there was a Constitutional Court Verdict No. 53/PUU-VI/2008 on Article 74 of Act No.40/2007 on Limited Company Liability.

Hence, the provision has been called “Mandatory CSR Legal Provision”, which carries specific objectives: (1) to speed up the implementation of the CSR programmes of companies whose businesses are in the natural resources sector, (2) to strengthen the economy of local people as beneficiaries, (2) to strengthen the partnership and relationship between the companies and local people, and (2) to ensure that the model is compatible with the current global campaign on preventing and conserving the environment from destruction. The research is also intended to provide the chance to enhance the legal provision by studying the CSR policies, rules and regulations within Indonesian legal context.

The study focuses on the major reasons behind the changing policy of CSR from being voluntary to mandatory. Further, the thesis will also study the characteristics of the surveillance body of mandatory CSR in Indonesia. Finally, the specific objectives of the study are as follows:

1. To examine the philosophical rationale behind the mandatory CSR legal provision in Indonesia.
2. To examine the guidelines of mandatory CSR in Indonesia.
3. To analyse the functions, jurisdictions and liabilities of the surveillance body of mandatory CSR in Indonesia.

4. To suggest an alternative model of law on the mandatory CSR in Indonesia.

1.5 Significance of the Study

The study is highly significant for the development of CSR policy reform in Indonesia. It also helps to clarify the current policy of CSR in Indonesia. Hundreds and even thousands of business institutions and stakeholders of CSR programme in Indonesia are now waiting for the effectiveness of the government's regulations on CSR. The CSR programme may reduce poverty and provide greater job opportunities. It was proven by the implementation of voluntary CSR that CSR contributed to the poverty alleviation and to the creation of more employment opportunities. Hopefully by upgrading a voluntary action to a mandatory one will render positive impact for the society. This study is helpful in term of improving the CSR laws and regulations in Indonesia.

The research contributes significantly to the body of knowledge particularly in the field of mandatory CSR policy. It enriches the literature on CSR particularly in the field of mandatory CSR in the sense that mandatory CSR is a relatively new term and very few countries are implementing it. Recently, CSR is becoming a cross-cutting issue which has significant impact on economic empowerment, environmental protection, societal relationship, the financial reports of business institutions and the performance of good corporate governance.

In addition, the research will also benefit CSR stakeholders in the public and private sectors such as government officials, universities focusing on CSR studies, legal practitioners, CSR consultants and practitioners, and corporate employees in CSR section. These stakeholders will have an understanding of the

mandatory CSR provision, legal sanctions to be taken for disobedience companies, and the characteristic of the CSR surveillance body in Indonesia. Moreover, the results of this study may be used as the basis of establishing an effective mechanism of CSR the surveillance body in Indonesia. Finally, the findings can also be an entry point to initiate the necessary legal drafting of other rules and regulations on CSR in Indonesia.

1.6 Limitation of the Study

This study is intended to explore the philosophical reasoning behind the mandatory CSR provision in Indonesia, the clear guidelines of the mandatory CSR in Indonesia and the functions, jurisdictions and liabilities of the surveillance body of mandatory CSR in Indonesia. The scope of the research is limited to studying, defining, and analysing several relevant Indonesian acts on the CSR laws and regulations.

The research also has a few limitations as the mandatory corporate social responsibility is a very sensitive issue in Indonesia particularly for corporations. This is due to the term “mandatory”, which is still unfamiliar to CSR experts such as academics, practitioners, non governmental organizations and corporations. Moreover, current CSR practitioners and government officials within particular ministries and agencies are still reluctant to use the term “mandatory” for CSR as they are used to the term “voluntary”.

There may be major constraints in getting the information, thoughts and feedbacks regarding the past, current and future corporate social responsibility programme within the corporations. There are still very limited academic references, books, thesis and dissertations on mandatory CSR. Another

constraint is in finding academic literatures on mandatory CSR in Indonesia or other countries. Yet few existing academic literatures can be the most relevant resources in aiding the researcher to meet the research objectives.

Another constraint is the difficulty to interview prominent CSR experts in corporations, particular those in nongovernmental organizations which are concerned with CSR advocacy and particular ministries and state agencies who are currently dealing with CSR policies and project implementation. Most of these subjects probably disagree with mandatory CSR legal provision and this may also due to their refusal to accept the mandatory CSR policy itself.

Personal and formal communication is going to be applied to overcome the reluctance and refusal of the subjects to be interviewed. Furthermore, if the situation persists, then the researcher will choose another expert from the list of the interviewees. Regarding the lack of academic references on mandatory CSR, it will be overcome by choosing academic references such as articles, books, thesis or dissertations that are the most relevant to the objectives of the research. This is also the major reason for using pure normative legal research in order to allow the researcher to use acts, statutes, laws and regulations as the main source of data.

CHAPTER TWO LITERATURE REVIEW

2.1 Introduction

This section systematically presents the research objectives, challenges and opportunities based on the most relevant available literatures. These literatures have significantly helped to position the current situation on mandatory CSR policies in Indonesia. Literature review is the most important part of the research because the process analyses the research objectives by using primary and secondary data. Therefore, primary data such as journal articles, books, statutes, laws and regulations will be used as sources of references. All of the references have facilitated the reviewing of the research objectives which may also fruitful in defining and finding out answers for the research questions.

2.2 Theory and Philosophy of Mandatory Corporate Social Responsibility

Indonesia is a a unitary state whereby the authority of lawmaking is under the jurisdiction of the People's Representative Council or *Dewan Perwakilan Rakyat* (DPR).²⁷ In practice, the government has been initiating more statutes to be jointly discussed with the DPR, although the DPR also has the right to initiate drafting an Act based on its concern. Indonesia has been divided into provinces which consisted of municipalities and regencies government.²⁸ Each of them has its own authorities based on the principles of autonomy and the duty of assistance from the central government.²⁹

²⁷Article 20 of the 1945 Constitution of Republic of Indonesia "DPR shall hold the authority to establish laws".

²⁸Article 18 of the 1945 Constitution of Republic of Indonesia.

²⁹Ibid

Further, each province, regency and municipality has its own People's House of Representatives (DPRD). Even though the local governments have their own authorities to manage their own affairs, they still have to follow the policies and guidelines were made by the Ministry of Home Affairs. For this reason, the autonomy concept in Indonesia has not fully provided full authority to the local governments. Other special autonomous areas such as Aceh, Jogjakarta and Papua within the Unitary State of Indonesia have to follow the policies made by the central government.

The policies from the central government must be respected by the local government (provinces, regencies or municipalities), which must be abided based on the guidelines provided by the respective ministries. Therefore, when the national policy on mandatory CSR has been passed by the central government through Act No.40/2007 on Limited Company Liability, the local governments are required to abide by passing the local regulations to each level of authority.

Act No.40/2007 itself is an Act that concerns the procedures and mechanism to establish a limited company and some other relevant arrangements such as board of directors, board of commissioners, shareholders composition, annual reports and the governance of enrolling a limited company. The members of DPR have only recently inserted a specific article on mandatory CSR within the act. That is why the legal provision become legally binding for all companies who is operating their businesses in the sectors of natural resources. The position of Act No.40/2007 is a *lex specialis* or become more specific to be implemented for companies who are operating their businesses in such sector.

In the beginning, prior to the enactment of the mandatory CSR legal provision, there was a same legal provision that has been inserted in advance to Act No.25/2007

on Investment. The legal provision in the Act is for companies to oblige without any limitation in implementing the mandatory CSR within their business activities. Further, when the DPR approved the specific, mandatory legal provision for companies who are operating in the natural resources sector, several companies and three other major business associations had rejected the legal provision.

During the trial session within the constitutional court, the businesses associations and representatives of companies who rejected the mandatory CSR legal provision argued that the legal provision was drafted without academic studies as required by Act No. 10/2004 on Regulatory Drafting. In fact, the drafting has generated inconsistency, overlaps and legal uncertainty, and vagueness which have discriminated them, particularly the provision because has been implemented only in businesses in the natural resources' sector and it is clearly against the spirit of the constitution.³⁰ Further, the government representative replied that the legal provision has not discriminated those companies because it is not against the definition of discrimination as prescribed by Article 1 (3) Act No.39/1999 on Human Rights and Article 2 International Covenant on Civil and Political Rights.³¹

Further, the government representative explained that the concept of Environmental and Social Responsibility/*Tanggung Jawab Sosial dan Lingkungan* (TJSL) has been regulated on Article 74 is distinct from the concept of CSR in general.³² CSR in general is the commitment of business enterprises to be more socially and environmentally responsive to their social and environmental

³⁰Constitutional Court Verdict No.53/PUU-VI/2008 on Judicial Review of Article 74 of Act No.40/2007, p. 33.

³¹Constitutional Court Verdict No.53/PUU-VI/2008 on Judicial Review of Article 74 of Act No.40/2007, p. 58.

³²Constitutional Court Verdict No.53/PUU-VI/2008 on Judicial Review of Article 74 of Act No.40/2007, p. 55.

circumstances surrounding their business operations. Afterwards, the commitment is part of the Rio De Janeiro Agreement of 1992 regarding sustainable development.³³

The concept of TJSL is part of the implementation strategy of Article 33 (4) of the 1945 Constitution of the Republic of Indonesia.³⁴ Then, the constitution mandated the government to implement it by an Act.³⁵ Afterwards, the panel of judges within the Constitutional Court considered that there is a strong relationship between social interest, business interest and legal obligation. Companies must follow all the existing rules because the rules are the legal policies of a certain state.³⁶

The TJSL legal provision is the policy of the state for which the government, business enterprises and society will cooperate each to implement it without attempting to seek loopholes to avoid it. Article 74 is not only to be respected, but also to be co-operated among stakeholders for its implementation.³⁷ Further, Article 74 directly affects the health and the level of safety for the society who live around business operations; therefore, the act needs moral obedience from the stakeholders in order to be implemented well.³⁸

Afterwards, the judges considered that the environmental destruction in Indonesia has reached the level of endangering the lives of human beings either of the present or future generation. Therefore, the responsibility to protect and to

³³Ibid

³⁴Article 33 (4) of the 1945 Constitution of the Republic of Indonesia “The organization of the national economy shall be conducted in the basis of economic democracy upholding the principles of togetherness, efficiency with justice, continuity, environmental perspective, self-sufficiency, and keeping a balance in the progress and unity of the national economy.”

³⁵Article 33 (5) of the 1945 Constitution of the Republic of Indonesia “Further provisions relating to the implementation of this article shall be regulated by law.”

³⁶Constitutional Court Verdict No.53/PUU-VI/2008 on Judicial Review of Article 74 of Act No.40/2007, p. 89.

³⁷Ibid

³⁸Constitutional Court Verdict No.53/PUU-VI/2008 on Judicial Review of Article 74 of Act No.40/2007, p. 90.

conserve is in the hands not only of the state's society's but also of the investors'.³⁹ Companies should be aware that the sustainability of their businesses strongly depends on the support of local society and environment in which they operate. It seems there is a social contract between the companies and the local society to cooperate in creating harmony and benefiting one another.⁴⁰

Based on those facts and evidences above, the panel of judges panel decided that Article 74 of Act No.40/2007 on Limited Company Liability is not against the spirit of the 1945 constitution of the Republic of Indonesia. The implementation of voluntary CSR in the UK, Canada, France, Germany, Australia and the United States cannot be equated to the implementation of TJSL policy as prescribed in Article 74 of Act No.40/2007 on Limited Company Liability.⁴¹ This is because of the CSR principle applies to different culture and place.

Further, the phrase "mandatory" is often interpreted as the legal obligation under a particular law in a particular country. Therefore, "corporate social responsibility" means that as a core business matter, a certain company in a particular country should be socially responsible. Further, managers of corporation are not only working for their shareholders but also responsible for a broader constituents including customers, suppliers, employees and the community.⁴²

According to Black's Law Dictionary, "mandatory" is "relating to, or constituting a command, required, pre-emptory". Hence, mandatory CSR is derived from a theory of corporation's responsibility due to its negative impacts of their

³⁹Ibid

⁴⁰Constitutional Court Verdict No.53/PUU-VI/2008 on Judicial Review of Article 74 of Act No.40/2007, p. 91.

⁴¹Constitutional Court Verdict No.53/PUU-VI/2008 on Judicial Review of Article 74 of Act No.40/2007, p. 92.

⁴² Adolf A. Berle and Gardiner C. Means, *"The Modern Corporation and Private Property,"* [New Jersey, Transaction Publishers, 1968] xv.

businesses.⁴³ There are a lot of cases involving multinational companies violating human rights principles as well as unaware with their local environment. Organization for Economic Development and Cooperation (OECD) has standard rules and regulation concerning multinational companies to behave in their business operations. Despite of some international standards on CSR have been released by some international agencies, there should be a national policy in each country to make it real in the field. The national policy is not only cover rules on specific issues in term of its implementation mechanism but also stakeholders engagement, tax reductions policy, monitoring and evaluation procedures.

The rules and code of conducts have been established by OECD just a voluntary instruments, so that, it has been interpreted by the companies in particular country in a very different way between one and another. Therefore, it has no a binding legal power to force the companies to implement it. It depends on the degree of the company's awareness. There are a lot of examples where corporations do not care of social and environmental circumstances surrounding them.⁴⁴ This research is intended to describe the importance of mandatory corporate social responsibility in a such of that circumstances.

As a good example and also a lesson learnt, during Sierra Leone civil war, many armed groups and big diamond corporations involved in illegal diamonds trading.⁴⁵ They have done their business without take care of responsibility to the social and environment circumstances around them. Instead, the armed rebellion movement made it as their source of fund to fuel their rebellion movement in Sierra

⁴³Steven R. Ratner, "Corporations and Human Rights: A Theory of Legal Responsibility,"[Yale, Yale Law Journal Vol. 111, November 2001], 443.

⁴⁴Loc. Cit, Steven R. Ratner, "Corporations and Human Rights: A Theory of Legal Responsibility,"[Yale, Yale Law Journal Vol. 111, 2001], 443.

⁴⁵Ibid

Leone.⁴⁶ That kind of situation is really hurt the sense of social justice of the local people in the war area. It is a good reason to encourage all stakeholders involve in the business operation to implement the highest standard of ethics. Even in the war area, people are banned to take profits with illegal way by avoiding rules, regulations and local wisdoms. Therefore, in the peace and calm area all stakeholders must also implement the most accountable and credible rules and principles. One of the ways to make it work is by implementing mandatory CSR framework.

Different areas and ages need different policy to be applied.⁴⁷ Each area has its own characteristic and the survival and successful in particular area can not apply the same in other areas. It is not just simply like the successful in the Gobi desert as on the North Pole.⁴⁸ There is also numerous community that believes if multinational corporations are socially irresponsible.⁴⁹ Therefore, many social critics have noted the failure of corporations to behave socially responsible.⁵⁰ A few have taken the next important step how to collaborate the society, company and state to go together to achieve a better corporate social responsibility implementation.

If it is only a few have taken CSR into their accounts as a way to engage with local communities and to be socially responsible then the government should take a necessary and more binding policy to force them to implement it such as mandatory CSR policy. The government has the right to impose the corporations to behave in

⁴⁶Ibid

⁴⁷Elmar Bouma, "Interview with Rio Praaning Prawira Adiningrat (PA CSR) About Corporate Social Responsibility," [Jakarta, INA Magazine 19, No. 3, 2007], 15.

⁴⁸Ibid

⁴⁹Vanessa M. Strike, Jijun Gao, and Pratima Bansal, "Being Good While Being Bad: Social Responsibility and the International Diversification of US Firms," [United Kingdom, Journal of International Business Studies 37, No. 6, 2006], 857.

⁵⁰H. Gordon Fitch, "Achieving Corporate Social Responsibility," [New York, The Academy of Management Review 1, No. 1, 1976], 38.

the interest of the society, to prohibit, to mandate or even to encourage positive behavior by enacting binding regulations.⁵¹

Indonesia is the first country in the world to have enshrined corporate social responsibility policy as a mandatory provision. It makes Indonesia the most concern country to tackle environmental damages, forestation, and land degradation. As the most leading country in mandatory CSR policy, Indonesia is attempting to create and develop a framework to implement the regulation in the field. Two other countries, Nigeria and India, are following Indonesia in formalizing CSR onto their codes. Indonesia made it legally as an obligation for natural resources-based companies to impose corporation in implementing CSR programme within their business areas.

The concept of “*responsibility*” is referring to a legal obligation under the legal terminology.⁵² It becomes mandatory because of its negative environmental impacts caused the suffering to the human being and also other creatures within the ecosystem. There was a strong commitment of the government of Indonesia to conduct and protect environment, preserve the natural resources sustainability and ensure clean development mechanism principles are well-implemented. The application of mandatory CSR policy will encourage extractive industries to be socially responsible. The enactment of that kind of policy must be appreciated as a quantum leap in preventing gross-environmental human rights violations in the area where the extractive industries are operating. The policy will be implemented by a very tight guidance, monitoring and evaluation mechanism.

⁵¹ Aneel Karnani, “*Doing Well by Doing Good; The Grand Illusion,*” [California, University of California Press, California Management Review, Vol. 53. No. 2, 2011], 12.

⁵²*Op.Cit,* Act Number 40/2007 on Limited Company Liability.

There is a meaningful quotation which is “*Great power comes with great responsibility.*”⁵³ It means that the big corporations with big capital and resources should also have big social responsibility. The rise of corporate social responsibility issue was initially started in the early of 1990.⁵⁴ It was the most tangible result of longstanding discussion over the relationship how to synergize and to integrate between business and society.⁵⁵

Further, any person who obtains fortune from the God in term of wealth, scholarly and physical strength are the selected creatures of God. As selected creature from the God then they were obliged to perform more social responsibility than others in order to disseminate benefits for other who does not obtain it. Hence, the absence of specific legislation on environmental protection should not excuse the companies for polluting the environment as whole.⁵⁶

Philosophically legal positivism is a dominant interpretation to the nature of law.⁵⁷ Legal positivism is translated on the development of laws and regulations by making it through a formal law making process in accordance with constitution in a certain country. By contrast, legal positivism was also criticised as it is not able to answer the important questions of law, the objectivity of morality and the role of judges in society.⁵⁸ Consequently, the philosophy would create some legal norms that people will follow it.

⁵³ Ben Parker, Peter Parker’s Uncle in Spiderman’s Movie.

⁵⁴David Henderson, “*Misguided Virtue False Notions of Corporate Social Responsibility*,” [Wellington, New Zealand Business Roundtable, 2001], 1.

⁵⁵ Rhys Jenkins, *Globalization, Corporate Social Responsibility and Poverty*. [Royal Institute of International Affairs No. 3, 2005], 525.

⁵⁶*Op. Cit*, David Henderson, “*Misguided Virtue False Notions of Corporate Social Responsibility*,” [Wellington, New Zealand Business Roundtable, 2001], 3.

⁵⁷ Martin P. Golding and William A. Edmundson, *The Blackwell Guide to The Philosophy of Law and Legal Theory*, [Australia, Blackwell Publishing, 2006], 29.

⁵⁸ Martin P. Golding and William A. Edmundson, *The Blackwell Guide to The Philosophy of Law and Legal Theory*, [Australia, Blackwell Publishing, 2006], 32.

The norms guide the people's conduct on daily social interaction.⁵⁹ Norms and law have a very strong impact on each other.⁶⁰ Further, a vigorous moral ethical codes of a certain society are a strong foundation of social stability which encourages a vibrant economic lives.⁶¹ Strong norms encourage people to comply with the law even it is against their own self interests.⁶²

Thereafter, everyone is under *prima-facie* moral duty to abide by laws within his or her society.⁶³ The obligation-to-obey-the-law is absolute and the existence of the laws is essential for the viability of a civilized way of life in any society.⁶⁴ Legal provision that have been agreed and passed implicitly or explicitly impose people to act which the legal provisions require.⁶⁵ Moreover, the legal provisions themselves are independent and of anyone's interest. In some cases, it sometimes against the interest the interest of certain groups or persons. In fact, even though the legal provisions against their interest, indeed there is a moral obligation for them to comply with the law's requirement.⁶⁶

In the philosophy of criminal law, the law should seek a way to prevent or reduce by means of criminal sanctions.⁶⁷ Further, it is logic if the law-breakers should be punished and they were morally blameworthy by the people.⁶⁸ In the theory of responsibility, there are four (4) classification of responsibility as the following; role-responsibility, causal-responsibility, liability-responsibility and

⁵⁹ John N. Drobak, *Norms and The Law*, [Cambridge, Cambridge University Press, 2006], 1.

⁶⁰ Ibid

⁶¹ Ibid

⁶² Ibid

⁶³ Martin P. Golding and William A. Edmundson, *The Blackwell Guide to The Philosophy of Law and Legal Theory*, [Australia, Blackwell Publishing, 2006], 180.

⁶⁴ Martin P. Golding and William A. Edmundson, *The Blackwell Guide to The Philosophy of Law and Legal Theory*, [Australia, Blackwell Publishing, 2006], 181.

⁶⁵ Martin P. Golding and William A. Edmundson, *The Blackwell Guide to The Philosophy of Law and Legal Theory*, [Australia, Blackwell Publishing, 2006], 182.

⁶⁶ Ibid

⁶⁷ Martin P. Golding and William A. Edmundson, *The Blackwell Guide to The Philosophy of Law and Legal Theory*, [Australia, Blackwell Publishing, 2006], 221.

⁶⁸ Ibid

capacity-responsibility.⁶⁹ The most concerned one is liability-responsibility, which is divided into moral liability responsibility and legal liability-responsibility. Further, moral liability-responsibility is a situation whereby someone or any party is blame worthied or morally obliged to make amends for the harm.⁷⁰

Whereas, legal liability responsibility is situation in which someone of any party should responsible to any harm that was regulated by criminal sanctions.⁷¹ In practice, even though the moral view and the law are linked between one and another but in fact it is not suppose to have a perfect coincidence between the law and moral views because the law has its own methods and it is not merely indetical to the moral views in everyday moral discourse.⁷² It is widely known that in the legal tradition there is an old proverb: *actus non facit reum nisi mens sit rea* or an act is not wrongful unless the mind is wrongful.⁷³ It says that any laws or regulations that have been passed through a formal legal process is never obnoxious unless the mind of the people are wrongful.⁷⁴

From an evolutionary perspective, a rapid industrialization in the late of nineteenth century has changed the way of life and the way of thinking of many people from traditional paradigm into modernity paradigm.⁷⁵ The changes have also affected the law as the tool of social engineering. People are not only trust to moral

⁶⁹Ibid.

⁷⁰*Loc. Cit*, Martin P. Golding and William A. Edmundson, *The Blackwell Guide to The Philosophy of Law and Legal Theory*, [Australia, Blackwell Publishing, 2006], 221.

⁷¹Ibid

⁷²Ibid

⁷³ Martin P. Golding and William A. Edmundson, *The Blackwell Guide to The Philosophy of Law and Legal Theory*, [Australia, Blackwell Publishing, 2006], 222.

⁷⁴Ibid

⁷⁵ John R. Sutton, *Law and Society: Origins, Interactions and Change*, [California, Pine Forge Press, 2001], 25.

commitment in making a contract or agreement but also needs a legal certainty by doing contract or agreement in writing document.⁷⁶

Further, law is a very important ornament for any individual within any society because the law affect the people on how they behave and do not behave.⁷⁷ Afterwards, the law has some following social functions such as law as social control which is the law helps the government and the society to mantain social order because without law the situation would be much for chaotic.⁷⁸ Further, the law is also functioning as dispute settlement and conflict resolution.⁷⁹ It helps any conflicting parties to resolve their disputes through an independent, objective and non-bias mechanism. Thereafter, the law is also functioning as as social change.⁸⁰ The law may affect social behavior of particular society by enacting a specific law to the society. Some of the examples are gay marriages or the use of cell phone and internet.⁸¹

By contrast, the law may also create a dysfunction of the society because of its over-regulation and rigidity so that the people and organizations may not accomplish their goals due to inefficient procedures.⁸² Nortwithstanding, the purpose of the law itself is to create harmony among different societies, colors, social status and religions. Therefore, the law requires an appreciation of its positive contribution to the society as of idealized conception of it.⁸³

Consequences, there 3 (three) theoretical theories is going to be used for the research. Those theories are as the following;

⁷⁶Ibid

⁷⁷ Steven E. Barkan, *Law and Society An Introduction*, [New Jersey, Pearson Prentice Hall, 2008], 4.

⁷⁸Ibid

⁷⁹ Steven E. Barkan, *Law and Society An Introduction*, [New Jersey, Pearson Prentice Hall, 2008], 5.

⁸⁰Ibid

⁸¹Ibid

⁸² Steven E. Barkan, *Law and Society An Introduction*, [New Jersey, Pearson Prentice Hall, 2008], 6.

⁸³Ibid

1. Legal System Theory

Legal theory comprises of two important elements which are philosophy and political theory.⁸⁴ In some legal theories, it contains political theory but all legal theories should have philosophy elements.⁸⁵ One of the main problems of law that is still remaining until today is about the divergence between justice and positive law itself. Justice is basically derived from custom and tradition and it is merely identical with order and authority.⁸⁶ Unlike the source of the law, in the early age of ancient Greek, the King has received an authority to govern the society from Zeus. The divine power was given to the King for establishing law and order. Hence, the situation makes the King has full power to establish the law and mostly it is against the sense of social justice of the citizen.⁸⁷

Subsequently, there are 3 (three) key elements on the concept of law which are coercive character, social acceptance and generality.⁸⁸ Coercive character is based on the source of authority and enforceability by sanctions.⁸⁹ The successfulness of enforceability consists of legal substance, legal structure and legal culture. The three (3) elements are interplay between one and another.

Further, social acceptance is an actual observance from the society based on “living law” of communities.⁹⁰ In addition, generality is also an important

⁸⁴ William Friedmann, *Legal Theory*, [New Delhi, Universal Law Publishing, Fifth Edition, 2008], 3.

⁸⁵ *Ibid*

⁸⁶ *Op. Cit*, William Friedmann, *Legal Theory*, [New Delhi, Universal Law Publishing, Fifth Edition, 2008], 6.

⁸⁷ *Ibid*

⁸⁸ *Op. Cit*, William Friedmann, *Legal Theory*, [New Delhi, Universal Law Publishing, Fifth Edition, 2008], 14.

⁸⁹ *Ibid*

⁹⁰ *Op. Cit*, William Friedmann, *Legal Theory*, [New Delhi, Universal Law Publishing, Fifth Edition, 2008], 15.

element whereby the legal norms that passed by legislative and executive is the result of a constant interplay among them.⁹¹

Hence, legal substance covers about laws and regulations that have been made by formal institutions within a specific legal system. It covers not just limited to “*living laws*” but also law in the books. Indonesia has applied a formal and positivist paradigm of law which is there is no law if it is not written on the Act.⁹² Moreover, the legality principle on the criminal code of Indonesia has clearly mentioned that “*there is no crimes can be punished if there is no the provision prior to the crime is committed*”.⁹³

Afterwards, legal structure comprises of legal institutions that will implement the provisions such as police department, court, prosecutor and prison system. The legal enforcement institutions interplay between one and another.⁹⁴ Those legal institutions must be independent and can not be interfered by other powers. Further, they should also be given a clear authority and full power to conduct their mandate to enforce the law. Institutionalization of legal structure is more developed in ad advanced and complex society than in a primitive society.⁹⁵

Futhermore, legal culture is also an important element to establish a good law and order in a modern society. Legal culture is a sense of attitude of particular member of society to a specific laws and regulations.⁹⁶ Further, legal culture is a process of social reflection of attitude from particular society on how the law is used, avoided or misused.⁹⁷

⁹¹Ibid

⁹²Ibid

⁹³Ibid

⁹⁴Ibid

⁹⁵*Op. Cit*, William Friedmann, *Legal Theory*, [New Delhi, Universal Law Publishing, Fifth Edition, 2008], 16.

⁹⁶Ibid

⁹⁷Ibid

The enforceability of specific provision is not merely depends on the legal system such as legal substance, legal structure and legal culture but also depends on fundamental of law such as legislation process, court and enforcement mechanism.⁹⁸ The law is obviously interlinked with politics, economics, social life and ethics.⁹⁹ Those elements are steadily influencing the implementation of the law in a particular society and legal system.¹⁰⁰

In the positivist society, there 3 (three) key elements that are influencing interchangeably the laws which are stability, formalism and effect.¹⁰¹ Stability is a vital component for enforcing the law and order in a certain society because without stability of conditions, then the legal provision can not be upheld. Further, formalism is a way for the law to be enforced. It is a kind of strategy to put a corcieve power to the society to be respect for the law.¹⁰² At last, effect of the law comes from the willingness of the society to change the situation from disorder into secure one.¹⁰³ Indeed, it is a universal desire of human beings to have a better circumstance by ordering a new law for a specific issue.

2. Stakeholder Theory

Corporations put stakeholders as the most important part of its long-term business strategy.¹⁰⁴ Stakeholder's apparoach is more taken into account by the corporations than government regulations.¹⁰⁵ It because of the corporations are

⁹⁸ Satjipto Raharjo, *Hukum Progresif*, [Jakarta, Rajawali Press, 2006], 8.

⁹⁹ *Op. Cit*, William Friedmann, *Legal Theory*, [New Delhi, Universal Law Publishing, Fifth Edition, 2008], 70.

¹⁰⁰ *Ibid*

¹⁰¹ *Ibid*

¹⁰² *Ibid*

¹⁰³ *Ibid*

¹⁰⁴ Kristel Buysse and Alain Verbeke, *Proactive Environmental Strategies: A Stakeholder Management Perspective*, [Chicago, Strategic Management Journal, Vol. 24, No.5, May, 2003], 453.

¹⁰⁵ *Ibid*

willing to have the best reputation from the standpoint of their stakeholders.¹⁰⁶

Stakeholders perspective encourage the companies to conduct business practices in which meeting the needs and satisfaction of multiple stakeholder groups.¹⁰⁷

Thereafter, stakeholder approach is to encourage the management of the companies to do the right thing for the interest of the society and for the long-term profitability achievement of the companies.¹⁰⁸ Further, the stakeholder approach requires that the entire process of companies for seeking profits are not merely consider the interest of shareholders but also should should benefits the stakeholders.¹⁰⁹

The corporation survival depends on their strategies to fullfill the needs and interests of their primary stakeholders.¹¹⁰ It demonstrates that stakeholder has a very strategic position to ensure the sustainability of particular company. The companies need to consider the interest of their stakeholders, especially who most affected by their operational business practices.¹¹¹

The only intention of the stakeholder theory development is to build social responsiveness of the managers to the society in which the corporation are operating.¹¹² For an example, the inclusion between environmental regulations

¹⁰⁶ Ibid

¹⁰⁷ Manuel Castelo Blanco and Lucia Lima Rodrigues, "Positioning Stakeholder Theory within the Debate on Corporate Social Responsibility," [Journal of Business Ethics and Organization Studies, Vol. 12, No. 1, 2007], 11.

¹⁰⁸ Kamel Mellahi and Geoffrey Wood, The Role and Potential of Stakeholders in "Hollow Participation": Conventional Stakeholder Theory and Institutional Alternatives, [Business and Society Review, 2003], 183.

¹⁰⁹ Joseph T. Mahoney, *Toward a Stakeholder Theory of Strategic Management*, [University of Illinois Publishing, 2007], 9.

¹¹⁰ I.M. Jawaharar and Gary L. Mclaughlin, *Toward The Descriptive Stakeholder Theory: An Organizational Life Cycle Approach*, [New York, Academy of Management Review, Vol. 26, No.3, July 2001], 397.

¹¹¹ *Op. Cit*, Kamel Mellahi and Geoffrey Wood, The Role and Potential of Stakeholders in "Hollow Participation": Conventional Stakeholder Theory and Institutional Alternatives, [New York, Business and Society Review, 2003], 184.

¹¹² R. Edward Freeman and John McVea, *A Stakeholder Approach to Strategic Management*, [Virginia, Darden Graduate School of Business Administration Publishing, 2001], 3.

and companies' strategic plan is a strategy to meet the legal requirement in a particular country.¹¹³ Moreover, for some global companies, the inclusion is part of their strategies to improve their companies' alignment to existing regulation and to meet the expectation of their stakeholders.¹¹⁴

It demonstrates that stakeholder's expectation is ideally expect that the corporations conduct business practices that socially responsible and environmental friendly. The stakeholder's expectation is similar to social control that a particular society should have because social control is essential for any society.¹¹⁵ In a traditional society, norm violations commonly occur and it is not a great problem.¹¹⁶ It happens due to lack of socialization and no available of strong handling disputes mechanism. Further, in a modern society, even more disputes than it is found in a traditional society but the legal system in the modern society provides a strong and clear handling disputes mechanism.¹¹⁷

In a modern society, legal rules were enacted by legislatures and courts are provided to serve the citizen on legal disputes, but at the same time the law enforcement officer enacted their behaviours that in some circumstances and cases may differ with the legal rules itself.¹¹⁸ Therefore, there are two major factors interplay in the situation that people respect and obey social norms and legal rules.¹¹⁹

¹¹³*Loc. Cit*, Kristel Buysse and Alain Verbeke, *Proactive Environmental Strategies: A Stakeholder Management Perspective*, [Chicago, Strategic Management Journal, Vol. 24, No.5, May, 2003], 453.

¹¹⁴*Ibid*

¹¹⁵*Op. Cit*, Steven E. Barkan, *Law and Society An Introduction*, [New Jersey, Pearson Prentice Hall, 2008], 135.

¹¹⁶*Ibid*

¹¹⁷*Ibid*

¹¹⁸*Op. Cit*, John R. Sutton, *Law and Society: Origins, Interactions and Change*, [California, Pine Forge Press, 2001], 135.

¹¹⁹*Loc. Cit*, Steven E. Barkan, *Law and Society An Introduction*, [New Jersey, Pearson Prentice Hall, 2008], 135.

The two major factors are socialization and social bonding. In a certain society that has already have good socialization and strong social bonding they obey the norms and legal rules not because they are afraid of punishment if they disobey, but because they feel that those things ought to be obeyed.¹²⁰

3. Enterprise Entity Theory

Enterprise is considered as an artificial person who entitles to perform any activities as required by the law.¹²¹ Therefore, an enterprise should behave socially and environmentally responsible in performing its business activities. Even though, there are some differences between the real person and artificial person but both of them are eligible to act on legal disputes or to sign agreements. Further, the real person basically has sense of morality and sense of social responsiveness. Unlike enterprise, they do not have any feelings on adopting the sense of morality and sense of social responsiveness, but as long as they are perceived as artificial persons. Then, they should have also social responsiveness and morality as the real person owned.¹²²

“*The artificial personality*” was developed to enable the enterprise entity to carry on its duty and responsibility in a business process.¹²³ Hence, the artificial personality was designed to own as much as possible the real person’s personality. Then, it may help the corporation to conduct its business activities.

¹²⁰Ibid

¹²¹ Adolf A. Berle Jr, *The Theory of Enterprise Entity*, [Columbia, Columbia Law Review, Vol, 47 No. 3, April 1947], 343.

¹²² Peter A. French, *The Corporation as A Moral Person*, [New York, American Philosophical Quarterly, Vol.12, No.3, July 1979], 208.

¹²³ *Op. Cit*, Adolf A. Berle Jr, *The Theory of Enterprise Entity*, [Columbia, Columbia Law Review, Vol, 47 No. 3, April 1947], 344.

Subsequently, the concept of corporate legal personhood is derived from an idea that they would have some essential characteristics that biological human beings have.¹²⁴ The characteristics are as the following moral responsibility, social responsiveness and moral obligation to its surround environment.¹²⁵

Even though, the corporation is perceived as a legal personhood, indeed it has restricted capacity to do something rather than a natural person can make. As an artificial personality, the corporations are restricted by the law in performing its rights and liabilities.¹²⁶ It looks that the corporation can not make all things that natural person can do. Hence, the scopes and limits of enterprise entity are as the following; corporation is an artificial person that has limitation on liabilities, legal actions and other things that human beings can do.¹²⁷

The current confusion and long debates of CSR is not so much on how CSR is defined but mostly how CSR is socially constructed and implemented in a specific context with a specific characteristic.¹²⁸ The critics of corporate social responsibility which being undertaken by local communities and NGOs are in no doubt of its fundamental opposition to the profit motive.¹²⁹

Currently, CSR scope it not only purely aspects of corporate conduct such as accounting, marketing and public relations but also the role of business in relation to poverty alleviation in developing world, engaging with local communities to create

¹²⁴ *Loc. Cit*, Peter A. French, *The Corporation as A Moral Person*, [New York, American Philosophical Quarterly, Vol.12, No.3, July 1979], 208.

¹²⁵ *Ibid*

¹²⁶ Murray A. Pickering, *The Company as A Separate Legal Entity*, [The Modern Law Review, Vol 31, No.5, September 1968], 484.

¹²⁷ George F. Canfield, *The Scopes and Limits of The Corporate Entity Theory*, [Columbia Law Review, Vol.17, No.2, 2011], 128.

¹²⁸ A. Dahlsrud, *How Corporate Social Responsibility Is Defined: An Analysis of 37 Definitions*, [Corporate Social Responsibility and Environmental Management 15, No. 1 2008], 11.

¹²⁹ Neil Mitchell, *Corporate Power, Legitimacy, and Social Policy* [The Western Political Quarterly 39, No. 2, 1986], 199.

economic opportunities and preventing massive environmental destruction.¹³⁰ Even though, there are still a number of reasons for doubting the claim that adopting CSR will make national economic growth of particular country, local economic more inclusive and equitable, and thereby reduce poverty.¹³¹ This study is mainly discuss about the development and improvement of CSR policy Indonesia from voluntary basis become mandatory. In other aspect, it might be also really helpful to strengthen a policy for poverty reduction throughout Indonesia.

Business is intended to provide solution to the problem of world poverty and also to strengthen social engagement between business and society through the promotion of equal economic opportunities and the closely relationship of small and medium-sized enterprises in global supply chain¹³² but the main ways in which corporations can alleviate poverty is through job creation and a close private-public sectors partnership.¹³³ The business is not only encouraged to create jobs but also to pay more attention to the social, environmental and local economic circumstances around them.

The government of particular country is also responsible to create jobs for its citizen. In addition, foreign direct investment (FDI) policy may increase to government's revenues through taxes and other retribution payments. Then it might be used to reduce poverty by developing physical infrastructures and providing social and economic assistance package to its citizen.

¹³⁰ M. Prieto-Carron, P. Lund-Thomsen, A. Chan, ANA Muro, and C. Bhushan. *Critical Perspectives on CSR and Development: What We Know, What We Don't Know, and What We Need to Know* [International Affairs 82, No. 5, 2006], 980.

¹³¹ *Op.Cit*, Rhys Jenkins, *Globalization, Corporate Social Responsibility and Poverty*. [Royal Institute of International Affairs No. 3, 2005], 525.

¹³² *Loc.Cit*, M. Prieto-Carron, P. Lund-Thomsen, A. Chan, ANA Muro, and C. Bhushan. *Critical Perspectives on CSR and Development: What We Know, What We Don't Know, and What We Need to Know* [International Affairs 82, No. 5, 2006], 980.

¹³³ *Loc.Cit*, Rhys Jenkins, *Globalization, Corporate Social Responsibility and Poverty*. [(Royal Institute of International Affairs No. 3, 2005), 525.

But in practice, the taxes payment is reduced by tax holidays scheme offered by host government as a strategy to attract more investors to come to its country. Moreover, the tax reduction policy is provided in term of CSR programmes implementation.¹³⁴ If it is not well- guided, monitored and evaluated by a reliable mandatory CSR framework it may loss the government's revenues, jobs opportunities and reducing the national economic growth.

Corporate social responsibility is not a new phenomenon, although its substance may have changed over time.¹³⁵ The definition of current CSR policy pays a lower attention to environmental dimension rather than other dimensions such as social and economic empowerment.¹³⁶ It is contrary with the definition of mandatory CSR within Indonesia context and law system in which mandatory CSR policy has paid the most of its attention to environmental preservation and conservation. In the early definition of CSR has been made by international agencies, the environmental element was not included as major principle because it is considered to be part of CSR as whole and still remain as it is until now.¹³⁷ Moreover, the establishment of United Nations Global Compact on 2000 has obviously taken into account environmental reason as one of the most major issues.¹³⁸

According to some CSR experts there was a new changes and perspective how people see CSR before the year of 2000 and after the year of 2000. Further, in the recent years, environmental issues are being a major issue of all activities relate to business practices. Many studies and real CSR programmes have explained that

¹³⁴Ibid.

¹³⁵*Op.Cit.* .Neil Mitchell, *Corporate Power, Legitimacy, and Social Policy* [The Western Political Quarterly 39, No. 2, 1986], 199.

¹³⁶*Op. Cit.* A. Dahlsrud, A. Dahlsrud, How Corporate Social Responsibility Is Defined: An Analysis of 37 Definitions.

¹³⁷A.B. Carroll, *Corporate Social Responsibility*. [Business & Society 38, No. 3, 1999], 268.

¹³⁸*Op. Cit.*, Rhys Jenkins, *Globalization, Corporate Social Responsibility and Poverty*. [Royal Institute of International Affairs No. 3, 2005], 525.

CSR initiatives were very effective to alleviate poverty, increase local and national economic growth and eliminating environmental destruction small and medium income countries.¹³⁹

Nowadays, corporate social responsibility has become an integral part of the business operation as well as it is become a sensitive issue in management.¹⁴⁰ Most of college of business in Malaysia has allocated a specific discussion on CSR. It shows that CSR is become an important agenda of business practices in the current age.

Sustainability of strategic social responsibility is an agenda that requires corporations to pay significant attention to economic, social and environmental factors and fully integrating and synthesizing the basic concepts of the three factors with local wisdoms.¹⁴¹ It expected that there will be strong relationship between the corporations and local communities. Furthermore, CSR is also a concept that encourage corporations to fulfil the highest standard of ethical conduct to their stakeholders by showing the most of their business concerns on social and environmental factors.¹⁴²

There are some important principles must be taken into account in recognizing corporation's social responsibilities to the local context in low and middle-income countries, firstly is the institutional and historical circumstances of the local communities, secondly is equal communication approach with local

¹³⁹*Op. Cit.*, M. Prieto-Carron and others, Critical Perspectives on CSR and Development: What We Know, What We Don't Know, and What We Need to Know, [International Affairs 82, No. 5, 2006], 980.

¹⁴⁰ N. Cornelius, M. Todres, S. Janjuha-Jivraj, A. Woods, and J. Wallace. *Corporate Social Responsibility and the Social Enterprise*, [Journal of Business Ethics 81, No. 2, 2008], 358.

¹⁴¹E. Van Velsor, *Introduction: Leadership and Corporate Social Responsibility*, [Corporate Governance 9, No. 1, 2009], 6.

¹⁴²K. Tanimoto, and K. Suzuki. *Corporate Social Responsibility in Japan: Analyzing the Participating Companies in Global Reporting Initiative*, [Stockholm School of Economics, EIJIS, Working Paper 208, No. 2005.3, 2005], 7.

beneficiaries and thirdly is degree of social and economic recovery and improvement might able be given by the corporations to local stakeholders.¹⁴³ The three factors above is correlating between one and another and may differ from one area to another area. There must be specific circumstances for particular area with its own local characteristic.

It is also align with the spirit of millennium development goals whereby there must be a close engagement of private sectors to enhance social prosperity. Moreover, Daniri stated that at least there are four benefits for corporations when they implement CSR programmes namely, they will gain a positive image within the society and among their consumers, they will have easier access to capital, they may get qualified human resources, and they will reduce their business risks.

CSR can be a significant factor for improving infrastructure and non-infrastructure facilities within the society especially for local people's who is living surrounding the companies' business operation. CSR is also dedicated as a tool to maintain excellent relationship between companies and the community in a particular area of operation. Moreover, CSR would strengthen the sense of belonging of the community if the companies apply integrated and comprehensive CSR projects under its business operation.

At the local level, CSR is also regulated by the Law on Governing Aceh.¹⁴⁴ All companies are investing or would like to do investment in Aceh must allocate at least one percent of their annual net profit for community economic empowerment projects.¹⁴⁵ Therefore, due to the status of Aceh as a special autonomous region within the Unitary State of Indonesia, Aceh has to implement the

¹⁴³ F. Bird, and J. Smucker. *The Social Responsibilities of International Business Firms in Developing Areas*, [Journal of Business Ethics 73, No. 1, 2007], 5.

¹⁴⁴ Article 157 and 159 of Act No.11/2006 on Governing Aceh.

¹⁴⁵ Ibid.

Law on Governing Aceh No. 16/2006. According to the Aceh's Special Act, companies should allocate at least 1% of its profit for social responsibility. On the other hand in Act No.40/2007 on Company Liability, there is no fix percentage for the companies to allocate CSR funds.

It also leads confusion because which law will be binding concretely for a current company is doing business in Aceh. In the Company Liability Act, there is no specific percentage of number on CSR funds should be allocated by the companies. It is contradicting with the Law on Governing Aceh, the companies must allocate at least one percent of its annual net profit to empower local community around the companies. The fund is called as community development fund.

On the other hand, the central government promised a tax holiday to all companies that are consistent in implementing CSR programmes that will be gradually and comprehensively implemented for a certain period of its investment duration.¹⁴⁶ Moreover, the tax holiday policy has been passed by the central government.¹⁴⁷ The regulation provides a 5% tax deduction for companies implementing CSR by mainly providing assistance to disaster affected areas throughout Indonesia.¹⁴⁸

In some districts and provinces throughout Indonesia, eventhough no Government Regulation on CSR on national level before April 2012 as instructed by Article 74 of the Act No. 40/2007 on Limited Company Liability, the Province of East Java has passed a provincial regulation that regulates CSR issues within the

¹⁴⁶*Op.Cit*, Government Regulation No. 93/2010 on Donation for National Disaster, Research and Development, Educational Facilities, Sports Empowerment, and Social Infrastructure Development Cost Deductible from Gross Revenue.

¹⁴⁷Wahyu Sudoyo, "CSR Dan Sumbangan Bencana Kurangi Pajak Perusahaan." [Jakarta, Investor Daily, January 12, 2011], 11.

¹⁴⁸Faisal Rachman, "CSR Ditetapkan Jadi Faktor Pengurang Pajak." [Jakarta, Sinar Harapan, January 2011], 17.

province.¹⁴⁹ In addition, Kutai Timur District in West Kalimantan Province has also passed a district regulation on CSR according to former *Bupati Kutai Timur, Awang Faroek Ishak*, there were at least five kinds of benefits that he got while he convened CSR programmes in the East Kutai district while he was in power, such as; “providing assistance for religious sector, reducing illiteracy by providing scholarships for the poor students, alleviating poverty by empowering micro, small and medium scale enterprises, allocating more jobs and revitalizing public healthcare system”.¹⁵⁰

The concept of mandatory has been criticised by international CSR experts, Indonesian business associations and Indonesian CSR based NGOs because they thought that the concept of CSR should be on voluntary basis.¹⁵¹ Some of CSR practitioners that reject the notion of mandatory CSR are Achmad Daniri,¹⁵² Jalal¹⁵³ and Budi R. Minulya.¹⁵⁴ Nevertheless, they supported in establishing a better policy and environment for making CSR implementation in Indonesia more socially responsible and transparent.

Currently, CSR has become a cross-cutting issue and interdisciplinary subject of academic discussion either international, regional, national, and local spectrum. It because of CSR is not just cover the issues on management, marketing and financial but also it covers some other issues like social cohesion, peace, justice, international relations, public policy, and law enforcement. Further, the Minister of Environment

¹⁴⁹ Provincial Government of East Java, Provincial Regulation of East Java Province Number 4/2011 on Corporate Social Responsibility.

¹⁵⁰ Awang Faroek Ishak, “Business Sector’s Involvement on Community Empowerment Programmes in Kabupaten Kutai Timur,” www.kutaitimurkab.go.id, [Accessed 6th March, 2012].

¹⁵¹ Ali Darwi, Director of National Center Sustainability Report (NCSR), [Interview on 15 September 2013 in Jakarta].

¹⁵² Achmad Daniri, Head of Indonesian Good Governance Commission, [Interview on 27 September 2013 in Jakarta].

¹⁵³ Jalal, Lingkar Studi CSR/A+ CSR Indonesia, [Interview on 13 September 2013 in Jakarta].

¹⁵⁴ Budi R. Minulya, CSR-Community Development Consultant at ICON Institute, [Interview on 19 October 2013 in Depok, Jakarta].

Republic of Indonesia urged business enterprises to implement green economic policy to create efficiency in utilizing natural resources.

The concept of mandatory CSR is to push the companies to allocate some amount of money for their social responsibilities programmes. In certain countries in Europe, Denmark is one of the countries supported the implementation of CSR mandatory reporting.¹⁵⁵ It shows that the importance role of government to manage business enterprises to behave in the interest of the society in Denmark.

Indonesia has enshrined mandatory legal provision because of environmental cases. There are two (2) environmental cases that affected most the people who living around the business operation, they are Buyat case in North Minahasa and Lapindo mud volcano in Porong, Sidoarjo. The two (2) cases have politically and socially pushed the national parliament to insert mandatory legal provision into the amendment of Company Liability Act on 2007. Apparently, it is nearly 7 years of the enactment, the mandatory legal provision can not be implemented well due to unclear executing regulations on mandatory CSR alone and overlapping of CSR management among relevant ministries.

Recently, Indonesian Environmental Consortium/WALHI has released a publication that there are fifty two (52) companies have destructed environment in Indonesia since 2012-2013. It shows that the number of companies have destructed environment are increasing. It means that mandatory legal provision has not yet been implemented well by the government towards the companies who are operating their businesses in Indonesia.

Further, the concept of mandatory CSR is more fair for the indigenous people; it preserved and and conserves natural resources. Currently, international

¹⁵⁵ Danish Financial Statement Act of 8 October 2008.

agencies and extractive industries are campaigning carbon trade mechanism in combating and alleviating global warming, illegal logging, and forest destruction. Further, the mechanism is being implemented under the framework of reducing emissions, deforestation and forest degradation (REDD).¹⁵⁶

The fairness of mandatory CSR concept for conserving environment is solely stated on the 1945 constitution of the Republic of Indonesia. It is obviously stated on the constitution that every citizen has the right to work and to have a humane livelihood and also has the right to live and to defend his/her existence.¹⁵⁷ Further, it is quite complex, controversy and challenging in demanding development policies against human rights principles.¹⁵⁸ The critical issue is about in the level of implementation of some human rights laws and standards either national and international or in other words is the most challenging issue is about the legal enforcement of those provisions.¹⁵⁹

Aliansi Masyarakat Adat Nusantara/Indigenous Peoples' Alliance of the Archipelago (AMAN) demands to the international agencies such the World Bank to be fair with the Indigenous peoples.¹⁶⁰ Further, indigenous peoples in Indonesia through AMAN resists that carbon trade mechanism is not fair and injustice for the sustainability of their lives. It because of the mechanism does not recognise the forest customary ownership status of the indigenous peoples.¹⁶¹ Further, it seems that the

¹⁵⁶Naomi Johnstone. Indonesia in the "REDD": Climate Change, Indigenous Peoples and Global Legal Pluralism, [Asian-Pacific Law and Policy Journal, Vol. 12, 2009.], 93.

¹⁵⁷ Article 27 clause (2) and Article 28A, the 1945 Constitution of the Republic of Indonesia as amended by the First Amendment of 1999, the Second Amendment of 2000, the Third Amendment of 2001 and the Fourth Amendment of 2002.

¹⁵⁸ Irene I. Hadiprayitno, "Challenges Facing the use of Human Rights to Address Negative Impacts of Development: The Case of Indonesia", [The Law and Development Review, Vol. 4. No.1,2011], 246.

¹⁵⁹Ibid

¹⁶⁰Loc. Cit,Naomi Johnstone,"Indonesia in the "REDD": Climate Change, Indigenous Peoples and Global Legal Pluralism," [Asian-Pacific Law and Policy Journal, Vol. 12, 2009.], 108.

¹⁶¹Ibid

responsibility of conserving the environmental is in the side of indigenous peoples rather than extractive industries. Indeed, extractive industries cause more pollution and environmental destruction than the community.

Therefore, based on the researcher opinion mandatory CSR concept introduces more reasonable, fair and balance mechanism to conserve the environmental and natural resources. One of the fairness of mandatory CSR mechanisms is the responsibility to conserve environmental and natural resources sustainability is under the responsibility of the extractive industries. It because of mandatory CSR concept was derived from the concept who is cause the destruction so that the party should be more responsible to rehabilitate the environment than others. If mandatory CSR is consistently implemented by business enterprises, then it may provide a wider impact towards the conservation of environmental and natural resources as well as local people's economic.

In some countries, extractive industries are more powerful than the government itself.¹⁶² It encourages human rights groups and other interested parties to advocate and to develop any necessary legal enforcement mechanism.¹⁶³ As it is mentioned that there are two types of challenging issues incorporating development policies and human rights standards, those are namely the fulfilment of some basic principles such as transparency, non-discrimination, participation, accountability and equality between national laws and international human rights standards.¹⁶⁴ Further, another challenges is to integrate relationship between the State and the individual.¹⁶⁵

¹⁶² Steven R. Ratner, Corporation and Human Rights; *A Theory of Legal Responsibility*, [Connecticut, The Yale Law Journal, Vol. 111, 2001], 48.

¹⁶³ Ibid

¹⁶⁴ *Op. Cit.*, Irene I. Hadiprayitno, "Challenges Facing the use of Human Rights to Address Negative Impacts of Development: The Case of Indonesia," [The Law and Development Review, Vol. 4. No.1. Article 7, 2011], 249.

¹⁶⁵ Ibid

Based on the researcher' opinion, the imbalance power and authority between the State and the individual encourages people to seek alternative way to strengthen the relationship between the State and the individual. One of the most appropriate alternatives ways is by enforcing the law and regulations. It is also the same with the relationship between the corporation and the individual. Corporation is more powerful in many aspects than the Individual. Therefore, the alternative way to make it balance is by enacting the laws and regulations. It because of laws and regulations is the most democratic way to express the enterest of each parties. Every parties is given access to express its interest regarding a specific issue related to their interest.

Further, laws and regulations are also recognised as the means to create security, law order, stability and harmony. Yet, the laws and regulations are intended to protect some different interests among the citizen to be united. However, the mandatory CSR legal provision is also has been gone through the most democratic process, starting from legal drafting discussion within the House of Representative and the submission of judicial review by some business associations. Therefore, it is for no reason not to implement consistently the provision of mandatory CSR legal provision in Indonesia.

Contemporary debates between voluntary and mandatory CSR should not be longer persist because of no single solution fits all problems.¹⁶⁶ It means that voluntary CSR that has been implementing is not really accommodate the interests of the society. It feels can not solve a lots of environmental destruction in many parts of extractive industries are operating. Further, rapid development of international human rights standards requires states, individual and business enterprises to comply

¹⁶⁶ Marcel van Marrewijk, "Concepts and Definitions of CSR and Corporate Sustainability: Between Agency and Communion," [Journal of Business Ethics, 2003], 95.

with those international commitments.¹⁶⁷ At last, ratification of those international human rights standards encourages the State to align its national judiciary system with the provision of those human rights policies.¹⁶⁸

The concept of CSR is quite new for Asia region.¹⁶⁹ It seems like CSR concept is a new value for Asians and should be transferred from the West to Asia region. Whereas, traditional community in Asia region has recognised the value of respect for social and environmental. It because of most of Asian communities are living in the jungle areas and depending their lives with the sustainability of the nature itself.

It is also contradicting with the notion of mandatory CSR as a concept that comes from Asia region. The philosophy of CSR is social and environmental responsiveness for local community around the business operation and it is inseparable with the business function of any business enterprises.¹⁷⁰ Further, the notion of CSR comes as the response of Multinational Enterprise (MNE) to the demands of public interest of society and non-governmental organizations (NGOs).¹⁷¹ MNEs is always being mentioned as entity that only working to increase profits for their stakeholders and careless to social, economic and environmental circumstances around their businesses operation.¹⁷²

¹⁶⁷ *Op. Cit*, Irene I. Hadiprayitno, "Challenges Facing the use of Human Rights to Address Negative Impacts of Development: The Case of Indonesia", [The Law and Development Review, Vol.4, No.1, Article 7, 2011], 251.

¹⁶⁸ *Ibid*

¹⁶⁹ Joaquin L. Gonzalez III, "*Is There Room for More Social Responsibility in Asia's Business and Economic Turn Around ?*," [San Fransisco, Annual Publication of University of San Fransisco Center for Pacific, Vol.5 No. 2, 2005],1.

¹⁷⁰ *Ibid*

¹⁷¹ David Henderson, "*The Case Against Corporate Social Responsibility*", [Wellington, The New Zealand Business Roundtable, 2001], 29.

¹⁷² *Ibid*

2.3 Laws, Regulations, Guidelines and Policies on Mandatory CSR

Policy debates over corporate social responsibility in Indonesia between voluntary and mandatory policy have reflected the struggle between capitalist class over local community and environmental conservation interest.¹⁷³ The capitalist class is supported by important elements within the senior government officials and political support by several influence political leaders.¹⁷⁴ Whereas, local community was supported by NGOs either local or national wide who concern on advocacy, academics and minor part of the companies.¹⁷⁵

Article 74 of Act No.40/2007 on Limited Company Liability has given a new way in executing CSR programmes in Indonesia. The contents of the Article have become a legal basis for the government to encourage the companies in implementing it. The article has some following legal characteristic;

- a) The Article 74 and its elucidation have been drafted through a legal formal discussion within the House of Representative of Indonesia. According to the Constitution of Republic of Indonesia, President and House of Representative have the right to jointly agree or disagree on a certain Bill.¹⁷⁶
- b) The legal standing of an Act within the legal system of Indonesia is the executing regulation to implement the constitution.¹⁷⁷ Further, whenever the House of Representative has officially agreed a certain Act then it is fully the responsibility of the Government to implement it by providing a necessary Government regulation.

¹⁷³ Andrew Rosser and Donni Edwin, “*the Politics of Corporate Social Responsibility in Indonesia,*” [The Pacific Review, Vol. 23. No.1, 2010], 1.

¹⁷⁴Ibid

¹⁷⁵Ibid

¹⁷⁶Article 5 (1) The 1945 Constitution of Republic of Indonesia “The President shall be entitled to submit bills to DPR (House of Representative)”.

¹⁷⁷Article 5 (2) The 1945 Constitution of Republic of Indonesia “the President may issue the Government regulations as required to implement laws” and Article 7 (1) of Act No.10/2004 on Regulatory Drafting

c) The article 74 of Act No.40/2007 on Limited Company Liability was intended to implement the Article 33 of the 1945 Constitution of the Republic of Indonesia which is the Article 33 has mandated the government to implement the economic democracy based on the principles of togetherness, efficiency with justice, countinuity, environmental perspective, self-sufficiency and keeping a balance in the progress and unity of the national economy.¹⁷⁸

Further, public sector roles to strengthen the implementation of CSR is significant.¹⁷⁹ It because of public sector has at least four (4) key important approaches to address the clarity of CSR programmes implementation. The key roles are as follows mandating, facilitating, partnering and endorsing.¹⁸⁰ Mandating means that the public sector like legislative body passed relevant laws and regulations that is required to succeed the implementation of CSR programmes. Further, facilitating means that provides some guidelines and guidance regarding the CSR programmes. Then, partnering refers to a close engagement with multi-stakeholders processes. At last, endorsing is recognised those successful stories have been made by each stakeholders in implementing CSR programmes through a large publicity.

Aside of policy debates on voluntary and mandatory CSR in Indonesia, CSR has also translated into several types of definitions which is relatively confusing the local communities as beneficiaries. Some of terminologies are being used by experts and practitioners are as follows; corporate citizenship,¹⁸¹ charity and

¹⁷⁸Article 33 of the 1945 Constitution of Republic of Indonesia.

¹⁷⁹ Tom Fox, Halina Ward, Bruce Howard, “*Public Sector Roles in Strengthening Corporate Social Responsibility; A Baseline Study*,” [New York, The World Bank Publication, 2002], 3.

¹⁸⁰Ibid

¹⁸¹ Kim Davenport, “Corporate Citizenship: “A Stakeholder Approach for Defining Corporate Social Performance and Identifying Measures for Asssesing It”, [Business and Society of SAGE Publication, Vol. 39, No. 2, June 2000], 210.

philanthropy,¹⁸² corporate responsibility,¹⁸³ community development,¹⁸⁴ social responsibility,¹⁸⁵ corporate-community relations (CCR),¹⁸⁶ corporate responsiveness,¹⁸⁷ corporate social performance (CSP)¹⁸⁸ and corporate-community collaboration (CCC).¹⁸⁹ Those terminologies are being used inter-changeably by the experts and practitioners of CSR.

According to Universal Declaration of Human Rights, there are some basic human rights must be protected by state such as states everyone has the rights to life, liberty and security of person.¹⁹⁰ Then, everyone as a member of society has the right to social security and is entitled to realization, through national effort and international cooperation and in accordance with the organization and resources of each state, of the economic, social and cultural rights indispensable for his dignity and the free development of his personality.¹⁹¹

In the other international human rights law instrument, such as United Nations Declaration on the Rights of Indigenous Peoples, particularly article 26 clause 1 says that Indigenous peoples have the right to lands, territories and resources which they

¹⁸² Karen Wright, “Generosity and Altruism: Philanthropy and Charity in the United States and United Kingdom”, [the Centre of Civil Society Department of Social Policy London School of Economics and Political Science, Civil Society Working Paper 17, 2001], 1.

¹⁸³ Pietra Rivoli and Sandra Waddock, “First They Ignore You...?: The Time-Context Dynamic and Corporate Responsibility”, [California Management Review, Vol. 53, No.2, 2011], 87.

¹⁸⁴ Deanna Kemp, “Mining and Community Development: Problems and Possibilities of Local-Level Practice”, [Community Development Journal, Vol. 45, No.2, 2010], 198.

¹⁸⁵ Milton Friedman, “The Social Responsibility of Business Is to Increase Its Profit”, [New York, The New York Times Magazine, 1970], 1.

¹⁸⁶ Barbara W. Altman, “Transformed Corporate Community Relations: A Management Tool for Achieving Corporate Citizenship”, [Business and Society Review, Vol 102, 1998], 43.

¹⁸⁷ Murphy P.E, “An Evolution: Corporate Social Responsiveness”, [Michigan, University of Michigan Business Review, Vol. 36. No. 6, 1978], 19.

¹⁸⁸ Steven L. Wartick and Philip L. Cochran, “The Evolution of Corporate Social Performance Model”, [The Academy of Management Review, Vol. 10, No.4, October, 1985], 758.

¹⁸⁹ Loc. Cit, Joaquin L. Gonzalez III, “Is There Room for More Social Responsibility in Asia’s Business and Economic Turn Around ?,” [Annual Publication of University of San Francisco Center for Pacific Rim, Vol.5 No. 2, 2005], 1.

¹⁹⁰ Article 3 of Universal Declaration of Human Rights. New York: United Nations, 1948.

¹⁹¹ Article 22 of Universal Declaration of Human Rights. New York: United Nations, 1948.

have traditionally owned, occupied or otherwise used or acquired.¹⁹² Then, clause 3 of the same article says state shall give legal recognition and protection to these lands, territories and resources, such recognition shall be conducted with due respect to the customs, traditions and land tenure systems of the indigenous peoples concerned. In addition, Article 29 of the Constitution says indigenous peoples have the right to the conservation and protection of the environment and the productive capacity of their lands, territories and resources. State shall establish and implement assistance programme for indigenous peoples for such conservation and protection, without discrimination.

Based on some provisions of UDHR and UNDRIP above, it was clearly stated how many rights and interest of various peoples and/or communities related to environment, land and natural resources. Furthermore, it makes sense if state create a “one-stop service” system to accommodate all different and various rights between one and another by implementing mandatory corporate social responsibility.

In some countries, corporations are more powerful economic actors rather than its government itself in term of controlling over its natural resources or lack of willingness to control its natural resources.¹⁹³ The willingness of some least developed states welcome foreign investment because they need direct income through taxes payment but at the same time they have no sufficient resources either the system of monitoring or human resources to control extractive industries in their countries.¹⁹⁴ If corporations are allegedly may contribute to very serious human rights

¹⁹²United Nations, *United Nations Declaration on the Rights of Indigenous Peoples*, [New York, United Nations, 2007].

¹⁹³*Loc. Cit*, Steven R. Ratner, “Corporations and Human Rights: A Theory of Legal Responsibility,” [Yale Law Journal Vol. 111, November 2001], 443.

¹⁹⁴*Ibid*

violations then the states should develop the best and most suitable system for the country to anticipate and tackling the occurrence that kind of circumstances.

It is shortly being noted that mandatory CSR policy is an alternative solution to be taken by particular country to eliminate violations. According to the theory of international human rights law, it has been obviously stated on Universal Declaration of Human Rights (UDHR), Government is the only actor obliged to protect human rights of its people. While the government fail to conduct its obligation to protect it. then, individual can advocate its rights by using some recognized international human rights mechanism.¹⁹⁵

Recently, the interest of protecting environment and lands, of producing clean, safe, healthy and organic agricultural products, of sustaining natural resources are not only the interest of one single state and/or one single community but also has been interest of entire nations and states across the globe.¹⁹⁶ All of these people are living under the same planet, the same sun and the same air. Therefore, it is very urgent for states to create a better policy, rule and/or regulation to make sure all the same interest are well-protected and well-obeyed by all parties particularly corporations.¹⁹⁷

International law provides voluntary benchmarks for private sectors to respect for human rights principles.¹⁹⁸ It makes extractive industries sometimes make decisions against the international human rights standard because it is just a voluntary basis. The research is expected to describe the necessity of national policy intervention from particular country to impose extractive industries to respect for international human rights principles properly. International environmental law will

¹⁹⁵ *Loc. Cit*, United Nations, Universal Declaration of Human Rights.

¹⁹⁶ Christopher R. Duncan, "The Impact of Regional Autonomy and Decentralization on Indigenous Ethnic Minorities in Indonesia," [Journal of Development and Change, Vol. 38 No. 4, 2007], 711.

¹⁹⁷ *Ibid*

¹⁹⁸ Robert Howse, and Ruti Teitel. *Beyond Compliance: Rethinking Why International Law Really Matters*. [Global Policy 1, No. 2, 2010], 127.

only protect society as a whole,¹⁹⁹ it means that there is state's obligation there to provide reliable and appropriate procedures to protect its people's human rights-related to environmental violations. One of the most effective and efficient ways to prevent infringements of environmental law and basic human rights principles by corporations are by implementing mandatory CSR as a way out to prevent it.

Multinational corporations (MNCs) commonly developed their own codes of conduct and measures to implement their CSR programmes.²⁰⁰ They publicize and disseminate their own internal policies to their stakeholders regarding their strict policies in delivering CSR programmes.²⁰¹ Compared to the CSR regulations initiated by individual business enterprises, the CSR regulations provided by public authorities or relevant government office could better safeguard the implementation of CSR programmes.²⁰² This notion shows us that public authorities are the most acceptable party to pass any CSR regulation and whatever the regulations are. In the context of Indonesia, the public authorities have passed a mandatory approach for conducting CSR in Indonesia, despite the rejection received from business enterprises regarding its implementation.

Unfortunately, the government's provision has not been implemented well due to lack of political will and relevant regulations, policies, and guidelines from the central government.²⁰³ Improving the quality of CSR implementation in Indonesia

¹⁹⁹S  verine Fiorletta Leroy, *Can the Human Rights Bodies Be Used to Produce Interim Measures to Protect Environment-Related Human Rights?*, [Review of European Community & International Environmental Law 15, No. 1, 2006], 66.

²⁰⁰ Julien Levis, "Adoption of Corporate Social Responsibility Codes by Multinational Companies," [Journal of Asian Economics, Vol. 17, 2006], 50.

²⁰¹Ibid

²⁰²Ibid

²⁰³*Op. Cit.*, Andrew Rosser and Donni Edwin, "the Politics of Corporate Social Responsibility in Indonesia," [The Pacific Review, Vol. 23. No.1, March 2010], 2.

depends on the extent to which the government allows CSR to be implemented.²⁰⁴

After reviewing some evidence, the researcher concluded that there has been a vested interest of some groups who stood behind the screen to delay the implementation of mandatory CSR legal provision in Indonesia.²⁰⁵

The mandatory CSR will provide rules, regulations, general conditions and specific guidelines on how corporations must comply with the existing environmental principles and laws. In some cases, the extractive industries are more powerful entities; the states lack the sufficient human resources and capabilities following a vulnerable human development system.²⁰⁶ The CSR movement can act as a tool to pressure the multinational corporations to pay more their attention on how to tackle the possible negative environmental and social impacts of their business operations.²⁰⁷

Indigenous peoples are the most vulnerable groups related to environmental damages.²⁰⁸ In an increasingly interconnected world, transnational law and an expanding international legal system increases the repertoire of legal system available, providing new legal resources and sources of legitimacy for local peoples.²⁰⁹ Even the local communities have been given a greater access to manage

²⁰⁴ Melody Kemp, "Corporate Social Responsibility in Indonesia: Quixotic Dream or Confident Expectation?", [United Nations Research Institute for Social Development, Technology, Business and Society Programme Paper No.6,2001], 7.

²⁰⁵ Businessmen Association

²⁰⁶ *Op.Cit*, Steven R. Ratner, "Corporations and Human Rights: A Theory of Legal Responsibility,"[Yale Law Journal Vol. 111, November 2001], 447.

²⁰⁷ *Op.Cit*, Rhys Jenkins, *Globalization, Corporate Social Responsibility and Poverty*, [(Royal Institute of International Affairs No. 3, 2005)], 525.

²⁰⁸ *Op. Cit*, Christopher R. Duncan, "The Impact of Regional Autonomy and Decentralization on Indigenous Ethnic Minorities in Indonesia", [Journal of Development and Change, Vol. 38 No. 4, 2007], 712.

²⁰⁹ Naomi Johnstone, *Indonesia in the "REDD": Climate Change, Indigenous Peoples and Global Legal Pluralism.*, [Asian-Pacific Law and Policy Journal 12, No. 1, 2011], 7.

their own budget and revenues but still when it comes to extraction of natural resources then the best interest of indigenous peoples are ignored.²¹⁰

The adoption of international policies must reflect the needs of particular country in fulfilling its citizen rights over human rights, sustainable development, social justice and community empowerment.²¹¹ As a contemporary case study is the struggling of indigenous peoples to secure customary forest rights in the content of REDD-related law and policy creation at national, regional and international levels.²¹² There is probably also a need for more linkage between trade and human rights, social questions and environmental concerns.²¹³ In regard to sustainable development, there are some basic principles as follows equitable distribution of economic opportunities, alleviation of poverty, protection of human rights and respect for environmental conservation.²¹⁴

The researcher's is of opinion that mandatory CSR is a way out offered by Indonesia to adapt global environmental changes and securing sustainability of environmental resources for the next generation. It also stresses the significant of cross-cutting issues such as transparency, anti-corruption, accountability, participatory development, and the responsibility of civil society movement.²¹⁵

Sustainable development is not only discussing environment issue but also the most important is how to synergize and integrating between environmental, social and

²¹⁰ Loc. Cit, Christopher R. Duncan, "The Impact of Regional Autonomy and Decentralization on Indigenous Ethnic Minorities in Indonesia", [Journal of Development and Change, Vol. 38 No. 4, 2007], 712.

²¹¹ R. Mushkat, *Globalization and the International Environmental Legal Response: The Asian Context*, [Asian Pacific Law Policy Journal 4, 2003], 50.

²¹² Op. Cit, Naomi Johstone, Indonesia in the "REDD": Climate Change, Indigenous Peoples and Global Legal Pluralism, [Asian-Pacific Law and Policy Journal 12, No. 1, 2011], 9.

²¹³ Allan Rosas, *State Sovereignty and Human Rights: Towards a Global Constitutional Project*. [Political Studies No. 43, 1995], 68.

²¹⁴ Op. Cit, R. Mushkat, *Globalization and the International Environmental Legal Response: The Asian Context*. [Asian Pacific Law Policy Journal 4, 2003], 57.

²¹⁵ Ibid

economic empowerment aspect as together goals in a multicultural and dynamics society.²¹⁶

The fundamental rights of human beings are divided into three dimension as follows communal rights, personal rights and combination between communal and personal rights.²¹⁷ Therefore, mandatory CSR offers solution how to engage and combining between communal and personal rights by creating public-private partnership. The scheme offers more participatory efforts of local people as the main beneficiaries.

Normally fundamental rights should be protected by the state as the operator of sovereignty. For example; if state violates individual or collective individual rights then the individual or collective individual may take legal action against the state. In the case of human rights violations done by multinational corporations (non-state actor), individual or collective individuals may appeal their rights directly against the multinational corporations through appropriate channel of advocacy both national and international. In regard to channel of advocacy for individual or collective individuals at international level, if it is involved multinational corporations the victims may go through OECD dispute resolution and complaint handling mechanism and it is involved palm oil plantations corporations then the parties may go through RSPO complaint handling procedures.

Both are voluntarily basis of mechanism provided by these associations. Nevertheless, it is need to construct national dispute and complaint handling mechanism at the national level before it goes to international arena. One of the

²¹⁶ Marie-Claire Cordonier Segger, *Sustainability and Corporate Accountability Regimes: Implementing the Johannesburg Summit Agenda*. [Review of European Community & International Environmental Law 12, No. 3, 2003], 297.

²¹⁷ Gunther Teubner, *The Anonymous Matrix: Human Rights Violations by 'Private' Transnational Actors*, [United Kingdom, Modern Law Review, 2006], 327.

options is by strengthening mandatory CSR mechanism as a tool of internal and even national dispute and complaint handling mechanism in which extractive industries violate national rules and local wisdoms in relation to social, environmental and economic empowerment in particular country.

The existence of multinational corporations may cause several serious environmental and societal damages such as air pollution, land pollution, water pollution, forestation, land degradation, illegal logging, horizontal conflict local communities, force disappearance of local communities, disgraceful working condition, chemical accident, flood or landslide. All the negative effects against fundamental right of particular people and the people may take legal and/or non-legal action against the transnational corporations.

There are major human rights abuses in the context of human rights and globalization as following, state actors and transnational corporations.²¹⁸ As an example, in arctic also was found the most hazardous particles as of people consider it is the most pristine area on the earth.²¹⁹ There are several number of voluntary international instruments of human rights both implicit and explicit which consisting environmental conservation principles,²²⁰ such as 1972 Stockholm Declaration, 1992 Rio Declaration on Environment and Development, 1948 Universal Declaration of Human Rights (UDHR), United Nations Declaration on the Rights of Indigenous Peoples (UNDRIP), International Covenant on Civil and Political Rights (ICCPR)

²¹⁸Sumner B. Twiss, *History, Human Rights, and Globalization*, [Journal of Religious Ethics 32, No. 1, 2004], 67.

²¹⁹Henrik Selin, and Noelle Eckley Selin. *Indigenous Peoples in International Environmental Cooperation: Arctic Management of Hazardous Substances*, [Review of European Community & International Environmental Law 17, No. 1, 2008], 80.

²²⁰Marie Soveroski, *Environment Rights Versus Environmental Wrongs: Forum over Substance?*, [Review of European Community & International Environmental Law 16, No. 3, 2007], 261.

and International Covenant on Economic, Social and Cultural Rights (ICESCR), African Charter of People and Human's Rights²²¹ and Kyoto Protocol.²²²

It also necessary to provide the most reliable access to international environmental law in order to create more effective dispute resolutions and complaint handling mechanisms.²²³ It was found that local communities are lack of awareness and also not really familiar with the compliance concept of international law works.²²⁴ It requires transforming international human rights and environmental principles into national policies of each country to be reinforced by national and local procedures.²²⁵ One of the ways to do it is through such a mandatory CSR framework. Mandatory CSR policy has a legal power to uphold the rules because mandatory CSR policy is a binding rule for all CSR stakeholders.

Fundamental rights are not only binding the states but also multinational corporations.²²⁶ Human rights instrument and its mechanism should not be considered as only a tool of dispute resolutions between the state and citizen but also between multinational corporations.²²⁷ European institutions released its international policies in promoting human rights statutes or doctrines that allow multinational corporations under European law jurisdiction to be sued at home for human rights-based crimes abroad as part of corporate liability and transparency.²²⁸

²²¹Ibid

²²²Cinnamon Pinon Carlame, *Good Climate Governance: Only a Fragmented System of International Law Away?*, [Law & Policy 30, No. 4, 2008], 450.

²²³Ibid

²²⁴*Op.Cit.* Robert Howse, and Ruti Teitel. *Beyond Compliance: Rethinking Why International Law Really Matters*, [Global Policy 1, No. 2, 2010], 129.

²²⁵Ibid

²²⁶*Op. Cit.* Gunther Teubner, *The Anonymous Matrix: Human Rights Violations by 'Private' Transnational Actors*, [United Kingdom, Modern Law Review, 2006], 335.

²²⁷Ibid

²²⁸*Op. Cit.* Marie-Claire Cordonier Segger, *Sustainability and Corporate Accountability Regimes: Implementing the Johannesburg Summit Agenda*. [Review of European Community & International Environmental Law 12, No. 3, 2003], 299.

In addition, at least there are three main factors to uphold corporate accountability, firstly voluntary instruments which are called as “corporate responsibility”, secondly, domestic or national courts through foreign direct liability which is called as “corporate liability” and thirdly, through a “corporate citizenship” scheme where usually governments have a specific international treaty with business entities and civil society as equal partners.²²⁹

As an example of pollution management system in United Kingdom where public considered it as activities against transparency, then public criticize it seriously because the dispute resolution has not followed environmental rules.²³⁰ A lot of multinational corporations have been implementing voluntary initiatives such as corporate social responsibility to engage with their stakeholders such as local people, governments and civil society organizations and internally they also developed a system to measure the impacts.²³¹

Many multinational corporations developed internal corporate codes of conduct to guide their CSR programmes and it may differ from one corporation and another, there should be a single standard of CSR programmes such as the same Standard Operating Procedures (SOP) that apply for all multinational corporations to measure their compliance with the rule of law system itself.²³² Mandatory CSR will also as a good way to produce such SOP to be applied for all multinational corporations in Indonesia. After all, beneficiaries may measure the degree of accountability of certain corporation.

²²⁹Ibid

²³⁰William Howarth, *Self-Monitoring, Self-Policing, Self-Incrimination and Pollution Law*, [United Kingdom, *The Modern Law Review* 60, No. , 1997], 200.

²³¹*Loc.Cit.* Marie-Claire Cordonier Segger, *Sustainability and Corporate Accountability Regimes: Implementing the Johannesburg Summit Agenda*. [Review of European Community & International Environmental Law 12, No. 3, 2003], 297.

²³²Ibid

Most of environmental policy makers in most countries have difficulties to synergize and integrating between environmental protection policy and economic growth policies.²³³ Unlike in Indonesia, Indonesia has implemented mandatory CSR policy since 2007 through the enactment of Limited Company Liability Act No.40/2007. That policy may synthesize environmental protection policy, social development aid and economic empowerment programme. There are a lot of international voluntary standards have been developed either by industries and business organizations or government representatives and civil society organizations to measure an effective environmental and forest protection.²³⁴

Corporate code of conducts itself may not be enough to affirm corporation's compliance, there should be more powerful tool to uphold corporation's compliance such as mandatory CSR policy.²³⁵ Even OECD guidelines for multinational enterprises, it just contains purely guiding principles on good business practices for all multinational corporations that voluntary become a member of OECD without any enforcement procedures.²³⁶ In relation to current global concern on environmental protection, it is very urgent to have a binding standard of services and universal reporting formats.²³⁷

If the idea is still voluntary principles and voluntary compliance then universality standard will never been achieved. People need to think out of the box in order to strengthen the current policy to be more powerful and comprehensive. One

²³³Suzanne Kingston, *Integrating Environmental Protection and EU Competition Law: Why Competition Isn't Special*, [European Law Journal 16, No. 6, 2010], 780.

²³⁴Paul R. Kleindorfer, and Eric W. Orts. *Informational Regulation of Environmental Risks*, [Risk Analysis 18, No. 2, 1998], 155.

²³⁵*Op. Cit.* Marie-Claire Cordonier Segger, *Sustainability and Corporate Accountability Regimes: Implementing the Johannesburg Summit Agenda*. [Review of European Community & International Environmental Law 12, No. 3, 2003], 301.

²³⁶*Op. Cit.* Sumner B. Twiss, *History, Human Rights, and Globalization*, [Journal of Religious Ethics 32, No. 1, 2004], 69.

²³⁷W.B.T. Mock, *Corporate Transparency and Human Rights*, [Tulsa. J. Comp. & Int'l L, 2000], 15.

of the choices is by strengthening mandatory CSR framework in the country in order public will have more access to information on the programme.²³⁸

International environmental law has emerged as a new issue to the global arena because of common global concerns of massive environmental destruction in many places around the world such as illegal logging, forestation, land degradation and global warming.²³⁹ Most of environmental rules and regulations regulates specifically on the process, technology use and output of the environmental resources.²⁴⁰ In addition, there is a direct link between rules makers and the users.²⁴¹

There should be a standard procedure for the rules makers and users to negotiate some disputes issues or complaints have been raised by beneficiaries.²⁴² Mandatory CSR policy is initially offer the standard of mechanism for both parties or even involve other group to have the same opportunity in the implementation process of CSR programme. It is expected to develop a check and balances mechanism for the accountability of CSR programmes.

There is a close relationship between human rights and human dignity.²⁴³ Human dignity was the major concern of human rights law making process.²⁴⁴ In addition, economic and social arrangements must be integral part of enhancing human dignity around the world.²⁴⁵ There is a new term which is called “social contract” between state and private sector in protecting and enhancing human

²³⁸ *Op. Cit.* Marie-Claire Cordonier Segger, *Sustainability and Corporate Accountability Regimes: Implementing the Johannesburg Summit Agenda*. [Review of European Community & International Environmental Law 12, No. 3, 2003], 304.

²³⁹ *Op. Cit.* Sumner B. Twiss, *History, Human Rights, and Globalization*, [Journal of Religious Ethics 32, No. 1, 2004], 71.

²⁴⁰ *Op. Cit.* Paul R. Kleindorfer, and Eric W. Orts. *Informational Regulation of Environmental Risks*, [Risk Analysis 18, No. 2, 1998], 157.

²⁴¹ *Ibid*

²⁴² *Ibid*

²⁴³ J. Donnelly, “*Human Rights and Human Dignity: An Analytic Critique of Non-Western Conceptions of Human Rights*,” [The American Political Science Review, 1982], 303.

²⁴⁴ O. Schachter, “*Human Dignity as a Normative Concept*,” [The American Journal of International Law 77, No. 4, 1983], 848.

²⁴⁵ *Ibid*

rights.²⁴⁶ The “social contact” is emerge in some international documents for example 1948 Universal Declaration on Human Rights, OECD Guidelines for Multinational Enterprises, But those are not work well because corporations are only comply voluntarily with these international standards and they just simply organize their resources to only reach maximum profits for their shareholders.²⁴⁷

In addition, many corporations in the field is quite reluctant to respect for human rights standard as well as corporate social responsibility.²⁴⁸ Rules and regulations have been made to encourage all these multinational corporations to respect for human rights standard in order to secure human dignity. There are some rights of the people ether collective and personal rights to be protected by the state and also at the same time there are some duties should be implemented by the state to ensure that these rights are well protected.²⁴⁹

Wars and horizontal conflict have occurred in many places around the world made people especially some interest groups such as business and society to make business and human rights stand together by producing some following international voluntary principles or treaties, for example CAUX Principles for Business and Interfaith Declaration, Standard of Principles for Canadian Business, The American Model Business Principles, The Pacific Basin Economic Council Charter on Standards for Transactions between Business and Government, AA1000 for Social and Ethical Accountability, SA8000 for Labour Rights Standard and ISO Environmental Management.²⁵⁰

²⁴⁶ W. Cragg, “*Human Rights and Business Ethics: Fashioning a New Social Contract*,” [Journal of Business Ethics 27, No. 1, 2000], 205.

²⁴⁷ Ibid

²⁴⁸ Ibid

²⁴⁹ H.L.A. Hart, *Are There Any Natural Rights?*, [The Philosophical Review 64, No. 2, 1955], 175.

²⁵⁰ *Op. Cit.* W. Cragg, *Human Rights and Business Ethics: Fashioning a New Social Contract*, [Journal of Business Ethics 27, No. 1, 2000], 207.

In addition, the emerging of those new “*post war social contract*” because of some reasons behind such as to run business to be more adaptive with social circumstances surrounding them, to protect human dignity by respect for human rights principles, to ensure participation of civil society organizations in the business practices.²⁵¹

The presence of multinational corporations has significantly increase national economic growth of particular country and many of its citizen may access job opportunities.²⁵² Multinational corporations may commit human rights violations are not only in an armed conflict area but also in a peace and calm area, for example; doing land conversion by forest burning and discriminating employees from local communities group.²⁵³

The demand of human rights is very natural response to change the situation into a better circumstance to ensure human dignity.²⁵⁴ Human rights abuses frequently affect minorities, the poor, marginalized, indigenous peoples, children, women and vulnerable groups.²⁵⁵ Therefore, the state should provide a system that may prevent multinational corporations doing that or at least eliminate these kinds of violations by imposing a more binding policy such as mandatory CSR.

Civil society organizations frequently organize a demonstration or public campaign against multinational corporations as part of the public pressure to impose

²⁵¹ R. McCorquodale, *Feeling the Heat of Human Rights Branding: Bringing Transnational Corporations within the International Human Rights Fence*, [Human Rights and Human Welfare 1, No. 4, 2001], 21.

²⁵² J. Nolan, *With Power Comes Responsibility: Human Rights and Corporate Accountability*, [University of New South Wales Faculty of Law Research Series, 2010], 11.

²⁵³ D. Weissbrodt, *Corporate Human Rights Responsibilities*, [Zeitschrift für Wirtschafts-und Unternehmensethik 6, No. 3, 2005], 279.

²⁵⁴ *Op. Cit.* J. Donnelly, *Human Rights and Human Dignity: An Analytic Critique of Non-Western Conceptions of Human Rights*, [The American Political Science Review, 1982], 306.

²⁵⁵ D. Weissbrodt and M. Kruger. *Norms on the Responsibilities of Transnational Corporations and Other Business Enterprises with Regard to Human Rights*, [The American Journal of International Law 97, No. 4, 2003], 901.

them to accommodate the local community's interest.²⁵⁶ In fact, moral pressure such as demonstration or blockade has significantly forced multinational corporations to respect for human rights.²⁵⁷ Accordingly, the good reputation of a particular corporation is an asset that may increase their profit while negative allegations of involvement in human rights violations that are raised by civil society organizations may affect the corporation's revenues.²⁵⁸

Multinational corporations have been increasingly investing their capital in developing countries through foreign direct investment schemes offered by the host government. They have been offered some profitable economic package such as cheap labour, tax reduction policy, and an easy licenses policy. Regardless of mandatory CSR legal provision, these corporations also have to be more responsible for the social, environmental and economic circumstances around them.

Local communities are resources for multinational corporations through which they operate. By having good relationship with the local communities, their business can go smoothly and sustainable. Therefore, mandatory CSR is expected to strengthen the relationship because then the corporations have not only a responsibility but also an obligation to empower their stakeholders properly. Most people believe that multinational corporation may cause indirect environmental damages such as pollution and discrimination among the society.²⁵⁹

Corporations always take responsive actions following a natural disaster that occurs at their operating places, and this is expected by the government and the local

²⁵⁶*Op. Cit.* R. McCorquodale, *Feeling the Heat of Human Rights Branding: Bringing Transnational Corporations within the International Human Rights Fence*, [Human Rights and Human Welfare 1, No. 4, 2001], 21.

²⁵⁷*Ibid*

²⁵⁸*Ibid*

²⁵⁹James E. Grunig, *A New Measure of Public Opinions on Corporate Social Responsibility*, [The Academy of Management Journal 22, No. 4, 1979], 738.

society,²⁶⁰ In Indonesia, the government has released a national policy through which corporations will be given a tax holiday scheme if they assist in certain social activities such as helping with national-wide natural disaster, research and development, education facilities, sport development support and social infrastructures expenses.²⁶¹ In fact, the response of one corporation is different than another following the voluntary rule.

Most of these corporations then consider that the above assistances are given as part of a CSR programme. In fact, some CSR experts say that those kinds of assistance are only recognized as philanthropies. Therefore, it needs to be made more powerful by giving a force authority in order to push these corporations to react the same and to quickly respond when a natural disaster occurs. Furthermore, mandatory CSR policy is highly recommended by a decision maker to be a smooth tool of pressure to these corporations.

One of the most effective strategies to protect the environment is by providing a powerful regulation.²⁶² Moreover, the lack of internal and external monitoring and evaluation process may contribute to illegal activities that may prevent a corporation's successful implementation of its CSR programmes.²⁶³ As a new policy, the mandatory CSR will replace the old system (the voluntary CSR) in trying to develop a system that may detect any internal and external fraud of a corporation. As

²⁶⁰ Dennis S. Mileti, Daniel M. Cress, and JoAnne DeRouen Darlington. *Earthquake Culture and Corporate Action*, [Sociological Forum 17, No. 1, 2002], 161.

²⁶¹ Government Regulation Republic of Indonesia No. 93/2010 on Charity for National Disaster Recovery, Research and Development, Education Facilities, Sports Development and Social Infrastructure Development Expenses that Can Be Deducted from Bruto Revenue.

²⁶² Neil Gunningham and Darren Sinclair. *Regulatory Pluralism: Designing Policy Mixes for Environmental Protection*, [Law & Policy 21, No. 1, 1999], 49.

²⁶³ Marie A. McKendall, and John A. Wagner, III. *Motive, Opportunity, Choice, and Corporate Illegality*, [Organization Science 8, No. 6, 1997], 624.

an example, the United States Sentencing Commission has provided a new set of compulsory sentencing guidelines for corporate and other institutional offenders.²⁶⁴

It was a culmination of a 25-year effort to develop and specify the statutory sentencing standards for individual and institutional. The state is more “*potentially armed*” to control corporate crime.²⁶⁵ In this context, mandatory corporate social responsibility policy may encourage corporations to avoid illegal activities because there will be several “*rewards and punishment*” rules within the policy.

Environmental rights are an integral part of the human rights system.²⁶⁶ This means that there is a strong link between environmental rights in particular and human rights law and principles in general. These issues are like two sides of a currency and it is indivisible between one and another. Many of international environmental conventions, treaties and agreements are made based on human rights principles and international actors, and it is clearly established that states have obligation in these areas.²⁶⁷

Unfortunately, all these international treaties have been made on voluntary basis rather than compulsory. It needs a strong national policy concept to implement each article of these international environmental treaties. Mandatory CSR is one of the most affordable and appropriate ways to be a “*custodian*” of these international environmental conventions within the national context.

This study will also connect human rights principles especially on the environmental rights and the CSR objectives whereby the state has obligation to keep

²⁶⁴ D.R. Dalton, M.B. Metzger, J.W. Hill, W.W. Simmers, J.L. Cobert, E.J. Conry, and K.H. Fox. *The New U.S Sentencing Commission Guidelines: A Wake-up Call for Corporate America [and Executive Commentary]*, [The Academy of Management Executive, 1994], 7.

²⁶⁵ W.S. Lofquist, *Legislating Organizational Probation: State Capacity, Business Power, and Corporate Crime Control*, [Law and Society Review, 1993], 741.

²⁶⁶ Marie Soveroski, *Environment Rights Versus Environmental Wrongs: Forum over Substance?*, [United Kingdom, Journal Compilation, 2007], 261.

²⁶⁷ Ibid

the rights of lives of its citizen away from environmental destruction. On the other hand, the government should also provide a conducive investment climate for extractive industries which also support the economic growth of a particular country and create more employment opportunities.

CSR is purely and traditionally part of business ethics and is usually treated as voluntary programmes of the corporations. Nowadays, people see that most CSR programmes are implemented by multinational corporations as a symbol of their commitment to be socially responsible with the economic social, and environmental circumstances around them. Business ethics can also be enshrined by rules and regulations to be implementable in necessary circumstances. Stakeholders cannot merely expect that the CSR implementation can depend on the goodwill of corporations to conduct it; there should be a system to guide its well implementation in corporations.²⁶⁸

As a good example, the U.S. Congress has enacted a set of code of ethics to improve public trust in the markets because of unethical conduct of shares brokers. The code of ethics was translated into writing rules which is called the *Sarbanes Oxley Act*.²⁶⁹ In line with the objectives of CSR programmes to restore public trust on the concerned and to instill, strong commitment and goodwill of corporations to be more responsible with social, economic and environmental circumstances surrounding them, it is necessary to formalize the programmes into a binding rule.

Good corporate values can be determined by good corporate governance. Factors that influence good corporate values are as follows: ownership structure,

²⁶⁸ *Op. Cit.* Marie Soveroski, Environment Rights Versus Environmental Wrongs: Forum over Substance?, [United Kingdom, Journal Compilation, 2007], 265.

²⁶⁹ D. Hess, *A Business Ethics Perspective on Sarbanes-Oxley and the Organizational Sentencing Guidelines*, [Michigan, Michigan Law Review, 2007], 1781.

board of directors' composition and stakeholder influence.²⁷⁰ Therefore, the stakeholder theory emphasizes that the corporation is encouraged to create as much good value for its important stakeholders.²⁷¹ In this case, stakeholders are actually divided into three key elements such as the government, corporations and society. The society is the primary beneficiary from these CSR programmes.

The stakeholders' roles are very important factor for the successful implementation of the CSR programmes. Furthermore, if well implemented by multinational corporations, the mandatory CSR framework may significantly contribute to alleviate poverty in low- and middle-income countries through its CSR programmes.²⁷² Additionally, those programmes are expected to be linked to other poverty alleviation projects within the country.

Indonesia also needs a single CSR surveillance body that is able to design, organize, monitor and evaluate the CSR programmes of various multinational corporations throughout Indonesia in a more credible and accountable manner, unlike the current situation in Indonesia in which few of the ministries²⁷³ are having a CSR section which takes control and implements the CSR programmes. These, ministries also release CSR standard of service, CSR awards, and other CSR gatherings that are intended for multinational corporations to comply with those tools.

Multinational corporations are mostly accused by civil society organizations for having organized crimes against public interest and guidelines have been made by the commission to prevent and even to sentence them while they are committed to

²⁷⁰S. Thomsen, *Corporate Values and Corporate Governance*, [Corporate Governance 4, No. 4, 2004], 29.

²⁷¹ M.B.E. Clarkson, *A Stakeholder Framework for Analyzing and Evaluating Corporate Social Performance*, [Academy of Management Review, 1995], 92.

²⁷²*Op.Cit.*Rhys Jenkins, *Globalization, Corporate Social Responsibility and Poverty*, [Royal Institute of International AffairsNo. 3, 2005], 530.

²⁷³ Ministry of Environmental Republic of Indonesia, Ministry of Social, Ministry of State-Owned Companies, and Ministry of Home Affairs.

do some following crimes such as forest destruction, fraud, tax manipulation, waste violation, money laundering, and antitrust.²⁷⁴ In relation to CSR strategic implementation and part of business ethic, it makes sense to create such a guideline to speed up the CSR adoption as a way to alleviate poverty, protect the environment, protect the basic rights of people and ensure that natural resources are sustainable.

It is effective to create a clearer picture of CSR strategic implementation by setting more specific policies, for instance, by setting up general guidelines or codes of conduct. Further, mandatory CSR is considered as one of the most strategic ways to engage with its primary beneficiaries. In fact, multinational corporations have great influences on government officials, and in some cases, they interfere with the state's economic strategic decisions.²⁷⁵ Government has legitimate power of coercion to enforce the regulation in order to prohibit or mandate certain activities that can ensure harmony and safety of all citizens, particularly when the communities are the living surrounding of the extractive industries in which they operate.²⁷⁶

Most of current governments are utilizing criminal laws or penalties on multinational corporations which have committed business violations.²⁷⁷ There are some clear examples in which multinational corporations were involved in environmental destruction, social mistreatment, discrimination and excessive violence on local indigenous groups during their businesses operations.²⁷⁸ In addition, there are at least two real examples in Indonesia in which multinational corporations have affected the sustainability living of the local population groups.

²⁷⁴ *Op. Cit.*, Steven R. Ratner, "Corporations and Human Rights: A Theory of Legal Responsibility," [Yale Law Journal Vol. 111, November 2001], 449.

²⁷⁵ *Ibid*

²⁷⁶ Anel Karnani, *Doing Well by Doing Good: The Grand Illusion*, [California, California Management Review 53, No. 2, 2011], 69.

²⁷⁷ D.M. Driscoll, W.M. Hoffman, and J.E. Murphy. *Business Ethics and Compliance: What Management Is Doing and Why*, [Business and Society Review No. 99, No. 1, 1998], 35.

²⁷⁸ *Op. Cit.* Gunther Teubner, *The Anonymous Matrix: Human Rights Violations by 'Private' Transnational Actors*, [United Kingdom, Modern Law Review, 2006], 331.

One of them is environmental destruction caused by Freeport-McMoran in Papua²⁷⁹ and another being mud volcanoes that accured in Porong, Sidoarjo, East Java.²⁸⁰ Moreover, much environmental damages in Indonesia were allegedly caused by multinational corporations. These are real examples for decision makers to refer when making policy changes on corporate social responsibility from being voluntary to mandatory.

Despite many human rights conventions, agreements, and treaties being made by states and civil society organizations, many of them do not work well yet. They need a further instrument to be implemented in the field and mandatory CSR is one of the best executing frameworks for human rights instruments.²⁸¹

2.4 The Functions, Jurisdictions and Liabilities of CSR Surveillance Body in Indonesia

Broadly, corporate social responsibility in Indonesia is divided into two major clusters. First, CSR is being implemented by state owned-companies.²⁸² It is monitored and coordinated by the Ministry of State Owned-Companies of Republic of Indonesia.²⁸³ Therefore, CSR is being implemented by private companies such as manufacturing- or natural resources-based companies, which are monitored and coordinated by the Ministry of Social of Republic of Indonesia²⁸⁴ and the Ministry of Environment of Republic of Indonesia.²⁸⁵

²⁷⁹ Freeport McMoran Corporation in Indonesia has allegedly caused environmental damages in Papua.

²⁸⁰ Lapindo Brantas was accused violates human rights in Porong Sidoarjo, East Java.

²⁸¹ M.S. McDougal, H.D. Lasswell, and L. Chen. *Human Rights and World Public Order: A Framework for Policy-Oriented Inquiry*, [The American Journal of International Law 63, No. 2, 1969], 237.

²⁸² Act No. 40/2007 on Limited Company Liability.

²⁸³ Act No. 19/2003 on State Owned Company.

²⁸⁴ Act No. 11/2009 on Social Welfare.

²⁸⁵ Act No 32/2009 Environmental Management and Protection.

There is still limited of jurisdiction of each law regarding CSR in Indonesia. Those laws are only concerned specific ministries. In other words, there is still no regulation that connects them to one another. Although the government regulation on CSR has just passed by the end of April, 2012, it only covered the general terms of CSR without specifying its jurisdiction, monitoring body and liability.²⁸⁶

The Indonesia Financial Institution and Stock Exchange Supervisory Body/*Badan Pengawas Pasar Modal dan Lembaga Keuangan* (BAPEPAM-LK) had released a regulation that all companies listed in the stock exchange is encouraged to submit its annual financial report together with the CSR annual report to BAPEPAM-LK.²⁸⁷ According to the rule, the body is also applying a whistle blower policy for complainants who report fraud or misconduct that is allegedly committed by any corporation. This will protect insiders or any person who would like to report any fraud or violations that might have been committed within a corporation.

Jurisdiction of mandatory CSR provision in Indonesia is still limited to natural resources-based corporations. It means that it is not compulsory for non-natural resources-based companies to comply with the rule.²⁸⁸ Notwithstanding, the Indonesia Chamber of Commerce and Industry Deputies on Research, Industry and Technology convinces that mandatory CSR is necessary because at times, the implementation of CSR programmes is misdirected.

Corporations believe that a CSR framework may help them to alleviate some of potential risks associated with uncertain circumstances in which they operate.²⁸⁹ The

²⁸⁶ Government Regulation No. 47/2012 on Environmental and Social Responsibility of Limited Company Liability.

²⁸⁷ Head of Stock Exchange and Financial Institution Supervisory Board Decree, No KEP-134/BL/2006 on Obligatory Annual Financial Report for Public Listed Companies.

²⁸⁸ Government Regulation Number 47/2012 on Environmental and Social Responsibility of Limited Company Liability.

²⁸⁹ D. Tzavara, *Can the Threat of Costly Litigation Be Incentive Enough for Companies to Engage in CSR?*, [Academic Management Review, 2009], 241.

general thought of the European commission is that CSR is a voluntary engagement rather than mandatory.²⁹⁰ It influences the way of European corporations engaged with the CSR programmes. As an example, the French corporate law is attempting to use hard law as a means to push assets managers to become more transparent and accountable.²⁹¹ Moreover, costly litigations may push corporations to implement the CSR programmes to avoid any damages or insolvency to their businesses.²⁹²

Currently, a lot of government agencies at national and sub-national level in Indonesia are eager to pass CSR rules and regulations. This is a good signal of CSR strategic implementation. CSR can be used as an alternative source of development fund. But it should be regulated in more detail in order to avoid any overlapping of tasks and responsibilities between the central government, the local governments and the private sectors. The involvement of private sectors in the development process should be on their portion as business entities because they also the have responsibility to pay for their labour salaries, tax, retributions, and profit target as demanded by their shareholders.

The development of mandatory CSR policies at sub-national level should be in line with higher rules and regulations. Yet, there is still no government regulation on CSR, although the provincial government of East Java has released East Java Provincial Regulation on CSR.²⁹³ Instead, some other districts, municipalities and provincial governments are on their way to pass their governmental regulations on CSR.

²⁹⁰ Ibid.

²⁹¹ I. Tchotourian, *Comparative Lessons on Corporate Law and CSR: Hard Law as Solution? Do the French Offer the Way Ahead?*, [Corporate Social Responsibility Journal, 2011], 261.

²⁹² *Op. Cit.* D. Tzavara, *Can the Threat of Costly Litigation Be Incentive Enough for Companies to Engage in CSR?*, [Academic Management Review, 2009], 245.

²⁹³ *Op. Cit.* Provincial Government of East Java, Provincial Regulation of East Java Province Number 4/2011 on Social Responsibility of Limited Company Liability.

The most important point of the process is that sub national governments must provide a better and more conducive circumstance to support the effectiveness of CSR implementation in their areas. The role of government should be in the areas of being a regulator, a motivator or a facilitator of CSR programmes rather than being the implementing agency of the programmes.²⁹⁴

Nowadays, conducting CSR studies and execution of the programme are not only the responsibility of the central and sub national governments; they have become multidisciplinary and inter-related institutional issues.²⁹⁵ Business institutions, Civil Society Organizations (CSO) and governments should establish a partnership among themselves to ensure sustainable development under the law system.²⁹⁶ Unfortunately, there is still some remaining issue in mandatory CSR such as the leaving of CSO's role behind. This was obviously seen during the discussion of government regulation on mandatory CSR, where there were no single CSOs involved by the legal drafting team.²⁹⁷

The role of civil society organizations is still not frequently mentioned by the government in any act of CSR such as the Investment Act,²⁹⁸ the Social Prosperity Act,²⁹⁹ the Micro Small and Medium Size Enterprise Act,³⁰⁰ the Company Liability Act and the State Owned-Company Act. Frequent involvement of CSOs in monitoring and supervising of CSR programmes may lead to the transparency and effective implementation of good corporate governance principles. In relation to

²⁹⁴Sri Yuliani. *Corporate Social Responsibility; Public Liability in Business Sector and its Implication to Public Administration Studies*, [Public Spirit Journal Vol.6 No.1,2010], 27.

²⁹⁵Ibid

²⁹⁶A.G. Scherer, A.G., and G. Palazzo. *The New Political Role of Business in a Globalized World: A Review of a New Perspective on CSR and Its Implications for the Firm, Governance, and Democracy*, [Journal of Management Studies 48, No. 4,2011], 899.

²⁹⁷*Op. Cit*, Government Regulation Number 47/2012 on Environmental and Social Responsibility of Limited Company Liability.

²⁹⁸*Op. Cit*, Act No. 25/2007 on Investment.

²⁹⁹*Op. Cit*, Act No.11/2009 on Social Welfare.

³⁰⁰Act No. 20/2008 on Micro, Small and Medium Scale Enterprise.

good corporate governance principles, many countries have performed and initiated legal, regulatory and institutional corporate governance reform.³⁰¹

The good corporate governance principles of the Organization for Economic Cooperation and Development (OECD) play a significant role to the CSR implementation strategy and reporting in Indonesia. The principles have been adopted by the Indonesia stock exchanges through BAPEPAM-LK regulation.³⁰² There are two important sections in the document namely whistle blower and CSR principles. These principles should be respected by all companies listed in to the stock exchange, which also should follow those principles while they are submitting their annual CSR reports to the stock exchange committee.

According to some previous reports, those listed corporations claimed that they have implemented the CSR programmes well during a budget year period. Unfortunately, there is still no standard monitoring and evaluation tool to measure their claims. Furthermore, the stock exchange committee should also provide a greater access to information for public such as the civil society organization groups and other CSR beneficiaries.³⁰³

In addition, a statement was made by the head of *BP Migas*, who suggested that CSR funds be converted to cost recovery fund that can be claimed back from the government.³⁰⁴ This suggestion has been included on the CSR provision within the

³⁰¹The World Bank, Report on the Observance of Standards and Codes, [New York, The World Bank Publishing, 2010], 7.

³⁰² Stock Exchange and Financial Institution Supervisory Board, OECD Principles Implementation Studies on BAPPEPAM regulation on Corporate Governance, [Jakarta, Stock Exchange Publishing, 2006], 4.

³⁰³*Op. Cit.* Stock Exchange and Financial Institution Supervisory Board No.KEP-134/BL/2006 on Obligatory Annual Financial Report for Public Listed Companies.

³⁰⁴*Op. Cit.* Government Regulation No, 93/2010 on Donation for National Disaster, Reserach and Development, Educational Facilities, Sports Empowerment, and Social Infrastructure Development Deductible from Gross Revenue.

Limited Company Liability Act.³⁰⁵ In the provision, natural resource based-corporations must allocate some amount of funds as CSR fund. Then the expenditures can be deducted by the government as a tax reduction policy for these corporations. The main focus of CSR provision in the Act is intended and directed to natural resource-based companies.

Nevertheless, the manufacturing, retail, banking and telecommunication business sectors are more responsive to adopting the CSR policy compared to the natural resource based-companies. This finding is surprisingly knocking the government's silence to reinforce the mandatory CSR legal provision towards the natural resource based-companies. The government should provide and release a standard manual of CSR programmes in Indonesia.

2.5 Conclusion

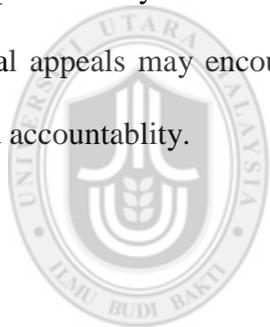
Standardization of the CSR policy strategy, jurisdiction, monitoring, and supervision process, at both national and sub-national level may lead to a one-stop service CSR office. This will likely bring a very positive impact to the execution of CSR programmes by the corporations in Indonesia.³⁰⁶ A more clear policy will contribute to the sustainability of the CSR programmes. Sustainability is also a key aspect of the CSR implementation strategy. CSR funds must enable the stakeholders or recipients to sustain their businesses when the support is no longer available. Instead, it has been proven in most developed countries that the partnership of three sectors – government, business sectors and community (civil society organizations) - may contribute significantly to the recovery of environment condition.

³⁰⁵ *Loc. Cit*, Act No. 40/2007 on Limited Company Liability.

³⁰⁶ *Ibid*

Sustainability should reflect triple-bottom-line principles which cover economic, social and environmental principles. It should also be reflected in practice by the close partnership between government, corporation and civil society organizations. Unfortunately, it has not yet been clearly stated within the government regulation on CSR.³⁰⁷ Sustainable development is an integrated promotion of economic, social and environmental approach towards a common objective.³⁰⁸

Basically, good corporate governance principles should be integrated with CSR provisions of any rules and regulations at national and sub-national level. It is no longer possible to differentiate between natural resource-based companies and other sectors in adopting the CSR standards.³⁰⁹ In addition, it has been established in an empirical study that making implementable of legal instruments and greater access to legal appeals may encourage corporations to practice CSR with more transparency and accountability.



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³⁰⁷*Op. Cit.*, Government Regulation Number 47/2012 on Environmental and Social Responsibility of Limited Company Liability.

³⁰⁸*Op. Cit.*, Marie-Claire Cordonier Segger, *Sustainability and Corporate Accountability Regimes: Implementing the Johannesburg Summit Agenda*, [Review of European Community & International Environmental Law 12, No. 3, 2003], 299.

³⁰⁹*Op. Cit.*, Government Regulation Number 47/2012 on Environmental and Social Responsibility of Limited Company Liability.

CHAPTER THREE RESEARCH METHODOLOGY

3.1 Introduction

The thesis applied a qualitative research methodology. A major part of the research adopted the qualitative research methods and a minor part applied a quantitative approach. Combining methodologies enabled the researcher to describe all the relevant information and updates on the CSR policies in Indonesia more comprehensively and specifically. Further, it will provide an exact justification of some relevant data and issues that have been reported.

In addition, a qualitative method was used by the researcher because of the lack of academic references on mandatory CSR legal provisions. It is the author's intention to find a new theory or concept on a particular issue being investigated.

3.2 Research Design

The design of the research is a pure normative legal research whereby a large portion of the data is qualitative. A normative legal research uses primary data as the main source of data for the research.³¹⁰ It will also use secondary data as complementary to the primary data. In fact, a legal normative research approach consists of seven different approaches, which are the statute, conceptual, analytical, comparative, historical, philosophical and the case study approach.³¹¹ It mainly uses statutes, laws and regulations to analyse the objectives of the research. Nonetheless, it is also supported by several raw

³¹⁰ Johnny Ibrahim, *Teori Dan Metode Penelitian Hukum Normatif*. 2 ed., Edited by Setiyono Wahyudi [Surabaya: Bayumedia Publishing, 2006], 267.

³¹¹Ibid

data to justify the analysis. The process of doing a legal research often involves interdisciplinary investigations.³¹²

Therefore, a purposive sampling method will be applied to recognize several eminent persons in the field of CSR. The structured interviews will produce quantitative data from 30 (thirty) key CSR expert persons in Indonesia that represent 5 (five) different background such as CSR government officials from the Ministry of Social Affairs, the Ministry of Environmental, the Ministry of State-Owned Companies, practitioners, academics, corporations and business associations. Legal normative research principles will hold the most important role in finding the answers and solutions for each research question.

Qualitative research methods have become the most chosen methodology and technique to answers some important inquiries in social sciences.³¹³ A qualitative research is essentially conducted through a library-based research.³¹⁴ Moreover, a qualitative research merits is used when the topic is new or the topic has never been addressed or little research has done on it.³¹⁵ It is very important for a researcher to gather data from the primary, secondary and tertiary sources such as acts, statutes, laws, regulations, government legal documents, registered journal articles, workshop and seminar proceedings, text books, newspapers and other relevant documents.³¹⁶ The research has discovered concepts, principles, guidelines,

³¹²J. Myron Jacobstein, Roy M. Mersky, Donald. J. Dunn. “*Fundamentals of Legal Research*,”[New York, The Foundation Press, 1994], 128.

³¹³Earl Babbie,“*The Practice of Social Research*,”[Belmont California, Publishing Co, 1982], 268.

³¹⁴Soerjono Soekanto, *Pengantar Penelitian Hukum*[Jakarta, UI-Press, 1986], 98.

³¹⁵ John W. Creswell, “*Research Design: Qualitative, Quantitative and Mix Methods Approaches*,” [California, Sage Publication Inc, 2009], 145.

³¹⁶Peter Mahmud Marzuki, *Penelitian Hukum* [Jakarta, Kencana Prenada Media Group, 2005], 78.

relevant statutes, legal opinion, facts and relevant provisions on corporate social responsibility in Indonesia.³¹⁷

A statutory approach was used to gather data and analyse the philosophical rationale behind the mandatory CSR provision in Indonesia.³¹⁸ The approach assisted the researcher to analyse several reasons and background of the mandatory CSR legal provision in Indonesia by using analytical descriptive analysis on the related CSR laws and regulations in Indonesia. The approach is very relevant to be applied for the first objective of this research because the mandatory CSR provision was passed by the Indonesian National Legislative in 2007.

An analytical descriptive approach was used to study and analyse constitutional court verdict Number 53/PUU-VI/2008 on mandatory CSR legal provision and also on CSR related laws and regulations.³¹⁹ The analysis focused on CSR verdicts in Indonesia, as well as the CSR legal provisions in the country and the overlapping and cross-cutting laws and regulations among them. Relevant corporate social responsibility provisions from several statutes would be analysed and criticized. The approach was also used to study and analyse the current guidelines being used by the government officials and corporations to implement the mandatory CSR projects in Indonesia. It covers the planning process, the implementation strategy, the monitoring and evaluation mechanism, and the punishment and reward system

³¹⁷Soerjono Soekanto dan Sri Mamudji, “*Penelitian Hukum Normatif Suatu Tinjauan Singkat*,” [Jakarta, Rajagrafindo Persada, 2003], 115.

³¹⁸Amiruddin dan Zainal Asikin, “*Pengantar Metode Penelitian Hukum*,” [Jakarta, Rajagrafindo Persada, 2008], 57.

³¹⁹*Op. Cit*, “*Teori Dan Metode Penelitian Hukum Normatif*,” 2 ed., Edited by Setiyono Wahyudi [Surabaya, Bayumedia Publishing, 2006], 269.

in implementing mandatory CSR. The legal instruments that would analysed include but is not limited to several CSR-related legal documents.

Apart from these laws made by the national parliament of Indonesia several instruments on national and international CSR are also analysed to obtain both national and international perspectives on the urgency of environment safeguarding and the building partnership between enterprises and communities, particularly in relation to describe the functions, jurisdictions, and liabilities of the CSR surveillance body in Indonesia. They would be conducted in a formal interview session together with a set of questions, and the results would be arranged in a logical order and would be recorded in appropriate columns.³²⁰ The approaches used enabled the researcher to conclude as well as to find up-to-date information on CSR developments in Indonesia. It is also to be noted that even though a structured interview method is applied in the research, the research is still considered as qualitative one.³²¹ Opinions from 30 (thirty) experts would strengthen the overall analysis of the research and would be used to answer the third objective of the research.

A minor comparative approach on the tax reduction policy in CSR implementation in Malaysia is very essential for the legal research. The comparative analysis can contribute to the comparative thoughts on the current situation of tax reduction scheme on the ground such as similarities and differences and advantages and disadvantages of the tax reduction issue.

³²⁰ Anwarul Yaqin, *“Legal Research and Writing,”* [Kuala Lumpur, LexisNexis, 2007], 28.

³²¹ *Loc. Cit.*, Johnny Ibrahim, *“Teori Dan Metode Penelitian Hukum Normatif,”* 2 ed., Edited by Setiyono Wahyudi [Surabaya: Bayumedia Publishing, 2006], 267.

This approach would assist the researcher in analysing the third objective as well. It is to be noted that, the researcher's adopting uses this approach does not mean that this research is a comparative study; rather, the decision was to acquire the foundation thoughts and comparative information about other countries' corporate social responsibility concepts especially on tax reduction schemes. Perhaps, it may be applied and adopted in the Indonesian tax reduction system later.

Subsequently, a few policies were analysed to gain a clear picture on the CSR system. The policies included international provisions, best practices or guiding principles on CSR such as the United Nations Guiding Principles on Business and Human Rights, Organization for Economic and Cooperation Development (OECD) Principles on Multinational Enterprises, ISO 26000 on Social Responsibility and other relevant manuals. However, this research is not a comparative study. The entire national and international provisions and guidelines on CSR were only referred to illustrate the current CSR system which is related to Indonesia's current situation. The strategy was also adopted for the purpose of comparative learning.

3.3 Research Scope

This research mainly discusses the CSR mandatory policy from the view point of legal perspective rather than from the business or accounting perspective. Mandatory CSR has been enshrined into Act Number 40/2007 of Company Liability Act. It brings a significant public impact especially to the companies within the business sectors that are related to natural resources

exploitation. A few of the following rules and regulations (both national and international) would constitute the scope of study:

1. Indonesian National Legal Instruments

1. Company Liability Act Number 1/1995
2. Company Liability Act Number 40/2007
3. Constitutional Court Verdict Number 533/PUU-VI/2008 on Mandatory CSR
4. Environmental Management and Protection Act Number 32/2009
5. Investment Act Number 25/2007
6. State Owned Company Act Number Number 19/2003
7. Oil and Gas Act Number 22/2001
8. Micro, Small and Medium Scale Enterprise Act Number 20/2008
9. Social Prosperity Act Number 11/2009
10. Coal and Minerals Mining Act Number 4/2009
11. Forestry Act Number 19/2004
12. Water Resources Act Number 7/2004
13. Governing Aceh Act Number 11/2006
14. Government Regulation Number 93/2010 on National Disaster Donation, Research and Development Donation, Educational Facility Donation, Sport Development Donation, and Social Infrastructure Development Expenses (can be deducted from Bruto Revenue).
15. Government Regulation Number 47/2012 on Corporate Environmental and Social Responsibility.

2. International Legal Instruments

1. Organization for Economic Co-operation and Development Guidelines for Multinational Enterprises
2. The 10 (Ten) Principles of the United Nations Global Compact
3. The United Nations Guiding Principles on Business and Human Rights
4. The ILO Tripartite Declarations of Principles on Multinational Enterprises and Social Policy
5. The ISO 26000 Guidance Standard on Social Responsibility

3. 30 (thirty) experts opinions consisting of corporations, business associations, academics, CSR practitioners, CSR Non-Governmental Organizations and government officials' representatives. The list of all 30 (thirty) expert persons are as follows;

1. Investment Coordinating Board Republic of Indonesia
2. Ministry of Environment Republic of Indonesia
3. Ministry of Social Republic of Indonesia
4. Ministry of State Owned Company Republic of Indonesia
5. Ministry of Cooperatives, Small and Medium Enterprises Republic of Indonesia
6. Ministry of Energy and Mineral Resources Republic of Indonesia
7. Constitutional Court Republic of Indonesia
8. Lingkar Studi CSR/A+ CSR Indonesia
9. Director of National Center Sustainability Report (NCSR)
10. Indonesian Good Governance Commission
11. Bank Rakyat Indonesia (BRI)

12. PT. Jamsostek
13. PT. Sinaraya Trading
14. Arun Natural Gas Liquefaction Company
15. Pertamina Geothermal Energy Company
16. Pancasila University
17. Krida Wacana Christian University
18. Special Task Force for Upstream Oil and Gas Businesses Republic of Indonesia (SKK MIGAS)
19. National Team for Accelerating Poverty Alleviation (TNP2K)
20. National Humanitarian Aid Agency (PKPU)
21. Microfinance Innovation Center for Resources and Alternatives (MICRA)
22. Indonesian NGOs Forum for Conserving Environment (WALHI)
23. Indonesian Corruption Watch (ICW)
24. Indonesian Legal Aid Foundation (YLBHI)
25. Indonesian Youth for Law Enforcement
26. Young Generation of People's Advocates (GEMPAR)
27. Indocita Foundation (Independent CSR Consultant)
28. Andrew Tani & Co (Independent CSR Consultant)
29. Publish What You Pay (PWYP) Indonesia
30. Indonesia Working Group for Business and Human Rights (IWGBHR)

The samples of this research is made of 30 expert persons consisting of corporations, business associations, academics, CSR practitioners, CSR Non-Governmental Organizations and government official representatives. These samples are very limited because the mandatory CSR legal provision is a newly applied mechanism and not a voluntary one. Thus, not all people are aware of it. The researcher chose the 30 (thirty) experts person based on the observation of each institution engaged with CSR or individual expertise on CSR. However, it was expected that the researcher may further explore to get the most updated data on mandatory CSR from the ground to support the primary legal data. Finally, all of the primary data was collected through face-to-face interview method based on prior appointment.

3.4 Types of Data

In a qualitative research, there are two sources of data namely verbal and nonverbal data sources.³²² Verbal data consists of letters, interviews, and fieldnotes. Nonverbal data consists of film, video, print documents and art.³²³

In relation to this research, the data would be classified into two categories as follows:

3.4.1 Primary Data

Some primary legal data is used in this research such as acts, statutes, laws, regulations, jurisprudence, and treaties.³²⁴ These data are going to support all the secondary data which have been gathered.

³²² Lisa M. Given (Ed), *“The SAGE Encyclopedia of Qualitative Research Methods, First Edition,”* [Los Angeles, SAGE Publication, Inc, 2008], 186.

³²³ Ibid

³²⁴ Salim HS and Erlies Septiana Nurbani, *“Penerapan Teori Hukum pada Penelitian Tesis dan Disertasi,”* [Jakarta, PT RajaGrafindo Persada, 2013], 16.

Primary data is the major data and is supported by the secondary data. The research is not a quantitative research but several supportive quantitative data would be included to support the findings. Interviews with 30 (thirty) experts and key persons were conducted to obtain the most updated information on the current CSR policy development in Indonesia.

3.4.2 Secondary Data

Secondary data is the complementary source of data for this pure normative legal research. The secondary data comprises thesis, magazines, unpublished laws and regulations, books, journal articles, newspapers, field notes, unpublished papers, unpublished thesis, and unpublished journal articles.³²⁵ The use of secondary data would enable the researcher to find relevant concepts, thoughts, past research, and theories that will facilitate in answering the research questions and objectives. The secondary data also served to support the primary data.

3.5 Data Collection Methods

In this research, at least three types of data collection methods that are often scientifically and usually used in pure normative legal researchers would be adopted in this study. The methods are observation, library search and structured interview.³²⁶ The research has adopted the following data

³²⁵*Op. Cit*, Soerjono Soekanto dan Sri Mamudji, “*Penelitian Hukum Normatif Suatu Tinjauan Singkat*,”[Jakarta, PT. Rajagrafindo Persada, 2003], 119.

³²⁶Sugiyono, “*Metode Penelitian Kombinasi (Mixed Methods)*,”[Bandung, Alfabeta, 2011], 288.

collection methods: library search and structured interview-which involved interviewing certain governmental officials and CSR experts in Jakarta, Indonesia. The observational method through field notes enabled the researcher to recognize current phenomena, challenges, advantages, and disadvantages regarding the mandatory CSR implementation in Indonesia.

More details were obtained through library search and structured interviews. Furthermore, it is expected that through the library search, data from several sources such as books, seminars or international conference proceedings, unpublished papers, unpublished laws and regulations, laws and regulations, electronic data, focus group discussion reports, magazines, theses, dissertations, and newspapers can be obtained.

Then face-to-face interview session with several corporate social responsibility experts consisting of representatives from academics, companies, governmental officials and nongovernmental organizations was expected to produce several field data that can strengthen the primary data. The interview method would significantly facilitate in collecting the most updated CSR data from the ground as part of the overall data collection of the research.

3.6 Analysis of Data

Firstly, all collected data would be interpreted by the following legal reasoning or interpretation methods: systematic, historical and comparative, all of which were based on their characteristic.³²⁷ The method enabled the researcher to analyse the past, current and expected future situations on

³²⁷ Shidarta, "*Hukum Penalaran dan Penalaran Hukum*," [Yogyakarta, Genta Publishing, 2013], 170.

mandatory CSR either on its regulatory framework or on its implementation strategy. Secondly, the data was presented by using inductive analytical descriptive method.³²⁸

Inductive analytical descriptive method was chosen because it allows the researcher to systematically and scientifically explain, define, examine, determine and even provide conclusions to the problems, research questions, current situations and several reasonable solutions. All the data would strengthen each other, which would also prevent misinterpretation of the data or having data that is unconnected to one another. Subsequently, the interview results would be analysed by using content analysis.³²⁹

The content analysis enabled the researcher to explain further the research questions. Later on, a written description was included to explain each research question. This method helped the researcher to lay out the interview data in order to answer the research questions.³³⁰ Finally, in-depth analysis by using inductive analytical descriptive method was utilized to conduct a deeper analysis in order to answer the research questions and research objectives.

³²⁸Abdurrahman Soejono, “*Metode Penelitian Suatu Pemikiran Dan Penerapan*,” [Jakarta, Rineka Cipta, 2005], 147.

³²⁹Matthew B.Miles & A.Michael Huberman, “*An Expanded Sourcebook Qualitative Data Analysis, Second Edition*,” [California, SAGE Publications, Inc. 1994], 240.

³³⁰Ibid

CHAPTER FOUR

FINDINGS:

PHILOSOPHICAL RATIONALE OF MANDATORY CORPORATE SOCIAL RESPONSIBILITY LEGAL PROVISION IN INDONESIA

4.1. Introduction

This chapter discusses some findings and issues of the philosophical rationale behind the enactment of the mandatory CSR legal provision in Indonesia. The findings were based on field interview sessions with 30 (thirty) respondents. The chapter elaborates the philosophical rationale from several different viewpoints, which are the mandatory CSR legal provisions from environmental, social, and economic empowerment perspectives. Further, the discussion also indicated CSR legal awareness, CSR legal substance, legal structures, and legal culture. At last, the discussion provided a comprehensive situation on the philosophical rationale behind the enactment of the mandatory CSR legal provision in Indonesia.

4.2. Mandatory CSR Legal Provision from Environmental Perspectives

Basically, the idea of CSR is that business enterprises are required to be more responsible in fulfilling their legal responsibility to their shareholders, employees, suppliers, or customers.³³¹ Before the enactment of the new Limited Company Liability Act³³², Indonesia had an old version of

³³¹ Fred Robins, *“The Future of Corporate Social Responsibility,”* [Adelaide, Palgrave Macmillan Ltd, 2005], 96.

³³² Act No.40/2007 on Limited Company Liability.

the Limited Company Liability Act³³³. Act Number 1 Year 1995 has no legal provision on mandatory CSR or even CSR in general.

During the time, voluntary CSR as a traditional way and strategy for CSR implementation is still being used by most companies in Indonesia including the natural resources-based companies. Most of companies are from diverse sectors. They include manufacturing services and natural resources-based companies, which have their own initiatives to draft and to implement their own CSR projects. There is no specific national manual and guidance or own CSR integrated standard to be followed by these companies.

The Porong Sidoarjo mud disaster was one of major reasons that prompted the enactment of the CSR provision as a mandatory and legal responsibility.³³⁴ The mud disaster had affected a lot of people and had sunk at least three villages around the drilling area. It became a national wide disaster news and discussion among NGO activists, government officials, and internationally interested people and organizations. Then, it became a leading disaster issue related the environmental destruction inflicted by companies during the revision of the Limited Company Liability Act.

Broadly, environmental issue was a major background that prompted the enacting of the mandatory CSR legal provision in Indonesia. There was a lesson learnt from the gulf environmental disaster in Minahasa, North Sulawesi Province and the mud disaster in Porong Sidoarjo, East Java Province whereby natural resources-based companies is allegedly can be a

³³³ Act No. 1/1995 on Limited Company Liability.

³³⁴ Minutes of Meeting on Act No. 40/2007 on Limited Company Liability's legal drafting discussion.

violator of gross human rights to the people around their operation areas. Therefore, there should be a provision that prevents these companies from inflicting such destructions by enacting a mandatory CSR provision. Following that point, companies should try to build a trust from the society, and they should be more socially and environmentally responsible.

National and international communities should pay more attention to social and environmental issues in which companies are operating their businesses. Social capital is a major factor for companies to conduct their businesses in certain changing areas. Social capital comprises of relations of trust, reciprocity, common rules, norms and sanctions.³³⁵ All these elements are influenced by the operational business of certain companies. Social capital should be developed by the company to obtain a social license from the society. This can be reached if the companies demonstrate a socially and environmentally relevant policy.³³⁶

Nevertheless, disasters that occur from mining activities in a particular area are either natural or caused by human error. According to R12, article 74 on CSR was an initiative of the members of the representatives who were also members of the Working Committee.³³⁷ They considered that increasing social responsibility and corporate environments will require a formal setting in the legislation³³⁸

³³⁵ Jules Pretty and Hugh Ward, "*Social Capital and the Environment*," [United Kingdom, Vol. 29 No. 2 Elsevier Science Limited, 2001], 207.

³³⁶ *Ibid*

³³⁷ Interview on 30 September 2013 in Jakarta.

³³⁸ *Ibid*

In contrary with above view, R4 mentioned that the government that was led by Vice President Jusuf Kalla during the regulation drafting discussion, had strictly declined CSR as a legal obligation because the essence of CSR itself was as a voluntary activity.³³⁹ However, members of the House of Representatives' standing committee remained adamant to include Article 74,³⁴⁰ although later there were a number of negotiations- the 2.5% removal of the value of CSR allocation and further adjustment- would be implemented in accordance with government regulations.³⁴¹ The refusal of the government delegation since the beginning of the preparation and discussion of CSR mandatory legal provision Article 74 were clear evidences that the government did not agree with Article 74.

Such condition obviously clarified that the government did not agree with the provision of mandatory CSR to be included to the revision draft of the Limited Company Liability Act. Therefore, R12 stated that we need a political will of the government to implement Article 74 and as well as supervision from the legislatives related to the implementation of the article.³⁴²

A number of negotiations conducted by the legal drafting team from the legislatives have further led Article 74 to remain in Act No. 40/2007 in Limited Company Liability. A group of entrepreneurs who were members of KADIN, IWAPI and HIPMI had proposed a judicial review to the constitutional court relating to Article 74. This is because since the beginning,

³³⁹ Interview on 15 September 2013 in Jakarta.

³⁴⁰ Ibid

³⁴¹ Ibid

³⁴² *Op. Cit.*, Interview on 30 September 2013 in Jakarta.

the business associations have been rejecting the enactment of CSR as a legal responsibility.³⁴³

According to data from the PROPER section of the Ministry of Environment, there were 283 companies in 2001 that received red ratings as they had violated the laws and regulations in the field of environment. Another 49 companies were ranked black from the total number of 995 companies which have followed the company's performance appraisal programme in environmental management (PROPER).³⁴⁴

The recent high number of companies violating against the environment is the evidence that despite the existence of written laws and regulations on environmental issues, a lot of companies are still not complying with the legislation. This is particularly when the CSR is not textually set or is conducted only voluntarily and not incorporated into laws and regulations. In such cases, it can be ascertained that these companies will be reluctant because they assume that CSR is a supplementary activity and is not a strategic programme priority for their companies.

CSR is indeed an activity programme to reduce the adverse impacts caused by the companies on both the society and the environment. CSR is actually beneficial for the company itself and the environment around the company if the company is carrying out CSR programme as part of their corporate strategy and is implementing it as in a scheduled, planned and measured activity. Thus, the inclusion of Article 74 on social and

³⁴³ Ibid

³⁴⁴ PROPER Publication 2011-2012, *Ministry of Environment Republic of Indonesia*, <http://proper.menlh.go.id/portal/?view=1&desc=0&iscollps=0&caption=PROPER>, [Accessed on 26th December 2013].

environmental responsibility by the members of Working Draft Committee for Bill No.40/2007 Limited Company Liability is in accordance with the spirit and expectation of the local and international community regarding the importance of environmental protection and preservation.

Article 74 on corporate social and environmental responsibility is not meant to take the CSR funds allocated by the company to be submitted to the central government or local governments; it is meant for the CSR funds to be allocated for the company in order to reduce, mitigate or compensate for the negative impact caused by the companies on society and environment.³⁴⁵

If the business enterprises realize that the allocation of CSR funds is beneficial for resource sustainability and its relationship with the environment around their business operations. Then, they can be ascertained that the rollicking company will allocate funds and use them for various CSR activities on environmental protection and preservation.

Based on the researcher's analysis, it was found that there are several inhibiting factors that can prevent the implementation of mandatory CSR legal provision in Indonesia. The factors are:

1. Legal substance: the substantive law governing the implementation of CSR programme in Indonesia of which the drafting process did not involve various components of related stakeholders. Further, there are only seven articles which is contradicting with the complexity of the CSR problems in Indonesia.

³⁴⁵Ibid

2. Legal Structure: the sectoral CSR implementation by some different ministries that leads to difficulty in conducting coordination and communication between one ministry and another. Then, each Ministry seems to go alone by its own policies in the field regarding the implementation of CSR. It needs to be considered to establish a free and independent CSR institution in Indonesia, which serves (a) to prepare and publish a variety of CSR-related policies, (b) to implement the monitoring and evaluation process, and (c) to establish an effective and transparent reporting system, punishment and rewards mechanism to companies that are not running the CSR programme well and companies that run the programme as expected.

3. Legal Culture: the legal culture in Indonesia is based on the positivist or formalism paradigm rather than the realism paradigm in which the new law is presumed to exist if there are written rules. Meanwhile, if there is no written rule, it is not regarded as a rule. It is therefore necessary to have a national CSR guideline in Indonesia that not only provides practical guidance for companies in implementing CSR programme, but also serves as guidance for the government and the public to gauge the level of success of the CSR programme.

The existence of the several inhibiting factors above necessitates the existence of an extra hard effort of the parties with an interest in CSR issues in order for the government to play its significant role in reducing or even completely eliminating all the limiting factors with its power and authority.

The government should not only hear the aspirations and interests of a single group (business enterprises) but they should also listen to the

aspirations and interests of other groups such as the intended beneficiaries and NGOs who have been concerned with the issues of CSR. Further, R12 stated that the inclusion of Article 74 in Act No. 40/2007 of Limited Company Liability was due to the pressure from the public and NGOs on the Parliament Legal Drafting Working Committee on Limited Company Liability Bill.³⁴⁶ Therefore, in preparing and discussing of the regulations on implementing Article 74, the government has to involve NGOs and community elements as part of the legal drafting team.

Overall, after studying the data and facts on the ground, it was concluded that the CSR mandatory legal provision was included in Act No. 40/2007 due to the following reasons:

1. The number of cases in the field of environmental violations committed by the company prior to the enactment of Article 74 has made CSR a legal obligation for companies operating in natural resources exploitation.³⁴⁷
2. The provision can act a way to prevent a repetition of the environment destruction by the companies when carrying out its business operations.³⁴⁸
3. The provision is a means of reduction to the adverse impact of a company's business activities.
4. The provision is a means of damage mitigation or to counter the adverse effects caused by the company's operations in a particular area.³⁴⁹

³⁴⁶*Op. Cit.*, Interview on 30 September 2013 in Jakarta.

³⁴⁷ Siti Maimunah, Aminuddin A. Kirom, Tracy Glynn, etc, *Tambang dan Pelanggaran Hak Asasi Manusia: Kasus-kasus Pertambangan di Indonesia 2004-2005*, [Jakarta, Jaringan Advokasi Tambang, 2007], 22.

³⁴⁸ Notes of Academic Study Act No. 40/2007 on Limited Company Liability.

³⁴⁹ *Ibid*

5. The provision can act as a compensatory mechanism towards the adverse effects caused by the companies' business activities.³⁵⁰

Thus, R4 mentioned that even mandatory CSR legal provision is beneficial for the community as stakeholders, but companies and business associations still refuse to implement CSR as a legal obligation.³⁵¹ In addition, R12 mentioned that the rejection of a number of Article 74 by business associations and companies provided evidence to the public, especially the victims of the company's business activities, which the companies are reluctant to be bound and burdened by legal responsibility for all their business actions that have led to a variety of environmental damages and disasters.³⁵²

Therefore, the victims and the people whose territory would serve as the mining companies' operations, along with the NGOs, must continue to fight for their rights so that the companies would remain burdened with legal responsibility and legal liability for their actions that could cause harm morally and materially as a result of the destruction of the environment caused by their presence.

With regards to the restrictions, number, and type of compensation mechanism that must be provided by the company, they required to facilitate a joint meeting that involve companies, communities, governments and other relevant groups.³⁵³ Further discussions with the relevant stakeholders are also necessary in order for the above mentioned aspects to be included in the implementation regulations of the CSR. However, the interests and

³⁵⁰ *Op. Cit.*, Notes of Academic Study Act No. 40/2007 on Limited Company Liability.

³⁵¹ *Op. Cit.*, Interview on 15 September 2013 in Jakarta.

³⁵² *Op. Cit.*, Interview on 30 September 2013 in Jakarta.

³⁵³ *Ibid*

aspirations of the people, especially the victims, are protected by the law in accordance with the current legislation.

4.3. Mandatory CSR Legal Provision from Social Perspectives

Corporate social responsibility is a noble way for corporations to behave more socially and environmentally responsible to the social circumstances around their business operations.³⁵⁴ Basically, CSR programme is implemented in order to improve the social welfare of the people especially those around the corporate environment.

Before the presence of mining companies in their village, people were living in deprivation socially and economically. Then, the presence of the companies in their region has directly and indirectly brought benefits to the local communities socially, culturally and economically.

According to the data from the Ministry of Social Affairs of the Republic of Indonesia, the several social types are as follows: poverty, neglecting, disability, remoteness, social behavioral aberrations, disaster victims and victims of violence, exploitation and discrimination.³⁵⁵

Nevertheless, it is certainly not the responsibility of companies to solve all the social problems. The responsibility to empower eliminates all the social issues are the government's because the state is given a full mandate by the constitution to empower the poor.

³⁵⁴ Henry Mintzberg, *The Case for Corporate Social Responsibility*, [United Kingdom, Journal of Business Strategy; 1986], 3.

³⁵⁵ Ministry of Social Manual on Corporate Empowerment and Social Responsibility in Establishing Social Welfare.

It was clearly and explicitly mentioned in the 1945 constitution of the Republic of Indonesia that the state would create a system of social security for all the poor and provide good health-care and public service facilities.³⁵⁶ It is the state's obligation to take a greater role in empowering the poor, the neglected children in Indonesia and people with other social problems.

One of the important elements in the CSR programme is the activity on the social aspect. However, R6 stated that social aspect of CSR needs to be described in further detail, particularly on the limitations of social activities that could be funded by the CSR programme and also the position of Government on the programme.³⁵⁷ It needs to be clearly defined is also the extent of corporate responsibility in which a certain company can support social, environmental and economic empowerment programmes. There must be a clear description of works related to each CSR's stakeholders positions and functions.

Further, R18 stated that if the extent of responsibilities are clearly mentioned, then the enterprises, the government and the community will be able to work together to carry out their obligations in according to their own roles and responsibilities.³⁵⁸ The obligation description is to avoid any overlapping of responsibilities between the companies, the society and the government.³⁵⁹ It can also avoid the companies' perception that the government seem to be off-handed with their responsibility in tackling

³⁵⁶Consitution Republic of Indonesia Article 34 clause (1) "Impoverished persons and abandoned children shall be taken care of by the State" and clause (2) "The State shall develop a system of social security for all of the people and shall empower inadequate and underpriveleged in society in accordance with human dignity", clause (3) "The State shall have the obligation to provide sufficient medical and public services facilities"

³⁵⁷ Interview on 17 September 2013 in Jakarta.

³⁵⁸ Interview on 19 October 2013 in Depok.

³⁵⁹ Ibid

poverty and other social problems. Hence, it is necessary to be stated in the legislation and regulations on the roles, functions, duties and responsibilities of each party, both the government and the companies.

In addition, R3 mentioned that companies can assist the local community in solving social problems which are directly related to the business activities of the companies such as unemployment, women's empowerment, youth empowerment, and financing of social activities.³⁶⁰ These areas can improve the companies' harmonious relations with the communities.³⁶¹

Social problems faced by the local community such as unemployment can be overcome by the company by providing access to employment in the enterprise. These companies can also provide entrepreneurship training for youth and other groups who are interested in developing their entrepreneurial skills.

In fact, skills enhancement training can be delivered to farmers and companies employees who are part of the social aspects of the CSR programme. It can be executed by the company on an ongoing and regular basis. Further, R22 stated that microfinance management training, technical marketing strategies, management and human resource management will improve the members of society's capacity and capability in improving their quality of life.³⁶²

³⁶⁰ Interview on 13 September 2013 in Jakarta.

³⁶¹ Ibid

³⁶² Interview on 24 October 2013 in Jakarta.

Commonly, not all members of the community in the surrounding area are interested to become labour and work in the company. Some of them should have goals to become successful entrepreneurs. The companies can facilitate their willingness by providing a variety of facilities, training and other infrastructures as necessary.

In other side, according to R14, the involvement of other vulnerable groups such as street children, beggars, the handicapped, women and children, and scavengers can make CSR programmes on social aspect to be more beneficial for the entire community.³⁶³ However, this does not mean that the government does not implement any supporting programme to support the implementation of CSR programmes undertaken by the companies. The government should also provide supporting programmes to strengthen companies' CSR programme so that there will be synergic and strategic partnerships between business enterprises, governments and society.

As a comparison, According to R20, companies based in rural areas will not find the vulnerable groups such as disabled people, beggars, scavengers, and street children in significant number because these vulnerable groups are mostly present in urban areas.³⁶⁴ However, companies located in rural areas will be in contact with vulnerable groups such as women and children, indigenous peoples, and persons with disabilities.³⁶⁵

R18 mentioned that it is necessary to have a social and community mapping needs assessment in advance for any company intending to

³⁶³ Interview on 3 October 2013 in Jakarta.

³⁶⁴ Interview on 21 October 2013 in Jakarta.

³⁶⁵ Ibid

implement CSR programme in a certain area.³⁶⁶ However, different business sectors will have different impact on the interests, strategies, approaches and stakeholders.³⁶⁷

The innovation and improvement of social programme is the most important part that should be a priority for every company in order for people to feel the positive benefits of its presence. Further, R23 mentioned that it is necessary not to let people feel overwhelmed or even disturbed by the presence of the company.³⁶⁸

Nevertheless, in the past, there were many cases in which, the company used security forces in certain areas to safeguard the interests of business rather than to build a good relationship with the community through social and the economic approaches. Such cases occurred because of that time, the company assumed that by using the power of the security forces they could accelerate the achievement of their interests.

In fact, for the long-term interests, such ways would be very detrimental to the credibility and would disrupt the chain of the company's sustainability because people will continue striving to promote their aspirations and interests. Moreover, with the improvement of communication media and NGOs incessant fighting for the aspirations and interests of the community, the situation would further exacerbate the gap between the company and the community. Therefore, R18 emphasized that companies

³⁶⁶ *Op. Cit*, Interview on 19 October 2013 in Depok.

³⁶⁷ *Ibid*

³⁶⁸ Interview on 28 October 2013 in Jakarta.

should strive to change the policy paradigm that tends to see people as objects rather than as the subject of development.³⁶⁹

Social problems arising around the company will be very varied and will always change from time to time. Hence, the company must also conduct an ongoing effort to participate in solving them or provide a solution to handle the social problems. For sure, there will be limitations of responsibility and the liability of programme in social empowerment of the community between the company and the state. This is because companies have a limited budget and human resources, while the state has unlimited resources in terms of finance and human resources.

Further, besides carrying out the social CSR programme, business enterprises must also pay high taxes to the state either at the national or the sub-national level. So this seems to be another constraint faced by the company in empowering communities. Therefore, the implementation of CSR mandatory legal provision should be followed by a tax holiday policy. Then, all the tax they obliged to pay to the state can be converted to the company's carrying out a variety of social empowerment programme.

4.4. Mandatory CSR Legal Provision from Economic Empowerment Perspectives

According to R21, CSR is a systematic and planned effort undertaken by a company in order to boost society's economy.³⁷⁰ Many companies use economic empowerment pattern by empowering cooperatives, small and

³⁶⁹ *Op. Cit*, Interview on 19 October 2013 in Depok.

³⁷⁰ Interview on 22 October 2013 in Jakarta.

medium enterprises in implementing their CSR programme. What needs to be considered is that the companies should develop a better economic empowerment system such as by including cooperatives and small- and medium-sized enterprises into their supply chain.

According to R5, economic empowerment pattern through a low interest aid to groups of cooperatives and small and medium enterprises have to be synergic with similar empowerment policies and programme undertaken by the Ministry of Cooperatives, Small and Medium Enterprises of the Republic of Indonesia.³⁷¹ This would avoid overlapping and repetition of the mandatory CSR programme. Further, R7 stated that it is believed that strong coordination, communication and strategic partnership between the companies and the Ministry may increasingly provide value added to the independency and the development of cooperatives and small and medium enterprises, especially in areas where the companies operate.³⁷²

Most companies still perceive cooperatives and small and medium enterprises as groups that are beyond the companies' business activities. Thus, the pattern of economic empowerment seemed to be done by using conventional methods. The strengthening of cooperatives and small and medium enterprises can be achieved if the companies combine the pattern of empowerment with the integration of a CSR programme.³⁷³ This is because while government provides soft grants in the amount of trillions dollars to co-

³⁷¹ Interview on 17 September 2013 in Jakarta.

³⁷² Interview on 18 September 2013 in Jakarta.

³⁷³ Ibid

operatives and small and medium enterprises, many of them are not able to access these loans which are not bankable.³⁷⁴

Further, R10 mentioned that a large number of not bankable cooperatives, small and medium enterprises are one of the responsibilities of the companies to empower them by CSR programme.³⁷⁵ It should help them to be bankable and have direct access to the capital in the bank. They should be able to access the capital that provides low-interest loans for cooperative groups, small and medium enterprises.

Thus, CSR interventions are not always channeling cash funds into cooperative groups, small and medium enterprises which turned out a lot to make them more dependent and not bankable.³⁷⁶ In fact, many of these loans are used not for their core business purpose but are used for other commercial purposes that are not related directly to their business.

The method of economic empowerment by combining integration and technical support method is used to empower cooperatives, small and medium enterprises to be bankable. It can be applied by the companies as an alternative solution against the current patterns of conventional economic empowerment. The companies should not only pursue CSR spending rate funds available in the budget of the company but also should make efforts of empowerment patterns that will further strengthen the presence of cooperatives, small and medium enterprises.

³⁷⁴Ibid

³⁷⁵Interview on 27 September 2013 in Jakarta.

³⁷⁶Ibid

The method of economic empowerment through the integration method is also in accordance with the recommendation of Millennium Development Goals (MDGs).³⁷⁷ It suggests a partnership between companies, governments and society in poverty reduction and improving the people's welfare. It needs a rule in writing to make it all becomes real. In addition, R8 stated that it needs a clear manual that provide clear guidelines and explaining about the role, functions, duties, responsibilities and authority of the companies in the implementation of CSR programmes.³⁷⁸

Economic empowerment is a key important aspect for empowering beneficiaries who are living around the companies operation. Most of the people there only aware of CSR programmes as a cash money assistance. They do not aware of sustainability factor of the CSR programmes. It needs a specific attention to the priority needs of the local community.

Therefore, R27 stated that it needs a clear guidelines to be used by the companies in delivering their CSR-based economic empowerment programmes.³⁷⁹ The absence of clear and written guidelines so that the pattern of economic empowerment as defined above will not be performed well in line with beneficiaries's expectations.

Afterwards, some evidences were found from the ground that the the presence of mandatory CSR legal provision has still nnot touched the basic interest of majority of beneficiaries in Indonesia.³⁸⁰ There are no specific guidelines on the implementation of mandatory CSR and no leading

³⁷⁷ Ibid

³⁷⁸ Interview on 25 September 2015 in Depok.

³⁷⁹ Interview on 30 September 2013 in Jakarta.

³⁸⁰ Ibid

ministries or governmental body in-charged with the supervision, monitoring, and evaluation of the implementation of mandatory CSR legal provision.

R4 stated that misperception about CSR programme is one of inhibiting factors towards the successful implementation of CSR programme.³⁸¹ It is because of the public assumes that the CSR programme is a corporate donation programme. It seems just like a kinds of corporate's responsiveness towards the social and environmental conditions by the companies in which they operate.

The wrong perception must be straightened out by governments, companies and NGOs.³⁸² So that more people will understand that CSR programme is not solely charitable programmes in the form of cash donations to the community. Society must fully understand that CSR programme is part of the company strategies in order to empower the public in social, environmental and economic aspects.

4.5. Legal Substance on Mandatory Corporate Social Responsibility In Indonesia

It was pointed out that the existence of such large and seductive CSR funds would make various ministries and local governments try to make CSR funds as an alternative fund to finance government programmes. Despite, it needs to keep in mind that the government cannot automatically assign the responsibility for the development and fulfillment of social welfare to the company because they are also subject to a high tax. According to R28, each

³⁸¹ *Op. Cit.*, Interview on 15 September 2013 in Jakarta.

³⁸² *Ibid.*

year the total tax to be paid by oil and gas companies to the government is in the amount of 40% of total net revenues.³⁸³

R8 mentioned that the clarity of legal substance on mandatory CSR is really important to implement the legal provision.³⁸⁴ Further, it needs to harmonize all the authorities on CSR policy making based on sectoral law into a single government's policy.³⁸⁵ The policy could be an Act or government regulation. In the absence of a clear government's policy then the implementation of mandatory CSR legal provision would not be going smoothly.

If the government really wants to hand over their responsibility in delivering social welfare to the companies, the companies must create a system that is able to carry out the responsibilities of the government. Moreover, According to R4, if the government want to share its responsibility with the company in the public welfare, the government must also be fair to the company by offering a number of incentive packages and other attractive economic policies.³⁸⁶

Further, R17 pointed out that the presence of the company's investment in a region in fact has highly improved economic growth in the region. Other benefits include increased employment and business opportunities³⁸⁷ However at the same time, R24 stated that companies are also required to be socially and environmentally responsible for the

³⁸³ Interview on 31 October 2013 in Jakarta.

³⁸⁴ *Op. Cit.*, Interview on on 25 September 2013 in Depok.

³⁸⁵ *Ibid.*

³⁸⁶ *Op. Cit.*, Interview on 15 September 2013 in Jakarta.

³⁸⁷ Interview on 18 October 2013 in Jakarta.

sustainability of society and the environment around their operational areas.³⁸⁸

On the other hand, government should not constantly provide a number of workload to the companies with various corporate strict rules. At the same time do not provide attractive economic package that can drive interest for companies to implement CSR properly. Concepts, strategies and good, equitable and sustainable CSR policy development must be reflected in the laws and regulations in Indonesia.

Based on the analysis for the researcher, there are several laws and regulations discussed on CSR or CSR as a source of funding. The diversity of laws and regulations is governing CSR or making CSR as an alternative source of funding for government programmes. So that it is necessary to have CSR guidelines that can accommodate cross-cutting interests of both national and local. This is to avoid CSR funds to be a source of corruption and fraud by parties that are not socially and environmentally responsible.

4.6. Legal Structure on Mandatory Corporate Social Responsibility in Indonesia

There is no official institution which acts as regulator, monitor, evaluator or receiver of reporting from companies that implement mandatory CSR programmes in Indonesia. Mandatory CSR legal provision in Indonesia has not yet been implemented well because no official ministry or state institution is responsible to pass further executing regulation. Currently, Its

³⁸⁸ Interview on 28 October 2013 in Jakarta.

policy is being passed by the relevant sectoral ministries. In fact, within almost 6 (six) years of the enactment of Article 74 on Social and Environmental Responsibility, there has not been in place any system of monitoring, standardized evaluation and reporting, effective and well-planned organized by each of the relevant ministries. Therefore, it appears that the government in this case the relevant ministries- has not been seriously implementing the article 74.

R13 stated that they are currently evaluating that the implementation of the Partnership and Community Development in the Ministry for the component activities of the partnership is not a CSR activity.³⁸⁹The partnership programmes include activities of savings and loan programme with low interest rates. These activities which are provided by state-owned enterprises to small and medium-sized businesses are selected in the respective areas of the MSOE operation.³⁹⁰

The absence of systematic monitoring, evaluation and reporting standard recently was because the MSOE was still skeptical about whether PKBL could be categorized as CSR programme or not.³⁹¹ However, the MSOE is drafting a blue print associated with the Standard Operating Procedures (SOP). It is expected can be used by SOEs in the implementation of their CSR programme. It is expected that the SOP can improve transparency and accountability in the implementation of CSR programme in the future.

³⁸⁹ *Op. Cit*, Interview on 1 October 2013 in Jakarta.

³⁹⁰ *Ibid*

³⁹¹ *Ibid*

However, the MSOE strongly supports the enactment of Article 74 on Corporate Social and Environmental Responsibility because the existence of Article 74 will encourage companies to comply with and care about the social and environmental aspects particularly around the area of operation. The MSOE observes that recently many companies were less adherence to the social and environmental aspects in which they operate. Therefore the MSOE hopes that with a CSR policy mandatory legal provision will encourage companies to carry out its social and environmental responsibilities consistently.

In addition, the MSOE also has a special section on CSR under the Deputy for Business Development and Restructure. It handles matters associated with CSR. The MSOE encourages strategic partnerships between companies and cooperatives and small and medium enterprises through CSR funds access for their development in Indonesia.

The MSOE has also issued a book consisted of examples of strategic partnership patterns between companies and cooperatives and small and medium enterprises in Indonesia. The book is based on the results of the assessment conducted by the MSOE on some patterns of CSR programme implementation activities undertaken by several companies in Indonesia.

Moreover, the Ministry strongly supports the enactment of Article 74 on Corporate Social and Environmental Responsibility in Indonesia because with the existence of the article, companies will be more socially and environmentally responsible. Until now, the MSOE does not have any

applied standard on the implementation of CSR programme within its authority.³⁹²

So far, the MSOE has not yet implemented the monitoring, evaluation and reporting systems on the mandatory CSR programme related to strategic partnerships between companies and cooperatives and small and medium enterprises. The MSOE defined CSR as a method of strategic partnership and strategy of economic empowerment between the company and cooperative groups, small and medium enterprises in order to boost economic growth. Therefore, the MSOE is increasingly encouraging for long-term partnership in the form of economic empowerment undertaken by companies on cooperative groups, small and medium enterprises.

Further, the Ministry of Social Affairs has also issued several other policies regarding the implementation of CSR in social aspect.³⁹³ Unfortunately, those policies are not intended to implement the mandatory CSR legal provision. The policies presented some important points of CSR roles and functions of the forum Social Welfare, programme priorities, scope, models and success indicators of a programme.³⁹⁴

The most interesting part about these guidelines is the evaluating and reporting of the CSR programme evaluation and reporting. Nonetheless, it requires further elaboration related to the factual verification method that will be conducted to verify the truth of the reports submitted by the implementing

³⁹²Ibid

³⁹³Minister Regulation of Social Affairs of the Republic of Indonesia No.13/2012 on Social Responsibility Forum of Business in Social Welfare.

³⁹⁴ Ministry of Social Republic of Indonesia, *Empowerment Guidelines for Corporate Social Responsibility in Accelerating Social Welfare* [Jakarta, Ministry of Social Republic of Indonesia, 22 November 2012],. v.

agency of the CSR programme. If the chance is given and it is clearly stated within the evaluation and reporting section, then there is a strong commitment toward the transparency and accountability developed by the Ministry of Social Affairs of the Republic of Indonesia in implementing the CSR programme. The commitment should be appreciated and continued to be developed so as to further improve the substance and methods of evaluating and reporting of the mandatory CSR programme.

Further, the R14 mentioned that Ministry of Social Affairs of the Republic of Indonesia has established a CSR forum called Social Welfare (*Forum CSR-Kessos*) at some provinces/districts/cities in Indonesia. As the first step, the forum will be set up in the provinces level, but it will be established in all districts and cities in the future.³⁹⁵ The forum is a gathering media for governments, companies and universities and community leaders. In fact, the CSR forum not only serve as a facilitator but also serve as an executing body for the implementation of CSR programme that have been agreed upon in the CSR forums.³⁹⁶

Such patterns of programme implementation have led to the companies' dependence on the government, and they have tended to government "intervention" and dependency in formulating and implementing the CSR programme. In addition, there would be an overlap between the role of government as a regulator and its role as an adviser, supervisor as well as the executive element of the forum activities. The government should serve

³⁹⁵*Op. Cit*, Interview on 3 October 2013 in Jakarta.

³⁹⁶*Ibid*

only as a regulator and should be only involved in the aspect of monitoring, evaluation and reporting of the CSR programme.

As with the Ministry of Energy and Mineral Resources (ESDM), the ministry also does not have a standard guideline related to the implementation of CSR programme for companies in the oil and gas sector. However, R9 stated that the ministry of energy and mineral resources is working on a draft regulation on corporate social and environmental responsibility in oil and gas sector.³⁹⁷ The draft regulation is expected to be a guide for companies to be engaged in the oil and gas sector in implementing other CSR programme.³⁹⁸

The Ministry of Energy and Mineral Resources has been conducting a series of Focus Group Discussions (FGD) as part of its effort to develop and publish policies on corporate social and environmental responsibility in oil and gas sector.³⁹⁹ The activity is aimed to obtain constructive feedback from the focus group participants in order to improve and perfect the concept and to draft the ministerial regulation on corporate social and environmental responsibility in the oil and gas sector.

Such real commitment from the Ministry of Energy is worthy to be appreciated by related stakeholders because the effort can fill the vacuum of policy on manual for the implementation of CSR programmes in the oil and gas industry sectors in Indonesia. Before drafting the regulations, the Ministry of Energy has already had some policies related to the reduction of the impact of environmental risks posed by the oil and gas industry.

³⁹⁷ Interview on 25 September 2013 in Jakarta.

³⁹⁸ Ibid

³⁹⁹ Focus Group Discussion (FGD), Social Risk and Impact Assessment Oil and Gas Industry towards Local Community [Jakarta, Ministry of Energy and Mineral Resources Republic of Indonesia, 4th October 2013].

The policies aim to reduce the impact of the environmental risks caused by the oil and gas industry.⁴⁰⁰ It includes reclamation and closure activities to be carried out in compliance with the environmental principles such as the quality of surface water, ground water, sea water, soil and air; it also intends to pay attention to the stability and security of overburden stockpiles, mined land and artificial structures (man-made structure), and to the biodiversity, social, cultural and economic aspects.⁴⁰¹

Moreover, the policy regarding the protection of consumer rights has also been published in which oil and gas companies are obligated to protect the rights of consumers including the security of supply and distribution of oil, the safety and security of oil and gas products, the projecting of reasonable prices of oil and gas, dose conformity and easy and on-time services.⁴⁰² In fact, there have been mitigation guidelines for volcanoes, earthquakes and tsunami disasters.⁴⁰³ These guidelines were issued in order to reduce the adverse impacts that may result from the mining activities.

The obligation of a mining license holder to conduct a feasibility study and Environmental Impact Assessment (AMDAL) study prior to carrying out mining activities is a realistic example of the Ministry of Energy's commitment to reduce the risks related to the mining activities.⁴⁰⁴ In fact, it should be clearly outlined in the feasibility study about the

⁴⁰⁰ Ibid

⁴⁰¹ Article 3 Ministry of Energy and Mineral Resources Regulation No.18/2008 on Reclamation and Mining Closure.

⁴⁰² Article 3 Ministry of Energy and Mineral Resources Regulation No.19/2008 on Consumer Protection Manual and Procedure in Downstream Oil and Gas Industry.

⁴⁰³ Ministry of Energy and Mineral Resources Regulation No.15/2011 on Guidelines for Disaster Mitigation of Volcano, Mountain, Landslides, Earthquakes, and Tsunami.

⁴⁰⁴ Article 13 clause (2) Ministry of Energy and Mineral Resources Regulation No.11/2009 on Geothermal Business Manual.

empowerment and community development planning that will be implemented by the business enterprise.⁴⁰⁵ Although the rules were very clear and firm, there has not been any regular report submitted by the oil and gas companies relating to their empowerment and community development activities especially those around the area of mining operations.

Some aspects of the law enforcement, monitoring, evaluation and effective, transparent and accountable reporting system have become an essential study in the implementation of good CSR governance. Even until today the Ministry of Energy is still in the process of formulating policies regarding the management and execution system on corporate social and environmental responsibility programmes. In addition, the procedure of affixing labels to energy-efficient lighting has also been published by the Ministry of Energy and Mineral Resources.⁴⁰⁶

Oil and gas companies who are willing to move their rig offshore facilities shall comply with the requirements as prescribed by the Ministry of Energy and Mineral Resources.⁴⁰⁷ The policy is an environmentally responsible policy which is aware of the human rights principles and standards in the field of the environment, and of the efforts to reduce the negative impact of dismantling offshore oil and gas installations. In fact, the policy of using new energy and renewable energy has also been published by

⁴⁰⁵ Article 14 point (d) Ministry of Energy and Mineral Resources Regulation No.11/2009 on Geothermal Business Manual.

⁴⁰⁶ Ministry of Energy and Mineral Resources Regulation No.06/2011 on Energy-Efficient Labelling for Eco-Friendly Lamp.

⁴⁰⁷ Ministry of Energy and Mineral Resources Regulation No.01/2011 on Technical Manual on Oil and Gas Offshore Facilities Dismantle.

the Ministry of Energy in order to support sustainable development in the energy sector.⁴⁰⁸

In addition, the policy of reducing 20% of electricity energy use in public facilities such as in state roads, the state officials, and state-owned enterprises is a green policy issued by the Ministry of Energy. The policy was created in order to reduce the adverse impacts of global warming and to adapt the behavior of a friendly environment.⁴⁰⁹ According to R9 such guidelines was an evidence that the Ministry of Energy and Mineral Resources is strongly committed to oversee the process of exploration and exploitation of oil and gas in Indonesia to be environmentally responsible.⁴¹⁰

Further, the Director-General is the one who will be in-charged of the formulation and implementation of policies and technical standardization in the Ministry of Energy.⁴¹¹ The Director General will supervise on the mining licenses issued by the governors and mayors in accordance with their respective authorities. The Ministry of Energy may cooperate with the Ministry of Interior or other relevant agencies to conduct its function in overseeing that those licenses were passed by the local government.⁴¹²

The instruments of internal control implemented by the Ministry of Energy shows that the administration of mining license must be carried out in a responsible manner by the governors and the mayors In the future, it is

⁴⁰⁸ Ministry of Energy and Mineral Resources Regulation No.10/2012 on the Implementation of Physical Activities of Utilizing Renewable Energy.

⁴⁰⁹ Ministry of Energy and Mineral Resources Regulation No.13/2012 on Saving Power Consumption.

⁴¹⁰ *Op. Cit*, Interview on 25 September 2013 in Jakarta.

⁴¹¹ Article 2 clause (1) and (2), Article 3 clause (1) and (2), Article clause 4 (1) and (2), Article 5 clause (1) and (2), Article 6 clause (1) and (2) Ministry of Energy and Mineral Resources Regulation No.02/2013 on Supervision towards Mining Activities Are Conducted by Provincial, District/City Government.

⁴¹² Article 2 clause (2) Ministry of Energy and Mineral Resources Regulation No.02/2013 on Supervision towards Mining Activities Are Conducted by Provincial, District/City Government.

necessary to be considered to involve an external supervisor from outside the Ministry of Energy and Mineral Resources in order to increase transparency and accountability. At this point, even though the regulatory framework that is related to CSR is passed by the ministry, they are not in line with the spirit of mandatory CSR. In other words, all the regulations must be revised accordingly to be in line with the spirit of mandatory CSR.

In addition to that, R2 mentioned that the Ministry of Environment of the Republic of Indonesia has also passed a few regulations that support the CSR implementation strategies in Indonesia.⁴¹³ Unfortunately, those regulations again and again does not explicitly state to support the mandatory CSR legal provision. The ministry has also issued a number of policies as well as guidance on the environmental aspects of implementing CSR programme.

Companies' compliance with the law and principles of human rights is at the same level with individuals' adherence to them even in certain cases. The level of companies' adherence to the principles of human rights must be more than the compliance level of an individual. This is because they have more resources and greater potential violations of human rights as contained in the United Nations Guiding Principles on Business and Human rights.

The legal structure of mandatory CSR in Indonesia should be encouraged to be developed in a better way. This is because the issue of CSR is a complex issue and related to various aspects of social life such as social, environment, law, human rights, economic empowerment, and culture.

⁴¹³*Op. Cit.*, Interview on 12 September 2013 in Jakarta.

Further, R30 stated that the mandatory CSR is an effective instrument to uphold the principles of the United Nations Guiding Principles on Business and Human Rights in the Indonesian context.⁴¹⁴ Therefore, the implementation system must be strengthened in order to be able to contribute significantly to the reduction of social and environmental risks due to the presence of extractive industries that tend to ignore their social and environmental obligations.

4.7. The Legal Culture on Mandatory CSR in Indonesia

The culture of the Indonesian law is positivistic in which people tend to obey written rules more than unwritten ones. In practice, the customary law is still recognised by the people of Indonesia even though in its application, it is only limited to the resolution of a misdemeanor such as the fights in village, light violence and violations of social norms.

In fact, in the Constitutional Court's decision regarding the constitutional review on Article 74 on Corporate Social and Environmental Responsibility against Republic of Indonesia 1945 constitution stated that the legal culture in Indonesia is different from the legal culture in which CSR was firstly introduced.⁴¹⁵ Then, the enactment of the mandatory CSR legal provision was intended to give a legal certainty for all citizens of Indonesia regarding the implementation of CSR programme.⁴¹⁶ At this point, the legal provision is also in line with the economic system of Indonesia, which is

⁴¹⁴ Interview on 7 November 2013 in Jakarta.

⁴¹⁵ Constitutional Court Verdict No. 53/PUU-VI/2008, [Jakarta, Constitutional Court, 2008], 83.

⁴¹⁶ Constitutional Court Verdict No. 53/PUU-VI/2008, [Jakarta, Constitutional Court, 2008], 64.

based on togetherness principle and not based on individualistic and liberal economic principle that is prevailing in western countries.⁴¹⁷

It was also obvious in the past for companies which ignored social and environmental responsibilities. There would have been many violations and environmental damage which caused remarkably moral and material lost. Especially for people who lived around the companies' area such as environmental case in Buyat Bay in North Minahasa regency, North Sulawesi by PT Newmont Minahasa Raya (NMR) and environmental cases of Porong mudflow in Sidoarjo, East Java, which was caused by PT Lapindo Brantas.

Environmental cases which clearly occurred in the field in which the company paid little attention to the environmental aspects of their activities from the operational phase of exploration and exploitation of natural resources. It caused tremendous disaster for the people in the surrounding area of the companies. Nevertheless, some business associations such as the Indonesia Chamber of Commerce and Industry (KADIN), the Indonesia Young Businessmen Association (HIPMI), and The Indonesia Business Women Association (IWAPI) in a lawsuit of constitutional review to the Constitutional Court rejected CSR as a legal obligation for some reasons:

1. CSR is an ethical and moral activity which is made as written rules in the Article 74 of constitution No.40/2007 on Limited Company Liability. Therefore, Indonesia is the only country in the world that formalizes CSR into laws and regulations.⁴¹⁸

⁴¹⁷ Constitutional Court Verdict No. 53/PUU-VI/2008, [Jakarta, Constitutional Court, 2008], 88

⁴¹⁸ Constitutional Court Verdict No. 53/PUU-VI/2008,[Jakarta, Constitutional Court, 2008], 13.

2. The enactment of Article 74 that stated CSR as a legal obligation leads to uncertainty of law between CSR on voluntary and the content of Article 74 which stated it a legal obligation.⁴¹⁹
3. The Article 74 is discriminative because it is only applicable for companies operating in the field of natural resources. While in fact so far the companies have been running the rule of sectoral law, but they are still compounded by the burden of implementing CSR as a legal obligation in accordance with the article 74.⁴²⁰
4. There is a difference meaning of article 1 (3) about the definition of CSR "as a commitment from the company to participate in sustainable economic development and to improve the quality of life and the environment" with the text in Article 74 which stated CSR as a legal obligation.⁴²¹
5. Potential for higher fraud in the bureaucracy and society due the use CSR a legal obligation because people will narrowly interpret CSR as compensation, while CSR has broader meaning rather than just replace the lost.⁴²²
6. The unification of CSR as a legal obligation seems to force the companies to implement CSR as formal obligation only, whereas CSR has broader meaning than just a formal legal obligation.⁴²³
7. There is uncertainty and non-integrated relationship between academic study of Law No.40/2007 on Limited Company Liability and the Article

⁴¹⁹ Ibid

⁴²⁰ Constitutional Court Verdict No. 53/PUU-VI/2008, [Jakarta, Constitutional Court, 2008], 19 and 23.

⁴²¹ Constitutional Court Verdict No. 53/PUU-VI/2008, [Jakarta, Constitutional Court, 2008], 14.

⁴²² Ibid

⁴²³ Constitutional Court Verdict No. 53/PUU-VI/2008, [Jakarta, Constitutional Court, 2008], 22.

74 because in the academic study the law does not mention any reason for making CSR as a legal obligation.⁴²⁴

8. In accordance with the constitution, the state is the one that has an obligation on the welfare of its people and the enactment of Article 74 to make CSR as a legal obligation clearly shows that the state seems to try to divert part of its responsibilities to the companies.⁴²⁵
9. The enactment of a new norm in the elucidation of Article 74 which states that CSR as a legal obligation is not just required for companies are utilizing natural resources but also for companies who cause adverse impacts to the society and environment.⁴²⁶

Some of the legal reasons mentioned above delivered by some of the businessmen and business association in the constitutional review article 74 to the Constitutional Court.⁴²⁷ Indeed, in the verdict document of Constitutional Court, one of the witnesses Prof. Maria R. Nindita Radyati⁴²⁸ stated that up to today there is no common definition of CSR between one country and another which resulting the CSR interpretation is in accordance with their own culture.⁴²⁹ This statement strengthens the evidence that Indonesia embraces the positivist law culture where one thing is abide by the society when it is written and enshrined in the constitutional regulation.

⁴²⁴ Constitutional Court Verdict No. 53/PUU-VI/2008, [Jakarta, Constitutional Court, 2008], 15.

⁴²⁵ The 1945 Constitution of the Republic of Indonesia, The Preamble to the Constitution “...the independence of Indonesia shall be formulated into a constitution of the Republic of Indonesia which shall be built into a sovereign state based on a belief in the One and Only God, just and civilised humanity, the unity of Indonesia, and democratic life led by wisdom thoughts and deliberation amongst representatives of the people and achieving social justice for all the people of Indonesia”

⁴²⁶ Elucidation of Article 74 of Act No.40/2007 on Limited Company Liability.

⁴²⁷ Constitutional Court Verdict No. 53/PUU-VI/2008, [Jakarta, Constitutional Court, 2008], 16.

⁴²⁸ A lecturer on Corporate Social Responsibility of Trisakti University

⁴²⁹ Constitutional Court Verdict No. 53/PUU-VI/2008, [Jakarta, Constitutional Court, 2008], 43.

The culture of law and different point of view appearing amongst European and Indonesian society also construct the different concept and interpretation of CSR. By having a high awareness of the importance of business ethic is a part of company sustainability. It makes CSR programme as highly important and strategic in Europe. European society especially English are the society who embrace Anglo-Saxon system of law where the law is based on the habitual action developed in the community. So that the law is always developed and is dynamic along with the change of the time.

Eventhough in another country such as the United States of America which is assumed as country which has implemented the high business ethics, but there are a lot of frauds found in the financial reports of the big companies.⁴³⁰ Business ethics is intertwined with the culture of the law embraced by certain countries, the better the culture of the law is, the better the implementation of the business ethics.

According to R10, the business ethic is interpreted into the principal of good corporate governance (GCG) which encourages companies to implement the good ethic of business in the operational activities.⁴³¹ Some of examples such as not to be disobedient company, paying the tax right and on time, not to manipulate the financial report, and not to use the unacceptable ways in competition.⁴³² If it is described in details, then there will be a powerful relationship between the culture of the law and business ethic as it is shown in the following figure:

⁴³⁰ David Hess, A business Ethics Perspective on Sarbanes Oxley and The Organizational Sentencing Guidelines, [Michigan, Michigan Law Review, 10 October 2006], 2.

⁴³¹ *Op. Cit*, Interview on 27 September 2013 in Jakarta.

⁴³² *Ibid*

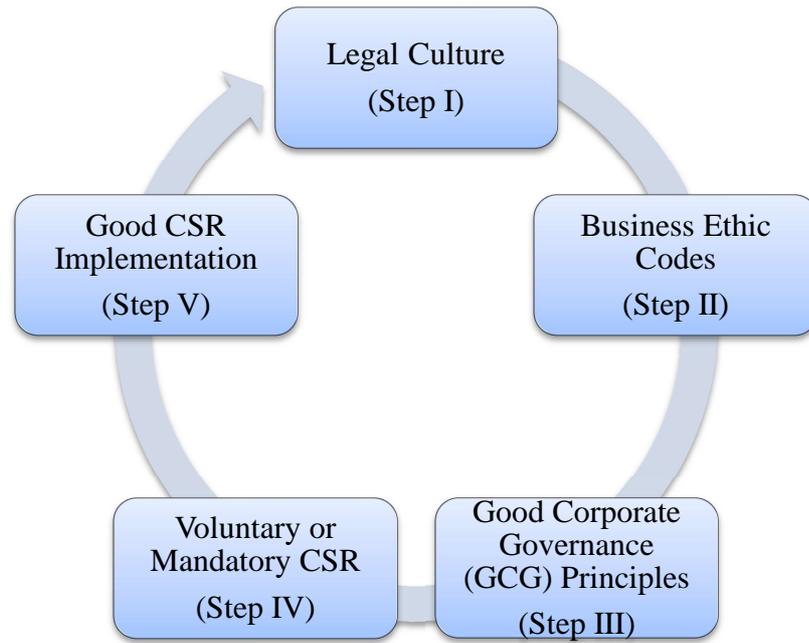


Figure 1.1 Correlations between Legal Culture and Business Ethics

The disappointing and pathetic implementation of business in Indonesia make the social condition and company environment become worse. It is proven by various cases of the living environment taking place in various places in Indonesia, such as the contamination in Buyat bay, North Minahasa district and volcanic mud in Porong, Sidoarjo, East Java.⁴³³ Moreover, based on the result of the PROPER evaluation of the Ministry of Living Environment period 2010-2011, it was found that there were 283 companies achieved Red level and 49 companies achieved Black level.⁴³⁴

The law culture of Indonesian society is tending to be a positivist which makes the country to formalise each and every principle, good values

⁴³³*Op. Cit.*, Siti Maimunah, Aminuddin A. Kirom, Tracy Glynn, etc, *Tambang dan Pelanggaran Hak Asasi Manusia: Kasus-kasus Pertambangan di Indonesia 2004-2005*, [Jakarta, Jaringan Advokasi Tambang, 2007], 22.

⁴³⁴ Ministry of Environmental Republic of Indonesia, PROPER Publication 2010-2011, [Jakarta, Ministry of Environmental Republic of Indonesia, 2007], 37.

and culture which are expected to be abided by all Indonesian people. For instance, the government expects that the companies not to take monopoly actions in their business activities and fundamentally the companies have to comply the good business practice and not to take monopoly actions.

Nevertheless, the principles and expectation only are not enough without clear indicators. For example what are the boundaries used by government to clarify that certain company has taken monopoly actions, how is the monitoring mechanism, how is the evaluation procedure, for examples, and there are still a lot of things to be regulated.

Therefore, the government issues the constitution about the *Anti Trust* which can be used as the guidance and guidelines for all related parties in evaluating, monitoring and determining whether or not certain company has conducted monopoly actions. Clear process and procedure about the anti-trust, transparent and foremost is it has gone through the constitutional process regulated by the constitution.

Likewise, the implementation of CSR in Indonesia is also in positivist law culture of Indonesian society context. It cannot be expected that mandatory CSR programme in Indonesia can be implemented well with only voluntary mechanism without standard guidance or guidelines in writing about the implementation of mandatory CSR in Indonesia. Supporting this, there are a lot of evidence and real facts in the field showing that there are a

lot of companies which do not comply with the environment principals in operating their business activities.⁴³⁵

In spite of there are a lot of written law in environment sector have been passed by the government and legislative body, but there are still a lot of companies do not comply the rules. Even though there were obviously legal sanctions and types of punishment can be imposed to the disobedient companies.

Moreover, to the present day, the companies' level of compliance on the implementation CSR programme in Indonesia is still questions. It because of the regulation is still multi-interpreting, less clear and less strict and even the level of the implementation of CSR programme is still pathetic and far from society expectations.

Law culture applied in the society which has been imprinted and institutionalised for such a long time will be difficult to be changed in a sudden. If for years the society has been directed to comply with the written rules. When the new unwritten rules come from outside them without any guidelines at all, it is for sure that the policy will not be complied because they assume that to comply or not to comply those rules will not give them any legal sanctions.

According to R8, one of the reasons why the society comply the law is because the law has the firm and clear legal sanctions.⁴³⁶ Similarly with the implementation of CSR programme in Indonesia, without firm and clear punishment mechanism on the companies disobeying the mandatory CSR

⁴³⁵ *Op. Cit.*, Siti Maimunah, Aminuddin A. Kirom, Tracy Glynn, etc, *Tambang dan Pelanggaran Hak Asasi Manusia: Kasus-kasus Pertambangan di Indonesia 2004-2005*, [Jakarta, Jaringan Advokasi Tambang, 2007], 43, 49, 91, 157, 251, and 279.

⁴³⁶ *Op. Cit.*, Interview on on 25 September 2013 in Depok.

legal provision, it can be assured that those companies have not yet implemented their CSR programme well.

The law culture of Indonesian society is step by step shifting to revolution to become the law which respect as well as implementing the human right principles in daily life. The change of the law culture is also expected to be implemented by the companies as corporate citizen entities in their business practices. The law culture of Indonesian society especially in relation with the implementation of CSR programme is still in transitional stage toward the right format in accordance with the society condition and situation and other socio-cultural context.

Today, the law makers see that the legal provision of CSR mandatory is in accordance with the law culture of Indonesian society. Regarding the CSR programme itself, the law makers who are the representative of legal culture of Indonesia society reflect the socio-culture law condition of Indonesia Society into article 74 on Corporate Social and Environmental Responsibility on Act No.40/2007 on Limited Company Liability.⁴³⁷

Directly or indirectly, the law culture of certain society will influence corporate values of corporate entity because the entity employs the society from that law culture. For instance, if certain society has positivist law culture as a result directly or not directly the companies will have the positivist law culture as well because those companies are employing members of the society who have positivist law culture.

⁴³⁷Ibid

Business enterprises should introduce, implement and even maintain its own law culture as a part of universal corporate values which is believed can make it sustainable. The companies have to develop their own corporate values in order to assure their business sustainability based on its context and the different society social structure between one country to another. By sticking on well-adapted corporate values then the sustainability of business of the companies can continue to be guaranteed although they are in the middle of unstable social and politic situation.

Based on stakeholder's theory, a company has responsibility to provide positive added values for its stakeholder.⁴³⁸ The positive added values can be interpreted as a maximum effort not to damage the environment where the company operate, empower the local society economic and improve a better life for local society socially.⁴³⁹ Further, basically the presence of investment companies alone in a mining area or plantation has provided positive impacts on the society economic progress in that area.

Furthermore, those things are the initial assets owned by the companies by continuing to maintain the good relationship, so that the companies will gain more trust from local community. A lot of the mining and plantation companies are declined by the community in certain region because their presence is assumed not to give any significant benefits for the local community. In contrary, their presence bring a lot of negative effects always becomes the cause of social conflict between community and related

⁴³⁸Steen Thomsen, *Corporate Values and Corporate Governance*, [Denmark: Emerald Group Publishing Limited, Vol.4 No.4. 2004], 34.

⁴³⁹Ibid

companies about the issue of land ownership dispute, the accessibility to works and other social issues.⁴⁴⁰

According to R18, the more positive added values given by the companies for the local community is to improve the social ownership between companies and community.⁴⁴¹ One of the solutions to minimize the conflict between companies and local community is by fostering ownership of social spirit among the local community towards the running companies in their region.⁴⁴²

One of the ways to foster a sense of community ownership of the company is to carry out CSR programmes according to the needs of the community and is given to the appropriate beneficiaries. Mandatory CSR legal provision was inserted into the Act No.40/2007 on Limited Company Liability in order to encourage companies that have not yet properly implemented CSR programmes to implement its CSR programmes well.

The programme should be conducted in relation with the reduction of environmental damage around their operational areas. In fact, many countries use the system of "*sticks*" and "*carrots*" to encourage companies to comply with the principles of ethical business practices in conducting their business. The use of criminal law to punish business practices in violation of the law or misconduct business practices is also necessary.⁴⁴³

⁴⁴⁰Ibid

⁴⁴¹Interview on 19 October 2013 in Depok.

⁴⁴²*Op. Cit*, Steen Thomsen, *Corporate Values and Corporate Governance* [Denmark, Emerald Group Publishing Limited, Vol.4 No.4. 2004], 35.

⁴⁴³ Dawn Marie Driscoll, W.Michael Hoffman and Joseph E.Murphy, *Business Ethics and Compliance: What Management is Doing and Why*, [Oxford: Business and Society Review, Blackwell Publisher, 1998], 35.

It is similar to the implementation of mandatory CSR legal provision which is governing legal sanctions for companies that do not conduct their CSR programme properly. Legal sanctions may not be awarded to a company that has already conducted its CSR programme well. Therefore, there should be no concern for companies that have conducted their CSR programme satisfyingly of getting legal sanction from the government.

The positivist legal culture is a culture of law that is gradually evolving toward non-positivist law cultural with the increase of public education and welfare. With the increase in public education and welfare, it will automatically increase public awareness to do something which is considered appropriate for their social life.

Therefore, it is essential to have a structure of law able to maintain and guard so that any misconduct activity is not done by the companies or state official elements in their operational areas. In addition, R12 mentioned that it is the same goes to the mandatory CSR legal provision, because the regulation makers have studied from the past where there had been many environmental damages due to companies' business activities which lead to a long-term conflict between the companies and the society.⁴⁴⁴

Therefore, the regulation makers enshrined the article 74 into Act No.40/2007 on Limited Company Liability in order to maintain so that such environmental damages will never occur in the future.⁴⁴⁵ If anything happens, the negative impact can be minimized as early as possible with the implementation of CSR programmes that can improve the relationship between company and the community.

⁴⁴⁴*Op. Cit*, Interview on 30 September 2013 in Jakarta.

⁴⁴⁵*Ibid*

Thus, the Article 74 on Corporate Social and Environmental Responsibility in which the CSR was set as a legal obligation did not suddenly appear and was included in Act No.40/2007 on Limited Company Liability without proper reason. It was formally enshrined because there were many evidence and facts on the ground indicating that companies were less concerned about the social and environmental conditions in their operational areas. Therefore, the enactment of Article 74 is the best option that can be done by lawmakers in protecting the fundamental rights of the people related to a clean and comfortable environment and a healthy social condition.

Following is the chart on the policy process of CSR which should be performed by the government.

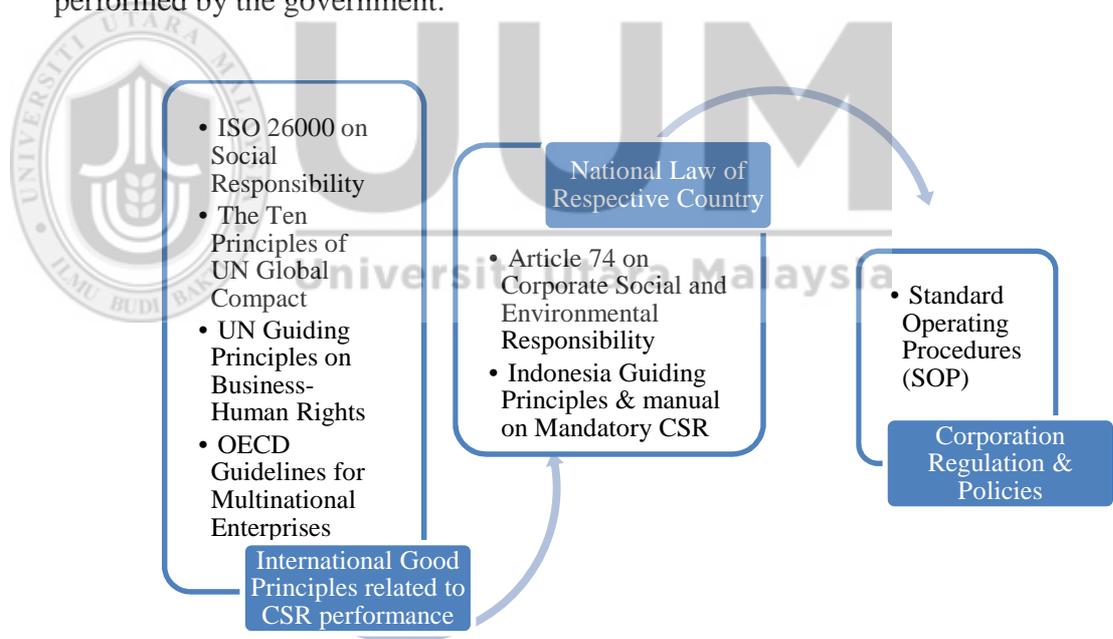


Figure 1.2. Policy Evolution Related to Corporate Social Responsibility

4.8. Conclusion

Based on some findings above, it was found that philosophical rationale behind the enactment of mandatory CSR legal provision is due to

environmental disaster that have occurred in some areas in Indonesia. Further, there was a significant social pressure from the local community in which the extractive industries are doing their business activities to be more socially and environmentally responsible. Nevertheless, since the beginning of discussion of Limited Company Liability Bill, there was a different view between the government and member of the House of Representative on mandatory CSR legal provision. In one side, the Government represented the interest of business associations, business leaders and companies insisted on rejecting the legal provision.

In the contrary, the members of the parliament insisted on inserting the legal provision to the bill in order to be legally bounded to all the citizen including the companies. At last, the Bill was stipulated and officially passed by the parliament with Article 74 which is require all companies to implement CSR programmes. In other words, CSR becomes a legal responsibility of the companies. Finally, the implementation of legal provision has been getting slow because of minor political will from the government to comprehensively implement it.

At last but not least, the philosophical rationale of enacting the legal provision is not just limited to preserve the nature and to ensure the sustainability of the natural resources but also to empower economic's situation of the local community and to strengthen social cohesion and harmony between the local community and the companies.

CHAPTER FIVE
FINDINGS:
LEGAL ANALYSIS ON CORPORATE SOCIAL
RESPONSIBILITY LAWS, REGULATIONS, GUIDELINES AND
POLICIES IN INDONESIA

5.1 Introduction

CSR has been perceived as a cross-cutting and inter related issue. It is not just an issue about economic and business but also about society, law, environment, and human rights. The legal provision on mandatory CSR in Indonesia has been officially enacted since 2007 through Act No.40/2007 on Limited Company Liability. Unfortunately, it is almost 7 (seven) years after the enactment yet the provision could not be implemented well. The findings have found two major constraints which are no clear policy in terms of government regulation, guidelines, and standard operating procedures regarding the implementation of the legal provision.

Further, there is no specific ministry or state institution that has been given mandate by the law to take lead in the implementation of the legal provision. Subsequently, the legal provision could not be implemented due to those constraints. The relevant ministry and even members of the house of representative have to encourage the government to revise and harmonize all regulations and policies related to CSR in order to be aligned with the legal provision on mandatory CSR.

5.2 Legal Analysis of Article 74 on Mandatory Corporate Social Responsibility Legal Provision in Indonesia

Findings from the field research conducted between September 2013 and October 2013 in Jakarta further further strengthened the researcher's

assumption that Indonesia does not have mandatory CSR guidelines and voluntary CSR completely and codified in a written guideline.

In fact, 4 (four) companies clearly supported the implementation of mandatory CSR in regard of its purpose to minimize the social and environmental impacts which benefit the society.⁴⁴⁶ R6 mentioned “I agreed towards mandatory CSR policy. It needs a standardization in order to obtain the same results in implementing CSR programmes in Indonesia and for a longer term it may increase the company’s efficiency.”⁴⁴⁷ Further, R11 stated “I agreed to mandatory CSR policy because this policy may encourage the companies to draft a CSR programme that is right on target and then the companies will also involve local people in their activities. Without the support of the society, the company cannot be sustainable.”⁴⁴⁸

Meanwhile, the ministries and government agencies have different views on the mandatory CSR. The Ministry of Environment and Ministry of Social obviously deny the existence of a CSR mandatory legal provision. For instance, R2 mentioned “I disagreed towards the mandatory CSR policy because it makes the companies in Indoneasia uncompetitive. There is additional burden in operational cost, and further CSR is beyond compliance so that the companies should be encouraged to implement it freely and flexibly.”⁴⁴⁹ R14 mentioned: “I disagreed towards the implementation of mandatory policy because the companies should be given a freedom to

⁴⁴⁶ Arun NGL, Bank Rakyat Indonesia, Worker’s Social Security Company (PT Jamsostek) and Sinaraya Trading (Export-Import Company).

⁴⁴⁷ *Op. Cit*, Interview on 17 September 2013 in Jakarta.

⁴⁴⁸ Interview on 30 September 2013 in Jakarta.

⁴⁴⁹ *Op. Cit*, Interview on 12 September 2013 in Jakarta.

implement its CSR programmes without any compulsion from the Government.”

R3 mentioned: “On the contrary with the two ministries, some other ministries support it (mandatory CSR). I supported mandatory CSR policy and moreover we already circulated a letter of guidance to all state-owned companies to implement the provision of article 74.”⁴⁵⁰ In addition, there is a state’s company which partially support the implementation of mandatory CSR policy. Then, R7 mentioned that “I supported the implementation of mandatory CSR policy because by the provision companies will be more focused to draft and implement CSR programmes for the people’s benefits.”⁴⁵¹

Further, there are several NGOs and CSR consultants who support the implementation of mandatory CSR.⁴⁵² For instance, R27 mentioned that “I supported mandatory CSR and the provision may encourage CSR programmes to be more transparent, objective, and accountable.”⁴⁵³ Even the law and CSR experts from universities also support the implementation of the policy. For instance, R8 mentioned: “I supported mandatory CSR and one of the state’s function is to regulate any aspect of people’s life including CSR. The mandatory CSR provision does not mean that the government takes over

⁴⁵⁰ *Op. Cit*, Interview on 1 October 2013 in Jakarta.

⁴⁵¹ *Op. Cit*, Interview on 18 September 2013 in Jakarta.

⁴⁵² Indonesian Legal Aid Foundation (YLBHI), Young Generation of People’s Advocates (GEMPAR), National Humanitarian Agency (PKPU), Indonesia Working Group for Business and Human Rights (IWGBHR), The Microfinance Innovation Center for Resources and Alternatives (MICRA), National Team for Accelerating Poverty Alleviation (TNP2K), Indonesian Youth for Law Enforcement, Publish What You Pay (PWYP) Indonesia, Indonesiaan NGOs Forum for Conserving Environment (WALHI), and Indonesia Corruption Watch (ICW).

⁴⁵³ *Op. Cit*, Interview 30 October 2013 in Jakarta.

the implementation of CSR programmes but the provision is made to protect the right of the citizen.”⁴⁵⁴

Whereas, there are also some organizations which obviously deny the implementation of mandatory CSR policy. For instance, R3 mentioned that “I disagreed towards the implementation of mandatory CSR provision because the spirit of CSR based on voluntarism and the state cannot force the companies to do CSR.”⁴⁵⁵ At last, two NGOs and two state agencies partially support the implementation of mandatory CSR policy.

In Article 74 on mandatory CSR legal provision, there are four clauses that regulate the mandatory CSR legal provision in Indonesia.

(1) Companies doing business in the field of and/or in relation to natural resources must put into practice environmental and social responsibility. According to R8, the phrase above is still general and should be described in more detail. There should be specific regulations and manual to expand the definition “doing business in the field or and/or in relation to natural resources.”⁴⁵⁶ Further, the second phrase “environmental and social responsibility” is also unclear because there is no proper guidelines or standards on the measurement of environment and social responsibility projects.⁴⁵⁷

(2) Environmental and social responsibility constitutes an obligation of the company which shall be budgeted for and calculated as a cost of the company performance. Hence the responsibility shall be carried out with due attention to decency and fairness. According to R12, several

⁴⁵⁴ *Op. Cit*, Interview on 25 September 2013 in Depok.

⁴⁵⁵ *Op. Cit*, Interview on 13 September 2013 in Jakarta.

⁴⁵⁶ *Op. Cit*, Interview on 25 September 2013 in Depok.

⁴⁵⁷ *Ibid*

definitions should be described in this clause, for instance, the phrase “environmental and social responsibility program shall be budgeted and calculated as a cost of the company performance”, should be supplemented with guidance from a relevant agency to provide direction in terms of what can or cannot be put on the budget.⁴⁵⁸ Further, the phrase “decency and fairness” is still general and can be interpreted differently either by companies, beneficiaries, or government officials.⁴⁵⁹

- (3) Companies who do not put their obligation into practice shall be liable to sanctions in accordance with the provisions of legislative regulations. In regard with phrase “sanctions in accordance with the provisions of legislative regulations” is also still too general. It needs further legislation on appropriate sanctions that can be imposed to uncompliant companies. Rewards or benefits can be given to such companies which have successfully implemented the mandatory CSR projects. Further, the sanctions are based on respective laws and regulations, for instance, if the company ruins the environment then the environmental act will be imposed to that company. Such measures should be described in a more specific regulation on mandatory CSR.
- (4) Further provisions regarding environmental and social responsibility shall be stipulated by government regulation. It is the responsibility of the government to provide a very clear guidance and executing regulation on mandatory CSR.⁴⁶⁰

⁴⁵⁸ *Op. Cit*, Interview on 30 September 2013 in Jakarta.

⁴⁵⁹ *Ibid*

⁴⁶⁰ *Ibid*

In addition, the government has passed Government Regulation No. 47/2012 on Environmental and Social Responsibility. Unfortunately, this regulation has been drafted and passed without the involvement of wider CSR stakeholders especially NGOs and beneficiaries representatives. It sounds that the government regulation has been passed to fulfill the implementation of Article 74 only without an intention to resolve a number of mandatory CSR problems in Indonesia.

Such dilemma is that those companies have to carry out mandatory CSR programmes without clear guidelines. They are continuously being blamed by the community when they do not implement such a programme. Therefore, in the absence of national guidelines on mandatory CSR, companies deciding to invest in Indonesia are uncertain as to how and how much they should allocate for their CSR and what are the priority programmes.

These companies will be persistently forced by the society regardless whether they implement the CSR programmes. The criticism is raised by certain group of people around their business operations. This happens because there is no legal certainty in term of mandatory CSR guidelines, and the problem will persist until such guidance is issued.

The current implementation method of CSR is that the companies are directed to involve in executing the projects by themselves, through particular grantees or involved in CSR forums made by related ministries. There should be an integration between the needs and interests of the beneficiaries, national and sub-national development plan and the availability budget of CSR provided by those companies. In addition, the companies are also should be

given independency and autonomous in implementing the programme according to their operational needs.

Moreover, currently, at least there are 3 ministries which are most actively dealing with CSR programmes; they are Ministry State-Owned Enterprises, Ministry of Environmental and Ministry of Social. However, based on the findings, there are 11 (eleven) ministries involved in arranging policy of CSR programmes in Indonesia.

Those are as follow: Ministry for People's Welfare of the Republic of Indonesia, Ministry of Economic Affairs of the Republic of Indonesia, Ministry of State-Owned Enterprises, Ministry of National affairs, Ministry of Environment of the Republic of Indonesia, Ministry of Social Affairs of the Republic of Indonesia, Ministry of Cooperation Affairs, Ministry of Small Business and Medium Enterprises, Ministry of Rural Development of the Republic of Indonesia, Ministry of Forestry, Ministry of Labor of the Republic of Indonesia and the Ministry of Energy and Mineral Resources of the Republic of Indonesia.

Some ministries have issued certain policies regarding to the CSR guidelines where the rest of them are still in the phase of preparing the CSR policy draft. Further, there are some facts that each ministry prepares and then issue CSR-related policies with limited coordination and communication involving other ministries. It happens because of they use their own law as the legal basis in preparing and issuing CSR policy.

The situation causes confusion among the companies as the affected parties of all rules drawn up and issued by the respective ministries. The business enterprises are the most affected by the issuance of these rules. At

last, even the business enterprises are voluntarily to implement all the rules and regulation were made by the respective ministries but in facts, it becomes compulsory in practice due to NGOs pressure.

In addition, most of beneficiaries do not know about sectoral regulations have been passed by the respective ministries. It is due to lack of socialization and dissemination of information related to the preparation and issuance of ministerial regulations. The relevant ministries should organize information dissemination programmes regarding the new CSR-related policies have been passed.

It would make the beneficiaries aware of the policies and the nature of the CSR programmes. Therefore, it is necessary to have information dissemination programmes and codification of all decrees from ministries related to separated CSR into the Indonesian CSR manual.

There are a number of ministries regulation have been passed before the passing of mandatory CSR legal provision, but those can be still acceptable as long as all the rules and regulations may support and strengthen the implementation of mandatory CSR in Indonesia. In fact, some of the rules did not explicitly mention its association with mandatory CSR legal provision because those have been passed before the legal provision. Therefore, it needs synchronization and harmonization by a government regulation. In addition, it may align with the spirit of mandatory CSR legal provision.

There are several ministries which have had regulations related to CSR such as Ministry of State-Owned Company is implementing a PKBL programme. Moreover, PKBL is being reviewed to be carried out as a social

activity of the state-owned companies. There are two (2) options to be offered by the section of PKBL at the Ministry of State-Owned Enterprises.

Those options are as the following, transfer the partnership programme to another institution and to continue implementing the community development programme as usual or to eliminate the programme altogether and replace it with mandatory CSR programme in accordance with Article 74 of Act No.40/2007 on Limited Company Liability.

A newly model of CSR programme will be implemented for all state-owned company in 2014. The PKBL head strongly supported mandatory CSR to be a legal responsibility of the companies because it will encourage companies to increasingly aware of the social and environmental conditions in the areas in which they operate.

Until now, MSOE still did not have a fix guidelines or guidance in implementing mandatory CSR programmes.⁴⁶¹ Moreover, there is no yet monitoring and evaluation process conducted by internal and external agencies to CSR activities undertaken by the state-owned enterprises.⁴⁶²

The reporting process conducted by the MSOE was also only for the accountability of the use CSR funds to the Board and Commissioner of the concerned state-owned company in the Annual General Meeting of Shareholders (RUPS). The partnership programme that has been implemented by the state-owned enterprises along with community development programmes could not be called as a CSR programme.

Therefore, the state-owned enterprises requested interest in distributing their low-interest loans to small and medium enterprises. Then,

⁴⁶¹ *Op. Cit*, Interview on 1 October 2013 in Jakarta.

⁴⁶² *Ibid*

the state-owned enterprises require them to pay back the loan in accordance with the loans contract that has been agreed both the borrower and the relevant state-owned enterprises.

The loan interest is around 6% per year.⁴⁶³ Therefore, the MSOE is reviewing the programme in order to develop a strategic framework for the implementation of mandatory CSR programmes. It will be more comprehensive by applying the principles which had been recognised either internationally or nationally.

Ministry of social affairs is one of the most active ministries in drafting regulations and guidelines related to the implementation of CSR. In fact, the ministry is recently proposing a Bill draft on Social Development of Business Enterprises to the national parliament. In addition, several CSR-related policies that have been passed by the Ministry of Social Affairs.

Nevertheless, the ministry of social affairs itself has yet had an effective monitoring, evaluation and reporting system regarding to the implementation of CSR programme under its authority. However, this ministry step by step has been developing an effective reporting system for its CSR programme. Further, the ministry basically supports the implementation of Article 74 on Social and Environmental Responsibility which demands that companies especially those are exploiting natural resources are required to implement CSR programmes. With the existence of the Article, it encourages participation and awareness of the companies to be more socially responsible.

Further, According to R2, State Ministry of Environmental Republic of Indonesia has also issued both several ministerial regulations and technical

⁴⁶³Ibid

guidelines for the implementation of CSR in environmental aspect.⁴⁶⁴ In fact, based on some data the researcher conclude that there are several governmental regulations related to environmental issues which are considered relevant to the implementation of CSR.

Afterwards, Ministry of Cooperatives, Small and Medium Enterprises Republic of Indonesia. This ministry has issued guidelines on the types of CSR activities. The Ministry is currently drafting policies related to CSR in terms of empowerment of cooperatives, small and medium enterprises through partnerships with the business community by utilizing CSR funds.

Hence, R9 stated that Ministry of Energy and Mineral Resources Republic of Indonesia has been preparing a policy which is the regulation of Minister of Energy and Mineral Resources of the Republic of Indonesia regarding to CSR.⁴⁶⁵ Nevertheless, based on the existing data the researcher concludes that there are some government regulations and ministerial regulations that are relevant to the implementation of the CSR.

Further, R3 was also mentioned that State Ministry of Underdeveloped Area Republic of Indonesia has issued some regulations related to the application of CSR in the department.⁴⁶⁶ In fact, the ministry has conducted some activities by signing a Memorandum of Understanding (MoU) with several related partnership companies in implementing CSR with business entities.

Further, Coordinating Ministry of Economy Republic of Indonesia also has a certain field that handles issues on entrepreneurship and CSR

⁴⁶⁴ *Op. Cit*, Interview on 12 September 2013 in Jakarta.

⁴⁶⁵ *Op. Cit*, Interview on 25 September 2013 in Jakarta.

⁴⁶⁶ *Op. Cit*, Interview on 13 September 2013 in Jakarta.

programme implementation. There are government regulations relating to the use of CSR funds. Afterwards, Coordinating Ministry of Social Welfare Republic of Indonesia has passed a minister regulation related to CSR. The minister regulation recommended to establish a forum which is called as *Gema Mitra*. Hence, the team has been established in provincial, district and urban areas in order to mobilize CSR as a source of funds for the implementation of their community development programmes.

Subsequently, Ministry of Home Affairs Republic of Indonesia along with the Directorate General of Rural Community Development is working on CSR-related policies and economic empowerment of rural communities. In addition, there has been a policy issued by the Ministry of Home Affairs relating to the use of CSR funds for financing community based programmes. Then, Ministry of Forestry Republic of Indonesia. This Ministry also has a number of laws and regulations related to the implementation of community development and CSR.

Thereafter, Ministry of Worker and Transmigration Republic of Indonesia has also passed a number of nuanced CSR policies particularly with regard to the protection of workers' rights. There are several national policies related to the protection of workers that must be implemented by companies in term of CSR programmes.

With the complexity and complication of mandatory CSR issues in Indonesia either in terms of policy substance, policy makers agencies, monitoring and evaluation system and reporting mechanism. Further, R26 convinced that, based on some evidence, it requires a single guideline that can

accommodate all the interests of the stakeholders.⁴⁶⁷ Moreover, the former chairman of the Bill drafting committee for Limited Company Liability No.40/2007 mentioned that due to the complexity of mandatory CSR issues and then the Government Regulation No. 47/2012 on Social and Environmental Responsibility must be revised to accommodate all interests.⁴⁶⁸

Although many parties either from the ministries, practitioners, academics or companies themselves are supporting the enactment of Article 74 of ActNo. 40/2007 on Limited Company Liability, but there is some others especially from business associations and business enterprises who rejected either directly or indirectly related to the enactment of CSR mandatory legal provision. However, those who rejected the enactment of the Article 74 are also predominantly from practitioners, academics, and business associations. It seems there is divided opinion between some academics and practitioners and the others.

According to R4, since the beginning of mandatory CSR legal provision has been raised, there were some business associations rejected the enactment of Article 74 of Act No. 40/2007 those are the Indonesian Chamber of Commerce and Industry (KADIN), the Indonesian Business Women Association (IWAPI), Indonesian Young Entrepreneurs Association (IWAPI) and the Entrepreneurs Association of Indonesia (APINDO).⁴⁶⁹ In addition, the rejection of the enactment of Article 74 also comes from the

⁴⁶⁷ *Op. Cit*, Interview on 29 October 2013 in Jakarta.

⁴⁶⁸ *Ibid*

⁴⁶⁹ *Op. Cit*, Interview on 15 September 2013 in Jakarta.

Ministry of Environment of the Republic of Indonesia.⁴⁷⁰ The Ministry is the only state agency that is formally disagrees with the enactment of the mandatory legal provision.

Pro and contra on the enactment of Article 74 will persist if there is no initiative from the executive body to maintain the implementation of mandatory CSR programmes in Indonesia. Further, the implementation is also should avoid any overlapping between a certain ministry and others. The business enterprises should not feel the legal provision as a burden. Hence, the local government should not make CSR funds as a source of local revenue (PAD) by issuing new local regulations about CSR that resulted to disharmonize between the society and the business enterprises.⁴⁷¹

Indeed, in the initial discussion of the Bill draft, the government (the executives) is the one that did not agree with the inclusion of Article 74 on mandatory CSR legal provision into it. Therefore, it is reasonable if the implementation of Article 74 is stagnant because the Article 74 is an "illegitimate child" that its "birth" was unwanted by the government.

According to R25, the existence of mandatory CSR guidelines as an original product of Indonesia is essential.⁴⁷² It is needed as guidance for the implementation of mandatory CSR programmes in Indonesia. These guidelines are very urgent to be passed by the government. The urgency is because of some following reasons such as the large potential of CSR funds, stakeholders complexity related to CSR issues and diversity interpretations on CSR itself.

⁴⁷⁰ Ibid

⁴⁷¹ Ibid

⁴⁷² Interview on 29 October 2013 in Jakarta.

In addition, R25 convinced that if there is no standard guideline on the implementation of mandatory CSR, it may cause misuse and fraud of the use of CSR funds.⁴⁷³ In some cases, the business enterprises claimed that they have disbursed the CSR funds for funding some projects. Apparently, the funded activities were not classified as CSR programmes or even the beneficiaries were not identified well. It may persistently occur in the absence of a clear and explicit references.

5.3. Mandatory Corporate Social Responsibility Regulations in Indonesia

Multi interpretation on CSR is lead to the different interpretations on a working unit that handle CSR programme in some oil and gas companies in Indonesia. There are companies that named their CSR programmes unit as CSR section, community relations, government relations, public relations or community development. CSR institutional differences between a company and others possibly appear due to the lack of guidelines for mandatory CSR in Indonesia. In addition, each company is free to interpret the legal provision because no guidance from the Government.

However, according to R6 there are some companies that voluntarily utilize the international CSR instruments as guidance in implementing their CSR programme.⁴⁷⁴ It occurs because of the absence of national CSR guidelines. Up to now, there are a number of international organizations that publish some guidance in implementing CSR programmes.⁴⁷⁵

⁴⁷³ Ibid

⁴⁷⁴ *Op. Cit*, Interview on 17 September 2013 in Jakarta.

⁴⁷⁵ Ibid

5.3.1 Corporate Social Responsibility Regulations Both National and Sub-National Laws Level

Companies' participation in adopting those guidelines is voluntary basis because it depends on the willingness and good faith of the particular company to voluntarily accept the entire applicable standards and regulations within those guidelines. The guidelines are divided into several types of guidelines which are CSR guidelines on human rights and business, CSR guidelines on sustainability, and CSR guidelines on international trade and investment. Further, it is also classified between national rules and regulations regarding CSR and international guidelines and policies on CSR as a whole.

Some of national and sub-national laws and regulations in relation with CSR that are currently prevailing in Indonesia are as follows;

1. Act Number 40/2007 on Limited Company Liability

This act has been passed by the House of Representative of Indonesia in 2007. The Act is replacing the old version of the Company Liability Act No. 1/1995. It says obviously in its article 74 about CSR provision. Moreover, the provision is as the legal basis of mandatory CSR implementation in Indonesia. It was argued many times in many occasions by business associations in Indonesia.⁴⁷⁶ Further, the government regulation on CSR which is mandated by the Act is delay to be drafted by the Government. It because of too many interventions from business associations. Finally, the government regulation is ultimately was passed

⁴⁷⁶ The Indonesia Chamber of Commerce and Industry (KADIN), The Indonesia Young Businessmen Association (HIPMI), The Indonesia Business Women Association (IWAPI), and The Indonesia Businessmen Association (APINDO)

by the Ministry of Law and Human Rights in April 2012. It has been almost 4 years after the enactment of Mandatory CSR legal provision. Apparentely, the content is still not consistent with the beneficiarie's aspiration and expectation.

The beneficiaries may see the drafting and discussion process takes a couple of years. It shows that so many interests either economic or political should be accommodated into the government regulation. Further, R4 mentioned that many times those business associations argue that the mandatory CSR may reduce the competitiveness of Indonesia's products in international market because by implementing mandatory CSR the production cost will be much higher.⁴⁷⁷

Further, it will automatically increase its selling price.⁴⁷⁸ In other public gathering, sometimes the business association said that they ready to implement it if the government is also release a tax reduction policy and other kinds of economic incentives package for the companies which successfully implement it.

Based on some information provided on the Article 74, the researcher concludes that the Article 74 is not fully regulated the things about mandatory CSR. for example; there is no specific legal sanction can be granted to companies who are not implemented well the legal provision. the Act should be revised to add more provisions regarding mandatory

⁴⁷⁷ *Op. Cit.*, Interview on 15 September 2013 in Jakarta.

⁴⁷⁸ *Ibid*

CSR or the Government establishes another Act to specifically regulate mandatory CSR.

2. Act Number 25/2007 on Investment

This Act also mentioned about CSR is a must and part of investors' commitment. It is said obviously in the article 15 as follows; every investor is required to: a) apply the principle of good company management; b) implement the company's social responsibility; c) make report on investment activity and submit it to the Investment Coordinating Board; d) respect cultural tradition of communities around the location of investment business activity; e) comply with all the rules of law.⁴⁷⁹

Then, according to Article 5 the form of companies who obliged to conduct the provision above is as follows; 1) domestic investment may be in the form of corporation, non-corporation, or individual business, in accordance with the rules of law; 2) unless otherwise stipulated by the law, any foreign investment shall be in form of limited liability company based on the law of the Republic of Indonesia; 3) both domestic and foreign investors making an investment in form of limited liability company shall be carried out by: a). having shares when such company is established, b). purchasing the shares and 3) executing any other way pursuant to the rules of law.⁴⁸⁰

In fact that the obligation to fulfill social responsibility is not just limited to the foreign investment but also to domestic investors as well. It is a clear message that the policy is a non-discriminatory policy as some

⁴⁷⁹ Act No. 25/2007 on Investment

⁴⁸⁰ Ibid

investors raised in the recent years. Moreover, the policy applies for both domestic and foreign investors who are doing business in Indonesia. A step forward of investment Act than Company Liability Act is that the Act was significantly providing legal sanctions for those companies which do not comply with it accordingly.

Meanwhile, several types of legal sanctions can be given to disobedience companies in accordance with Article 34 such as; 1) any companies or individuals set forth in Article 5 that fails to fulfill their obligation pursuant to Article 15, they may receive administrative sanction in form of: a) written warning; b) business restriction; c) suspension of business and/or investment facility; d) revocation of business license and/or investment facility; 2) authorized agency or institution pursuant to the rules of law shall issue administrative sanction set forth in paragraph (1) above; 3) in addition to administrative sanction, such companies or individuals may receive other sanctions pursuant to the rules of law.⁴⁸¹

Based on information provided by the Act, the researcher assumes that mandatory CSR is legally binding for all companies either domestic or foreign companies who are operating in Indonesia. Further, legally mandatory CSR legal provision is not only binding companies which is exploiting natural resources but also for companies in other industries such as manufactures, services, and banking.

The most interesting part of the Act is about legal sanction. The Act has provided some types of legal sanction for companies who disobey the provision. At last, it needs a synchronization between Act No. 40/2007 on

⁴⁸¹Ibid

Limited Company Liability and Act No. 25/2007 on Investment at least in terms of legal sanctions to be imposed on companies which do not implement the mandatory CSR legal provision properly, and the state agency is authorized to do surveillance and evaluation of the mandatory CSR projects.

3. Act Number 19/2009 on State-Owned Enterprise

According to Article 2 of Act Number 19/2009, state-owned enterprises (SOE) are established to support the national economic growth of Indonesia and to generate state's national income, gain profit, and produce high quality of goods and services that are accessible for all citizen. The article serves as a pioneer for business activities that have not been conducted by cooperative and private sector. It actively provides guidance and assistance for small and medium scale enterprises, cooperatives, and communities.⁴⁸²

In the mean time, R13 stated that as part of a business entity, an SOE does not purely seek profit in its business practices; it also actively supports small and medium scale enterprises, cooperatives, and communities.⁴⁸³ Article 88 clearly states that an SOE may allocate its net profit to the development of small and medium scale enterprises, cooperatives, and communities around where the company is located.⁴⁸⁴

⁴⁸² Act No.19/2003 on State-Owned Enterprise.

⁴⁸³ *Op. Cit*, Interview on 1 October 2013 in Jakarta.

⁴⁸⁴ *Op. Cit*, Act No.19/2003 on State-Owned Enterprise.

It can also be translated from the article that an SOE is to pass some policies to support its social purpose. On a legal basis the Ministry of SOE has launched a programme called Partnership and Community Development Programme (*Programme Kemitraan dan Bina Lingkungan or PKBL*). Five years before the enactment of Act No. 40/2007 on Limited Company Liability, the ministry has passed some policies to implement the PKBL programme within all SOEs.

Some of the policies are as follows: (1) Ministry of SOE Regulation Number PER-05/MBU/2007 on PKBL, (2) Circulated Decree Number SE-07/MBU/2008 on the Implementation PKBL, and (2) Article 74 of Company Liability Act Number 40/2007.⁴⁸⁵ The two executing regulations are the basis of implementing PKBL and CSR programmes within the SOEs. Moreover, the SOEs have been implementing two types of social programmes which are PKBL and CSR in accordance with Article 74 of the Limited Company Liability Act.⁴⁸⁶

The issuance of SOE ministerial regulations acts as a legal basis for SOE corporates to implement their social programmes on PKBL and CSR. It can actually draw the attentions of SOEs to achieve a determined work plan and target. Long before the SOE Act was issued, SOE corporates are “obliged” to assist and empower groups of cooperatives, and small and

⁴⁸⁵Ibid

⁴⁸⁶Ibid

medium enterprises, as mentioned in the regulation of Ministry of Finance.⁴⁸⁷

Based on the information provided by the Act, the researcher concludes that the Ministry of SOE should establish standard operating procedures (SOP) regarding the implementation of PKBL programmes.

The ministry should also develop a public awareness programme on CSR, a transparent reporting mechanism, and a responsible monitoring and evaluation mechanism. The PKBL programmes should not contradict or overlap the spirit of mandatory CSR legal provision as mentioned in Act Number 25/2007 on Investment and Act Number 40/2007 on Limited Company Liability. There should be a synchronization between the two statutes and the Act on SOE.

4. Act Number 22/2001 on Oil and Gas

Oil and gas industry is one of industries that utilize natural resources.

According to Article 74 of Act No. 40/2007 of Limited Company Liability, all companies operating in the oil and gas industry are mandated to implement mandatory CSR legal provision.

Further, the Act enacts several legal provisions on CSR as follows: A corporate or permanent corporate ensures the applicable standard and quality according to the relevant regulations as well implements a proper technical rule.⁴⁸⁸ The company must also ensure workers' safety and

⁴⁸⁷Ministry of Finance Decree No.1232/KMK.013/1989 on the Manual of Cooperatives and Small Enterprise Development through State-Owned Enterprise.

⁴⁸⁸ Article 40 clause (1) paragraph 1 of Act No.22/2001 on Oil and Gas.

health as well as environmental management, and comply with all the applicable regulations in mining and oil business.⁴⁸⁹

Environmental management as mentioned in clause (2) is an obligation to prevent and mitigate any pollution as well as rehabilitate environmental damage, and it includes the post-mining activity obligation.⁴⁹⁰ Further, corporate or permanent corporates in oil and mining bussiness as mentioned in Article 5 should transparently and competitively prioritize the use of local labours, goods, and service, as well engineering and design capabilities.⁴⁹¹

Corporate or permanent corporate in oil and mining bussiness as referred in article 5 should be responsible in empowering the local people and environment.⁴⁹² Further, the stipulations regarding work safety and health as well the environmental management as reffered in paragraph (1) and (2) will be further regulated in the government regulation.⁴⁹³

According to the legal provisions above, the researcher assumes that the Act has regulated some key points regarding labour and environment. So far, the Ministry of Energy and Mineral Resources has passed several ministry regulations about environmental aspect in oil and gas industries. Moreover, ministry of environmental also already passed some ministry regulations regarding environmental.

The two (2) different ministries regulations should be synchronized between one another. Therefore, it needs to be compiled in a single

⁴⁸⁹ Article 40 clause (1) paragraph 2 of Act No. 22/2001 on Oil and Gas.

⁴⁹⁰ Article 40 clause (1) paragraph 3 of Act No. 22/2001 on Oil and Gas.

⁴⁹¹ Article 40 clause (1) paragraph 4 of Act No. 22/2001 on Oil and Gas.

⁴⁹² Article 40 clause (1) paragraph 5 of Act No. 22/2001 on Oil and Gas.

⁴⁹³ Article 40 clause (1) paragraph 6 of Act No. 22/2001 on Oil and Gas.

handbook to be able read and implemented by relevant stakeholders. Further, the Ministry of Labour is also needs to develop a standard on labour as part of the implementation of mandatory CSR programmes.

5. Act Number 20/2008 on Micro, Small and Medium Scale Enterprise

This Act is officially passed to adapt the needs of micro, small and medium scale enterprise to do its business operation throughout the country. The micro, small and medium entrepreneurs are empowered by the Ministry of Cooperative and Small Medium Enterprise. The Act mentions that one of funding resources for the enterprise development and micro, small and medium enterprise empowerment is through CSR funds.

It is clearly stated on the Act mentions that “the SOE can provide source of funding from annual profit saving allocated for Micro and Small enterprise in the forms of loan, insurance, grant, and other items”.⁴⁹⁴

Further, following Article mentions that “national and international business enterprises may allocate funds to small and medium enterprise in the forms of loans, guaranty, grants, and others”.⁴⁹⁵

Both Articles reveal that the SOE, national and international business enterprise can allocate any loan, insurance, grant and other expenditures for cooperatives, micro, small and medium enterprises in Indonesia. It would have strengthen the commitment of business enterprises to support

⁴⁹⁴ Article 21 (2) Act No. 20/2008 on Micro, Small and Medium Enterprises.

⁴⁹⁵ Article 21 (3) Act No. 20/2008 on Micro, Small and Medium Enterprises.

the sustainability of cooperatives, micro, small and medium enterprises in Indonesia.⁴⁹⁶

They may save a little part of their annual profit for the purpose of assisting and empowering the cooperatives, micro, small and medium enterprises. Subsequently, Ministry of SOE also have released several policies to support them and launched social programmes such as PKBL and CSR.

According to the legal provisions of the Act, the researcher concludes that one of important aspects of mandatory CSR is about economic empowerment aspect. Therefore, it needs to develop a Standard Operating Procedures (SOP) on economic empowerment in the use of CSR funds. Further, there should be a synchronization between Act Number 25/2007 on Investment, Act Number 40/2007 on Limited Company Liability and Act Number 20/2008 on Micro, Small and Medium Scale Enterprise to provide alternative source of funding for micro, small and medium enterprises in Indonesia. Several issues should be synchronized are as follows; CSR funds disbursement mechanism, eligibility of beneficiaries, allocation of CSR amount, and format of proposal.

6. Act Number 11/2009 on Social Welfare

The Act of Social Welfare was enacted as the state responsibility to protect all Indonesia citizens and to realize a decent life in achieving social welfare. The Act is implemented by the Ministry of Social Welfare of

⁴⁹⁶Ibid

Indonesia as an authorized ministry in conducting social activities. It mentions that one of the funding resources of the social activities is “the saving funds are intended as the social and environmental obligatory.”⁴⁹⁷

It shows an expectation that the CSR funds from companies can be one of the potential fund resources to sponsor social activities conducted by the Ministry of Social Welfare. Therefore, the Ministry of Social Welfare initiates and supports any activities proposed to save the company profits as the source of funding for the social activities.⁴⁹⁸ One of regular activities conducted by the Ministry of Social Welfare is appreciating CSR works by giving CSR Awards.

Further, R14 mentioned that the Ministry of Social Affairs is also to facilitate the establishment of Consortium CSR which is a group of CSR organizations, both private and SOEs, non-governmental organizations and academics.⁴⁹⁹

This Act views that the CSR funds is one of the alternative funding resources that can be used to sponsor any social programmes in Indonesia. In one hand, it is useful but on the other hand, it needs to be clarified in what extent CSR fund may finance social programmes. It needs to be further regulated related to types and forms of social programmes might be funded by CSR fund, beneficiaries identification, procedures of supervision, evaluation, and reporting mechanism.

According to the information is provided by those articles, it needs to be further regulated in relation to social programmes that can be funded by

⁴⁹⁷ Article 36 sub-section d of Act No. 11/2009 on Social Welfare.

⁴⁹⁸ Ibid

⁴⁹⁹ *Op. Cit*, Interview on 3 October 2013 in Jakarta.

CSR funds. There should be clear arrangement between social activities that being the core mandate of the Ministry of Social Affairs as it is mandated by the constitution and social activities that is directly related to the presence of extractive industries that may socially affect the society surrounded the companies in which they operate.

7. Act Number 32/2009 on Environmental Management and Protection

The Act is also mention about environmental protection aspects which are correlating with mandatory CSR legal provision. It because of the legal provision mandated all companies are operating their businesses in Indonesia must implement CSR programme as mandatory. Further, the Act is also mention provision related to environmental protection as the following; in order to preserve the environment, the central and provincial government must develop and implement the economical instrument of environment.⁵⁰⁰ Further, the economical instrument of environment as mentioned in clause (1) includes; a) the development planning and economical activities, b) the funding on environmental; and 3) incentives and/or disincentives.⁵⁰¹

It affirms that the corporate whose run bussiness in natural resource sectors or their operations closely related to environments are obliged to draft an enterprise development plan on the economical and environmental matters. Unfortunately, due to lack of supervision and monitoring the provision are not implemented well in the field. It needs to be upgraded in term of monitoring and evaluation mechanism in the future.

⁵⁰⁰ Article 42 paragraph 8 of Act No. 32/2009 on Environmental Management and Protection.

⁵⁰¹ Ibid

Therefore, According to R24 emphasized that the business enterprises should draft its business based on the balance between natural resources availability and environmental protection interest.⁵⁰² Unfortunately, due to lack of supervision, controlling, monitoring and evaluation from authorised parties, then the provision is not yet well implemented.⁵⁰³

Moreover, it needs to be synchronized with Article 74 of Act No. 40/2007 on Limited Company Liability in order to avoid overlap arrangement between Act No.32/2009 on Environmental Management and Protection and Limited Company Liability. Unfortunately, due to lack of transparency from the business enterprises itself in publishing what they already paid to the Government, then the public as the main stakeholders of the natural resources are always insisting on the funds to companies. In the future, there should be developed a transparency mechanism on the payment to the Government related to the funds for environmental restoration and conservation.

Moreover, incentives and/or disincentives as mentioned in Article 42 (3) paragraph c includes: procurement of goods and services that are environmentally friendly, the application of taxes, levies, environmental subsidies, the development of system of financial institutions and capital market-friendly environment and the development of waste disposal permit trading system and/or emissions.⁵⁰⁴

⁵⁰² *Op. Cit*, Interview on 28 October 2013 in Jakarta.

⁵⁰³ *Ibid*

⁵⁰⁴ Article 43 Clause (3) of Act Number 32/2009 on Environmental Management and Protection.

Further, development of environmental service payment system, the development of environmental insurance, the development of environment-friendly labeling system and performance reward systems in the field of environmental protection and management.⁵⁰⁵ Finally, further provisions regarding environmental economic instruments referred in Article 42 and 43 paragraphs (1) to (3) stipulated in the Government Regulation.⁵⁰⁶

It says clearly on the Act that environmental service payment system is closely correlating with mandatory CSR legal provisions. The two (2) legal provisions have the same spirit which are the business enterprises should be more socially and environmentally responsible in conducting their business activities.⁵⁰⁷ At last, it needs a synchronization and harmonization between the 2 (two) legal provisions in the future.

In relation to the situation, it clearly shows that any corporates who exploit the natural resources and brings about a disadvantage broad impacts for the environment are urged to develop an instrument of environmental funding.⁵⁰⁸ It is previously regulated in Article 74 “where any corporates whose bussiness in/or the natural resource sector are obliged to implement Social and Environmental Responsibility.”

Moreover, the Article above is also reaffirm that the instrument of enviromental funding are categorized into 3 (three) types of funding, namely; the guarantee fund on environmental restoration, the funds for

⁵⁰⁵ Ibid

⁵⁰⁶ Article 43 Clause (4) of Act Number 32/2009 on Environmental Management and Protection.

⁵⁰⁷ Ibid

⁵⁰⁸ Article 43 Clause (2) of Act No. 32/2009 on Environmental Management and Protection.

pollution mitigation and/or environmental damage and restoration; and the trust funds/support for conservation.⁵⁰⁹

It will become increasingly interesting that Article 74 on the Social and Environmental Responsibility in the Act No. 40/2007 on Limited Company Liability is consistent with Article 43 (2) Act No. 32/2009 on the Environmental Management and Protection. Both has become increasingly apparent that there is such a strong correlation between CSR policy as a legal obligation for companies operating in the field and/correlated to natural resources to implement the social and environmental responsibility with instrument environmental funding as mentioned on Article 43 (2) Act No. 32/2009 on the Environmental Management and Protection.

According to the provisions above, the researcher concludes that it raises a set of further questions that whether the CSR funds allocated by the companies shall be used to sponsor activities or programmes as referred in Article 43 (2) or the CSR funds can only be used to support activities that has been classified as CSR programmes. It requires further discussion and in-depth research to find the answers.

There should be a clear provision relates to the 2 (two) issues above. It needs to be described to avoid any overlaps on the allocation and the use of the funds. However, at least this study can provide a depth analysis on the purpose and use of CSR funds as regulated in Article 74 on Corporate Social and Environmental Responsibility No. 40/2007

⁵⁰⁹Ibid

The synergy between Act No.40/2007 on Limited Company Liability and Act No. 32/2009 on the Environmental Management and Protection is absolutely necessary in enhancing the implementation of mandatory CSR programmes as a legal obligation in Indonesia. Basically, CSR has 3 (three) basic components called as three bottom-up lines namely social, environmental, and economic empowerment. Particularly with regard to the environmental protection has been regulated in the Act No.32/2009 on the Environmental Management and Protection.

8. Act Number 4/2009 on Coal & Mineral Mining

Act on Coal Mining and Minerals brings a particular interest on partnership issues between corporates and communities surrounding the mining location. Further, community development issue as an important, priority, and strategic aspects in the development of mining bussiness.

One of the most important provision is about the license for mining exploration must include at least the development planning and community development for the people surrounding the mining locations. It means that the provision requires any business enterprises are doing mining activities to draft their community development planning prior to conducting their exploration activities.

Moreover, it says that the license for mining production as mentioned in Article 36 (1) huruf b must consist of at least the development planning and community development for the people surrounding the mining

locations.⁵¹⁰ It shows clearly that the provision also requires any business enterprises to draft community development plan prior to conducting their production activities.

The technical steps for those things are still unavailable and not well informed to the society in which the business enterprises are operating. Further, lack of supervision, monitoring and evaluation for the implementation of the provision from authorised ministries.

There is an inter-related relationship between Act No.40/2007 on Limited Company Liability, Act No. 32/2009 on Environmental Management and Protection and Act No. 4/2009 on Coal and Mineral Mining. The inter-related relationship is shown in Article 74 on Social and Environmental Responsibility obliges the CSR programmes for any corporations who are operating their businesses in the natural resources sector.

Indeed, the sectoral laws are also had regulated the norms and standards concerning the implementation of CSR, unfortunately it is not a part of the implementation strategy for mandatory CSR programmes in the area of social, environmental and economic empowerment. Further, R3 mentioned that there should be alignment and adjustment regarding those relevant sectoral laws. In the long term, there should be a compilation and codification of those policies in the future.⁵¹¹

⁵¹⁰ Article 36 (2) Paragraph n of Act No. 4/2009 on Mineral and Coal Mining.

⁵¹¹ *Op. Cit*, interview on 13 September 2013 in Jakarta.

Meanwhile, the corporations are urged to prepare an instrument for environment funding.⁵¹² Further, the Act is also re-affirms community roles and participation on determining the mining location and the implementation of the obligation by enclosing the development and empowerment plan.

The local people is one of priorities of the mining companies to be developed because the people close to the mining location as the pre-requirement conditions to obtain mining production and exploration licenses.⁵¹³ It means that, if the government really control the implementation of the provision, therefore no single corporations may ignore their obligations to empower local community in which they operate.

The participation of communities, non-governmental organizations, and government both central and provincial are crucial in controlling and ensuring that all legal provisions are implemented well. Those legal provisions must be implemented properly in favour of the local people. It because of the local people are more vulnerable compared to the corporations.

9. Act Number 11/2006 on Governing Aceh

This Act was issued by the central government as the implementation of peace agreement between Indonesia Government and Free Aceh Movement in Helsinki, Finland. The issuance of this Act becomes the new

⁵¹² Article 43 (2) Act No. 32/2009 on Environmental Management and Protection.

⁵¹³ Article 10 of Act No. 4/2009 on Mineral and Coal Mining.

milestone for the Aceh people as the prolonged conflicts which has sacrificed thousands of deaths in Aceh.

The obligation of every mining corporation in Aceh is to provide community development funds.⁵¹⁴ The amount agreed by the provincial and regency government is at least 1% (one percent) of the total production sold each year.⁵¹⁵ Even, it is affirmed that the proposal of funding for community development programmes is drafted together by the people surrounding the corporations, other related communities and the corporations itself.

Moreover, the funding management and community development are directly administered by the corporations.⁵¹⁶ Particularly for Aceh as it has a right to regulate its domestic affairs based on a special Act, the implementation of CSR programme can ignore Act No. 40/2007 on Limited Company Liability and Government Regulation No.47/2012 on Social and Environmental Responsibility of Corporates. The government of Aceh is mandated to issue Aceh Qanun to further regulate the use mechanism of the fund and types of community development programmes.

The researcher concludes that the Act is specifically implemented for Aceh but the implementation should be clearly stated on the relevant Government Regulation that the implementation of special Act for Aceh on CSR is part of the implementation Article 74, as prescribed in Act Number 40/2007 of Limited Company Liability. There should be a clear

⁵¹⁴ Article 159 of Act No. 11/2006 on Governing Aceh.

⁵¹⁵ Ibid

⁵¹⁶ Ibid

public participation standard, reporting procedure, monitoring and evaluation mechanism for the implementation of CSR in Aceh.

10. Act No. 19/2004 on Forestry

This Act regulates several legal provisions related to CSR. Some of the articles are as the following; exploitation of forest is aiming at obtaining maximum benefit for the people's welfare and by ensuring its sustainability.⁵¹⁷ There is a concern to preserve and to conserve the environmental resources in the activities of natural resources exploitation. If it is fully obeyed by corporation in mining and other natural resources industries, then the sustainability of natural resources is beyond question.

Further, in order to empower the community economic sector, any state-owned enterprises, regional-owned enterprises, and Indonesian private corporations which obtain license for environmental exploitation, forestry product wood and non-wood, are obliged to collaborate with the local cooperative.⁵¹⁸ In relation to environmental conservation, the business enterprises are also encouraged to closely collaborate their businesses practices with local community resources as part of economic empowerment.

Moreover, some basic principles of human rights are also mentioned on the Act namely to ensure the principles of justice, equality, and sustainability.⁵¹⁹ Further, the license for forest exploitation shall be limited

⁵¹⁷ Article 23 of Act No.19/2004 on Forestry.

⁵¹⁸ Article 30 of Act No.19/2004 on Forestry.

⁵¹⁹ Article 31 Paragraph 1 of Act No.19/2004 on Forestry.

by considering the forest sustainability and business certainty aspects.⁵²⁰ Basic principles such justice, equality and sustainability should be further elaborated by business enterprises together with other relevant stakeholders. The 3 (three) basic principles are very crucial to create a harmony between the local community and business enterprise. If it is consistently implemented by the business enterprises, it may create a good and long term relationship among them.

The rights of indigenous peoples are also recognised by the Act. Customary law of a particular community as long as they are acknowledged and still exist is deserve for collecting the forest products to fulfill their basic needs.⁵²¹ Further, the indigenous peoples are also entitle to undertake forest management activities as the customary law applied and agraph with the Act and having a right for an empowerment in order to improve their prosperity.⁵²²

Finally, the communities are deserve for the benefits of a good environmental quality products by the forests besides the rights mentioned in paragraph (1).⁵²³ The people could make the best use of forest and its products according to the applicable Act.⁵²⁴ Further, acknowledge the plans for forestry allocation, the use of forestry product, and forestry information.⁵²⁵

⁵²⁰ Ibid

⁵²¹ Article 67 Paragraph 1 of Act No.19/2004 on Forestry.

⁵²² Ibid

⁵²³ Article 68 Paragraph 2 of Act No. 19/2004 on Forestry.

⁵²⁴ Ibid

⁵²⁵ Ibid

The researcher concludes that the Article has described obviously the rights of indigenous peoples concerning forestry exploitation and conservation. The Standard Operating Procedures (SOP) and monitoring and evaluation standards should be jointly developed by the business enterprises, local community, and government facilitation. Therefore, each party should be aware of its own position and functions to succeed the implementation of the legal provisions.

Moreover, the community participation is also recognised in which the community may also provide information, advise, and consideration for forestry development and to supervise the implementation of the forestry development either directly or indirectly.⁵²⁶ The implementation of public participation should be clearly regulated and developed a standard to ensure the provision can be implemented well.

12. Government Regulation Number 93/2010 on the National Disaster Recovery Donation, Research and Development Donation, Educational Facility Donation, Sport Development Donation, and Social Infrastructure Development Costs Deducted from Gross Profit

The government regulation provides a special treatment for corporations who support the social activities as stated in the regulation. Further, corporations are to draft their CSR programmes aligned to the regulation. Consequently they only implemented CSR programmes in the spirit of the social activities as mentioned by the regulation. The intention is to obtain tax deduction from the government based on the regulation.

⁵²⁶Ibid

The government passed the regulation to encourage corporations to support the social activities as mentioned in the regulation. Further, there is a demand on tax deduction policy from the corporations. R8 stated that there should be a synchronization and harmonization between Government Regulation No.93/2010 and Government Regulation No. Corporate Social and Environmental Responsibility.⁵²⁷

The regulation offers tax deduction to corporations who (1) participate in national disaster mitigation activities, (2) contribute in research and development, (3) lead educational development, and (4) contributes sport and social infrastructure development costs in Indonesia.⁵²⁸ Therefore, R3 mentioned that there are still many coprorations which consider CSR programmes as donation activities without a sustainability aspect.⁵²⁹ Whereas, CSR programmes are derived from a spirit of empowerment.⁵³⁰ Hence it is not only seen as a donation but also as a process of empowering the local community as part of the corporations' long-term business plan.⁵³¹

However, several corporations might have campaigned that they have already implemented CSR programme by donating some amount of money for national disaster recovery, research and development activities, educational development, sport development donations, and social

⁵²⁷ *Op. Cit*, Interview on on 25 September 2013 in Depok.

⁵²⁸ Article 1 paragraph a, b, c, d and e of Government Regulation No.93/2010 on National Disaster Recovery Donation, Science and Knowledge Development Donation, Educational Facility Donation, Sport Development Donation, Social Infrastructure Development Cost Deductible from Gross Revenue.

⁵²⁹ *Op. Cit*, Interview on 13 September 2013 in Jakarta.

⁵³⁰ *Ibid*

⁵³¹ *Ibid*

infrastructure development costs in Indonesia. In fact, there is no specific mechanism used by these corporations to identify their main beneficiaries and to avoid any overlap with other government empowerment programmes. Given these points there should be a clear coordination and communication among the stakeholders.

R8 stated that the government should provide a standard and legal certainty relating to several social activities that are still considered blur and overlapping.⁵³² A standard and legal certainty are needed to prevent any fraud in practice.⁵³³ Otherwise, if there is no proper information and manual on the CSR categories of programmes, whether it is called a philanthropy or community development. Those companies who claimed they have implemented CSR activities might have just donated some cash money to the people. Some of the activities may not even be categorised as CSR activities as mentioned in other regulations.

Based on a description above, the researcher assumes that the government, together with the corporations and local community as the main beneficiaries, should discuss further regarding the standard of implementation for CSR programmes in Indonesia. The discussion should include ascertaining the classification and categories of CSR programmes.

13. Government Regulation Number 47/2012 on Corporates Social and Environmental Responsibility (TJSL)

The regulation was issued as a response on the mandate of Act No.40/2007 regarding Limited Company Liability where each corporations

⁵³² *Op. Cit*, Interview on 25 September 2013 in Depok.

⁵³³ *Ibid*

who operates business in natural resource sectors are obliged to perform the social and environmental responsibility.⁵³⁴ Further, R8 stated that mandatory CSR legal provision is intended to increase an awareness of the corporations toward the implementation of social and environmental responsibility in Indonesia.⁵³⁵

Further, it encourages the corporations to fulfill the interest of local community regarding their social and environmental responsibilities.⁵³⁶ Indeed, it may also strengthen the arrangement of social and environmental responsibility has been enacted in other sectoral regulations according to the corporations business sector. Eventhough, the government regulation passed in April 2012 after nearly 4 (four) years since the enactment of Act. No. 40/2007 in August 2007.

The prolonged progress of CSR legislation is caused by the affinity interest between the government and the corporations. The corporations insist that the government regulation will motivate local government either provincial government or district or city government to pass local regulations on CSR.

Further, R4 as CSR expert mentioned that the enactment of CSR mandatory legal provision may burden the corporations financial status in the midst of the uncertainty condition of the world economy situation.⁵³⁷

Whereas, the implementation of the mandatory CSR programmes is

⁵³⁴ Article 74 of Act No. 40/2007 on Limited Company Liability.

⁵³⁵ *Op. Cit*, Interview on 25 September 2013 in Depok.

⁵³⁶ *Ibid*

⁵³⁷ *Op. Cit*, Interview on 15 September 2013 in Jakarta.

implemented based on decency and fairness principles of the corporation's financial ability.⁵³⁸

The corporations, even, states that the issuance of the government regulation affects the competitiveness of good and services were produced by the corporations in Indonesia. It will be uncompetitive because of the obligation to allocate fees for implementing mandatory CSR programmes which is it may increase the selling prices of their products.

The legal drafting process of government regulation on CSR has not fully considered the involvement of community as beneficiaries and also has not fulfilled justice principle. It showed where there is no single article affirms the community participation. Moreover, there is no specific provision to differentiate between CSR, philanthropy, and community development programmes. The obscurity in determining beneficiaries, audit institution on mandatory CSR activities and penalties for the companies who do not properly implement their mandatory CSR programme are some examples of incomplete of the regulation drafting process.

Any limitations and crucial points have not yet been accommodated on the government regulation shows that mandatory CSR as a legal obligation in Indonesia is still being debated among some business associations, practitioners and ministry. Despite Constitutional Court which affirms that Article 74 on CSR is still consistent with the constitution of Indonesia.

⁵³⁸ Article 74 Clause (2) of Act No. 40/2007 on Limited Company Liability.

14. Provincial Regulation of the East Java Province Number 4/2011 on Corporate Social Responsibility

This local regulation was initiated by the provincial government of East Java. It was passed before the Government Regulation No. 47/2012 regarding Social and Environmental Responsibility of Corporates issued. Article 11 point 1 states that “ the corporate social responsibility includes social and community development, small, micro, and enterprise cooperation partnership and direct programme for communities.”⁵³⁹

Moreover, Article 11 point 2 mentions “the programmes as proposed in point 1 are intended to improve the social welfare, increase the economical growth of the community, strengthen the sustainability of entrepreneur, and maintain sustainable environmental functions.”⁵⁴⁰

The provincial regulation is considered a proper and strategic sample in arranging CSR activities on the regional level, regardless of the absence of Government Regulation on CSR. The provincial government of East Java Province passed the provincial regulation on CSR although the government regulation was still not available yet. The legislation process should be appreciated as a breakthrough on legal matters especially for CSR issues.

Nonetheless, drafting the local regulation requires an appropriate guideline from the central government so that the regulation meets with the national interest of CSR. The provincial regulation of the East Java Province regarding the Corporate Social Responsibility is a quantum leap

⁵³⁹ Provincial Regulation of East Java Province No. 4/2011 on Corporate Social Responsibility.

⁵⁴⁰ Ibid

taken by the provincial government to establish a legal basis for implementing CSR in the province.

The provincial regulation of the East Java Province was passed by the Provincial Assembly before government regulation on CSR is passed by the central government. The provincial regulation has been challenged by business enterprises. They considered the legislation process illegal due the absence of a legal basis for the Provincial Assembly to pass the provincial regulation without government regulation in advance. This has led to a pro-contra between the provincial government and the business enterprises.

R8 mentioned that without any appropriate coordination, synchronization, and harmonization, the existence of various policies concerning CSR may lead to an unhealthy business and investment climate in Indonesia.⁵⁴¹

Moreover, the substance becomes “wider” and is not fully focused on regulating the implementation of mandatory CSR in Indonesia. The issuance of Government Regulation No.47/2012 on CSR has proven that the substance of the government regulation is really wide and is not really focused on answering some problems regarding mandatory CSR in Indonesia. Apparently the substance merely includes normative articles, and there is no particular and profound articles related to CSR implementation in Indonesia.

⁵⁴¹*Op. Cit*, Interview on 25 September 2013 in Jakarta].

The fact that the number of CSR experts is lacking in Indonesia can lead to the mandatory CSR implementation being less effective. Implementing the provision still requires a special and independent institution to manage, control, supervise, and evaluate the programmes.⁵⁴² It is expected that the institution can bridge the interests between ministries and provincial government on the implementation of CSR.⁵⁴³

Following is the chart of CSR changing process in Indonesia in which there will be a policy evolution from voluntary to mandatory point, and will be in the post-mandatory point in the future where the company is enforced to be more socially and environmentally responsible.

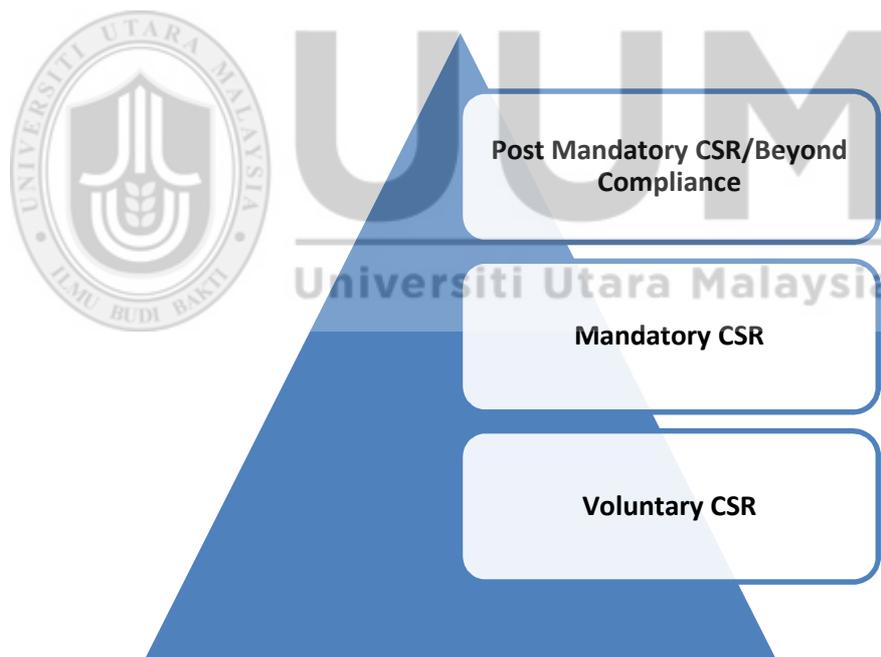


Figure 1.3. Corporate Social Responsibility Policies Cyclus in Indonesia

A number of acts and regulations on CSR has indicated that many stakeholders have put their concerns on CSR projects. Hence these projects

⁵⁴² Ibid

⁵⁴³ Ibid

should be arranged in a more detailed regulation and also there should be a specific agency mandated by the law to manage the day-to-day CSR implementation process in Indonesia. It is expected that all the CSR issues currently scattered in many different acts and regulations can be compiled in one single regulation.

5.3.2 Corporate Social Responsibility Guidelines in International Arena

Each of the following guidelines listed below has its own characteristics, standards, and procedures in providing a certification to companies. The guidelines are currently implemented in the country.

1. ISO 26000 on Social Responsibility

ISO 26000 on Social Responsibility is the standard used by buyer of products and services in order to assess the sustainability level of the products or services exported by the exporters from countries outside the European Union. The standard is an international consensus that consists of requirements regarding social responsibility principles.

ISO 26000 was launched to the public in November 2010 to provide technical and practical guidance about the procedures of (1) implementing CSR activities, (2) identifying and communicating with stakeholders, (3) increasing the credibility and accountability reports, and (4) settling public claims and disputes related to the CSR programme.

ISO 26000 can be used universally either by various countries, organizations, companies, operations management, or supply chain management in order to improve their performance in carrying out CSR

programmes. Although it can be universally applicable, its application is still voluntary in accordance with the acceptance of stakeholders.

ISO 26000 on Social Responsibility was launched by an organization called the International Organization for Standardization.⁵⁴⁴ The organization has spent about 19500 international standards covering almost all aspects of life from technology, manufacturing, agriculture, computer, health, and food safety.

ISO is an acronym derived from the Greek language "*isos*" which means equal.⁵⁴⁵ Due to differences in language and meaning of each member country, the founders of the International Organization for Standardization later established that the standard acronym would be issued by name ISO so that every member country will have the same perception of meaning.

ISO has published several important standards used by the producers as well as consumers in the exporting and consuming goods and service. Among them are ISO 9000 on Quality Management, ISO 14000 on Environmental Management, ISO 3166 on Country Codes, ISO 22000 on Food Safety Management, ISO 26000 on Social Responsibility, ISO 50001 on Energy Management, ISO 31000 on Risk Management, ISO 4217 on Currency Codes and ISO 639 on Language Codes.⁵⁴⁶

A standard of goods and services products is needed in order to provide either requirement, specifications, guidelines, or characteristics that should be obeyed by manufacturers in producing goods and services.

⁵⁴⁴ International Standardization Organization, www.iso.org [Accessed on 24th August 2013].

⁵⁴⁵ Ibid

⁵⁴⁶ Ibid

Process of goods and services production includes materials, processes, and types of goods and services produced.

With the presence of a universally accepted standard, consumers can be protected from products and services that are not qualified and not safe for health. ISO as international standards exist in order to provide security for the consumers of goods and services so that there will be no significant concern for consumers to buy goods and services that have acquired ISO International standards.

Social responsibility means an obligation of an organization to the impact of decisions and activities related to social and environment. The impact contributes to sustainable development, expectations of stakeholders, obedience to law and consistency to international norms of behavior which is all carried out in a transparent and ethical behavior.

From the definition, it can be seen that the arrangement of the Social Responsibility is very broad covering several aspects such as sustainable development and adherence to international law and norms of behavior. Hence, transparency and suitable with ethical behavior, and thus the implementation of the principles of Social Responsibility is a must for producers of goods and services.

There are seven key principles in ISO 26000 on Social Responsibility, which are; accountability, transparency, ethical behaviour, respect for the interest of organization, respect for the rule of law, respect for international norms of behaviour and respect for human rights principles.

ISO 26000 is only an ethic standard developed by the International Organization for Standardization in order to provide protection to the health and quality of goods and services traded by the manufacturers. ISO 26000 on Social Responsibility can not be used as standard to audit, conformity test or compliance statements.

The principles contained in ISO 26000 on Social Responsibility are merely a number of principles governing the socially responsible behavior that must be implemented by the parties in the implementation of CSR programmes. If the buyers of goods and services in the European Union demand a certain standard certification for goods and services sold, the manufacturer may request special certification related to issues that are more specific depending on market demand. For example, ISO 9001 on management quality certification, ISO 14001 on environment, OHSAS 18001 on Occupational Health and Safety or SA 8000 on Social Accountability.

There are several advantages that can be achieved by the producers when applying the principles of ISO 26000 on Social Responsibility, such as; competitive advantage, reputation, able to attract and retain workers, consumers, or users. Further, it can maintain the employees morale, commitment and productivity, positive view of share holders, investors, donors, sponsors and the financial community.

More over it is able to maintain good relationship with customers, stakeholders, government, suppliers, media and local community in which it operates. The benefits are long-term social investment to be achieved by the company in order to improve its performance as business

institution which is as a part of the community within the framework of corporate citizenship.

7 (seven) principles contained in ISO 26000 on Social Responsibility is independent factors and are not able to partially operate between one aspect to another. In fact, ISO 26000 can be applied in all types and sizes of organizations either in multinational, national, regional local levels companies. That is because ISO 26000 is universally designed so that it can be applied in all situations without terms conditions.

ISO 26000 is designed to complete the instruments and initiatives in order to strengthen aspects of company social responsibility. Hence, encouraging companies to implement CSR programmes beyond compliance where one of its most important aspects is the adherence to applicable laws. ISO 26000 can also help companies to produce goods and services more competitive and more sustainable.

The companies are implementing ISO 26000 on Social Responsibility are advised to consider the aspects of social, environmental, differences in economic conditions, politic, culture, and legal law as well as to remain consistent with international norms of behavior.

Thus, the existence of ISO 26000 on Social Responsibility is a source of inspiration and encouragement for its users in order to improve the performance of the companies. Although it is voluntary and not legally binding, many international organizations provide training for the implementation of ISO 26000 on Social Responsibility as Global Reporting Initiative (GRI) and other consulting firms in each country.

In relation to Article 74 on Social and Environmental Responsibility of Act No.40/2007 concerning Limited Company Liability, there is a difference in meaning between voluntary and mandatory. The Article 74 confirmed that the implementation of CSR for companies engaged in natural resources fields or related will have a legal obligation to implement mandatory CSR.

Further, R8 stated that the mandatory CSR framework is based on laws of the Republic of Indonesia.⁵⁴⁷ As mentioned in one of the principles of ISO 26000 on Social Responsibility which is “*accept to respect the rule of law as mandatory*”,⁵⁴⁸ the application of Article 74 is not contrary to international norms of behavior as well as the principles set forth in ISO 26000 on Social Responsibility.

The major issue in Indonesia is the lack of guidance, guidelines and basic standards related to the implementation of mandatory CSR.⁵⁴⁹

However, Indonesia should pass ideas and policies about standards, guidelines or guidance for the implementation of mandatory CSR. It is needed by companies engaged in natural resources or related directly to the use of natural resources. Further, mandatory CSR guideline is needed in order to complete or as complement all guidelines or existing CSR standards such as ISO 26000 on Social Responsibility.

While the standards or guidelines for Indonesian version of mandatory CSR is under the drafting process, companies may use international standards or guidelines for the implementation of

⁵⁴⁷ *Op. Cit*, Interview on on 25 September 2013 in Depok.

⁵⁴⁸ *Ibid*

⁵⁴⁹ *Ibid*

mandatory CSR translate in accordance with the content and spirit of Article 74 on Social and Environmental Responsibility. In fact, there are some important and strategic points in the ISO 26000 on Social Responsibility that can be used as an initial discussion in order to draft and to develop Indonesian CSR Mandatory Guidelines.

The drafting process of ISO 26000 on Social Responsibility was also carried out over a long time and involved many relevant stakeholders. It consists of various parts of the world such as business associations, companies, government organizations, non-governmental organizations and some organizations of the European Union. Therefore, the applicability is based on voluntary commitment and the principles are not legally binding to Indonesia as a state entity because the signatories are not state entities.

Similarly, the process of preparing Indonesian Mandatory CSR Guidelines demands the involvement of multi stakeholders. Those are business associations, non-governmental organizations, representatives of ministries/state agencies, professional organizations, and provincial associations/districts/cities in Indonesia. In addition, the inputs and views presented in the draft of the guidelines may reflect the aspiration of the majority of stakeholders that are directly related to the implementation of CSR programmes.

Further, the researcher's opinion is the guidelines should be formalized through Government or Presidential Regulation to be legally binding and obeyed by all stakeholders. Finally, it will be used as a

manual for the process of controlling, supervision and evaluation of the implementation of mandatory CSR programmes in Indonesia.

According to some information were given by CSR experts from various background, ISO 26000 on Social Responsibility can be used as an entry point for CSR stakeholders in Indonesia to draft Indonesian Mandatory CSR Guideline. The principles were provided by the ISO 26000 on Social Responsibility is really helpful for determining the basic needs of the local community as the main stakeholders of the CSR. At last, the drafting of ISO 26000 on Social Responsibility had involved a wider spectrum and stakeholders from various level and background.

2. Organization for Economic Cooperation and Development Guidelines for Multinational Enterprises

OECD stands for Organization for Economic Cooperation and Development.⁵⁵⁰ OECD principles are non-binding principles and standards for business enterprises in a global context.⁵⁵¹ It is align to regulatory frameworks and international recognized standards.⁵⁵² The principles stated in OECD guidelines are those which encourage positive contribution from world business towards economic development, environment protection and social life in every company in which it operates.⁵⁵³

⁵⁵⁰ Organization for Economic Cooperation and Development, <http://www.oecd.org/>, [Accessed on 5 April 2014].

⁵⁵¹ Organization for Economic Cooperation and Development, OECD Guidelines for Multinational Enterprises [Paris, OECD Publishing, 2011], 3.

⁵⁵² Ibid

⁵⁵³ Ibid

Although OECD is voluntary, in practical there is an institution called the National Contact Points (NCP) agencies of which duty is to assist companies and other stakeholders in translating these principles in practice. NCP was formed by the respective governments of the countries that joined the OECD. NCP also provides mediation services and consolidation towards disputes which may arise between the parties.

With the implementation of such mechanism, the OECD Guidelines can quickly implement CSR programmes and resolve disputes arising between the parties through mediation and conciliation. Up to now, there are 42 (forty-two) countries that have been registered as members of the OECD. Indonesia is not a member country of OECD. In fact, OECD provides opportunities for non-OECD member countries to implement the OECD guidelines in their respective countries as long as they sign a waiver stating that they will voluntarily subject to the OECD guidelines.

OECD guidelines were designed by involving various stakeholders in many parts of the world such as Governmental Organizations, Non-Governmental Organizations, worker's organization, and business associations.⁵⁵⁴ Moreover, there have been conducted several consultative regional meeting in the following areas such as Asia, Africa, Latin America, the Middle East and the North Africa.⁵⁵⁵

Wide range of experts and scholars has been also actively engaged within the Advisory Group of the Chair of the Working Party

⁵⁵⁴ Organization for Economic Cooperation and Development, OECD Guidelines for Multinational Enterprises [Paris, OECD Publishing, 2011], 4.

⁵⁵⁵ Ibid

Responsible for the Update of the *Guidelines*.⁵⁵⁶ It shows extremely that a very diverse stakeholders and participants were involved during the updating process of the guidelines.

The guidelines were stated on the document as entirely voluntary basis and not legally enforceable.⁵⁵⁷ Nevertheless, some part of it can be implemented by national law and international commitment. Subsequently, it should also consistent with applicable laws and internatinally recognised standards. Obeying domestic laws is the first obligation of the enterprise.⁵⁵⁸

In accordance with Article 74 of Act No. 40/2007 on Limited Company Liability, then the researcher concludes that it is very clear that international standard or guidelines like OECD is also recognise and acknowledge domestic laws as the first obligation to be followed by the enterprises.

In relation to above opinion, it means that there is no major contradiction between mandatory CSR legal provision that has been enshrined by Indonesiaan government with international norms of behaviour or even written guidelines like OECD guidelines.

The guidelines is also not to make different treatment between multinational enterprises and local enterprises but the guidelines is only a good practice of business to guide the enterprises to behave in the interest of society. Furthermore, the guidelines may be able to prevent enterprises

⁵⁵⁶Ibid

⁵⁵⁷ Organization for Economic Cooperation and Development, *OECD Guidelines for Multinational Enterprises*, [Paris, OECD Publishing, 2011], 17.

⁵⁵⁸Ibid

to do misconduct or any other business activities that may against the domestic law in which they operate.

The government of a country is subject signatures to the guidelines voluntarily, and then the government (which is already a signatory to the guidelines) can use the guidelines as a guide in monitoring and controlling the business activities of enterprises in each country. Hence, compared with mandatory CSR legal provision, the provision is intended to legally binding all enterprises within Indonesia territory without any signatories. The mandatory CSR legal provision is a policy that comes from the state itself to implement human rights principles through to protect, respect and remedy framework.

Therefore, the most important point at the guidelines is the acceptance of particular government to the OECD guidelines and being its signatory party. Consequences, the government would be expected to establish a National Contact Points (NCPs) in its own country. Moreover, the signatories can not use the guidelines as a tool to protect of its domestic products against other products from other countries either member state of OECD or non-member state of OECD.⁵⁵⁹

There are a number of points that should be obeyed by enterprises in the framework of OECD guidelines voluntary implementation are as follows; enterprises should contribute to economic, social and environmental development in the view of sustainable development, respect for international recognised human rights principles and

⁵⁵⁹ Organization for Economic Cooperation and Development, *OECD Guidelines for Multinational Enterprises* [Paris, OECD Publishing, 2011], 18.

encourage strong cooperation with local communities around its business operation.⁵⁶⁰

The enterprises are encourage to implement the guidelines to its supplier, contractors or sub-contractors in order to prevent or mitigate adverse impacts of its business practice, engaging with relevant stakeholders when its decisions may bring significant impacts to the local communities and stay away from direct or indirect involvement of any political activities within the countries.⁵⁶¹ At this point, the main words that has been used by the guidelines is to encourage or to recommend, there is no word to impose because the guidelines is generally is intended for implementing international good business practices on voluntary basis.

The guidelines recommend the enterprises not to involve or to contribute to any human rights violations in which country they operate either direct of indirect involvement.⁵⁶² The guidelines also encourage the enterprises to develop their internal policies to demonstrate their strong commitment to human rightst principles.⁵⁶³ Moreover, the enterprises are also advised to seek any solutions or alternative way out to prevent or mitigate any adverse human rights impacts that linked to their business operations.⁵⁶⁴

⁵⁶⁰ Organization for Economic Cooperation and Development, OECD Guidelines for Multinational Enterprises [Paris, OECD Publishing, 2011], 19.

⁵⁶¹ Organization for Economic Cooperation and Development, OECD Guidelines for Multinational Enterprises [Paris, OECD Publishing, 2011], 21.

⁵⁶² Ibid

⁵⁶³ Organization for Economic Cooperation and Development, OECD Guidelines for Multinational Enterprises [Paris, OECD Publishing, 2011], 32.

⁵⁶⁴ Ibid

In addition, the enterprises are also recommended to carry out human rights due diligence to identify the nature and complexity of human rights impacts.⁵⁶⁵ If they cause or contribute to the adverse human rights impact, then, they should provide a cooperative remediation and rehabilitation as necessary.⁵⁶⁶

Furthermore, in relation to environment matters the guidelines suggests the enterprises to protect environment, public health and safety within the framework of laws.⁵⁶⁷ Hence, regulations and administrative practices in the country in which they operate as well as respect to international principles, agreements and standards on environmental protection policies.⁵⁶⁸

There are two mechanisms that have been developed by OECD to ensure all guidelines principles are well implemented and adhered by by signatories' parties.⁵⁶⁹ They established National Contact Point (NCP) and Investment Committee which is functioning as a supervisory board in which reviewing the relevancy of guidelines principles from time to time upon request by its member.⁵⁷⁰

Overall, the guidelines fully cover all specific issues related to responsible business conduct principles.⁵⁷¹ Apparently, the guidelines still recognize and respect for applicable domestic laws and regulations in a

⁵⁶⁵ Organization for Economic Cooperation and Development, OECD Guidelines for Multinational Enterprises [Paris, OECD Publishing, 2011], 33.

⁵⁶⁶ Ibid

⁵⁶⁷ Ibid

⁵⁶⁸ Organization for Economic Cooperation and Development, OECD Guidelines for Multinational Enterprises [Paris, OECD Publishing, 2011], 42.

⁵⁶⁹ Organization for Economic Cooperation and Development, OECD Guidelines for Multinational Enterprises [Paris, OECD Publishing, 2011], 68.

⁵⁷⁰ Ibid

⁵⁷¹ Ibid

specific countries regarding good business practices.⁵⁷² Further, the applicable domestic laws and regulations should also align to the spirit of international human rights principles and other recognised responsible business standards.⁵⁷³

The guidelines said that the first obligation and observance of the enterprises are respecting for domestic laws and regulations in which they operate.⁵⁷⁴ The guidelines will never discriminate between multinational or domestic enterprises or even replace any existing applicable laws and regulations in a specific country.⁵⁷⁵ The applicability of the guidelines are strictly applied to the members of OECD. Indonesia is not a member of OECD countries so that the OECD principles are not legally binding for Indonesia as a state entity.

Indeed, the guidelines will be functioning as complementary tools of the existing one and enhancing it.⁵⁷⁶ In addition, the guidelines are also encouraging the business enterprises to develop self-regulatory instruments which is align to the spirit of domestic laws in which they operate and international recognised standards.⁵⁷⁷

Hence, according to the above description, the researcher's opinion is the voluntary based principles on OECD guidelines is not contradicting with mandatory CSR legal provision that is currently being applied by government of Indonesia for natural resources based companies. Indeed,

⁵⁷² Organization for Economic Cooperation and Development, OECD Guidelines for Multinational Enterprises [Paris, OECD Publishing, 2011], 17.

⁵⁷³ Ibid

⁵⁷⁴ Organization for Economic Cooperation and Development, OECD Guidelines for Multinational Enterprises [Paris, OECD Publishing, 2011], 18.

⁵⁷⁵ Ibid

⁵⁷⁶ Ibid

⁵⁷⁷ Organization for Economic Cooperation and Development, OECD Guidelines for Multinational Enterprises [Paris, OECD Publishing, 2011], 23.

the legal provision not against with the spirit of the guidelines and should also be observed by the companies who are doing business in Indonesia.

3. The Equator Principles

Equator Principles Financial Institutions (EPFIs) was formally established as an association which was named the Equator Principles Association (EPA) on 1 July 2010.⁵⁷⁸ The Equator Principles (EP) was established by several banking institutions to assess and to determine environmental and social risks. The aim was to provide guidance to the implementation of the principles in relation to management, administration and development within its membership organization.⁵⁷⁹

Currently, the equator principle has 78 members of financial institutions all over the world in 35 countries.⁵⁸⁰ Indonesia is not a member of the equator principles because the membership is banking institution only and not a state entity.

The membership is covering over 70% of international high scale project finance debt throughout the world. It showed that high impact of the equator principles has been playing in supporting financial institutions decision-making to finance international projects around the world. The membership of the association is on voluntary basis but once they being the association's member then it become mandatory for them to comply with all the equator principles.

⁵⁷⁸ The Equator Principles, <http://www.equator-principles.com/index.php/about-ep/about-ep/38-about/about/12> [Accessed on 29 August 2013].

⁵⁷⁹ Ibid

⁵⁸⁰ Ibid

The principles are adopted by financial institutions for determining, assessing and managing environmental and social risk. Hence, it is also to provide minimum due diligence to support responsible business decision-making. Further, by adhering to these principles its members can not just simply provide project finance or project-related corporate loans to clients in which unable to comply with the equator principles. It will prevent the financial institutions to provide loans to the clients that are not environmentally and socially responsible.

The principles are functioning as a risk management framework that will support financial sector and banking industry to identify, to define and to recognize its client before they agree to finance their projects.⁵⁸¹

The principles are being used by diverse financial institutions to reduce and to minimize environmental and social risks may appear during the execution of the funded-project.⁵⁸²

Moreover, the principles have greatly developed its scope of determining, assessing and managing responsible financial institutions conduct. It is not just limited to environmental and social risks factors but also cover indigenous peoples, labour standards and consultation mechanism with locally affected communities within the project's location.

As it is clearly stated on its guidance on environmental and social consideration that the equator principles are not require legal

⁵⁸¹ The Equator Principles, The Equator Principles June 2013 Version [The Equator Principles Publishing, 2013], 2.

⁵⁸² Ibid

framework.⁵⁸³ In another word, it is not legally-binding document that all members of the association should adhere to.⁵⁸⁴ If mandatory legal provision, the provision is legally-binding policy that all companies are doing business in relation to natural resources must respect for and adhere to the provision.⁵⁸⁵

Otherwise, the respective governmental institution will impose a punishment to the certain disobey company.⁵⁸⁶ Nonetheless, there are also benefits, economic incentives or rewards will be granted by the governments for those companies who are implementing mandatory CSR in a satisfied manner.⁵⁸⁷

Members of EPFIs may use the EP as a tool to measure reliability, accountability and complexity of specific project finance or project-related corporate loans within their institutions before they granted the loans to their clients.⁵⁸⁸ Loan agreement or sometimes people called it as investment agreement which is a legally-binding document signed by the borrower and representative of the financial institution.⁵⁸⁹

If the loan agreement has been signed and the loans have been granted but in the future, apparently the borrower did not comply with

⁵⁸³The Equator Principles, Guidance to The Equator Principles for Financial Institutions on Incorporating Environmental and Social Considerations into Loan Documentation, [The Equator Principles Publishing, 2013], 1.

⁵⁸⁴Ibid

⁵⁸⁵ Article 74 of Act No.40/2007 on Limited Company Liability.

⁵⁸⁶Ibid

⁵⁸⁷Ibid

⁵⁸⁸*Loc. Cit.*, The Equator Principles, The Equator Principles June 2013 Version, [The Equator Principles Publishing, 2013], 2.

⁵⁸⁹The Equator Principles Guidance to Equator Principles Financial Institutions on Incorporating Environmental and Social Considerations into Loan Documentation, [The Equator Principles Publishing, 2013], iii.

the agreed loan document.⁵⁹⁰ Then, which are environmental and social prohibitions were found then the lender will remind the client to promote compliance as agreed.⁵⁹¹ If the borrower fails to do so then the lenders reserve the rights to withdraw the loan without any condition.⁵⁹²

The EP is significantly able to encourage the borrower to comply with environmental and social requirements because it is included to the loan agreement. Consequences, best to his knowledge as agreed on the loan agreement to conduct such environmental and social measurement because he was signed and agreed based on voluntary agreement basis. There is a reciprocal situation there when the borrower needs some money then the lender may give them the money if they follow some rules as agreed by both parties.

The EP is a benchmark for environmentally and socially risk management system that is adhered by financial industry.⁵⁹³ Additionally, the EP is not applying retroactively, so that the principles will cover social and environmental risks since the project officially signed by borrower and lender.⁵⁹⁴

There are 9 (nine) Equator Principles that were agreed among EPFI members. Those principles are as the following; review and categorisation, social and environmental assessment, applicable social and environmental standards, action plan and management system,

⁵⁹⁰The Equator Principles, Guidance to Equator Principles Financial Institutions on Incorporating Environmental and Social Considerations into Loan Documentation, [The Equator Principles Publishing, 2013], 1.

⁵⁹¹Ibid

⁵⁹²Ibid

⁵⁹³The Equator Principles, The Equator Principles June 2013 Version [The Equator Principles Publishing, 2013], 2.

⁵⁹⁴ The Equator Principles, The Equator Principles June 2006 Version [The Equator Principles Publishing, 2006], 2.

consultation and disclosure, grievance mechanism, independent review, independent monitoring and reporting.⁵⁹⁵

Further, the EP is also offering guidance on implementation reporting which can be used by the borrower as a technical guidance to draft their periodic reports.⁵⁹⁶ EPFIs also provide templates as required to be included to the periodic and annual reports.⁵⁹⁷ Commonly, EPFIs required the borrower to provide a webpage link to be able for others in accessing the annual equator principles reports.⁵⁹⁸ Then, EPFIs will publish it as well at its own webpage.⁵⁹⁹ It was implemented by EPFIs for many years to demonstrate that how the project was agreed to finance and how EP works to monitor it.⁶⁰⁰

Based on the information above, the researcher opinion is that the Equator principles are implemented voluntarily and currently no adequate information on the implementation of the codes within Indonesia context. Further, Indonesia is not signatory to the principles because the principles were set up by banking industries to measure the level of compliance of their banking customers before being granted a loan. Therefore, the principles are not legally binding to Indonesia as a state entity. The EP principles can be enhanced by implementing

⁵⁹⁵The Equator Principles, The Equator Principles June 2013 Version [The Equator Principles Publishing, 2013], 6-21.

⁵⁹⁶ The Equator Principles, Guidance to Equator Principles Financial Institutions on Incorporating Environmental and Social Considerations into Loan Documentation The Equator Principles Publishing, 2013], 2.

⁵⁹⁷Ibid

⁵⁹⁸ The Equator Principles, Guidance to Equator Principles Financial Institutions on Incorporating Environmental and Social Considerations into Loan Documentation The Equator Principles Publishing, 2013], 4.

⁵⁹⁹Ibid

⁶⁰⁰ The Equator Principles, Guidance to Equator Principles Financial Institutions on Incorporating Environmental and Social Considerations into Loan Documentation The Equator Principles Publishing, 2013], 3.

mandatory CSR legal provision. The EP principles can be adopted as source of references and information to enhance the guidelines of mandatory CSR in Indonesia.

4. Performance Rating Programme in Environmental Management (PROPER) Ministry of Environmental Republic of Indonesia

Ministry of Environment of the Republic of Indonesia launched a programme which is called as PROPER to measure the degree of environmental compliance of companies are operating in Indonesia.⁶⁰¹ Hence, the award is given to individual or corporation that in charge of performing responsible business conduct in the environmental field.⁶⁰²

PROPER is stand for the Performance Rating Programme in Environmental Management. PROPER programme was started in 1996 which aimed to encourage the companies' compliance with environmental regulations in the field in order to achieve environmental excellency.

The implementaion of PROPER has been performing differently from mandatory CSR legal provision as mentioned on Article 74 of Act No.40/2007 on Limited Company Liability. Therefore, the implementation of PROPER has not yet been integrated with the implementation of mandatory CSR legal provision. Consequences, the implementation of Constitutional Court Verdict No. 53/PUU-VI/2008 on

⁶⁰¹ Article 43 (3) paragraph h of Act Number 32/2009 on the Environmental Management and Protection.

⁶⁰² Article 1 Ministry of Environmental Republic of Indonesia Regulation No. 5/2011 on Corporate Performance Rating & Appraisal Programme in Environmental Management.

Judicial Review of mandatory CSR legal provision had become unclear until now.

In one side, no one ministry is fully responsible to implement the legal provision. In the other side, the legal provision related to environment, social and economic empowerment are still scattered at a few different ministries. It needs to be integrated in one single laws and regulation and mandated to a particular ministry as the operator of the legal provision.

However, as an environmental tool, PROPER should be appreciated as a strategy of surveillance conducted by the Ministry of Environment in order to monitor the level of companies' compliance in Indonesia on the environmental aspect. Unfortunately, the participation of companies in PROPER assessments is on voluntary basis.

PROPER is even just a media of appreciation or award given by the Ministry of Environment for companies that complied with the rules and regulation in the environmental field.⁶⁰³ Hence, R24 mentioned that PROPER does not fundamentally contain the guiding principles, standards or guidelines on how the companies should behave in order to comply with the environmental rules and regulations in Indonesia.⁶⁰⁴

Due to PROPER being only limited as appreciation of a company, it has been under the impression that PROPER seems just a strategy of

⁶⁰³ Article 2 clause (2) Ministry of Environmental Republic of Indonesia Regulation No. 5/2011 on Corporate Performance Rating & Appraisal Programme in Environmental Management.

⁶⁰⁴ [Interview on 28 October 2013 in Jakarta.

improving a company's public image rather than a strategy to oversee the level of companies's compliance on the environmental aspect.⁶⁰⁵

PROPER is limited by the Minister of Environment Regulation as part of the Ministry's oversight activities on environmental issues. It is conducted to measure the level of company's compliance with environmental rules and regulations. The policy has not granted any incentives and/or disincentives to the companies.⁶⁰⁶

Incentives are given in the form of PROPER award to companies which are considered to have performed the environmental standard well and to have complied with all the laws and regulations in the field of environment.⁶⁰⁷ However, it was not stated clearly which types of punishment are given by the Ministry of Environment for companies which do not comply with the legislation in the environmental field, either partially or wholly.

PROPER assessment is based on several aspects, namely prevention of pollution and/or destruction of the environment, prevention of pollution and/or environmental damage and recovery of environmental damages. In general, PROPER assessment is just aimed to prevent, mitigate and recover environmental damage. Therefore, a strong link should be developed between PROPER's policy and the use of CSR funds from a particular company for prevention, mitigation and recovery of environmental pollution.

⁶⁰⁵Ibid

⁶⁰⁶Article 2 Ministry of Environmental Republic of Indonesia Regulation No. 5/2011 on Corporate Performance Rating & Appraisal Programme in Environmental Management.

⁶⁰⁷Article 2 Clause (2) Ministry of Environmental Republic of Indonesia Regulation No. 5/2011 on Corporate Performance Rating & Appraisal Programme in Environmental Management.

In addition, there are several several types of colours regarding a company's level of compliance against the laws and regulations on environment, which are as follows: the yellow colour is given to companies that have achieved the highest level of compliance in implementing the responsible business conduct in environmental aspect.⁶⁰⁸

Further, the green colour is given to companies that have obeyed the operational aspects of the business environment in excess of what is required (beyond compliance) by implementing management systems and environmental control systems through reducing, reusing, recycling and recovery.⁶⁰⁹ Blue is given to companies that complied with the environmental aspects in accordance with the requirements in the legislation⁶¹⁰

Red is given to companies that do not comply with the environmental aspects of their business operations in accordance to the requisite in the law.⁶¹¹ Finally, black is given to companies that have obviously performed actions that violate the laws and regulations on the environment either intentionally or due to negligence.⁶¹²

⁶⁰⁸ Article 4 paragraph a Ministry of Environmental Republic of Indonesia Regulation No. 5/2011 on Corporate Performance Rating & Appraisal Programme in Environmental Management.

⁶⁰⁹ Article 4 paragraph b Ministry of Environmental Republic of Indonesia Regulation No. 5/2011 on Corporate Performance Rating & Appraisal Programme in Environmental Management.

⁶¹⁰ Article 4 paragraph c Ministry of Environmental Republic of Indonesia Regulation No. 5/2011 on Corporate Performance Rating & Appraisal Programme in Environmental Management.

⁶¹¹ Article 4 paragraph d Ministry of Environmental Republic of Indonesia Regulation No. 5/2011 on Corporate Performance Rating & Appraisal Programme in Environmental Management.

⁶¹² Article 4 paragraph e Ministry of Environmental Republic of Indonesia Regulation No. 5/2011 on Corporate Performance Rating & Appraisal Programme in Environmental Management.

Further, there are several steps that must be undertaken to implement PROPER assessment.⁶¹³ The steps are as follows:

- (1) Business determination listing stage by the technical team, field inspections, preparation of interim rating and evaluation of temporary ranking.⁶¹⁴
- (2) Preliminary ranking results notification, objection, preliminary rank determination, determination of green candidates, the evaluation of green rating and submission of the final report.⁶¹⁵

All of the above stages must be passed for the PROPER assessment process so that the level of objectivity and quality of the assessment results can be accounted for in public.⁶¹⁶ The minister will officially announce the results of the assessment and companies that have received the gold ratings, and those which receive the green will be given a certificate and a trophy while those which receive the blue will only be awarded a certificate.⁶¹⁷

Meanwhile, it is not clearly stated what kind of action that will be taken by the ministry on those companies which receive the red and the black, and this was one of the weaknesses of the assessment. The ministry should be encouraged to force the companies to obey the rules and regulations in the environmental aspects.

⁶¹³ Article 6 Ministry of Environmental Republic of Indonesia Regulation No. 5/2011 on Corporate Performance Rating & Appraisal Programme in Environmental Management

⁶¹⁴ Article 6 Clause (1) Ministry of Environmental Republic of Indonesia Regulation No. 5/2011 on Corporate Performance Rating & Appraisal Programme in Environmental Management.

⁶¹⁵ Ibid

⁶¹⁶ Article 6 Clause (2) Ministry of Environmental Republic of Indonesia Regulation No. 5/2011 on Corporate Performance Rating & Appraisal Programme in Environmental Management.

⁶¹⁷ Article 10 Ministry of Environmental Republic of Indonesia Regulation No. 5/2011 on Corporate Performance Rating & Appraisal Programme in Environmental Management.

However, during the publicity of the PROPER results period (2011-2012), there were 49 (forty nine) companies that were granted with the black status. Therefore, the Deputy of Planning for Environmental Law in the Ministry of Environment recommended two (2) companies to be investigated, 37 (thirty- seven) companies to be subjected to government coercion to build waste treatment units, 6 (six) companies to receive administrative penalties, 2 (two) companies to receive written penalties another 2 (two) companies to close.⁶¹⁸

Other than PROPER, the ministry has also issued a policy on the watch list of environmental management for mining companies in 2013.⁶¹⁹ The policy clearly states that there were 7 (seven) aspects of monitoring conducted by the Ministry of Environment on mining companies' operations.⁶²⁰ Some of the aspects are as follows: Environmental Impact Assessment (EIA), water pollution control, air pollution control, hazardous waste management and toxic (B3), the potential damage to land, post-mining land management, community development and CSR.⁶²¹

Hence, the Ministry of Environment has initiated a guideline for the implementation of CSR in the environmental sector. This guideline contains a number of principles and standards on the implementation of CSR-related environmental aspects. Unfortunately, the guidelines have

⁶¹⁸ Ministry of Environmental Republic of Indonesia, PROPER Publication Period 2011-2012 [Jakarta, Ministry of Environmental Republic of Indonesia Publishing, 2012], 12.

⁶¹⁹ Deputy Decree of Ministry of Environmental Republic of Indonesia on 2013 List of Monitoring Scope for Mining Sector.

⁶²⁰ Ibid

⁶²¹ Decision No. 2 of Deputy Decree of Ministry of Environmental Republic of Indonesia on 2013 List of Monitoring Scope for Mining Sector.

not yet been aligned with the mandatory CSR legal provision. This is because of the relevant ministry has not yet considered the mandatory CSR legal provision as a final and binding legal provision in accordance to the verdict of the Constitutional Court.

Indeed, according to the information above, the researcher believed that the CSR guidelines on the environment aspect should be part of the Government Regulation No. 42/2012 on CSR and not passed by the Ministry of Environment Regulation. If it is passed by the latter, then there will be a perception that the sectoral CSR is divided among some different ministries.

Further, the guidelines would also contribute to the sustainability of the social and environmental aspect.⁶²² Based on the definition, there are 4 (four) major components that have been highlighted in the CSR guidelines, which are: beyond legal compliance, ethical business practices, increased prosperity and sustainable contribution to economic, social and environmental aspect.⁶²³

The four (4) components illustrate the wide range of definitions of the CSR guidelines in the environment sector. Despite the definitions being sectoral, they are later expanded into other areas such as beyond compliance, business ethics, stakeholders welfare and respected contribution to the sustainable economic, social and environmental.⁶²⁴

⁶²² Ministry of Environmental Republic of Indonesia, “*CSR Manual on Environmental Aspect*,” [Jakarta, Ministry of Environmental Republic of Indonesia, 2011], 7.

⁶²³ Ibid

⁶²⁴ Ministry of Environmental Republic of Indonesia, “*CSR Manual on Environmental Aspect*,” [Jakarta, Ministry of Environmental Republic of Indonesia, 2011], 7.

The definitions should remain focused on the issues related to environmental aspect.⁶²⁵

Additionally, the guidelines do not mention anything regarding the position of the mandatory CSR legal provision as a strategy of adherence to the existing sectoral laws. Hence, there is no specific provision that mentions about the connection between the CSR guidelines on environmental aspect and the mandatory CSR legal provision as prescribed by Article 74 of Act No.40/2007 of Limited Company Liability. Whereas the legal provision has clearly mentioned that the mandatory CSR is a legal obligation for companies who exploit the natural resources in Indonesia.⁶²⁶

In addition, based on the information above, the researcher believed that complying with the mandatory CSR legal provision means complying with the sectoral law, while the CSR guidelines on the environmental aspect do not mention the connection between Article 74 and the guidelines itself. Therefore, how can a particular company possibly comply with the sectoral law while at the same time consider itself having already complied with the mandatory CSR legal provision?

Hence, this issue requires a systematic and focused effort for the mandatory CSR legal provision to be well implemented in Indonesia. The commitment should come from the related ministries/agencies because they are the the state institutions responsible for implementing the legal provision. In fact, the enactment of constitutional court verdict No.

⁶²⁵Ibid

⁶²⁶ The CSR Guidelines on Environmental Aspect has been developed in August 2011. In fact, mandatory CSR legal provision has been enshrined into the Act No.40/2007 on Limited Company Liability on 2007.

53/PUU-VI/2008 declines the judicial review of Article 74 of Act No 40/2007 of Limited Company Liability.

Since the constitutional court has passed a verdict on the mandatory CSR legal provision, there should be no more debates between voluntary CSR and mandatory CSR in Indonesia. This is because the court has passed its verdict which finally binds every single person or corporation in Indonesia. In addition, it is obviously stated by the court that the mandatory CSR legal provision is still declared valid and legally binding based on the verdict of the constitutional court.

The Ministry of Environment is the government agency responsible for supervising and drafting regulations on environmental aspects. However the ministry has been passively functioning in encouraging companies to continuously implement CSR programmes related to environmental issues.

During the drafting process of the guidelines, there was very minimum involvement of civil society organizations (CSOs) and nongovernmental organizations (NGOs), particularly those who are currently active in advocating the rights of the community on the ground. This was evident from the composition of the technical team which did not include any representative from the relevant CSOs or NGOs.

Further, the formulation and the legal drafting process of the CSR guidelines was less for public consultation at the grassroots level. Whereas the process should be organized with public consultation that involves the main beneficiaries in order to get their feedback on the guidelines'

draft. The beneficiaries invited might be from diverse backgrounds in order to obtain objective and comprehensive inputs.

It is also crucial to involve beneficiaries who are directly living around the business's operation. Therefore, due to the lack of public consultation, the substance of the guidelines has gained less valuable inputs from the groups of community that were directly affected by the negative impact and/or the environmental damages.

In addition, the CSR guidelines still use the terminology *voluntary CSR* instead of *mandatory CSR*. In contrary, the verdict on mandatory CSR has already been passed by the constitutional court. Hence the legal provision has become legally enforceable and binding.

Further, the CSR guidelines also do not mention the type of sanctions and rewards given to either bad companies or good companies that have implemented CSR programmes. In fact, the complaint mechanism has also not been regulated by the CSR guidelines yet. In addition, the monitoring and evaluation mechanisms have also not been described explicitly and clearly. These aspects should be given a greater access to the third parties such as the CSOs and NGOs in order for them to be involved in the monitoring and evaluation processes.

The involvement of civil society organizations is not mentioned clearly in the guideline. As a result, these organizations do not have space and access to engage actively in the process of monitoring and evaluation of their CSR programmes. The guideline dictates that project management issues such as planning, implementation, and

documentation of the CSR programmes be implemented by the companies.

The mechanism of allocation and the use of CSR funds were also not regulated in the guidelines whereas it should be set so that the funds are not misused. In some areas, there were evidences that the CSR funds were utilized to finance projects which are not sustainable apart from bringing high impact to the local society.

The development of certain physical infrastructures should be the main obligation of the central and local government and not be the responsibility of companies through the use of CSR funds. Indeed, in the absence of a clear guideline, these circumstances are likely to occur.

Therefore, developing a guideline of mandatory CSR in Indonesia becomes necessary.

CSR funds is better to be used to implement nonphysical activities such as community capacity building in the form of training, media campaigns, workshops, focus group discussions and other activities. By this way, the funds can serve as supporting funds to assist the programmes of both central and local governments. It would also tailor to the wishes and aspirations of the beneficiaries.

There should be an intensive socialization on the utilization of CSR funds to relevant stakeholders. Through this way, the stakeholders may have a comprehensive understanding on the benefits of CSR apart from accessing the CSR funds. This may lead to a good synergy and collaboration between the central and local governments, companies, CSOs, NGOs and beneficiaries in the implementation of the CSR

programmes. Therefore, every party will have a sense of belonging to the programmes. This will ultimately foster a sense of responsibility among them for the successful implementation of particular CSR programmes.

The CSR guideline is considered as sectoral regulation that was passed by the Ministry of Environment. Indeed, it is necessary to upgrade the substance of CSR guidelines by referring it to mandatory CSR legal provision. Hence, the process should involve more diverse components and relevant CSR stakeholders especially from the main beneficiaries, private sector, CSOs, NGOs and academics at local level.

The Ministry of Environment has also issued other CSR guidelines on environment which is named as manual on the implementation of the CSR guidelines. It is more technical rather than the guidelines. There are several additional provisions have been inserted to the CSR guidelines in environmental aspect as follow;

1. Integrated and sustainable CSR implementation in environmental aspect.⁶²⁷ The process stage must be applied in order to achieve the implementation of an integrated and sustainable CSR by implementing a process of planning, implementation, monitoring and evaluation, reporting, and sustainable improvement.⁶²⁸
2. Integrated and sustainable CSR programme planning.⁶²⁹ It is implemented by formulating the vision and mission of the company's business policy, vision and mission of quality, health, safety and

⁶²⁷Ministry of Environmental Republic of Indonesia, “*CSR Implementing Manual on Environmental Aspect*,” [Jakarta, Ministry of Environmental Republic of Indonesia, 2011), 23.

⁶²⁸Ministry of Environmental Republic of Indonesia, “*CSR Implementing Manual on Environmental Aspect*,” [Jakarta, Ministry of Environmental Republic of Indonesia, 2011), 24.

⁶²⁹Ministry of Environmental Republic of Indonesia, “*CSR Implementing Manual on Environmental Aspect*,” [Jakarta, Ministry of Environmental Republic of Indonesia, 2011), 26.

environmental (QHSE) and the vision and mission of the company's CSR policy.⁶³⁰ Later on, it needs to conduct environmental impact assessments,⁶³¹ actively involve relevant stakeholders,⁶³² and alignment/synchronization programme with other CSR programmes.⁶³³

Normally, the government either central, provincial, district or city have also economic empowerment, social and conservation programmes. It can be synchronized between the companies's CSR programmes and some programmes are being implemented by the government at the central, provincial, district or city level.⁶³⁴

3. Companies are expected to set goals and targets of CSR programmes to have measurable achievement indicators.⁶³⁵ Formulation of objectives and targets can be done by using the SMART method; Specific, Measurable, Achievable, Realistic and Timely.⁶³⁶

4. The implementation of CSR programme on environment should consider the availability of human resources, budget allocation, documentation and media communication activities between the company and stakeholders.⁶³⁷ It is an important thing to do in order

⁶³⁰ Ministry of Environmental Republic of Indonesia, "CSR Implementing Manual on Environmental Aspect," [Jakarta, Ministry of Environmental Republic of Indonesia, 2011), 27.

⁶³¹ Ministry of Environmental Republic of Indonesia, "CSR Implementing Manual on Environmental Aspect," [Jakarta, Ministry of Environmental Republic of Indonesia, 2011), 28.

⁶³² Ministry of Environmental Republic of Indonesia, "CSR Implementing Manual on Environmental Aspect," [Jakarta, Ministry of Environmental Republic of Indonesia, 2011), 29.

⁶³³ Ibid

⁶³⁴ Ministry of Environmental Republic of Indonesia, "CSR Implementing Manual on Environmental Aspect," [Jakarta, Ministry of Environmental Republic of Indonesia, 2011), 32.

⁶³⁵ Ibid

⁶³⁶ Ministry of Environmental Republic of Indonesia, "CSR Manual on Environmental Aspect," [Jakarta, Ministry of Environmental Republic of Indonesia, 2011), 33.

⁶³⁷ Ibid

to ensure the achievement of goals and targets of the CSR programme.⁶³⁸

5. Monitoring and evaluation of CSR programme on environment aspect. The monitoring is done against the achievement of the goals, objectives and targets in accordance with the performance achievement indicators.⁶³⁹ Regular monitoring is expected to encourage the stakeholders to strive in achieving the targets, objectives and goals set.⁶⁴⁰ While the evaluation aims to see the relevance, impact, effectiveness, sustainability and efficiency of the implemented CSR programme.⁶⁴¹ Hence, the decision-makers will be able to suggest improvements to the CSR programmes in the future.⁶⁴²

6. The reporting of CSR programme on environment aspect.⁶⁴³ The manual recommended a reporting system was developed by the Global Reporting Initiative (GRI).⁶⁴⁴ The reporting method provides comprehensive guidance systems for companies in preparing reports on the implementation of CSR programmes.⁶⁴⁵ The manual also provide guidance on the substance that must be included in the report such as a description of the company, a description of the CSR

⁶³⁸ Ministry of Environmental Republic of Indonesia, “*CSR Manual on Environmental Aspect*,” [Jakarta, Ministry of Environmental Republic of Indonesia, 2011), 36.

⁶³⁹ Ibid

⁶⁴⁰ Ministry of Environmental Republic of Indonesia, “*CSR Manual on Environmental Aspect*,” [Jakarta, Ministry of Environmental Republic of Indonesia, 2011), 37.

⁶⁴¹ *Op. Cit*, Budi R. Minulya, CSR-Community Development Consultant at ICON Institute, [Interview on 19 October 2013 in Depok, Jakarta].

⁶⁴² Ministry of Environmental Republic of Indonesia, “*CSR Manual on Environmental Aspect*,” [Jakarta, Ministry of Environmental Republic of Indonesia, 2011), 42.

⁶⁴³ Ministry of Environmental Republic of Indonesia, “*CSR Manual on Environmental Aspect*,” [Jakarta, Ministry of Environmental Republic of Indonesia, 2011), 46.

⁶⁴⁴ Ministry of Environmental Republic of Indonesia, “*CSR Manual on Environmental Aspect*,” [Jakarta, Ministry of Environmental Republic of Indonesia, 2011), 47.

⁶⁴⁵ Ibid

strategy and environmental strategy, a description of the vision, mission and policy on environment.⁶⁴⁶

Further, it should also include a description of the goals, objectives, and performance indicators of CSR programmes and a description of stakeholders and beneficiaries.⁶⁴⁷ At last, it should be also explain about a description of the implementation of activities in the field, a description of the achievements of the activity, a description of the evaluation programme, and a description of the suggestions and recommendations⁶⁴⁸

7. The Sustainability of CSR programme depends on the conformity between the substance and the method of the programmes.⁶⁴⁹ So that at the early stage of the programme is very necessary to have a needs assessment. The assessment would identify the priority needs of the beneficiaries. Further, the availability of adequate human resources and availability of funds to finance CSR programmes. A good monitoring and periodic evaluation mechanisms is necessary to minimize the occurrence of the fail and are not well targeted programmes. Therefore, the process of monitoring and evaluation should be carried out gradually and measurable.

According to some information have been provided above regarding the guideline on CSR in environmental aspect and CSR implementing manual on environmental aspect, the researcher concludes that the

⁶⁴⁶Ministry of Environmental Republic of Indonesia, *CSR Manual on Environmental Aspect* [Jakarta, Ministry of Environmental Republic of Indonesia, 2011), 46.

⁶⁴⁷Ibid

⁶⁴⁸ Ministry of Environmental Republic of Indonesia, *CSR Manual on Environmental Aspect* [Jakarta, Ministry of Environmental Republic of Indonesia, 2011), 47.

⁶⁴⁹ Ibid

guideline should be drafted based on the spirit of mandatory CSR legal provision. It should be as part of the implementation of the legal provision. Further, the implementation should be done by other independent institution other than the Ministry of Environment itself. The Ministry can provide resources and other facilities to support the improvement of the policy.

5. Roundtable on Sustainable Palm Oil (RSPO)

Roundtable Sustainable Palm Oil (RSPO) is an organization was established since 2004 to promote a production and use of sustainable palm oil.⁶⁵⁰ The RSPO considered that palm oil is an environmental friendly product.⁶⁵¹ Then it should be promoted through an intensive and massive dialogues and cooperation within the supply chain and its stakeholders.

Some of its stakeholders such as the palm oil growers, palm oil processors and traders, social development NGOs, consumer goods manufacturers, banks and investors, environmental organizations and retailers.⁶⁵² The membership of RSPO is not a state entity, therefore Indonesia is not a member of RSPO. However, many of palm oil growers, palm oil processors, traders and development NGOs from Indonesia are members of RSPO.

⁶⁵⁰ Roundtable Sustainable Palm Oil, http://www.rspo.org/en/who_is_rspo, [Accessed on 31 August 2013].

⁶⁵¹ Ibid

⁶⁵² Article 3 of Roundtable Sustainable Palm Oil, RSPO by-laws, [Kuala Lumpur, RSPO Publishing, 2002].

Further, RSPO has some following tasks in accordance with its by-laws namely; research and development on sustainable palm oil.⁶⁵³ Hence, it undertakes practical project to demonstrate a sustainable palm oil best practices, mechanism and verification tool development for plantation establishment, management, procurement, trade and logistics.⁶⁵⁴

RSPO as a multi-stakeholders palm oil organization has issued a standard or principle on promoting sustainable production and use of palm oil. Therefore, RSPO has developed a certification mechanism to ensure the sustainability production and use of palm oil.⁶⁵⁵ There are some following basic elements of the certification scheme such as certification standards which are contain several sets of requirements.⁶⁵⁶

Hence, accreditation requirements which is an approval mechanism to ensure that the request of certification come from a credible palm oil stakeholders or not.⁶⁵⁷ At last, certification process requirement is a final endorsement stage whether such application has met the requirements or not.⁶⁵⁸

Palm oil growers or any other parties that have been certified by RSPO certification body will be granted a certificate of recognition or

⁶⁵³ Article 3 Paragraph a of Roundtable Sustainable Palm Oil (RSPO) by-laws, [Kuala Lumpur, RSPO Publishing, 2002].

⁶⁵⁴ Ibid

⁶⁵⁵ Roundtable Sustainable Palm Oil, “*RSPO Certification System*,” [Kuala Lumpur, RSPO Publishing, 2007], 1.

⁶⁵⁶ Roundtable Sustainable Palm Oil, “*RSPO Certification System*,” [Kuala Lumpur, RSPO Publishing, 2007], 7.

⁶⁵⁷ Ibid

⁶⁵⁸ Roundtable Sustainable Palm Oil, “*RSPO Certification System*,” [Kuala Lumpur, RSPO Publishing, 2007], 8.

endorsement by the executive board of RSPO.⁶⁵⁹ Subsequently for the production of sustainable palm oil they are legally-bounded to obey all the principles and criteria such as commitment to transparency, and compliance with applicable laws and regulations.⁶⁶⁰

Each of the principles above has a few criteria to be addressed by the certified RSPO members: commitment to transparency, compliance with applicable laws and regulations, commitment to long-term economic and financial viability, the use of appropriate best practices by growers and millers, environmental responsibility, conservation of natural resources and biodiversity, responsible consideration of employees and of individuals and communities affected by growers and mills, responsible development for new replanting, and commitment to continual improvements in key areas of activity.⁶⁶¹

RSPO principles and criteria are based on voluntary basis. One of the principles still acknowledges that complying with the applicable domestic laws and regulations of certain country is the members' first obligation.⁶⁶² Consequently, a mandatory CSR legal provision is not against the RSPO principles and criteria for the production of palm oil.

Additionally, based on information above the researcher concludes that the mandatory CSR legal provision is compatible with the RSPO principles because the principles recognise their members to respect the

⁶⁵⁹Roundtable Sustainable Palm Oil, "*RSPO Certification System*,"[Kuala Lumpur, RSPO Publishing, 2007], 24.

⁶⁶⁰ Roundtable Sustainable Palm Oil (RSPO), "*Principles and Criteria for the Production of Sustainable Palm Oil*,"[Kuala Lumpur, RSPO Publishing, 2007], 5.

⁶⁶¹Roundtable Sustainable Palm Oil (RSPO), "*Principles and Criteria for the Production of Sustainable Palm Oil*,"[Kuala Lumpur, RSPO Publishing, 2007].

⁶⁶² Roundtable Sustainable Palm Oil (RSPO), "*Principles and Criteria for the Production of Sustainable Palm Oil*,"[Kuala Lumpur, RSPO Publishing, 2007], 38.

applicable laws and regulations in a country they operate.⁶⁶³ Moreover, the provision becomes one of compliance indicators to the RSPO principles.⁶⁶⁴

The membership of RSPO comprises of business enterprises, NGOs, and other public and private sectors. Therefore, the applicability is only binding to its members. Indonesia as a state entity is not legally binding to the RSPO principles. Finally, a mandatory CSR legal provision can be considered a complementary tool to implement any international principles, standards, criteria, or guidelines within the Indonesia legal system.

6. United Nations Guiding Principles on Business and Human Rights

The United Nations particularly the human rights council together with its signatories has an obligation to protect, respect, and remedy the basic rights of human being in any territory. Related to the issues of business and human rights, the UN Secretary-General delegates the Special Representative of the Secretary-General on the issues of human rights, transnational corporations, and other business enterprises to draft a specific principle for a guideline of government, business entities, and society at large to protect, respect, and remedy some issues that may appear in the field of business and human rights.

The guiding principles were drafted in recognition of some basic principles, such as the state's existing obligations to respect, protect, and

⁶⁶³Roundtable Sustainable Palm Oil (RSPO), "*Principles and Criteria for the Production of Sustainable Palm Oil*," [Kuala Lumpur, RSPO Publishing, 2007], 5.

⁶⁶⁴Ibid

fulfill human rights and fundamental freedom. The role of business specialized organs of society performing specialized functions (I don't understand this sentence). Consequently the enterprises are required to comply with all applicable laws and regulations and respect for human rights, and they need to provide a channel to remedy when the rights and obligations are violated.

It is the duty of the state to protect human rights and fundamental freedoms of its citizen by developing a system that it fit to protect, respect, and remedy the framework of the United Nations. Therefore, there are two foundational principles of the United Nations Guiding Principles on Business and Human Rights (UNGPHR). First, the states must protect against human rights abuse within their territory and/or jurisdiction by third parties, including business enterprises.

Business enterprises as private sector can also be allegedly classified as human right violators. In a boader context, business enterprises have a potential to conduct massive and countinous misconduct against human rights principles. Some of them are even involved in environmental destructions by killing protected species, illegal logging, and setting up forest fire for planting, or other types of environmental misconduct. Given this point the state must take necessary means to protect the human rights of its citizens.

Access to clean water and air and sustainable natural resources are the basic rights of citizens. The states must be able to protect their citizens' rights properly. Within the Indonesia context and in relation to the implementation of the framework for protecting, respecting, and

remedying, the government of Indonesia has enacted a mandatory CSR legal provision in order to impose business enterprises to be more socially and environmentally responsible.

The mandatory CSR legal provision is one of the most effective ways established by the government of Indonesia to prevent and redress such abuse through preventive measures within the context of the Indonesian legal system. Further, the states also have the duty to promote the rule of law by taking some measures to ensure equality before the law, fairness in its application, adequate accountability, legal certainty and consistent procedure and transparency.

Second, states should ensure that all business enterprises domicile in their territory and/or jurisdiction in respect of human rights during the period of their operations. The states have strong reasons to apply national hard-law instruments within its territorial to protect its national interest.

Nonetheless, the multilateral soft-law instruments such as the OECD Guidelines for Multinational Enterprises and other performance standards are already in place. As a frontliner party, the states have an obligation to protect and ensure that all business enterprises within their territory or jurisdiction respect the human right principles.

Further, there are some other principles on business and human rights that have been agreed and passed by the office of high commission on human rights. The principles can be a guide for any interested countries to develop its national policy to protect the rights of its citizen from the abuse of human rights conducted by business enterprises.

Additionally, the researcher concludes that the mandatory CSR legal provision is a nontraditional way for Indonesia to ensure that all companies in natural resources core business or associated to natural resources exercise socially and environmentally responsible business conduct in their business practices. Further, Indonesia is not legally binding to the principles because the applicability is based on voluntary basis. Finally, the legal provision is the real action in policy-making that has been issued by Indonesia to secure its citizens' human rights and to meet its responsibility to respect for human rights.

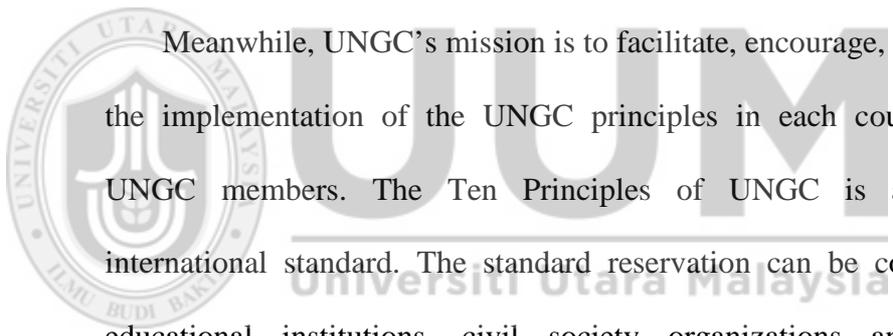
7. Ten Principles of United Nations Global Compact

The Ten Principles of United Nations Global Compact was derived from some basic principles in the field of human rights, labour rights, environmental rights and anti-corruption. The principles in the UN Global Compact (UNGC) are generated from some international recognised human rights principles namely the Universal Declaration of Human Rights, the International Labour Organization's Declaration of Fundamental Principles and Rights at Work, the Rio Declaration on Environment and Development and the United Nations Convention Against Corruption.

The UN Global Compact is a working group comprises business enterprises, NGOs, universities and other civil society organizations. They set up a practical framework based on human rights principles to support a sustainable development and to disclosure sustainability policies and practices. The membership of UNGC is voluntary basis of

different agencies, private sectors, and organizations. Therefore, Indonesia as a state entity is not a signatory to the UNGC principles.

Therefore, there is a connection between a principle, or an international standard, and another international standard. UNGC combined several international standards to produce the Ten Principles UNGC. It has a vision to become an agent of change which accelerates the reinforcement of the human rights principles implementation, the sustainable environmental development, the implementation of the ethical business practice and the respect toward labor rights in countries where UNGC is exercised.



Meanwhile, UNGC's mission is to facilitate, encourage, and promote the implementation of the UNGC principles in each country of the UNGC members. The Ten Principles of UNGC is a voluntary international standard. The standard reservation can be conducted by educational institutions, civil society organizations and business institutions (small and medium enterprises, national or multinational) through Global Compact Local Networks (GCLN).

A petition to voluntarily obey the Ten Principles is performed by becoming a member of UN Global Compact by submitting an application to the UN Global Compact representative in the respective member countries. Furthermore, there are also some activities conducted by GCLN such as activities to increase awareness on the UNGC principles, policy dialogue on a number of critical issues, cultural activities, learning through training, regional meetings and voluntary activities.

There are several advantages of joining the GCLN membership. The member can collaborate with another global compact network of both national and international entities; encourage to develop joint action initiatives; participate in a policy dialogue on the Ten Principles implementation; share experience and knowledge through seminars, workshops, and training; enhance leadership skills; improve productivity; gain broader access to other UN resources; and provide promotional opportunities for goods and services through GCLN.

Further, the Ten Principles of UNGC include a number of principles related to good business practices which comprise 4 (four) main parts, namely human rights, labour right, environmental right dan anti-corruption. In the field of human rights, some of the principles are as follows: business enterprises should promote and respect the protection of international human rights standards and ensure that the company is not involved in any human rights abuses.

The principles in the area of labour rights are as follows: (a) business enterprises should uphold the association's freedom and the effective recognition of the right for collective bargaining, (b) all forms of forced and compulsory labour should be eliminated, (c) child labour should be abolished, and (d) discrimination in respect to employment and occupation should be eliminated.

Hence, some principles in the field of environmental rights are as follows: (a) Business enterprises should support the precautionary mechanism of environment challenges, and (b) they should also

undertake initiatives to promote greater environmental responsibility and encourage the development and diffusion of the environmental friendly technologies. The last principle in the field of anti-corruption dictates that business enterprises should work against all forms of corruption, including extortion and bribery.

The Ten Principles of UNGC were mostly inspired by four international principles which is The Universal Declaration of Human Rights, the International Labour Organization's Declaration on Fundamental Principles and Rights at Work, the Rio Declaration on Environment and Development 1992 and the United Nations Conventions Against Corruption.

This shows that the UNGC principles are a digest of the four international frameworks that are currently covering issues on human rights, labour rights, environmental rights and anti-corruption. Therefore, the UNGC principles are very relevant to be implemented by business enterprises in order for them to comply with the international human rights standards.

Notwithstanding, the Ten Principles of UNGC is still an international guidance on voluntary basis with no mechanism to enforce business enterprises to adopt and to implement those principles. Therefore, it is beyond question that the national legal system of each country is playing a strategic role for a proper mechanism in the implementation of UNGC principles or any other international CSR principles and standards. Particularly for Indonesia, the country has

passed a mandatory CSR legal provision so that all the international CSR standards and principles can be well implemented by using the mandatory CSR legal provision mechanism and framework.

8. International Finance Corporation's Policy and Performance Standard on Social and Environmental Sustainability.

As a subsidiary of the World Bank, the International Finance Corporation has also issued and released a sustainability policy which is called Policy and Performance Standard on Social and Environmental Sustainability (PPSSES). The performance standard is launched to provide and apply a comprehensive strategy, resources and approach on social and environmental impacts in which companies may be involved in whenever they operate.⁶⁶⁵

The performance standard uses an outcome-based approach that enables IFC's clients and other stakeholders to polish their social and environmental performance from time to time. It can be implemented as appropriate to the nature, scale of the projects and level of social and environmental risks. The performance standard is a manual that is used by IFC to measure social and environmental risks of any project before financing it.

It is fully the responsibility of companies to manage their social and environmental impacts by consistently following and applying the performance standard as appropriate. By adhering to the standard,

⁶⁶⁵International Finance Corporation (IFC), *Policy and Social Environmental Sustainability*, [International Finance Corporation Publishing, 2006], 1.

companies may improve their social and environmental performances because those factors are crucial for the sustainability of certain projects.

IFC is committed to provide a transparent and accountable project finance mechanism by adhering to the performance standard. Moreover, the social and environmental aspects are the integral part of good and responsible business practices because they may improve a company's competitive advantage and create added values to all its stakeholders.

According to the performance standards files, certain standards are recommended by IFC for its clients to perform business practices such as (a) social and environmental assessment and management system,⁶⁶⁶ (b) labour and working conditions,⁶⁶⁷ (c) Pollution Prevention and Abatement,⁶⁶⁸ (d) Community Health, Safety and Security,⁶⁶⁹ (e) Land Acquisition and Involuntary Resettlement,⁶⁷⁰ (f) Biodiversity Conservation and Sustainable Natural Resources Management,⁶⁷¹ (g) Indigenous Peoples,⁶⁷² and (h) Cultural Heritage.⁶⁷³

The performance standards drawn up by IFC above are used as a tool to review every proposal admitted by IFC. IFC will conduct a review of the financial proposals based on the levels and scales of particular

⁶⁶⁶International Finance Corporation (IFC), *Policy and Social Environmental Sustainability*, [International Finance Corporation Publishing, 2006], 13.

⁶⁶⁷International Finance Corporation (IFC), *Policy and Social Environmental Sustainability*, [International Finance Corporation Publishing, 2006], 19.

⁶⁶⁸International Finance Corporation (IFC), *Policy and Social Environmental Sustainability*, [International Finance Corporation Publishing, 2006], 23.

⁶⁶⁹International Finance Corporation (IFC), *Policy and Social Environmental Sustainability*, [International Finance Corporation Publishing, 2006], 27.

⁶⁷⁰International Finance Corporation (IFC), *Policy and Social Environmental Sustainability*, [International Finance Corporation Publishing, 2006], 30.

⁶⁷¹International Finance Corporation (IFC), *Policy and Social Environmental Sustainability*, [International Finance Corporation Publishing, 2006], 36.

⁶⁷²International Finance Corporation (IFC), *Policy and Social Environmental Sustainability*, [International Finance Corporation Publishing, 2006], 40.

⁶⁷³International Finance Corporation (IFC), *Policy and Social Environmental Sustainability*, [International Finance Corporation Publishing, 2006], 44.

projects and tailored them to possible risks and social and environmental impacts that may be caused by the projects.⁶⁷⁴ IFC principles provide lots of ethical standards that is relevant to develop Indonesia mandatory CSR guidelines. Several points of the principles can be taken as point of discussion further to develop the mandatory CSR guidelines.

Indonesia is not a signatory to the IFC principles so that it is not legally binding for Indonesia as a state entity. Therefore, the implementation of the voluntary international principles such as the IFC principles is important in the implementation practical mechanism and they should be adopted as part of the national law in Indonesia.

The adoption process can be carried out through the development of a national guideline of Indonesia regarding the mandatory CSR, which is stipulated in a regulation either in the presidential decree, the government regulation, the local regulation, or other sectoral regulations.

Therefore, the researcher assumed that the codification draft of written or nonwritten regulation, either local, national or international principles regarding a good CRS practice, will generate a guideline of CSR mandatory implementation in Indonesia. Later, this can be adopted into the provision of legislation of Indonesia in order to provide a legal certainty for the CSR stakeholders in Indonesia such as companies, beneficiaries, and the government.

⁶⁷⁴ IFC projects categories are as follows; Category A project ; Any projects with significant adverse, irresistible & unprecedented social and environmental damage, Category B project; any project with definite social and environmental potential damages, such as enumerated, specified, and mitigated damages, Category C project; any project with minimal or, even, no social and environmental impacts and Category Financial Intermediary project: any project with does not cause any social and environmental impacts such as; lending projects, microfinance, housing and trade finance.

9. Global Reporting Initiative (GRI)

The global reporting initiative (GRI) is a nonprofit organization that promotes economic, environmental, and social sustainability. GRI contributes to the global economic sustainability by providing specific organizational sustainability reporting.⁶⁷⁵ GRI's reporting sustainability frameworks enable many organizations, companies and other private sectors to measure and report their sustainability performances in a very accountable way. The mechanism would enable the trust of their stakeholders who are involved in their business practices.

GRI's reporting sustainability is beneficial for stakeholders who want to know about the social and environmental strategies and approaches of certain companies who publish reports on their strategies. To the government, the sustainability report is very helpful because (a) it assists the government to understand the social and environmental impacts within the companies' jurisdiction, (b) it creates transparency, (c) it creates dialogue between company and other stakeholders, (d) it makes the companies more accountable for the impacts of their activities, and (e) it helps the government to identify the contribution of a company to national sustainability efforts.⁶⁷⁶

Further, the following principles and steps should be considered in preparing the sustainability report in accordance to the GRI standards: (1) Types of reporting should be defined, whether they are core or comprehensive reports; (2) afterwards, the content of the reports should

⁶⁷⁵The Global Reporting Initiatives (GRI), <https://www.globalreporting.org/Information/about-gri/Pages/default.aspx>, [Accessed on 1 September 2013].

⁶⁷⁶Ibid

be determined based on GRI specific standards on the following principles: stakeholder inclusiveness, sustainability context, materiality, and completeness.⁶⁷⁷

According to the information above, the researcher believed that the GRI reporting guideline is widely used as a sustainable reporting mechanism by a wide range of organizations throughout the world. Hence it can exemplify a standard for the mandatory CSR reporting in Indonesia, and the standard may reflect a company's performance on its social, economic, and environmental aspects in which it operates. The mandatory reporting standard will be required for companies which are operating in the exploitation of natural resources or are associated to natural resources.

In addition, the reporting standard may also adapt some local wisdom that fits the Indonesian context and culture. This which has not really been captured in other international recognized guidelines, principles, or standards, such as the GRI reporting guidelines. The mandatory CSR reporting guideline was not intended to replace or compete with the GRI reporting standard or any other international principles. It was merely intended to provide alternative thoughts and ways on reporting mechanism within the Indonesian CSR system.

At last, GRI reporting standard is based on voluntary CSR and it has been developed by an international organization. Indonesia as a state entity is not a signatory to the GRI reporting guideline. Therefore, its

⁶⁷⁷Global Reporting Initiative, *G4 Sustainability Reporting Guidelines* [Amsterdam, Global Reporting Initiative Publishing, 2013].

applicability is only for parties who voluntarily use it as their reporting guidance on sustainability.

5.4. Conclusion

Mandatory CSR laws, regulations, guidelines and policies in Indonesia are scattered in some different laws and regulations. Currently, there has been released a government regulation on CSR but the existing government regulation on CSR has not fulfilled yet the major problems in the implementation of the mandatory CSR legal provision. Further, extractive industries and other companies that are exploiting natural resources are utilizing one of or several international voluntary guidelines on CSR.

In addition, the sub-national government is also trying to pass policies on CSR to mobilize CSR funds for various motives. If there is no clear policy from the central government to adjust the current policies on CSR, then the implementation of mandatory CSR legal provision will be delayed.

However, it is necessary to have a codification of all separated laws, regulations, guidelines and policies into a single policy to enhance the implementation of the mandatory CSR legal provision in Indonesia. At last, the central government is encouraged to restructure and revise the government regulation on CSR to accommodate more inputs and feedback from a wider spectrum of CSR stakeholders in Indonesia.

CHAPTER SIX FINDINGS; THE FUNCTIONS, JURISDICTIONS AND LIABILITIES OF THE MANDATORY CSR SURVEILLANCE BODY IN INDONESIA

6.1 Introduction

The chapter presents the functions of the mandatory CSR surveillance in Indonesia to oversee the implementation of mandatory CSR projects in the country. Further, it discusses about the existing jurisdiction of surveillance mandatory CSR in Indonesia with some other possibilities of improvement in the future. The chapter also discusses the liabilities of surveillance mandatory CSR in Indonesia in order to present the highest level of transparency and accountability of the implemented mandatory CSR projects in Indonesia.

A mandatory CSR surveillance body has not really been established in Indonesia because the government regulation on CSR does not clearly mention about the establishment of such an institution in the policy that they have passed. Therefore, there are two (2) divided CSR surveillance's functions, jurisdictions and liabilities in Indonesia. The current functions, jurisdictions and liabilities of CSR surveillance are being conducted by relevant governmental supervisory agencies for CSR programmes such as the SOEs.

Hence, there is no specific surveillance body to supervise and evaluate the CSR programmes that have been implemented by private companies. Hence, it is necessary to consider establishing a specific CSR surveillance body to strengthen the level of transparency and accountability of the implemented CSR programmes in Indonesia.

6.2 The Functions and Scope of Mandatory CSR Surveillance Body

Currently, a mandatory CSR surveillance body in Indonesia has not been formally established yet. Therefore, the functions are being handled by relevant governmental supervisory bodies which also have some limitations on their mandates, particularly in monitoring and evaluating the mandatory CSR projects in Indonesia in accordance to their respective acts and other relevant regulations. Accordingly, the limited jurisdiction and liabilities are affected in overseeing the implemented mandatory CSR projects in Indonesia. At last, the NGOs participated to monitor and evaluate the mandatory CSR projects in Indonesia in order to increase the transparency and accountability of the projects.

Act No. 40/2007 on Limited Company Liability comprises 161 articles as a whole and only 3 articles that govern the CSR. One of the articles entitled “social and environmental responsibility is a commitment of a company in the development of a sustainable economy to improve quality of life and the environment which is beneficial for the partnership, the local community, and the public.”⁶⁷⁸

Further, business enterprises are obliged to disclose their annual narrative and financial reports which relate to Article 74 on corporate social and environmental responsibility.⁶⁷⁹ There should be more detailed rules and regulation on mandatory CSR to be passed in addressing the CSR issues in

⁶⁷⁸ Article 1 paragraph 3 Act No. 40/2007 on Limited Company Liability.

⁶⁷⁹ Article 66 of Act No. 40/2007 on Limited Company Liability.

Indonesia.⁶⁸⁰ One of the unsolved issues that remain is the absence of a specific rule that governs the surveillance mechanism for mandatory CSR in Indonesia.

The surveillance of CSR in Indonesia is now being conducted by each ministry in-charged according to the authority granted by the constitution. In other words, implementation, operation, monitoring, and evaluation of CSR programmes that have been implemented by the companies are conducted sectorally by the respective related ministry and not integrated in a certain state institution. Meanwhile, CSR reporting mechanism is conducted voluntarily by using reporting tools that have been provided by the Global Reporting Initiatives (GRI).

The reporting mechanism is recognized worldwide, and currently, there are many companies in Indonesia that have been utilizing the mechanism as a tool for CSR reporting. Further, the copy of the report is handed to the related companies' commissioner.⁶⁸¹ Unfortunately, until nearly five (5) years of mandatory CSR legal provision promulgation, there is still no specific and clear compliance reporting mechanism on the implementation of the mandatory CSR legal provision in Indonesia.

Until now, there is no specific surveillance body on mandatory CSR programmes other than Act No.40/2007 on Limited Company Liability or Act No.25/2007 on Investment or Government Regulation No.47/2012 on Corporate Social and Environmental Responsibility. In fact, the current mandatory CSR legal provision regulates that the implementation is given to the respective sectoral ministries.⁶⁸² For example, environmental issues are

⁶⁸⁰Ibid

⁶⁸¹Article 60 of Act No. 40/2007 on Limited Company Liability.

⁶⁸²Ibid

addressed to the Ministry of Environment of the Republic of Indonesia while social issues are addressed to the Ministry of Social Affairs of the Republic of Indonesia.⁶⁸³

Mandatory CSR policy has been enshrined into Article 74 since 2007 but until now, there has been no specific agency or ministry that carries out the monitoring and evaluation of the CSR programmes in Indonesia. In fact, while the mandatory CSR policy has been enshrined into Article 74 since 2007, the surveillance body has not yet been established by the government. This has resulted in the unavailability of a standard reporting, monitoring, and evaluation.

While there are a few national voluntary guidelines on CSR that have been made by the Ministry of Social Affairs of the Republic of Indonesia and the Ministry of Environment of the Republic of Indonesia, unfortunately the policies were not drafted based on Article 74 on Corporate Social and Environmental Responsibility. In other words, the guideline was not developed to implement the mandatory CSR legal provision and it was drafted to implement other types of CSR strategies in Indonesia.

Further, the CSR guidelines that have been passed by the two ministries were drafted based on the sectoral laws of the respective ministries. As mentioned, the promulgation of the two policies was not intended to execute Article 74. Therefore, up to now, the mandatory CSR guidelines in Indonesia have yet to be compiled and codified by the government. While the government has issued a government regulation on environmental and social

⁶⁸³Article 7 Government Regulation No. 47/2012 on Corporate Social and Environmental Responsibility.

responsibility, unfortunately, the substance of the policy has not covered as many mandatory CSR issues in Indonesia.

The government regulation was actually developed by the government and it has declined the implementation of the mandatory CSR policies backward. This is because the government regulation states that the implementation of mandatory CSR must be implemented by relevant respective ministries. In fact, the enactment of Article 74 has resulted in the rising of two types of CSR implementation strategies: (a) voluntary CSR policies that apply to the business sector for non-utilization of natural resources, and (b) mandatory CSR legal provision which applies to the business sector such as mining, oil, and gas, and plantation that utilizes natural resources.

In fact, Article 15 of Act No. 25/2007 on investment says that the mandatory CSR applies to all companies, whether it exploits natural resources or otherwise.⁶⁸⁴ Such a condition was not realized by the ministry and other CSR stakeholders who actually considered that the mandatory CSR legal provision applies only to companies which are exploiting natural resources. Further, the guideline was not aligned with the mandatory CSR legal provision because the two (2) guidelines have not clearly stated its adherence to the mandatory legal provision. In fact, both guidelines do not expressively state that Article 74 is the legal basis for their preparation.

Afterwards, there was not a single word or phrase in the substance of both guidelines that alluded the mandatory CSR mandatory legal provision.

⁶⁸⁴ Article 15 of Act No. 25/2007 on Investment. Article 15 says that “Every investor is required to: apply the principle of good company management, implement the company’s social liability, make report on investment activity and submit it to the Investment Coordinating Board, respect cultural tradition of communities around the location of investment business activity, comply with all of the rules of law.

Nevertheless, both guidelines, which have been developed by the two ministries, can be used as entry points for the preparation and issuance of the mandatory CSR guideline in Indonesia.

The presence of the CSR guideline for environmental and social welfare should enhance the implementation of mandatory CSR in Indonesia. By contrast, the CSR guideline has precisely strengthened the sectoral CSR implementation by the relevant ministries, particularly by ignoring the existence of mandatory CSR legal provision. Indeed, companies and other relevant CSR stakeholders expect to have clear directions, forms, methods and types of mandatory CSR activities. As a result, there have been no efforts from the ministries to issue a guideline for mandatory CSR in Indonesia based on the mandate of Article 74.

The government is in dilemma to implement the mandatory CSR legal provision because since the beginning, it has not agreed on the mandatory CSR legal provision. During the legislation process, the government proposed a variety of reasons to refuse the mandatory CSR legal provision. One of the reasons is that CSR is a voluntary activity since its conceptual age.

Further, the implementation of such a policy may reduce the competitiveness of Indonesian manufactured products. It may also increase the company's production costs, causing the investment climate in Indonesia to not become competitive. By contrast, the parliament members of the Limited Company Liability Bill insisted to include the provision of mandatory CSR in the Bill.⁶⁸⁵

⁶⁸⁵Ibid

Finally, through a tough negotiation, Act No.40/2007 of Limited Company Liability has been agreed among the members of the parliament, and it included Article 74 on mandatory CSR legal provision. Eventually, the businessmen group totally disagreed with the inclusion of Article 74 to Act No.40/2007 on Limited Company Liability. Consequently, they sued Article 74 to the Constitutional Court because they argued that the contents of Article 74 are against the spirit of the constitution Republic of Indonesia. Then, the Constitutional Court decided that Article 74 is not against the Constitution of Indonesia 1945, thus, the lawsuit proposed by the businessmen group was rejected by the court.

Such circumstances made the government reluctant to implement the provisions of Article 74. Conversely, as a state of law, the government must uphold the rule of law and as well as respect the decisions of the Constitutional Court. The adherence of government against the verdict would be a good example of the development of a good law culture in Indonesia.

In fact, the stagnation phase on the implementation of Article 74 could be a lesson learnt for the parliament to revise the legislation system especially in developing an implementing the regulation as mandated by specific acts. Further, the member of parliament should be directly involved in drafting the regulations at national level so as to ensure that each mandate is well implemented by the government.

The stagnation of Article 74 is a good lesson on policy-making for all parties in Indonesia because the government is the only party that is given full authority by the constitution to execute laws by passing the executing regulations. Therefore, if the specific legal provision or some of the legal

provisions are not agreed by the government, then the executing regulations can not be passed in time. In other words, the substance cannot be fully implemented by the government.

Based on the case of Article 74, it seems that all the substances of any act should be in accordance with the willingness and interest of the government. Otherwise, the rule cannot not be implemented well. The constraint is due to the absolute power of the government to establish some executing regulations of any Act. In fact, Article 74 is a willingness and aspiration of the people especially the victims of the environmental disasters whose voices are represented by the members of parliament that represented them in the legislature.

Notwithstanding, there is a denial of the government towards the inclusion of Article 74 as if the inclusion of the act is not the will of the people but the will of the members of the parliament unilaterally. In fact, the representatives of the people have fought for the inclusion of Article 74 in order to protect and to anticipate the negative environmental damage that may affect the society.

The government is supposed to realize that Article 74 is a will and aspiration of the people particularly the environmental damage victims. They have been harmed by the negligence of the companies in protecting and conserving the environment. Indeed, the mandatory CSR legal provision is the strategy of the people as the main victims of the environmental damages to protect their rights through formal mechanisms so that there is no reason to not implement Article 74.

However, it became more complicated to implement the legal provision when the government regulations have been passed but there is no surveillance

body specifically established to oversee the implementation of the mandatory CSR in Indonesia.

The unavailability of the surveillance body was due to unclear government regulation on social and environmental responsibilities that have been passed by the government. The regulation does not clearly mention the establishment of a surveillance body. The situation resulted in the uncertainty of the mandatory CSR implementation framework because some ministries passed the CSR policies without referring to the mandatory CSR legal provision.

In fact, some related ministries also did not take any appropriate means to conduct monitoring and evaluation on the CSR projects. Indeed, as a governmental body, the ministry should not be directly involved in the execution of CSR projects. It is better for the ministry to participate as a monitor and evaluator of the projects or as a regulatory provider for the implementation of the mandatory CSR legal provision.

Constitutional Court verdict stated that Article 74 does not conflict with the constitution of the Republic of Indonesia. It is also not against the spirit of the constitution of Indonesian state. Apparently, the Verdict was not able to encourage the business enterprises in implementing mandatory CSR programmes. At this point, political will has become a major deterrant factor in implementing mandatory CSR legal provision.

Nevertheless, number of parties, especially the Non-Governmental Organizations (NGO) expected that the government establish a special agency that handles issues of mandatory CSR such as policies making, monitoring, evaluation and reporting procedures. Further, the agency is encouraged to have

strong coordination with relevant institution either national, sub-national or international.

In the future, if the government set up a special state institution to handle CSR issues, then the institution should synergize its programmes with other social, environmental and economic empowerment from other ministries or state institutions. Regarding to CSR surveillance functions, some expert persons from NGOs claimed that the agency should function as policy maker, supervisor and evaluator for the implementation of CSR programmes implemented by the companies.

While R6 as the representatives of the companies have mentioned that mandatory CSR become pro and contra in which some of them assumed that the surveillance CSR is better handled by respective ministries.⁶⁸⁶ Then, some others stated to create special institution on the surveillance activities. But experts from academia like R8 supported the idea of establishment a specialized institution that handles the issue of mandatory CSR because the agency will focus on overseeing various mandatory CSR monitoring, evaluation and reporting issues in Indonesia.⁶⁸⁷

The functions of mandatory CSR surveillance body must be able to resolve the various issues on monitoring, evaluation, and reporting related to the implementation of mandatory CSR. Theoretically, the recent surveillance functions are performed either by an internal surveillance agency within the respective ministries or by other governmental surveillance agencies.⁶⁸⁸

Unfortunately, in practice the surveillance functions of relevant ministries has

⁶⁸⁶ *Op. Cit*, Interview on 17 September 2013 in Jakarta.

⁶⁸⁷ *Op. Cit*, Interview on on 25 September 2013 in Depok.

⁶⁸⁸ *Ibid*

not improved. In fact, each ministry executes its surveillance function on the implementation of mandatory CSR by requesting its internal surveillance body to oversee the implementation of mandatory CSR programmes and some others have not done anything because they have no measures have been taken as yet.⁶⁸⁹

If such condition is left behind and have not been immediately taken a solution, it may cause irregularities and corruption practices in carrying out mandatory CSR programmes. In addition, the potential of CSR funds in Indonesia is very large at around 10 (ten) trillion rupiahs per year.⁶⁹⁰ Further, R25 mentioned that the huge fund is very possible to be misused if it is not completely governed by clear policies and if its implementation was not monitored by agencies that really focus on CSR programmes.⁶⁹¹

Therefore, the potential of such a large fund should be the strong reason for the government to improve the legal framework of CSR in Indonesia by establishing CSR policies as required and special CSR institution.⁶⁹² Hence, in absence of permanent and independent special CSR surveillance body in Indonesia, then the functions of CSR surveillance body have been doing by some of agencies as the following; Inspectorate General as an internal surveillance mechanism. In addition, there are two (2) other government agencies that carry out the functions of external oversight named the Supreme

⁶⁸⁹Ibid

⁶⁹⁰La Tofi, Head of Corporate Social Responsibility Forum on Social Prosperity, <http://www.antarakl.com/index.php/kesra/2044-dana-csr-perusahaan-di-indonesia-capai-rp10-triliuntahun> [Accessed on 14 October 2013].

⁶⁹¹*Op. Cit*, Interview on 29 October 2013 in Jakarta.

⁶⁹²Ibid

Auditor Agency (BPK)⁶⁹³ and the Financial and Development Auditor Agency (BPKP).⁶⁹⁴

Basically, the Supreme Auditor Agency (BPK) has the authority to conduct auditory on the financial matters undertaken by the Central Government, Local Government, other State Institutions, Bank Indonesia, State Owned Enterprises (SOEs), General Services Agency, Regional Enterprises and institutions or other entities that use state finances as source of its funding.⁶⁹⁵

BPK may conduct surveillance and audit on the management of state finances allocated by state-owned companies to implement CSR programmes. Even though the fund is taken from the state-owned companies annual profit but the initial capital of state-owned companies comes from the state budget, so that the BPK remains authorized to conduct an audit on management of CSR funds held by state-owned companies.⁶⁹⁶

According to R25, the condition shows evidence that the supervisory system of mandatory CSR programmes in Indonesia still needs to be improved in order to increase transparency and accountability in financial management CSR.⁶⁹⁷ Therefore, if the government gives tax reduction policy for companies that execute a good mandatory CSR programme. Then the government has to strengthen mandatory CSR surveillance system, controlling and financial reporting to be aligning with applicable standards of financial management.⁶⁹⁸

⁶⁹³ Act No. 15/2006 on State Auditor Body.

⁶⁹⁴ Government Regulation No. 60/2008 on Government Internal Controlling System.

⁶⁹⁵ Article 6 clause (1) Act No. 15/2006 on State Auditor Body.

⁶⁹⁶ Ibid

⁶⁹⁷ *Op. Cit*, Interview on 29 October 2013 in Jakarta.

⁶⁹⁸ Ibid

The recent weak surveillance systems, controlling and financial reporting of mandatory CSR programmes in Indonesia, both in state-owned companies as well as national and foreign private companies has made the Directorate General of Taxes of the Republic of Indonesia hesitate in issuing policies of tax reductions for companies that have properly execute mandatory CSR programmes. The improvement of monitoring systems, controlling and financial reporting of mandatory CSR programmes is pre-requisite for oil and gas companies that requested for CSR funds to be included as a component of cost recovery.

The mandatory CSR monitoring systems and controlling and financial reporting reform is part of the efforts to improve the transparency and accountability aspects in relation to the implementation of the mandatory CSR programmes in Indonesia. Afterwards, the results of the regular monitoring should be published to the public so that people would have access to the information about the progress in implementing particular CSR programmes.

BPK does not only oversee the management of financial aspects, but also examine the performance and conduct examinations for special purposes.⁶⁹⁹ Thus, the extent of BPK's authority in supervising and evaluating mandatory CSR programmes is essential to increase its role in supervisory, monitoring, controlling and evaluation of the use of CSR funds.

In addition to the implementation of the mandatory CSR programmes in Indonesia, which worth trillion rupiah, BPK is expected to play a more active role in monitoring, evaluating and supervising the use of the state budget in the

⁶⁹⁹ Article 6 clause (3) Act No. 15/2006 on State Auditor Body.

implementation of the mandatory CSR programmes in Indonesia.⁷⁰⁰ Particularly, the CSR programmes are implemented by state-owned companies which use funding from the state budget. Strict control over the use of the allocated CSR funds will improve the quality of implementation of the mandatory CSR programmes by the state-owned enterprises.⁷⁰¹

In performing its duties, BPK is authorized to determine the type of documents, data and information that must be provided and delivered by the parties in the process of examining financial management.⁷⁰² Further, BPK is authorized to determine the state audit standards that must be used in the financial examination after consultation with the central government and local governments.⁷⁰³ BPK is also authorized to establish a code in conducting inspection of financial management as well to use the services of experts or examiners from outside BPK.⁷⁰⁴

The scope of supervision conducted by BPK is only limited to financial management carried out by the central government, local governments, other state agencies, bank of indonesia, state-owned enterprises, public service agencies, provincial enterprises, institutions or other entities who manage state finances or carry out their duties and functions by using funds from the state budget.⁷⁰⁵

Moreover, for private companies, BPK is not authorized to audit their CSR funds because the auditory on private agencies is conducted by public accountants. Although the audit of the private companies is conducted by

⁷⁰⁰Ibid

⁷⁰¹Ibid

⁷⁰²Article 9 clause (1) paragraph d Act No. 15/2006 on State Auditor Body.

⁷⁰³Article 9 clause (1) paragraph e Act No. 15/2006 on State Auditor Body.

⁷⁰⁴Article 9 clause (1) paragraph f and g Act No. 15/2006 on State Auditor Body.

⁷⁰⁵*Op. Cit.* Article 6 clause (1) Act No. 15/2006 on State Auditor Body.

public accountant, it is expected that the results of the investigation can be reported to BPK to be published.⁷⁰⁶

Meanwhile, other surveillance mechanisms are conducted by Financial and Development Auditor Agency/*Badan Pemeriksa Keuangan dan Pembangunan* (BPKP), which is an internal government's surveillance body directly responsible to the President.⁷⁰⁷ Unlike BPKP, BPK is a free and independent financial supervisory agency.⁷⁰⁸ Ministers/ head of the institutions, governors, and mayors must control over the government's activities in accordance with each level of authority as prescribed by the relevant regulations.⁷⁰⁹

In carrying out its duties as an internal government's surveillance body, BPKP conducts surveillance activities in several steps; auditory, review, evaluation, monitoring and other oversight activities.⁷¹⁰ Then, BPK cooperates with government agencies such as the internal control inspectorate general, provincial inspectorates and districts/cities inspectorates.⁷¹¹

BPKP is to oversee the financial accountability of each ministry/state institution/local government so that in executing its function, BPKP can implement several activities such as overseeing the cross-sectoral, public treasury activities set by the Minister of Finance and overseeing other activities assigned by the president.⁷¹²

⁷⁰⁶ *Op. Cit.* Article 6 clause (4) Act No. 15/2006 on State Auditor Body.

⁷⁰⁷ Government Regulation No. 60/2008 on Government Internal Controlling System.

⁷⁰⁸ Article 2 Act No. 15/2006 on State Auditor Body.

⁷⁰⁹ Article 2 clause (1) and (2) Government Regulation No. 60/2008 on Government Internal Controlling System.

⁷¹⁰ Article 48 clause (2) Government Regulation No. 60/2008 on Government Internal Controlling System.

⁷¹¹ Article 49 clause (1) Government Regulation No. 60/2008 on Government Internal Controlling System.

⁷¹² Article 48 clause (2) Government Regulation No. 60/2008 on Government Internal Controlling System.

When viewed from the aspect of activities that can be implemented by BPKP, it is apparent that BPKP is not a purely free and independent supervisory agency because it is part of the government structure.⁷¹³ Further, in relation to the implementation of CSR programmes that cost trillions of rupiahs held by state-owned enterprises and the local government-Owned Enterprises, unfortunately BPKP has never done any special audit or evaluation on the performance of the mandatory CSR.

Due to the absence of a specific surveillance body on mandatory CSR in Indonesia, further the role and functions of surveillance authorities are being conducted by the governmental external and internal monitoring bodies. Aside that the surveillance regulatory framework still needs to be improved in order to minimize the occurrence of irregularities and corruption in the implementation of CSR programmes in Indonesia. The absence of a specific authority on mandatory CSR financial audit for internal and external surveillance body has shown that the mandatory CSR surveillance system in Indonesia is still at infancy.

From the exposures of some functions of the internal and external monitoring agencies of government, it is known the limits of their functions and duties in carrying out surveillance, monitoring and evaluation functions, especially on the implementation of CSR programmes. There is no specific provision yet governing the role and function of special surveillance that must be carried out with respect to transparency and accountability of the implementation of CSR programmes in Indonesia.

⁷¹³*Op. Cit.*, Agung Setiyo Wibowo, CSR and Community Development Consultant, [Interview on 30 October 2013 in Jakarta].

Therefore, R12 mentioned that it is necessary to revise the policy of mandatory CSR in order to include a clause on the existence of a special surveillance functions performed by any parties.⁷¹⁴ The establishment of such surveillance body would increase the transparency and accountability aspects in the implementation of the mandatory CSR programmes in Indonesia.⁷¹⁵ In addition, the sustainable involvement of NGOs as independent watchdogs to carry out the factual verification against any financial audit reports, CSR activity report, CSR compliance report and sustainability report is necessary.

Furthermore, the absence of a surveillance body on mandatory CSR in Indonesia will require more co-ordination, synchronization and harmonization of supervisory activities conducted by internal and external government's supervisory, independent monitoring and evaluation bodies as well as the one conducted by NGOs. Even if one day a special surveillance body is set up by the government, the role and function of an internal and external supervisory, monitoring and evaluation is still needed in order to strengthen the system of supervising the implementation of mandatory CSR programmes as a whole.

Meanwhile, the scope of supervision conducted by the internal and external government's supervisory agencies can only be applied to the CSR programmes implemented by the SOEs. The source of SOE's funding comes from the state's budget, the internal and external supervisors have the full authority and jurisdiction to oversee the CSR financial management and implementation of mandatory CSR programmes as a whole.

Based on the description above, the researcher assumed that there is still some unsolved problems behind the mandatory CSR surveillance, monitoring

⁷¹⁴*Op. Cit.*, Interview on 30 September 2013 in Jakarta.

⁷¹⁵*Ibid*

and evaluation system in Indonesia whereby the internal and external government's surveillance, monitoring and evaluation of CSR cannot monitor and evaluate the CSR programmes that have been implemented by private companies. Therefore, there is still a vacuum of law in the supervision, monitoring and evaluation on CSR financial management and the implementation of CSR programmes as a whole.

6.3 Jurisdictions and Legal Sanctions of Mandatory CSR Surveillance Body

In regarding with legal sanctions for companies that do not run well CSR programmes in Indonesia, there still no clear legal sanctions regarding disobey to the implementation of mandatory CSR legal provision but there are some sectoral constitutions which provide sanctions that can be imposed against firms who do not obey the law as follow:

1. Act No. 32/2009 on Environmental Protection and Management

There are 3 (three) types of business activities, only business activity with AMDAL and UKL-UPL are required to have an environmental permit.⁷¹⁶ While the business activity is not required to have an environmental permit then the business enterprises are only required to make a statement regarding the environmental compliance because the business activities do not have broad impact on environmental damage.

The Minister, Governor, and Regent/Mayor in accordance with their respective authorities shall reject the application for an environmental permit if it is not equipped with AMDAL and UKL-UPL.⁷¹⁷ In fact, environmental permits may be canceled if there are errors, misuse of

⁷¹⁶ Article 36 clause (1) Act No. 32/2009 on Environmental Management and Protection.

⁷¹⁷ Article 37 clause (1) Act No. 32/2009 on Environmental Management and Protection.

information, and legal defects in the process of filling the application for AMDAL.⁷¹⁸

Hence, if the publication does not meet the requirements listed in accordance with AMDAL and UKL-UPL review commission decisions and/or obligations agreed in the AMDAL and UKL-UPL documents are not applied by the company concerned.⁷¹⁹ Then the cancellation can also be done through a lawsuit in State Administrative Court.⁷²⁰

Government can also develop economic instruments to protect and preserve the environment in a way which is to encourage economic development plans that respect and preserve the environment, environmental financing system and the provision of incentives and disincentives to environmental protection.⁷²¹

Later, the Minister also demands business enterprises to conduct an environmental audit of the high-risk business activities on the environment and business enterprises which do not comply with the provisions in the environmental field.⁷²²

Administrative sanctions to companies will not deny their responsibility criminally.⁷²³ Thus, the sanctions received by companies denying adhering to environmental provisions may include a combination of administrative and criminal sanctions.⁷²⁴ Then, there are several kinds of government-imposed sanctions such as the suspension of production

⁷¹⁸ Article 37 clause (2) Act No. 32/2009 on Environmental Management and Protection.

⁷¹⁹ Ibid

⁷²⁰ Article 38 Act No. 32/2009 on Environmental Management and Protection.

⁷²¹ Article 42 clause (2) Act No. 32/2009 on Environmental Management and Protection.

⁷²² Article 49 clause (1) Act No. 32/2009 on Environmental Management and Protection.

⁷²³ Article 78 Act No. 32/2009 on Environmental Management and Protection.

⁷²⁴ Ibid

activities, demolition the source of pollution and closing the source of contamination.⁷²⁵ Further, other administrative sanctions are the removal of production facilities, seizure of goods or means of pollution sources or other required actions.⁷²⁶

Government-imposed sanctions can be applied on companies that do not adhere to the environmental aspects without prior written warning if the environmental damage caused is serious and threatening human life as well as the potential to cause huge losses.⁷²⁷ If the companies sanctioned by government coercion are late in implementing the sanctions, the government can impose additional penalties such as fines which are calculated according to the number of days of delay.⁷²⁸

Beside of administrative sanctions and criminal penalties that can be imposed on the environment damagers, the constitution also provides space for public to file a claim for compensation against the company that has made the destruction of the environment.⁷²⁹ In addition to the right to file a lawsuit through the courts, the community and the company can resolve the dispute through settlement out of court.⁷³⁰ The resolution outside the court can only be done for civil cases and not criminal cases.⁷³¹ In fact, the right of lawsuit can also be given against local government and government agency that are responsible for the protection and management of environmental life.⁷³²

⁷²⁵ Article 80 clause (1) clause (1) Act No. 32/2009 on Environmental Management and Protection.

⁷²⁶ *Ibid*

⁷²⁷ Article 80 clause (2) Act No. 32/2009 on Environmental Management and Protection.

⁷²⁸ Article 81 Act No. 32/2009 on Environmental Management and Protection.

⁷²⁹ Article 84 clause (1) Act No. 32/2009 on Environmental Management and Protection.

⁷³⁰ *Ibid*

⁷³¹ Article 85 clause (2) Act No. 32/2009 on Environmental Management and Protection.

⁷³² Article 90 clause (1) Act No. 32/2009 on Environmental Management and Protection.

Moreover, officials who provide environmental clearances are subject to punish if they issue an environmental permit without equipped with AMDAL or UKL-UPL document.⁷³³ The criminal threats include the threat of imprisonment up to 3 (three) years and a maximum fine IDR.3.000.000.000 (three billion rupiahs).⁷³⁴ The large amount of fines for officials who issue permits without equipped with AMDAL or UKL-UPL proves that environmental crime is an extraordinary crime).⁷³⁵

The officials who deliberately did not supervise the company which later caused pollution and/or destruction of the environment is liable to imprisonment for a maximum of 1 (one) year and a maximum fine of IDR 500,000,000.00 (five hundred million rupiahs).⁷³⁶ Therefore, with these criminal provisions, the competent authorities in the environmental field especially Ministers, Governors, and Regents/Mayors should absolutely perform their duties in overseeing the activities of the company in accordance with their respective authorities.⁷³⁷

Further, any person who gives false information or misleading information in the process of monitoring and enforcement in the environmental field may be liable to a maximum imprisonment of 1 (one) year and a maximum fine of IDR 1,000,000,000.00 (one billion rupiahs).⁷³⁸ The huge amount of fines to be paid by the person who gives false information is a sign for everyone that environmental crimes should together be eradicated through the full support of the people associated

⁷³³ Article 111 Act No. 32/2009 on Environmental Management and Protection.

⁷³⁴ Ibid

⁷³⁵ Ibid

⁷³⁶ Article 112 Act No. 32/2009 on Environmental Management and Protection.

⁷³⁷ Ibid

⁷³⁸ Article 113 Act No. 32/2009 on Environmental Management and Protection.

with the provision of the right information to the authorities about the alleged destruction of the environment.⁷³⁹

Beside of the implementation of payment of fines by the government against the owners of the companies that do not carry government-imposed sanctions.⁷⁴⁰The government can also apply criminal sanctions for them. Thus, beside of paying the fines, they are also charged maximum sentence of imprisonment of 1 (one) year in prison and a maximum fine of IDR 1,000,000,000.00 (one billion rupiah).⁷⁴¹ In conclusion, the criminal sanctions and fines against company leaders who do not want to implement the government-imposed sanctions will force management to comply with the provisions in the environmental field.

Nevertheless, if the criminal law is addressed to the business entity the one can be punished is the person who legally authorizes to represent the company's interests both inside and outside the court.⁷⁴² Apart from having to carry imprisonment, perpetrators of environmental crimes are also given an additional penalty which may provide deterrent effects to them such as deprivation advantage of the results of environmental crimes, partial and/or complete closure of the activities of the company, the obligation to restore the damaged environment, and closure of business activities company no later than 3 (three) years.⁷⁴³

According to the information above, the researcher concludes that in this law, there have not been criminal provisions which specifically

⁷³⁹ Ibid

⁷⁴⁰ *Op. Cit* Article 81 Act No. 32/2009 on Environmental Management and Protection.

⁷⁴¹ Article 114 Act No. 32/2009 on Environmental Management and Protection.

⁷⁴² Article 118 Act No. 32/2009 on Environmental Management and Protection.

⁷⁴³ Article 119 Act No. 32/2009 on Environmental Management and Protection.

regulated the threat of punishment that can be imposed on companies which did not implement mandatory CSR programmes in the environmental field. At least, the administrative and criminal sanctions related to environmental crimes will encourage the companies to better carry out their responsibilities.

2. Act No. 22/2001 on Oil and Gas

This Act provides a special arrangement on the implementation of the oil and gas industry in Indonesia. Partially, the oil and gas industries provide huge revenues for the state both in terms of taxes and profit-sharing between the government and the oil and gas contractors. However, the oil and gas industries have a greater potential to damage the environment and biodiversity in the surrounding area of their business locations. In fact, the objectives of oil and gas businesses in Indonesia are to create jobs, improve the welfare and prosperity of the people and preserve the environment.

Therefore, it is necessary to have maximum efforts from the government in order to minimize, mitigate or compensate for the people in areas around the oil and gas industries or those who suffered from the damage caused by the practices of the oil and gas businesses.

According to online data received from the Special Task Force for Upstream Oil and Gas Business Activities of Republic of Indonesia (*Satuan Kerja Khusus Kegiatan Usaha Hulu Minyak dan Gas Bumi/SKK MIGAS*) there are about 74 (seventy four) contractors for the oil and natural gasses, 178 (one hundred and seventy-eight) oil and gas companies

that are still doing exploration and 76 (seventy six) companies that have conducted production activities of oil and gas in Indonesia.

Based on the online data, it was learned that there are approximately 328 oil and gas companies operating in Indonesia.⁷⁴⁴ None of the companies there have implemented the mandatory CSR policy in accordance with Article 74 Act No.40/2007 of Limited Company Liability.

The researcher concludes that there is an obstacle in the form of limited access to information provided by SKK MIGAS towards the signed agreement of co-operation contracts. With such limited access to information as well as the unaccountability of the SKK MIGAS towards other CSR stakeholders, it is difficult for the society to know the commitment submitted by the companies that are related to community development and protection of the rights of indigenous people in their operational areas.

Government is authorized to impose sanctions against oil and gas business upstream and downstream activities that violated the license in oil and gas. The sanctions are in the form of a written warning, suspension of activity, freezing of the activity, or revocation of license.⁷⁴⁵ However, before revocating a license, the government has to provide a deadline for the relevant company to remeet the requirements of the permit.⁷⁴⁶

The act does not specifically set on the criminal penalties against companies which do not implement the mandatory CSR programme; however, it governs the threat of punishment for any person who commits

⁷⁴⁴ Ibid

⁷⁴⁵ Article 25 clause (1) Act No. 22/2001 on Oil and Gas.

⁷⁴⁶ Article 25 clause (1) Act No. 22/2001 on Oil and Gas.

a crime in the field of oil and gas. Every individual conducting a general survey of oil and gas without official permission will be charged of sanctions imprisonment of 1 (one) year or a fine of IDR 10,000,000,000.00 (ten billion rupiah).⁷⁴⁷ In fact, every person who moves data and information regarding oil and gas without any authority will be punished with 1 (one) year imprisonment and a fine of IDR 10,000,000,000.00 (ten billion rupiah).⁷⁴⁸

Further, every person doing the processing, transportation, storage and commercial activities of oil and gas without permission will be punished with imprisonment of each 5 (five) years, four (4) years, three (3) years and one (1) year and certain fines approximately IDR 50,000,000,000.00 (fifty billion rupiah), IDR 40,000,000,000.00 (forty billion rupiah), IDR 30,000,000,000.00 (thirty billion rupiah) and IDR 30,000,000,000.00 (thirty billion rupiah).⁷⁴⁹ Criminal sanctions and penalties governed by the act are still limited to the conduct of business activities of oil and gas without the official license of the government.

The criminal sanctions and fines are not specifically and obviously given to the perpetrators on environmental damages that are caused either by the companies as business entities or a private person.⁷⁵⁰ The aspects of environmental management, community development and health and safety have become major concerns of the legislators but the criminal aspect and penalties against the perpetrators of environmental destruction

⁷⁴⁷ Article 51 clause (1) Act No. 22/2001 on Oil and Gas.

⁷⁴⁸ Article 51 clause (2) Act No. 22/2001 on Oil and Gas.

⁷⁴⁹ Article 53 paragraph a, b, c and d Act No. 22/2001 on Oil and Gas.

⁷⁵⁰ Ibid

(particularly the oil and gas companies) which have not been explicitly stipulated in the act.⁷⁵¹

The absence of criminal sanctions and fines against oil and gas companies that do not execute the mandatory CSR programmes, either in accordance with Article 74 or in the contract agreement, has resulted in the weakness of the mandatory CSR implementation. Therefore, the researcher suggested that it is an urgent thing to strengthen the act for oil and gas that is firmly set on criminal sanctions and fines against oil and gas companies that do not comply with mandatory CSR legal provisions in accordance to the existing regulations and contract agreement as prescribed by the oil and gas joint co-operation proposal.

3. Act No. 41/1999 on Forestry

This act does not specifically regulate the mandatory CSR and the supervising function on the implementation of mandatory CSR programmes. This law regulates the implementation of companies' obligations in carrying out businesses in the field of forestry or forestry resource utilization. These companies are obliged not only to co-operate with local co-operatives in utilizing forest resources,⁷⁵² but also to undertake rehabilitation, reclamation and conservation of forest areas that have been exploited.⁷⁵³

In addition to the obligations as mentioned above, the company holding forest utilization license is also subjected to the obligation of

⁷⁵¹ Ibid

⁷⁵² Article 30 Act No. 41/1999 on Forestry.

⁷⁵³ Article 32 Act No. 41/1999 on Forestry.

paying business license fees, reforestation funds, and performance bonds.⁷⁵⁴ Then, the company's forest license holder is required to provide environmental services investment fund for forest conservation.⁷⁵⁵ Afterwards, the company's forest products permit that the holder is obliged to pay for a provision.⁷⁵⁶

Criminal provision against forest crimes sets about the threat of prison sentences and heavy fines against the offenders in the field of forestry.⁷⁵⁷ The severity of prison sentences and high fines imposed on the offenders in forestry shows that forest has a strategic role and function in human life, thus, forests perpetrators should be punished severely.⁷⁵⁸

Obviously, the forest products found at the time of the perpetrators' arrest will be seized by the state and then auctioned off, and the proceeds from the auction will be deposited into the state treasury.⁷⁵⁹ In addition to the criminal provisions, the government can also charge administrative sanctions against the perpetrators of such crimes in the forestry sector, who are required to pay a compensation in accordance to the level of environmental damage, the cost of rehabilitation and restoration of the land, the revocation of business licenses, and other administrative measures in accordance to the laws and regulations.⁷⁶⁰

Based on a description above, the researcher assumes that there should be an synchronization and harmonization between the act and the

⁷⁵⁴ Article 35 clause (1) Act No. 41/1999 on Forestry.

⁷⁵⁵ Article 35 clause (2) Act No. 41/1999 on Forestry.

⁷⁵⁶ Article 35 clause (3) Act No. 41/1999 on Forestry.

⁷⁵⁷ Article 78 Act No. 41/1999 on Forestry.

⁷⁵⁸ Ibid

⁷⁵⁹ Article 79 clause (1) Act No. 41/1999 on Forestry.

⁷⁶⁰ Article 80 clause (1) and (2) Act No. 41/1999 on Forestry.

mandatory CSR legal provision. Further, the process should involve as many CSR stakeholders in Indonesia as possible with the full support from the government and the companies. The synchronization would strengthen the existence of the mandatory CSR legal provision in Indonesia.

4. Act No. 4/2009 on Mineral and Coal Mining

Mineral and coal mining business activities are managed based on fairness, balance, benefit, nation interest-sided, participatory, transparency, accountability, and sustainability and environmentally sound principles.⁷⁶¹

The environment is one of the major concerns in the implementation of the mineral and coal mining policy in Indonesia. Mineral and coal mining operational activities can increase the risk of environmental damage and conflict of land ownership between companies and local community.

As part of sectoral regulation, the act regulates some important aspects on the environment in the implementation of the mandatory CSR.

It is apparent that the central, provincial, and district/municipality government have authorities to monitor mining activities. Indeed, the sectoral act in the mineral and coal mining does not explain firmly about the legal sanctions and fines oil and gas companies who do not implement CSR programmes under the mandatory CSR framework.

The government is encouraged to implement a participative, transparent, accountable public consultation mechanism before making a decision in granting a mining concession area. Doing so would imply that

⁷⁶¹ Article 2 Act No. 4/2009 on Mineral and Coal Mining.

the government has implemented a standard in accordance to the Free and Prior Informed Consent (FPIC) principle.⁷⁶² However, R24 mentioned that based on the data carried out in the field, the government has never conducted public consultation activities before granting a mining concession area.⁷⁶³

Administrative penalties can be made by the ministries, governors, regents/mayors to any companies who violate the act.⁷⁶⁴ The penalties can be a written memoranda, a temporary shutdown to partly or the whole exploration activities or operation and/or a revoke to IUP, IPR dan IUPK.⁷⁶⁵ However, the minister also has an authority to temporarily shutdown and/or revoke the IUP and IPR if the provincial governments do not control and monitor the mining activities within their territories.⁷⁶⁶ Then, the minister will pass the administrative penalties to the mining companies who violate the law.⁷⁶⁷

In spite of imprisonment and risk of being fined, offenders of the mineral and coal mining activities can also be applied a subsidiary punishment by revoking the operation licence and/or invalidating their legal statuses.⁷⁶⁸ In addition, the subsidiary can be the asset for closure used to commit the crimes in the mineral and coal mining sectors, and then profits have been obtained from criminal acts must be used to pay all related expenses inflicted by the criminal actions.⁷⁶⁹ Moreover, anyone

⁷⁶² Ibid

⁷⁶³ *Op. Cit*, Interview on 28 October 2013 in Jakarta.

⁷⁶⁴ Article 151 clause (1) Act No. 4/2009 on Mineral and Coal Mining.

⁷⁶⁵ Article 151 clause (2) Act No. 4/2009 on Mineral and Coal Mining.

⁷⁶⁶ Ibid

⁷⁶⁷ Article 152 Act No. 4/2009 on Mineral and Coal Mining.

⁷⁶⁸ Article 163 clause (2) Act No. 4/2009 on Mineral and Coal Mining.

⁷⁶⁹ Article 164 Act No. 4/2009 on Mineral and Coal Mining.

who issues IUP, IPR or IUPK which is against the law will be imprisoned for 2 (two) years and fined with IDR 200.000.000,00 (two hundred million rupiahs) at maximum.⁷⁷⁰

Any issue resulting from the environmental impacts caused by the mineral and coal mining operation activities will be resolved by this act.⁷⁷¹ Although the act does not explicitly regulate the administrative and criminal sanctions for any company who does not implement a good CSR programme, it has already made it obligatory for companies to introduce plans for the community development and empowerment programmes for the people in the mineral and coal mining operation areas. Further, the act also regulates the the environmental management aspect in order to ensure the sustainability of a healthy life.

The above description regarding the mineral and coal mining law reflects that the controls of the environmental aspects, and of the community development and economic empowerment programmes for the people living around the mining operation areas have been perceived as the minister's authority. Further, the minister may also delegate his supervisory authority to his subordinate.

Therefore, the monitoring will be under the jurisdiction of the General Inspectorate. Meanwhile, as the external supervisor, the Supreme Audit Agency has no any jurisdiction to monitor if the status of the companies are private companies.⁷⁷² Evenmore, the BPKP has only a supervising

⁷⁷⁰ Article 164 Act No. 4/2009 on Mineral and Coal Mining.

⁷⁷¹ Ibid

⁷⁷² Ibid

jurisdiction on the implementation of the community development and empowerment should it be requested by the President.⁷⁷³

The researcher's opinion is due to the complexity of the controlling mechanism and the separation of the monitoring institutions between the General Inspectorate, BPKP and BPK. Further, the authority and jurisdiction limitations of each institution urges the government to establish a special institution with a greater jurisdiction and authority attachment to conduct the monitoring and evaluation of the community development and the empowerment performed by the mining companies.

5. Act No. 27/2007 on Investment

In spite of Act No.40/2007 on Limited Company Liability regulating the legal obligation on CSR, apparently Act No.27/2007 also regulates an obligation for investors to implement social and environmental responsibility programmes.⁷⁷⁴ Thus, there are actually 2 (two) regulations in Indonesia that oblige business enterprises to implement the mandatory CSR programmes. Further, the Act on Investment, which regulates a legal obligation for companies to implement CSR programmes has previously been issued before the Act on Limited Company Liability was enacted.

Moreover, each investor is also obliged to (a)implement good principles of company management, (b) deliver regular reports to the Indonesian Investment Coordination Board (BKPM), (c) respect the culture and tradition of the surrounding communities, and (d) obey all

⁷⁷³Ibid

⁷⁷⁴ Article 15 paragraph b Act No. 27/2007 on Investment.

regulations stipulated in the act.⁷⁷⁵ Foreign investors are also obliged to invest in Indonesia by establishing business entities that are binding to the national law in Indonesia.⁷⁷⁶

Interestingly, the mandatory CSR legal provision stipulated in this law does not only regulate the obligation to implement CSR programmes but also set a number of administrative penalties that are passed by BKPM should the business enterprises do not perform their obligations.

The penalties can be in the form of a written warning, a business restriction, suspension of business and/or investment facility and revocation of business license and/or investment facility.⁷⁷⁷ The penalties are passed by the authorized governmental institutions as regulated in the Act.⁷⁷⁸ Moreover, the government can also give other forms of penalties to the corporates.⁷⁷⁹

Until now, R1 mentioned that BKPM has never drafted or issued yet any guideline or handbook related to the implementation of the CSR mandatory programme in Indonesia.⁷⁸⁰ Further, BKPM has never conducted any supervision on the implementation of the mandatory CSR programme in Indonesia so far.⁷⁸¹ In fact, it demonstrates how the mandatory CSR policy cannot be implemented even if it is officially enshrined to the formal Act.

⁷⁷⁵ Article 15 paragraph a, c, d and e Act No. 27/2007 on Investment.

⁷⁷⁶ Article 5 clause (2) Act No. 27/2007 on Investment.

⁷⁷⁷ Article 34 clause (1) Act No. 27/2007 on Investment.

⁷⁷⁸ Article 34 clause (2) Act No. 27/2007 on Investment.

⁷⁷⁹ Article 34 clause (3) Act No. 27/2007 on Investment.

⁷⁸⁰ Interview on 11 September 2013 in Jakarta.

⁷⁸¹ Ibid

The Investment Act differs from the CSR mandatory legal provision stipulated in Act No. 40/2007 in Limited Company Liability whereby the act does not manifestly regulate the sanctions imposed to any business enterprise who does not implement the mandatory CSR legal provision in accordance to Article 74 of Act No.40/2007. Further, the Investment Act strictly regulates the administrative penalties that are passed by the authorized institution should the investors do not perform their social responsibility.

Moreover, according to Article 74, the obligation to implement the CSR programme is only addressed to any business enterprise who executes business in the natural resource exploration. Meanwhile, Article 15 of Act No.27/2007 on Investment mentions that each investor is obliged to implement the company's social responsibility. This means that both local and international investors, either investor in the natural resource exploration or in the non-natural resource exploration, are obliged to implement the mandatory CSR programme.

The stipulation of CSR as a legal obligation in the Act on Limited Company Liability is the *lex specialis derogat lex generalis* (the special Act disregards the general Act). Therefore, both laws can be used as the strong legal ground for the implementation of the mandatory CSR legal provision in Indonesia. It is clearly proven that the CSR obligation is not only a political or personal interest of the standing committee members of the Limited Company Liability Bill, but also a legal obligation of the community's will and aspiration as stipulated in the laws.

The relevant ministry/government institutions should seriously perform their roles, functions, and responsibilities on the implementation of the mandatory CSR legal provision in Indonesia. The purpose is for the regulation to benefit the people particularly the ones who are directly affected by the environmental damages caused by the business activities of the companies.

The CSR issues are the cross sectoral and cross ministerial/government institution issues. Therefore, it is necessary for the implementation to have a good coordination, communication, and synchronization among the relevant ministries in order to strengthen the implementation of the mandatory CSR policy strategy. This is necessary in order to establish a good supervision and evaluation of the mandatory CSR programmes. This is to avoid any overlapping and conflict in terms of regulatory, implementation, supervision, and evaluation of the CSR programmes among the ministries and other governmental institutions.

The articles of the Investment Act clearly noted that any business enterprise which invests in Indonesia is obliged to implement the company social responsibilities and refusal of such obligations will be punished as mentioned in the regulations. Administratively, R1 mentioned that BKPM is the authorized institutions to pass the legal sanctions because BKPM is the most relevant institution which issues the investment licenses to any Foreign Direct Investment (FDI) in Indonesia.⁷⁸²

The mandatory CSR legal provision on the Investment Act should be upheld in Indonesia. It can be done by involving the relevant ministries

⁷⁸²*Op. Cit.*, Interview on 11 September 2013 in Jakarta.

such as the State Ministry of Environment, the Indonesian National Police, the Ministry of Trade and the Ministry of Industry.⁷⁸³ Regular and close communication and coordination among the relevant ministries will positively lead to a good legal supervision and law enforcement of the Investment Act.

The absence of a permanent, credible and independent CSR surveillance body in Indonesia has made the jurisdiction and monitoring authority of the CSR programme still being performed by the internal government's supervisory agencies in each ministry and external supervisory agency. However, the internal and external supervisory agencies have their own constraints in carrying out their supervisory tasks.

One of the constraints is that there is no clear mandate by the law for those institutions to supervise mandatory their CSR programmes or to audit their CSR financial performance. Even if they can supervise the CSR programmes, the only things they can supervise are the programmes that are funded by the state budgetary scheme.

The researcher believed that the restriction of monitoring jurisdiction have led to a loose and irregular supervision on the implementation of the CSR programmes by the private companies in spite of a number of ministries/governmental institutions being involved in the policy drafting of the CSR programme in Indonesia. Therefore, one of the alternatives is that BKPM should conduct a monitoring for both local and foreign investors as regulated in the Investment Act.

⁷⁸³Ibid

The Government needs to strengthen the CSR supervisory institutions in Indonesia in order to be able to monitor and evaluate all CSR programmes being performed by state-owned enterprises, local-owned enterprises and national or foreign private companies. The enhancing is intended to improve the CSR performance of each corporate. It will also improve the transparency and financial management accountability in practice.

Consequently, the restricted jurisdiction leads to a weak supervision on the implementation of the mandatory CSR programmes in Indonesia. From the beginning, since PKBL was implemented in 2003, there has been no specific audit regarding the financial management and performance conducted either by the government internal or external supervisory agencies. This is due to the in clarity of roles and functions of the internal and external supervisors on the existing rules and regulations.

Despite the lack of specific legal provision, the ministries are still obliged to conduct a specific audit on the financial management related to the CSR programme implementation performed by state-owned enterprises and local-owned enterprises. It can also be possibly caused by no particular demands from the ministries/governmental institutions to carry out the audit on the financial management of the CSR programme implementation.

It even has deteriorated the implementation of CSR programme in Indonesia as the million worthed programmes have never been specially audited and supervised regularly. This leads to the accusation that there

might be a great number of frauds and corruptions on the implementation of the CSR programmes.

Further, the Government Regulation of the Corporate Social and Environmental Responsibility has also not particularly stipulated and firmly mentioned that the supervising/monitoring, evaluating and reporting mechanism should be performed by all corporations, either state-owned enterprise, local-owned enterprise or private companies, in implementing the CSR programmes.

Indeed, there were some business associations and corporations which refused to implement the mandatory CSR policy since the beginning. Even it has been clearly stated in the Verdict of the Constitution Court that Article 74 was not against the spirit of the Indonesian Constitution. The unwillingness of the government to implement the mandatory CSR legal provision can be seen by lack of further follow-up on the policies by the relevant ministries related to the mandatory CSR legal provision.

It has been more than 6 (six) years since Act No.40/2007 of Limited Company Liability was amended and the implementation of the mandatory CSR legal provision is still “static”. Moreover, the government regulation which is expected to offer a solution for the policy implementation seems to be useless. It because the regulation is explicitly backward in terms of the implementation of mandatory CSR for each ministerial sector.

Hence, the researcher concludes that several ministries such as Ministry of Environment, the Ministry of Energy and Mineral Resources, the Ministry of State-Owned Enterprises and the Ministry of Social have

surprisingly shown that the ministries have not taken any concrete actions on the implementation of the mandatory CSR policy.

Public listed companies are required to submit CSR reports to Stock Exchange and Financial Institution Supervisory Board. This obligation is issued by the Supervisory Board to improve the information provided by the corporations to the stockholders as well as to give advanced information for people who are going to make an investment decision.

Social and environment are the most prominent aspects to be considered by the people investing their money in a certain company. If the company has a bad track record on the implementation of social and environmental programmes, people tend to be reluctant to buy the company's stocks because they are worried if the company will be confronted with the local community or other stakeholders in which they operate. Such a condition would disrupt the production activities which will later cause losses to the company and its shareholders.⁷⁸⁴

Nevertheless, another constraint is that the number of corporations that have been registered in the stock exchange are fewer than those who are not. If the registered companies are obliged to implement and submit the CSR report separately from the company's annual report, then those companies who are not registered in the stock exchange should also be obliged to submit their CSR reports through mandatory CSR legal provision.

However, the provision of CSR as a legal obligation only applies to companies whose businesses are in the natural resources exploitation

⁷⁸⁴ Ibid

sector. Further, the unregistered and non-natural resource exploration companies are not obliged to submit the CSR report.⁷⁸⁵ Therefore, if the implementation of the mandatory CSR legal provision which is referred to Act No.25/2007 on Investment can be implemented well, then all companies, either natural resources-based companies or not, must submit their CSR reports annually without conditions.⁷⁸⁶

Indonesia is a country that has earlier stipulated the CSR policy as a legal obligation within its legal system. It was a right decision and appropriate way to push the companies to be more responsible in social and environmental aspects in which they are operating.⁷⁸⁷ It is factually proven that in some parts of the western Europe, there is a tendency to require that companies disclose their nonfinancial information. This also encourages the companies to be more socially and environmentally responsible.

On the other hand, there is still a strong influence of businessmen and companies to intervene with the government's decisions making. Nevertheless, the government themselves has not fully cared about the importance of the mandatory CSR legal provision for companies who are operating their businesses in the natural resources sector.

Mining industries are at high risk of imposing environmental damages since they involve digging and drilling activities in a great scale. Those activities are intended to search, find, and produce commercially natural resources such as oil, gas, gold, coal, etc., within a particular area. If the

⁷⁸⁵Ibid

⁷⁸⁶*Op. Cit.*, Article 15 Paragraph b of Act No.25/2007 on Investment.

⁷⁸⁷Ibid

government does not encourage the companies to implement good ethical business practice through the implementation of mandatory CSR projects, the businesses may cause harm for the people who are living around the mining areas. One of the practical actions is by applying an environmental friendly and sustainable CSR programme.

6.4 Liabilities of Mandatory CSR Surveillance Body

As mentioned, the supervisory mechanism and the CSR supervisory in Indonesia is segmented in each sectoral ministry. Then, the supervisory institution was integrated permanently as the internal supervisory institution of a certain ministry. Moreover, the authority of the internal supervisory institution is limited to the general performance aspect that is generally performed by the government institution. There is no particular and strong regulation that states that the internal supervisory institution is authorized to conduct quality assurance on the implementation of the CSR programmes within the ministry.

Further, other supervisory institution such as the BPKP is excluded from the ministerial structure. Indeed, the institution still serves as the government's internal supervisory body so that the status is still under the executive structure. The supervisory body is directly responsible to the president. Hence, BPK's (Supreme Audit Agency) role as the external supervisory body is also considered less optimal. The supervisory body conducts a financial audit based on the annual financial reports of the ministries/institutions, the state-owned enterprises and province/district/city government.

The audit cannot be automatically carried out in the same year as the year in which the budget ends. The financial audit may be delayed for a few months after a certain budget year was over. For example, the financial audit in 2013 will be completed in 2014 or early 2015, and it has demonstrated the weakness of the supervisory body. Therefore, the researcher assumed that the situation is one of the strongest reasons for establishing a permanent and independent CSR supervisory body in Indonesia.

Given some weaknesses above, the researcher assumes that the Government needs to improve and enhance the roles of functions of a CSR surveillance body and its monitoring and evaluation system. This body can perform the supervisory functions more effectively and efficiently. However, it is very urgent to have a special supervisory body to regularly monitor and evaluate the implementation of the mandatory CSR programmes in Indonesia. The permanent and independent supervisory body may avoid intricate and bureaucratic procedures and it is able to achieve an in-depth, comprehensive, transparent and accountable surveillance.

From the description above, it can be understood that the liability mechanism of those internal supervisory agencies is responsible to its respective ministry. While BPKP is responsible to the president and BPK is responsible to the national parliament, provincial council, district/city councils in accordance to its respective authority. This is particularly for BPK's liability mechanism, when the parliament (national parliament, provincial and district/city council) officially receives BPK's liability reports in the forms of financial audit and final narrative reports. Then, the parliament in each level

will encourage the executive body to follow-up all the recommendations in accordance to the parliament statutory.⁷⁸⁸

Further, the parliament will declare that the BPK's final report is open for public and can be accessed by the public.⁷⁸⁹ Hence, as the external monitoring agency, BPK reports the results of its investigation to the legislature, and if the results require follow-up, it may also submit its final investigation report to the president, the governor, and the regent/mayor in accordance to their respective authorities.⁷⁹⁰

BPK's final investigation report is politically-characterized report. It makes the monitoring and evaluation less effective.⁷⁹¹ Even Act No.15/2007 of the State Auditor Body has never obviously stated that BPK authorizes to conduct a financial and performance audit on the implementation of mandatory CSR programmes in Indonesia. Further, in other related laws and regulations on social and environmental responsibility, there is no specific and clear arrangement provision on the roles and functions of BPK regarding its authority to supervise the implementation of CSR programmes in Indonesia.⁷⁹²

BPK is restricted by the State Financial Auditing Standard in implementing its roles. Yet, they are unable to audit CSR funds and programmes that have been performed by private companies. In fact, the numbers of foreign private companies and national private companies are much higher than the number of state-owned enterprises. Based on this fact, it is important to establish a permanent and independent CSR monitoring institution

⁷⁸⁸ Article 7 clause (2) Act No. 15/2006 on State Auditor Body.

⁷⁸⁹ Article 7 clause (5) Act No. 15/2006 on State Auditor Body.

⁷⁹⁰ Article 8 clause (1) Act No. 15/2006 on State Auditor Body.

⁷⁹¹ Ibid

⁷⁹² Ibid

specified to monitor and evaluate the implementation of CSR programmes between sectors, companies and ministries.

The establishment of special CSR supervisory body needs immediate attention. It because of how large CSR potential fund in Indonesia and how many CSR ‘players’ either local, national or international level. With this situation, it is necessary to set up a monitoring system or mechanism that is truly objective, transparent, and accountable. Afterwards, BPK as an external monitoring body is not responsible to President, Governor, Regent or Mayor. BPK is responsible for parliament either national and local level.

Nevertheless, BPK is given an authority to directly report any alleged criminal act such as bribery, corruption and other criminal offenses to relevant law enforcement institutions without need to wait for approval from House of Representatives and Provincial Council, District/City Council in accordance with its respective authority.⁷⁹³ The reporting is made within 1 (one) month since the criminal offense is detected.⁷⁹⁴ The authority of BPK is part of its roles and functions as an external inspector of state financial management.⁷⁹⁵

Indeed, BPK is institutionally free and independent institution and cannot be interfered by any other institutions.⁷⁹⁶ The characteristic is enable it to run its function inspecting financial management and performance of state’s institutions and State-Owned Enterprises objectively and accountably. The process will be going without any influence from the leaders of associated department/ministry/state institutions.⁷⁹⁷ The existence of permanent and

⁷⁹³ Article 8 clause (3) Act No. 15/2006 on State Auditor Body.

⁷⁹⁴ Ibid

⁷⁹⁵ Ibid

⁷⁹⁶ Article 2 Act No.15/2006 on State Auditor Body.

⁷⁹⁷ Article 2 Act No. 15/2006 on State Auditor Body.

independent supervisory institution like BPK is urgently needed in the process of CSR monitoring and evaluation mechanism in Indonesia. It may provide more accountable monitoring and evaluation result to the public at large.

Further, BPK is also authorized to calculate and to estimate the value of state losses was caused by financial management within the governmental institutions, state institutions, state-owned enterprises and local-owned enterprises. BPK is also authorized to determine which party is responsible to pay the state losses.⁷⁹⁸ Hence, BPK will monitor the process of re-payment and report the monitoring process to the parliament either national and sub-national level in accordance with its respective authority.⁷⁹⁹ Indeed, BPK also can give information as an expert in a court trial related to the state losses.⁸⁰⁰

BPK's accountability mechanism that requires it to deliver the result of the final inspection and investigation to the parliament either national and sub-national level in accordance with its respective authority.⁸⁰¹ Indeed, the researcher assumes that it is very political because parliament is a legislative institution whose members come from political parties. Because of that reason, it is necessary to establish and to develop a permanent and independent CSR supervisory agency.

Further, still according to researcher's opinion, by establishing permanent and independent mandatory CSR surveillance body therefore, it will enable relevant stakeholders to have a clear mechanism on supervision, monitoring and evaluation of CSR programmes in Indonesia. a better surveillance system in term of independent institution, permanent personnel and permanent budget

⁷⁹⁸ Article 10 clause (1) and (2) Act No. 15/2006 on State Auditor Body.

⁷⁹⁹ Article 10 clause (4) Act No. 15/2006 on State Auditor Body.

⁸⁰⁰ Article 11 paragraph c Act No. 15/2006 on State Auditor Body.

⁸⁰¹ Ibid

are absolutely necessary for the current situation of CSR surveillance system in Indonesia. At this point, it may increase transparency and accountability of the implementation of mandatory CSR programmes in Indonesia.

Further, another government's surveillance body is Inspectorate General is structurally integrated with each ministry, province, district or city government. Therefore, the institution is not independent and autonomous. The Minister, Governor, Regent or Mayor has direct power to influence the works of Inspectorate General. In the Ministry level, it was called as Inspectorate General and in the Province, District and City level, it was called Provincial, District or City Inspectorate. The institution involved to do monitoring activity which involves auditing, reviewing, and observing the performance of every governmental unit within the Ministry, Province, District and City level.

The supervision, controlling and monitoring tasks have been doing by the Inspectorate General is to ensure every governmental unit implemented good governance principles.⁸⁰² Inspectorate General is directly responsible to Minister or the leaders of state institution.⁸⁰³ Provincial Inspectorate is directly responsible to Governor.⁸⁰⁴ At last, District or City inspectorate are responsible to Regent or Mayor.⁸⁰⁵ The mechanism was developed because those supervisory institutions are State Internal Supervisory Apparatus (APIP). Therefore, it makes them structurally responsible to the Minister, State Institutions, Governor, Regent or Mayor.

⁸⁰² Article 1 paragraph 3 Government Regulation No. 60/2008 on Government Internal Controlling System.

⁸⁰³ Article 1 paragraph 5 Government Regulation No. 60/2008 on Government Internal Controlling System.

⁸⁰⁴ Article 1 paragraph 6 Government Regulation No. 60/2008 on Government Internal Controlling System.

⁸⁰⁵ Article 1 paragraph 7 Government Regulation No. 60/2008 on Government Internal Controlling System.

Their reports are considered bias because they are part of the governmental structure. Further, their authorities are also limited to supervise governmental funded projects. According to the laws, They have no mandate and jurisdiction to do supervision, controlling and monitoring for CSR programmes within their area of responsibility.

Hence, the researcher assumes that it is necessary to establish a permanent and independent CSR supervisory agency in Indonesia. Inspectorate basic tasks and functions do not specifically to supervise CSR programmes. It was established to supervise the state financial management to be more transparent and accountable based on state financial management principles.⁸⁰⁶

BPKP is also part of Government Internal Monitoring Apparatus (APIP) together with Inspectorate General, Provincial Inspectorate, District Inspectorate and City Inspectorate.⁸⁰⁷ BPKP is directly responsible to the President. Therefore, BPKP performs some supervisory task regarding financial audit and performance audit within the Ministries, State Institutions, Provincial, District and City level. BPKP can do other types of supervision in accordance with the assignment of the President.⁸⁰⁸

Based on its roles and functions BPKP is doing financial audit and performance audit in accordance with rules and regulations set up by the Minister of Finance. Therefore, BPKP has no independency and autonomus in defining of its supervisory object.

⁸⁰⁶ Article 2 clause (1) Government Regulation No. 60/2008 on Government Internal Controlling System.

⁸⁰⁷ Article 49 clause (1) Government Regulation No. 60/2008 on Government Internal Controlling System.

⁸⁰⁸ Article 49 clause (2) Government Regulation No. 60/2008 on Government Internal Controlling System.

Thus, the results of monitoring conducted by BPKP are not free from the influence of the Minister of Finance. Therefore, it is necessary to strengthen institutional capacity and its authorities of the BPKP to be more flexible, free and independent. It will make it more powerful to supervise financial management and to supervise the performance of governmental unit in each level. Further, the researcher concludes that it is also one of reasons the necessity to establish a permanent and independent CSR supervisory agency.

Further, there is no also a specific provision stated that BPKP authorized to supervise the implementation of CSR programmes implemented by the Ministry, State Institutions, State-Owned Enterprises and Local-Owned Enterprises. Then, BPKP's jurisdiction is only limited to ministries, agencies, provincial, district and city government level. BPKP can not reach the private companies. The jurisdictional limitations make BPKP could not perform its functions optimally in monitoring CSR programmes in Indonesia.

It is necessarily to consider for establishing permanent and independent CSR surveillance agency in Indonesia. The task of the established agency is to do monitoring and evaluation any CSR programmes have been or being implemented by any companies either state-owned companies or private companies.

By the existence of that special agency, then the agency would focus more on conducting monitoring and evaluation performance of both state-owned and private companies in implementing each of their own CSR programmes. Then, the special agency should be given the authority to carry out the investigative and adjudication tasks towards complaints submitted by the public related to the losses which is caused by the business activities of the company.

The other weaknesses of BPKP is the agency carry out supervision based on supervision standards were set up by the Minister of Finance. The supervision standards was not self-developed by BPKP. Therefore, it makes BPKP is not really free and independent from intervention from other parties. The weakness leads to the importance for establishing a permanent and independent CSR surveillance agency.

Further, the disclosure will be a motivating factor for concerned government, ministries or agencies to improve their financial and management performances. The strengthening of CSR surveillance system is absolutely necessary to be done in Indonesia because of the complexity of CSR issues are still remain unsolved yet until now.

People who are living around the extractive industry's area are expecting that the mandatory CSR programmes can be implemented more transparent and accountable. It is expected that the CSR programmes can solve social, economic and environmental problems that is the society being faced so far. Then, sustainability factor of the mandatory CSR programmes is the most important thing to be considered and solved by relevant CSR stakeholders.

In addition, it is also expected to bring a greater positive impact to the improvement of social conditions, economic and environmental situations around the extractive industries's area. Therefore, the researcher concludes that a better monitoring and evaluation system is absolutely necessary in order to realize the expectations of the community.

6.5 Conclusion

The absence of permanent and independent surveillance body on mandatory CSR in Indonesia is decreasing the level of transparency and accountability on the implementation of mandatory CSR programmes. A special surveillance body has not yet been established until now. Therefore, the jurisdiction and liabilities of surveillance body also become unclear. For SOEs, internal government's surveillance body may conduct monitoring and evaluation regarding the implementation of CSR programmes because the SOEs have source of funding from the government budget. Afterwards, external supervisory agency is also allowed to supervise, to monitor and to evaluate CSR funds have been disbursed by the SOEs.

Further, it becomes difficult when the internal government's surveillance body or external surveillance body are going to supervise, to monitor or to evaluate the implementation of CSR programmes have been implemented by private companies. They are not authorized by the law to conduct supervisory, monitoring and evaluation activities towards private companies. Therefore, the establishment of permanent, transparent and independent mandatory CSR surveillance body in Indonesia is essential to increase transparency and accountability performances of mandatory CSR programmes have been implemented by either SOEs or private companies in Indonesia.

CHAPTER SEVEN DISCUSSION

7.1. Introduction

Mandatory CSR legal provision is a cross-cutting issues and has been linked to other current global issues such as the clean development mechanism, Reducing Emissions from Deforestation and Degradation (REDD) and Public Private Partnership (PPP). Further, the mandatory and voluntary CSR should not be debated any longer in Indonesia since it has been formally enacted by Act No.40/2007 of Limited Company Liability. Nevertheless, there should be consistency from the Government as the regulations' provider to pass the relevant laws, regulations and policies for the implementation of the legal provision.

The oil and gas sector is the major sector that is obliged by the act to implement the mandatory CSR legal provision. The sector can cause more environmental damages than other industrial sectors. Therefore, the government should be encouraged to provide more integrated laws, regulations and policies to make the implementation of the legal provision more transparent, accountable, integrated and sustainable.

Finally, public access to information on the implementation of the legal provision and a wider public's participation or partnership between the government, company and local community for implementing the mandatory CSR projects are the key strategies for the successful implementation of the mandatory CSR legal provision.

7.2. Clarity of the Mandatory Corporate Social Responsibility Policy

Based on the researcher's analysis, the contents of the government regulation on the mandatory CSR above is incomplete to regulate a complex mandatory CSR issues in Indonesia. Further, the content of each article is very general and may not resolve the stagnation in performing the mandatory CSR legal provision. As a result, companies which are carrying out their mandatory CSR programmes do not actually have a strong legal basis as they lack the guiding principles, legal certainties, legal liabilities and accountability.

The situation causes legal uncertainty in the implementation of mandatory CSR programmes in Indonesia. In fact, it can also lead to practices of irregularities, corruptions and misappropriation of the company's social and environmental funds. In addition, some of the companies' owners became politicians when the implementation of the mandatory CSR programmes is not strictly and clearly regulated. Then, those funds allegedly can be used for personal and group's interests in the name of social concern on the economy and the community around the company.

In particular, companies under the the Ministry of State-Owned Enterprises (MSOE) can benefit from specific policies in the form of Ministerial Decree issued by the Minister of SOE on the implementation of social activities.⁸⁰⁹ Then, the policy is used as the legal basis for SOEs in organizing Partnership and Community Development Programme (PKBL). In fact, long before the establishment of the ministerial decree in accordance with the mandate in the Constitution of Indonesia 1945, state-owned enterprises

⁸⁰⁹Minister Decree of SOEs No. Kep-236/MBU/2003 on Partnership and Environmental Development Programme (PKBL)

were required to provide added value and assistance to create people's prosperity.⁸¹⁰ Afterwards, the regulation of the Minister of Finance of the Republic of Indonesia was issued, which governs the obligations of state-owned companies to assist in the development of cooperatives and small and medium enterprises in Indonesia.,⁸¹¹

However, private foreign national companies do not have a clear and definite legal basis on the allocation, disbursement, and accountability of mandatory CSR budget fund. Everything is performed voluntarily and adapted to the goodwill of their companies. This is because there was no specific percentage that has been regulated by the regulation. Each company may vary in allocating the mandatory CSR funds between one and another. This will lead to confusion for the beneficiaries and to legal uncertainty.

In accordance with the data received by the Indonesian NGOs Forum for Conserving the Environment (WALHI), there are about ten national and foreign mining and plantation companies nationwide operating in Indonesia. The companies have been causing incredible environmental pollution and forest damage. Likewise, the data from the Mining Advocacy Network (JATAM) showed dozens of plantation and mining companies that have caused tremendous damage to the environment and forests.

⁸¹⁰Article 33 clause (1), (2) and (3) of National Constitution of Indonesia; “ clause (1) the economy shall be organized as a common endeavour based on the principles of family system, clause (2) sectors of production which are important for the country and affect the life of the people shall be under the powers of the state and clause (3) the land, the waters and the natural resources within shall be under the powers of the state and shall be used to the greatest benefit of the people”.

⁸¹¹*Op. Cit*, Minister of Finance Decree No. 1232/KMK/.013/1989 on 11 November 1989 on on the Manual of Cooperatives and Small Enterprise Development through State-Owned Enterprise.

Explicitly, national and foreign private companies operating in Indonesia are required to submit an annual report to the Annual General Meeting of Shareholders (RUPS).⁸¹² Hence, for companies whose line of business is associated with the mobilization of public funds, the Limited Liability Company has issued a promissory note that requires the company's annual report be audited by a public accountant before being filed in the RUPS.⁸¹³

The absence of community involvement in the mandatory CSR projects' implementation for a certain company will lead to public's distrust toward the company's accountability.⁸¹⁴ Consequently, the data presented by the company in its annual final report can be challenged by the public. The beneficiaries should be involved in the process of budget allocation, implementation process and liability phase of the mandatory CSR.

Weak implementation of the transparency principle in the mandatory CSR fund management leads to irregularities, corruption, mark-ups, and other irregularities in the implementation of the mandatory CSR. Principles of good corporate governance (GCG) ruled by the Stock Exchange and Financial Institution Supervisory Agency (BAPEPAM-LK) only apply to companies that have gone public or listed companies.⁸¹⁵ As a result, the companies not registered in the stock exchange have no standard in their annual financial reports.⁸¹⁶

⁸¹² Article 56 of Act No. 1/1995 on Limited Company Liability.

⁸¹³ Article 59 clause (1) of Act No. 1/1995 on Limited Company Liability.

⁸¹⁴ Article 59 clause (4) of Act No. 1/1995 on Limited Company Liability.

⁸¹⁵ Article 13 clause (93) of Act No. 1/1995 on Limited Company Liability.

⁸¹⁶ Article 59 clause (4) of Act No. 1/1995 on Limited Company Liability

One of the principles of good corporate governance (GCG) is transparency.⁸¹⁷ Transparency will provide space for the participation of communities, particularly for the relevant stakeholders in mandatory CSR programme development, budget allocation, execution, and accountability.

There are several principles for good corporate governance (GCG) to be respected and implemented by a company in Indonesia. The principles include transparency, accountability, independence, and equality and decency. These principles are enshrined in the Indonesian Code of Good Corporate Governance which was released in 2006.

Further, the issuance of Indonesian Code of Good Corporate Governance in 2006 provided a great opportunity for the operating national and foreign private companies to create their own foundation voluntarily for the implementation of their GCG principles. That is often what makes it difficult for them to adjust their mandatory CSR programmes against the rules/new policies since they were used to carrying out their mandatory CSR programmes voluntarily and in their self-interpreted activities.

Act No. 1 of 1995 on Limited Company Liability does not provide for sanctions in the implementation of CSR programmes. This is because the law itself does not mention it clearly and firmly in the Act. Therefore, the monitoring of the implementation of companies' mandatory CSR programmes is not well managed. These activities have only been carried out in the goodwill of the company alone and state-owned enterprises have been doing

⁸¹⁷ Thomas S.Kaihatu, *Good Corporate Governance dan Penerapannya di Indonesia* [Jurnal Manajemen dan Kewirausahaan Vol. 8, Number 1,2006], 9.

the same by drafting, implementing and reporting of their CSR programmes by themselves. They receive less supervision, monitoring, controlling and evaluation from the Ministry of State-Owned Company.

The state (in this case the relevant governmental agencies in the areas of business), can monitor the implementation of such companies' CSR programmes through several stages: first, by ensuring that the aims and objectives of the company are not contrary to the laws, order and decency.⁸¹⁸ Public order can be the main consideration by the agency overseeing the major business entity to ensure that the business entity allocates a portion of its profits to social activities and environments. The principle of public order is closely related to the acceptance of the public about the operation of the company.

The second stage is to evaluate the implementation of the company's CSR programmes through scrutinizing the company's annual report.⁸¹⁹ After the company closes its financial year, the Board of Directors shall prepare annual financial statements with copies approved by the RUPS to be delivered to the government agency which oversees the business entity. In this way, the government agencies can check the CSR programmes which have been implemented by the company.

The role of government agencies that oversees the business entity should be dominant in monitoring the implementation of CSR programmes in Indonesia. It should happen that way because the government has an authority

⁸¹⁸ Article 2 of Act No. 1/1995 on Limited Company Liability.

⁸¹⁹ Article 56 of Act No. 1/1995 on Limited Company Liability.

to make policies concerning the implementation of CSR programmes, which are unambiguously stated in Act No. 1 of 1995 of Limited Company Liability.

The implementation of mandatory CSR programme requires a good monitoring and evaluation system to be used as a reference for the stakeholders. It is necessary especially for government agencies overseeing these activities of business entities to ensure good and on-target performance of the mandatory CSR programmes. The third stage is the presence of goodwill of the Board of Commissioners in carrying out the mandatory CSR programmes in their companies.

The Board of Commissioners is the most important component in the implementation of a company's activities as it constitutes representatives of the shareholders who will ensure that the company's activities run well and achieve profit as planned.

The Board of Commissioners should be aware that if their company does not have mandatory CSR programmes, then its operations will be disrupted and profit cannot be optimally achieved. Therefore, a good relationship between the company and the community is essential. Moreover, the Board of Commissioners can check the Board of Directors' annual report to ensure that the mandatory CSR programmes have been running properly. It is expected that the mandatory CSR programmes be implemented and that the beneficiaries can feel the positive impact from the presence of the company.

However, this goodwill is difficult to measure and is different from one corporation to another. If by chance the commissioner board are the ones that have a high social awareness, the implementation of the company's mandatory

CSR programme can run well and on target. Otherwise, the mandatory CSR programme is not a priority for the company.

Therefore, the role of the state in regulating the implementation of mandatory CSR programmes is necessary to ensure there is a standard reference for a company to carry out its mandatory CSR programmes. The difference in the interpretation of mandatory CSR programme implementation between one company and another thus can be avoided. The fourth stage is inserting the mandatory CSR programme implementation components in one of the components to be reported by a company in the Financial Accounting Standards.⁸²⁰

A company is obliged to prepare annual financial statements in accordance with Financial Accounting Standards. The accounting standards, which are prepared by the Ministry of Finance of the Republic of Indonesia, can be used as a guide for companies in Indonesia to prepare their annual financial statements. The implementation component of the mandatory CSR programmes can be included in the Financial Accounting Standards so that the reporting stage becomes mandatory although their implementation is voluntary as stated in Act. No.1/1995.

The company is also very often to publish its annual report in the form of summary of the actual annual report which makes it very difficult for the public to read the annual financial statements. Moreover, the annual financial report is usually published in a national mass media whose publications are extremely limited to only the upper middle class.

⁸²⁰ Article 58 of Act No. 40/2007 on Limited Company Liability.

Therefore, it remains necessary to have further state adjustment to the role of mass media in the process of monitoring and evaluating the implementation of mandatory CSR programmes in Indonesia in a form of a national mandatory CSR system framework.

The sources of CSR budget can be collected either from state-owned or private business enterprises and the allocated budget can be used to be more optimally useful for the beneficiaries by setting clear and unequivocal regulations. It will be able to provide a new source of funding for poverty alleviation programmes in Indonesia and for the realization of sustainable development by involving the community as a major stakeholder in the implementation of national development.

Legal sanctions for companies that do not perform the mandatory CSR programmes are not well organized and clearly visible in Act No. 1 of 1995 on Limited Company Liability. Sanctions imposed on the company for not properly implementing the mandatory CSR programmes are only social sanctions such as public demonstrations, road/operation location blockade, and the destruction or burning of the company's facilities.

7.3. The Stagnation of Mandatory CSR Policy in Indonesia

The new version of Limited Company Liability Act also contains a number of strategic and important provisions previously unavailable in the old version of Limited Company Liability Act. The most significant difference of Act No.40/2007 on Limited Company Liability is the existence of a specific chapter regulating on mandatory CSR. This is a step forward taken by the

government and the parliament in overseeing the good implementation of the CSR programmes in Indonesia.

Nevertheless, pro and contra still occurs in the implementation of CSR as a legal obligation, especially among businessmen who associate in several business associations such as the Indonesian Businessmen Association (APINDO), the Indonesian Young Entrepreneurs Association (HIPMI), the Indonesian Chamber of Commerce and Industry (KADIN) and the Indonesian Business Women Association (IWAPI).

They rejected the enactment of CSR as a legal obligation because it will add to the tax burden, reduce competitiveness, hinder the investment climate in the country, and lower exports and rising unemployment. However, the lawsuit filed by KADIN and several other business associations were rejected by the Constitutional Court because the court assumed that the mandatory CSR legal provision is a way to encourage companies to participate in the economic development of the society.⁸²¹

Thus, Article 74 on the mandatory CSR legal provision remains in effect as usual and the debate on voluntary and mandatory CSR issue has ended with the constitutional court decree on Article 74 on the mandatory CSR legal provision.

The pro and contra between mandatory and voluntary CSR should no longer exist since the Constitutional Court has passed its verdict that rejected

⁸²¹ Constitutional Court Verdict Number 53/PUU-VI/2008 on Judicial Review of Article 74 on Corporate Social Responsibility [Jakarta, Constitutional Court Publishing, 2008], 99.

the application of a judicial review of some business associations on the mandatory CSR legal provision.

The enactment of the legal provision as a legal obligation is one of the nonjudicial causes of the length of time in the issuance of government regulations concerning the CSR. For a period of approximately five (5) years, the Indonesian companies have de facto implemented CSR programmes voluntarily although CSR has been *de jure* a legal obligation since the publication of Act No.40/2007 on Limited Company Liability.

Even though there are some groups who oppose the implementation of CSR as a legal obligation, there are other groups and individuals who support it. In fact, the Danish government has issued a special law on CSR as a legal obligation. Hence, the issue of CSR as a legal obligation is not just a wishful thinking but an answer to the future challenges of environmental protection, economic empowerment, poverty alleviation and social welfare of the community.

As a matter of fact, another reason CSR serves as a legal obligation in Indonesia is that a number of multinational companies operating in Indonesia have been shirking their environmental responsibility.⁸²² With so many companies neglecting their duties, damage to the environment has caused the destruction of the ecology and produced an impact on people's livelihood. One apparent example is the case of waste pollution by PT Newmount Minahasa Raya (NMR) in Buyat Bay, district of South Minahasa, North Sulawesi and the

⁸²²Akil Mochtar, *Peraturan Saja Tidak Cukup*, (www.cifor.cgiar.org), [Jakarta, CIFOR Publishing No.2, April, 2010], 8.

case of PT Lapindo Brantas mudflow in Porong, Sidoarjo. These cases have prompted the government to make CSR as a legal obligation.⁸²³

In fact, a number of companies, among of which is Pertamina Company, have also accepted the application of CSR as a legal obligation. These companies hoped that CSR fund they have to allocate will not exceed 5% of the total of the company's net profit. Further, the Ministry of Environment of the Republic of Indonesia has been considering utilizing CSR as a way to overcome the negative effects of environmental degradation. It was stated by the deputy assistant of community and organization's role improvement of the Ministry of Environment during a national CSR forums on environmental issue.

Thus the importance of the mandatory CSR role as a counterweight to the relationship between companies and society requires highly detailed, systematic, focused and integrated regulations with a variety of elements and interests in the use of the CSR fund itself. Regulatory overlap between the ministries/agencies and ministries/institutions at the national level has deflected the CSR issue from its focus on substance and system reform to a long debate concerning whether CSR should be voluntary or mandatory.

The confusion is coupled with the initiatives of several autonomous regions/municipalities at district and province level which have published regulations on CSR. Accordingly, there are other local governments which are currently drafting regional regulations on the management of mandatory CSR funds. The East Java province, as a matter of fact, is the only province in

⁸²³Ibid.

Indonesia that has issued a Provincial Regulation on CSR before the government passed Government Regulation No.47/2012 on CSR.

The Ministry of Environment of the Republic of Indonesia has issued guidelines for its implementation in environmental field as a reference for companies in Indonesia to implement their companies' environmental CSR programmes. The implementation of the mandatory CSR programmes is so closely related to the aspect of community development that the government needs to issue guidelines for the implementation of mandatory CSR in the environmental field as an attempt to steer the company in remaining compliant with the laws and regulations in the environmental field.

There are several laws directly related to the implementation of mandatory CSR programmes in the environmental field.⁸²⁴ The mandatory CSR legal provision is set up clearly and firmly in Act No.40/2007 on Limited Company Liability, but the laws do not determine the specific sanctions/punishment for companies that do not implement the mandatory CSR legal provision. This is despite the act clearly stating that “companies which do not put into practice their obligation shall be liable to sanctions in accordance with the provisions of legislative regulations.”⁸²⁵

That means the legal sanctions for companies that do not comply with the Article shall be based on the sectoral Act governing legal sanctions either in Environmental Act, Mineral and Coal Mining Act, Forestry Act and other related laws. Nevertheless, the law also stipulates the administrative remedies

⁸²⁴ Act No. 32/2009 on Environmental Management and Protection, Act No. 18/2008 on Waste Management, Government Regulation No.82/2001 on Water Pollution Control and Government Regulation No. 41/1999 on Air Pollution Control.

⁸²⁵ Article 74 clause (3) of Act No.40/2007 on Limited Company Liability.

that can also be pursued by interested parties or prosecutors if the company violates the public interest or violates the prevailing laws and regulations.⁸²⁶

As a matter of fact, in the government regulations governing the mandatory CSR, the threat of criminal or administrative sanctions for companies that do not properly implement mandatory CSR programmes was not explicitly and clearly stated.⁸²⁷ On the contrary, what happens is that the repetition of the contents of Article 74 (3) on Article 7 of the government regulation on the CSR of Limited Company Liability.⁸²⁸ That proved that there was a fierce debate in the process of drafting the regulations.

According to the information has been provided above, the researcher assumes that a government regulation should become a rule that clarify ones that have not been regulated in details in the Act. Therefore, the initially ambiguous and unexecutable rule can otherwise be implemented with the publication of the government regulation without any different interpretations of mandatory CSR among the stakeholders in Indonesia. Nevertheless, the existence of Article 74 on mandatory CSR and Government Regulation No. 47 of 2012 on CSR of Limited Company Liability already fits the absence of CSR executing regulation in Indonesia.

⁸²⁶ Article 146 clause (1) paragraph a and b of Act No. 40/2007 on Limited Company Liability.

⁸²⁷ *Op. Cit*, Government Regulation Number 47/2012 on Corporate Social and Environment Responsibility

⁸²⁸ Article 7 of Government Regulation No. 47/2012 on Corporate Social Responsibility.

7.4. Partnership and Environmental Development Programme (PKBL)

Partnership and Environmental Development Programme (*Programme Kemitraan dan Bina Lingkungan/PKBL*) is a programme that was set up as part of the state policy to pass a responsive policy for the development of social and economic conditions in the macro and micro levels. It has been a long before the revision of ActNo.40/2007 on Limited Company Liability.

Further, Ministry of State-Owned Enterprises (MSOE) has been implementing what so-called CSR related programmes in Indonesia since 1989. Afterwards, the Ministry of Finance has also issued a Minister of Finance Decree concerning the guidelines for the development of economically weak entrepreneur and cooperative through state-owned enterprises.

The programme was then known as Partnership and Environmental Development Programme (PKBL), which after the implementation of Act No. 40/2007 on Limited Company Liability was transformed into CSR programme. It indicates that the name and the term has changed but the substance was still based on the CSR-related programmes.

Types of CSR projects may highly vary, it is caused of the difficulty in finding a standard and measurement for assessing whether a CSR programme has been implemented properly or not by a particular company. In addition to the lack of technical rules governing the minimum standards on the implementation of CSR programmes to be performed by the companies. Hence, it encourages many companies implement CSR programmes in various types of activities. Further, they also implement it either alone or by appointing a third party.

The expected mandatory CSR types of implementation is three-partnership-based involving companies, communities and non-governmental organizations. However, this form is rarely found and as a matter of fact, in the era when local government are already sniffing the companies' obligation to provide the CSR budget.

Hence, some local government quickly creates local regulations which aim to direct the companies to submit the CSR fund to their budget account. Then, they will take over the function of distributing the funds to the beneficiaries in the form of CSR projects to the community.

Standards of morality alone are still not enough to serve as an instrument for implementing the CSR programmes because morality constitutes social norms whose equivalence is difficult to seek, and does not have a standard measurable both quantitatively and qualitatively. The international community has produced a standard a guideline for the implementation of the CSR programme.

The guideline could be adopted by countries in interest including Indonesia and then applied through their laws and regulations. Even the Indonesian government has undergone a revolutionary change in the implementation of the CSR programmes by regulating them as a legal obligation and not just activities carried out based on the company's good intentions alone.

Article 74 on mandatory CSR receives both rejection and support from various parties, especially from the entrepreneur and business associations such as the Chamber of Commerce and Industry (*Kamar Dagang dan Industri/KADIN*), the Indonesian Business Women Association (*Ikatan Wanita*

Pengusaha Indonesia/IWAPI), Indonesian Young Entrepreneurs Association (*Himpunan Pengusaha Muda Indonesia/HIPMI*) and the Indonesian Employers Association (*Asosiasi Pengusaha Indonesia/APINDO*).

The refusal on the enforcement of Article 74 is manifested in a constitutional appeal of the content of Article 74 at the Constitutional Court (MK). Ultimately, after going through the tortuous proceedings, the Constitutional Court decided that the contents of Article 74 the CSR is not contrary to the Constitution of the Republic of Indonesia.

Mandatory CSR programmes should be implemented proportionally, according to the standards of appropriateness, feasibility and reasonability. A company also can not provide the mandatory CSR programmes beyond extraordinary and reasonable forms, like hot mix asphalt road construction, bridge construction worth billions of rupiahs, and other forms of programmes that will deteriorate its financial state.

Society should also be aware of the company is a form of profit-oriented business entity. They are not merely a social institution that becomes an arm of the government in implementing development programmes. It should be actually the obligation of the government as a carrier of mandate of the people who elected them through general elections.

The government also should not position the companies as *cash cows* that serve as a backup source of fund for the development of the state and society. If that is the case then the company's competitiveness will be weakened, the investment climate becomes lethargic, and many companies will go bankrupt due to excessive exploitation by the government and society. Aneel Karnani

stated that the concept of CSR is contradictory or irrelevant to the profit-oriented spirit of enterprises.

The CSR programmes initiated by large firms are sometimes used for *greenwashing* by those who have been doing business activities with no respect to social and environmental aspects such as mineral mining companies, petroleum extraction, coal mining, timber companies, and so on. They keep running the CSR programmes based on the prevailing laws but, on the other hand, violations and denial of social aspects, particularly to the environment, are still being practiced systematically.

The principles of the mandatory CSR programme implementation are embodied in the form of real field programmes such as cheap credit loan scheme for cooperatives and small and medium enterprises and regular and well-planned reforestation. Further, education assistance, and others, all of which must be implemented to meet several basic principles contained in the ISO 26000 on Social Responsibility, among others are accountability, transparency, ethical behavior, respect for stakeholder interests, adherence to the law, respect for international norms of behavior, and respect for human rights.

The mandatory CSR programmes will continue to seek their standardized format along with the strengthening needs and dependencies among local communities, government, NGOs and entrepreneurs. This will positively impact the community development process that aims to achieve the millennium development goals.

State Owned Enterprises should use the CSR as a means to encourage and to stimulate economic growth. It especially in the field of creative economy for obtaining financial aid that functions as revolving fund for training, marketing and financial reporting for business groups aided by public's CSR fund. These planned and systematic efforts are expected to contribute positively to the growth of the national economy.

Types of support and assistance provided by State Owned Enterprises' fund the Partnership and Community Development programme must truly meet the beneficiaries needs of the main CSR programmes. In fact, mandatory CSR programmes implemented by a state-owned company with others must have different specification and pressing points in order to avoid overlapping assistances. There should also be intensive coordination and communication with the local district/city so that the state-owned company's CSR activities can be synergized with short, medium and long term development plans in the district/town.

The implementation of PKBL programme in state-owned companies constitutes the implementation of the policy of the Minister of SOE on the PKBL programme.⁸²⁹ In the decree it is clearly stated that the main goal of CSR funding for the partnership programme is to improve the ability of small and medium enterprises and cooperatives to compete with state-owned companies by utilizing CSR funds.⁸³⁰ On the other hand, the community

⁸²⁹State Owned Enterprise Minister Decree Number KEP-236/MBU/2003 on Partnership Programme of State Owned Company and Small Enterprise and Environment Protection Programme.

⁸³⁰Ibid

development programme is an assistance to the social conditions surrounding the operational area of state-owned companies.⁸³¹

There are two (2) mainstreams State Owned Enterprise's CSR programmes, namely partnership programme and community development programme. Both are an integral part of State Owned Enterprise's CSR programme. However, small businesses that can participate in the partnership development programme with state-owned companies are ones with a net worth at least IDR 200,000,000.00 (two hundreds million rupiahs) excluding land, building and with maximum annual sales of IDR 1,000,000,000.00 (one billion rupiahs).⁸³²

This has caused many small businesses unable to meet these requirements. Meanwhile, according to the criteria in the Act, a small business has a net worth at most IDR 50,000,000.00 (fifty million rupiahs) excluding land and building, or has annual sales worth more than Rp 500,000,000.00 (five hundred million rupiahs).⁸³³ Moreover, the fund is distributed in the partnership programme is a revolving fund and is not in the form of an aid but a loan to be reimbursed to the state-owned company by way of installments.

This means the state-owned company has functioned as a non-bank financial institution that delivers loan to small business groups and cooperatives; a function that actually is performed by the banks. As a matter of fact, loan distribution to small and medium enterprises is actually conducted by

⁸³¹Article 1 point 4 of the State Owned Enterprise Minister Decree Number KEP-236/MBU/2003 on Partnership Programme of State Owned Company and Small Enterprise and Environment Protection Programme.

⁸³²Article 3 paragraph a and b of the State Owned Enterprise Minister Decree Number KEP-236/MBU/2003 on Partnership Programme of State Owned Enterprise and Small Enterprise and Environment Protection Programme.

⁸³³Article 6 clause (2) of Law No. 20/2008 on Micro, Small and Medium Enterprise.

commercial or joint venture banks, while technical assistance to them is organized by Bank Indonesia.⁸³⁴

On the other hand, the core of CSR programme is economic empowerment around the company's operational areas in the form of assistance, not in the form of loan. The grant is allocated by setting aside some amount of a company's profit which is calculated as the cost of the company. Therefore, based on the mandatory CSR legal provisions, PKBL programme is not classified in the category of CSR activities.

Partnership programme funding source is obtained from a state-owned enterprise's profit after tax deduction of 1% to 3% of its nett profit.⁸³⁵ This way the CSR fund managed by each state-owned enterprise will grow in line with the payment process with low-interest loan distributed by each enterprise.

Partnership programme funds can be channeled in the form of loan for working capital or the purchase of assets aiming to increase production and sales.⁸³⁶ They can later be used for special loan in the form of short term financing in fulfilling the orders of State Owned Enterprise business partner.⁸³⁷ They can also be used in the form of grants whose total amount should not exceed 20% of the total partnership fund distributed during the

⁸³⁴ Indonesian Bank Regulation Number 14/22/PBI/2012 on credit giving or financing by general bank and technical assistance in term of micro, small, and medium enterprise development.

⁸³⁵ Article 8 clause (1) and (2) of the State Owned Enterprise Minister Decree Number KEP-236/MBU/2003 on Partnership Programme of State Owned Enterprise and Small Enterprise and Environment Protection Programme.

⁸³⁶ Article 10 clause (1) paragraph a of of the State Owned Enterprise Minister Decree Number KEP-236/MBU/2003 on Partnership Programme of State Owned Enterprise and Small Enterprise and Environment Protection Programme.

⁸³⁷ Article 10 clause (1) paragraph b of of the State Owned Enterprise Minister Decree Number KEP-236/MBU/2003 on Partnership Programme of State Owned Enterprise and Small Enterprise and Environment Protection Programme.

current year.⁸³⁸ Assistances in the form of grants may be utilized by small businesses to increase their productivities by conducting marketing training, apprenticeship, promotion, special education, and research.⁸³⁹

Community development programme fund can be used to help victims of natural disasters, improve health and religious facilities, develop infrastructures, public facilities, education and/or training.⁸⁴⁰ However, there is no detailed description on the criteria of each of the assistance provided to each of these groups. There is even no provision regarding the mechanism of coordination and cooperation between these activities and the short, medium and long term development plans of the district/city where the state-owned company operates.⁸⁴¹

Loan mechanism for partnership programme is conducted by a relevant small business' applying for the loan to a certain State Owned Enterprise by attaching some required data or documents such as business unit identity, business owner identity, business field information, business license from government agencies, business development and cost plan.⁸⁴²

Afterwards, the application will be selected by the SOE after coordinating with the State Owned Enterprise's coordinator.⁸⁴³ In the activities, the Partnership and Community Development aid/loan providers are referred to as

⁸³⁸ Article 10 clause (1) paragraph c of the State Owned Enterprise Minister Decree Number KEP-236/MBU/2003 on Partnership Programme of State Owned Enterprise and Small Enterprise and Environment Protection Programme.

⁸³⁹ Ibid

⁸⁴⁰ Article 10 clause (3) of the State Owned Enterprise Minister Decree Number KEP-236/MBU/2003 on Partnership Programme of State Owned Enterprise and Small Enterprise and Environment Protection Programme.

⁸⁴¹ Ibid

⁸⁴² Article 11 point a of the State Owned Enterprise Minister Decree Number KEP-236/MBU/2003 on Partnership Programme of State Owned Enterprise and Small Enterprise and Environment Protection Programme.

⁸⁴³ Ibid

a State Owned Enterprise supervisor and assistance/loan beneficiaries as supervised partner.

The PKBL programme report is performed by each State Owned Enterprise supervisor to the Minister as the person-in-charge with a copy to each Commissioner of the supervising State Owned Enterprise.⁸⁴⁴The PKBL programme report is conducted regularly and separately from the company's annual report.⁸⁴⁵The PKBL reports consist of quarterly and annual reports.⁸⁴⁶

Quarterly report is authorized by the Minister no later than (30) days after the end of the quarter.⁸⁴⁷ As for the annual report audited by an auditor, it is to be approved by the Minister no later than 6 (six) months since the end of the budget year.⁸⁴⁸ With the approval of the audited annual report, the director's and commissioner's responsibility for the management and supervision of the PKBL programmes is ended.⁸⁴⁹

The Minister of SOE has also issued technical guidance related to the PKBL programme implementation in the vicinity of the ministry of SOE.⁸⁵⁰In the technical manual was stated that each supervising SOE is required to form

⁸⁴⁴Article 19 clause (1) of the State Owned Enterprise Minister Decree Number KEP-236/MBU/2003 on Partnership Programme of State Owned Enterprise and Small Enterprise and Environment Protection Programme.

⁸⁴⁵Article 19 clause (3) of the State Owned Enterprise Minister Decree Number KEP-236/MBU/2003 on Partnership Programme of State Owned Enterprise and Small Enterprise and Environment Protection Programme.

⁸⁴⁶Article 19 clause (2) of the State Owned Enterprise Minister Decree Number KEP-236/MBU/2003 on Partnership Programme of State Owned Enterprise and Small Enterprise and Environment Protection Programme

⁸⁴⁷Article 20 clause (1) paragraph a of the State Owned Enterprise Minister Decree Number KEP-236/MBU/2003 on Partnership Programme of State Owned Enterprise and Small Enterprise and Environment Protection Programme.

⁸⁴⁸Article 20 clause (1) paragraph b of the State Owned Enterprise Minister Decree Number KEP-236/MBU/2003 on Partnership Programme of State Owned Enterprise and Small Enterprise and Environment Protection Programme.

⁸⁴⁹Article 20 clause (3) of the State Owned Enterprise Minister Decree Number KEP-236/MBU/2003 on Partnership Programme of State Owned Enterprise and Small Enterprise and Environment Protection Programme.

⁸⁵⁰Circulating Decree of State Owned Enterprise Ministry Number SE-433/MBU/2003 on Technical Guidance on the Implementation of BUMN Partnership Programme with Small Enterprise and Environment Protection Programme.

a PKBL unit. This unit specifically functions to coach, to administer and to finance the PKBL project within a specific SOE. The implementation directive is a further elaboration of the State-ministerial decree on the Partnership and Community Development Programme.

The lack of third-party participation especially Non-Governmental Organizations (NGO) in the process of planning, budget allocation, implementation, monitoring and evaluation of the programme. It has prevented the maximum and consistency in the implementation of the principle of transparency as stated in the principles of good corporate governance of the PKBL programmes by state-owned companies. In fact, the Ministry of SOEs has issued a policy regarding the practice of good corporate governance in SOEs.⁸⁵¹

In the policy, it is stated that the SOEs are required to apply the principles of good corporate governance consistently or make them an operational basis.⁸⁵² This suggests a strong commitment of the Minister of SOEs in conducting transparent, accountable, responsible, independent, and fair corporate governance as prescribed in the principles of good corporate governance.

The role of NGOs is necessary for ensuring the spirit of transparency and accountability in the distribution of fund for partnership and community development programme by state owned enterprises. Therefore, the programme is on target and can reach main beneficiaries who are absolutely entitled to the capital loan scheme. With the involvement of a wide range of stakeholders in

⁸⁵¹ State Owned Enterprise Minister Decree Number KEP-117/M-MBU/2002 on the Implementation of Good Corporate Governance Practices to BUMN.

⁸⁵² Article 2 clause (1) of State Owned Enterprise Minister Decree Number KEP-117/M-MBU/2002 on the Implementation of Good Corporate Governance Practices to BUMN.

the management of fund, it is expected that the organization of the PKBL fund will improve from year to year.

In 2007, the Ministry of State Enterprises renewed its policy in the implementation of the PKBL programme by issuing a ministerial regulation.⁸⁵³ One of considerations is that the previous policy on CSR was still not enough to serve as the operational basis for the improvement of partnership programme between SOEs and small businesses and community development programmes.

In relation to the implementation of the PKBL programmes that are considered as part of their CSR activities by the state-owned companies, the Minister of SOE further has issued a new policy regarding the implementation of mandatory CSR legal provision as prescribed on Article 74 of the Limited Liability Act No.40/2007 on the CSR. As a result, in the Ministry of State Owned Enterprises there are two (2) applicable CSR programmes, which are the PKBL and CSR.

Therefore, a legal certainty and clearer setting for the mechanism of CSR programme implementation in Indonesia, as a form of corporate awareness on social, environmental and economic communities around the operational areas of a company, is needed.

According to the information was provided above, the researcher assumes that the publication of the policy of the Minister of State Owned Enterprises on the application of Article 74 on the CSR is a good signal and a positive step toward the implementation of CSR programme as a legal obligation. The Ministry of Enterprises already provides a good example for a change in the

⁸⁵³ State Owned Enterprise Ministry Regulation Number PER-05/MBU/2007 on BUMN Partnership Programme with Small Enterprise and Environment Protection Programme.

state policy in the implementation of CSR programmes in Indonesia from voluntary service to mandatory.

7.5 Overview of CSR Manual on Environment in Indonesia

In fact, there are several dimensions in term of understanding CSR itself, one of which is its environmental dimension.⁸⁵⁴ In the environmental dimension of CSR, some phrases intended to protect and create cleaner environment and to consider environmental factors in business operations, are found.⁸⁵⁵ As a matter of fact, based on Article 74 on the CSR, a company engaged in the business of natural resource management is required to implement CSR as a legal obligation. The main reason behind the establishment of CSR as a legal obligation is environmental reason.

Thus, the importance of environment as a reason in the establishment of CSR as a legal obligation in Indonesia has made Indonesia the first country in the world to require CSR from its companies because of the strong desire to preserve the environment. This monumental step should be appreciated and implemented in such earnest intentions that the goodwill of state legislators can be implemented appropriately.

State has legal obligation based on the constitutional mandate to ensure the sustainability of life of its citizens so that the state should take a significant role

⁸⁵⁴ Shafiqur Rahman, *Evaluation of Definitions: Ten Dimensions of Corporate Social Responsibility*, [World Review of Business Research Vol. 1 No. 1, March 2011], 168.

⁸⁵⁵ Alexander Dahlsrud, *How Corporate Social Responsibility is Defined: an Analysis of 37 Definitions*, [Wiley Interscience, 2006], 4.

in the process of environmental protection.⁸⁵⁶ Much of the environmental damage is caused by extractive industries operating their business in natural-resource-related field. Therefore, the state seeks to create good and clean environmental condition and to minimize environmental damage by applying Article 74 of the CSR.⁸⁵⁷

In fact, obtaining a clean and good environment to live in is one of the human rights protected by the Indonesian constitution.⁸⁵⁸ The policy encourages the business community to participate in the national development, along with other state components, and to achieve welfare for all the people of Indonesia.

As one of the measures in the implementation of CSR programmes in the environmental field, the Ministry of Environment of the Republic of Indonesia has issued guidelines on the implementation of CSR in the environmental field.⁸⁵⁹ In the guidelines it is stated that there are several CSR programmes in the environmental field, namely; cleaner production, environment-friendly office (eco office), conservation of energy and natural resources, waste management, renewable energy, adaptation to changes in the environment and environmental education.

The absence of NGOs and main beneficiaries representatives in the process of drafting the CSR guidelines for the environment has led to a lack of

⁸⁵⁶ Article 28H clause (1) of the Indonesian Constitution 1945, it says that “Every person shall have the right to live in physical and spiritual prosperity, to have a home and to enjoy a good and healthy environment, and shall have the right to obtain medical care”.

⁸⁵⁷ Ibid

⁸⁵⁸ Article 28I clause (4) of the Indonesian Constitution 1945, it says that “the protection, advancement, upholding and fulfilment of the human rights are the responsibility of the state, especially the government”.

⁸⁵⁹ Minister of Environment Affairs Republic of Indonesia, *Manual on CSR Environmental Programme in Indonesia*, (Jakarta, Ministry of Environmental Affairs Republic of Indonesia, 2011).

information and field input as well as community's aspirations regarding the implementation of environment-based CSR programmes. Actually, the people in the operational location of mining companies and large estates feel such direct impact of environmental pollution caused by the companies.

Indeed, their voices should be heard in the process of formulating policies that will affect their interests.⁸⁶⁰ There are several advantages in the process of regulation formulation that involves a wider community. For instance, it will give them an opportunity to express their aspirations and vision, people better understand what they really need, and it will provide an assurance on each side on the substances to be regulated in the policy, thereby reducing the risk of rejection and failure in the implementation phase.⁸⁶¹

The introduction section of the environment-based CSR guidelines still uses the phrase "to arouse concern and commitment of the company to voluntarily implement CSR activities in the environmental field". On the other hand, it ignored the existence of Article 74 of the CSR that has asserted the implementation of the CSR programme is a legal obligation for companies engaged in the field of or related to natural resources. This is reinforced by the publication of the Constitutional Court's verdict on a lawsuit over article 74 of

⁸⁶⁰Article 20 clause (2) and (4) of Act No.25/2009 on Public Service. Article 2 "in relation to draft and to stipulate service standard as mentioned on clause (1), the administrator is required to involve community and other relevant parties". Article 4 "Community involvement and other relevant parties as mentioned on clause 2 above, shall be done within non-discriminatory principle, direct connection with kind of service, competent and prioritizing consensus and pay attention to diversity.

⁸⁶¹Mark Coekelbergh, *Regulation or Responsibility?, Autonomy, Moral Obligations and Engineering*, [SAGE Publications Inc, Technology and Human Values Vol. 31, No.3, 2006], 237.

the CSR filed by a number of representatives of employers' associations and several companies.⁸⁶²

On the other hand, the CSR guidelines mention that CSR is a mandatory programme and in its implementation companies have to comply with all the provisions of the prevailing legislation. It covered especially the sectoral legislation governing the environment, investment, forestry, mineral and coal mining.

The presence of a company should be beneficial for people and it should operate within the framework of the legislation rules and economic framework stipulated by the government of a certain country.⁸⁶³ In fact, a CSR will deliver real change if the principles and practice are integrated in the company's daily activities and its development is monitored regularly.⁸⁶⁴

Both communities and their country have such different characters and cultures from one another that the aspirations and expectation of the community on the implementation of CSR also vary according to the level of their interest.⁸⁶⁵ It is, therefore, necessary to have a different approach between one society and another.⁸⁶⁶ Indonesia has implemented CSR as a legal obligation because the policy is deemed most suitable to the wishes, expectations and demands of the prevailing legal, social, economic and political situation of Indonesia.

⁸⁶²Ibid

⁸⁶³Louise Gardiner, Catherine Rubbens and Elena Bonfiglioli, "Big Business Big Responsibilities," [Journal of Corporate Governance Vol.3 No.3, 2003], 67.

⁸⁶⁴Ibid

⁸⁶⁵David Birch and Jeremy Moon, "Corporate Social Responsibility in Asia," [The Journal of Corporate Citizenship Vol.13, 2003], 20.

⁸⁶⁶Ibid

Nevertheless, the implementation of CSR in Indonesia should be more systematic, integrated, well-planned and sustainable by publishing more straight forward policy. Instead, CSR management in Indonesia now seems very sectoral and the ministries do not seem well-integrated.⁸⁶⁷ A specialized agency, therefore, is still required to manage the implementation of CSR in Indonesia in order for it to be better-managed, systematic, integrated and sustainable as expected in the technical guidance of CSR environmental field.

CSR is a very difficult aspect to describe in details because it will intersect other aspects such as business ethics, business sustainability, and corporate citizenship. It is necessary, therefore, to have firm arrangement in providing legal certainty for the companies to carry out mandatory CSR programmes in Indonesia. Hence, the government's role is very important and vital in outlining and regulating them.

The government can issue a policy that provides clarity for aspects of each activity of these business terms. Indonesia actually has taken a step forward in its effort to provide legal assurance for the implementation of CSR by implementing CSR policy as a legal obligation.

Based on Article 74 of the CSR, CSR is such an integral programme of environment, economic community development and social cohesion. Some of the processes comprises of planning, implementation, monitoring and evaluation. It should also be constituted an inseparable unit and held by a particular institution authorized for it. Otherwise, a persisting sectoral ego of each ministry/agency will occur, prompting them to issue some CSR policies

⁸⁶⁷Ibid

with their authority in the absence of coordination and good communication with other ministries/agencies/other groups.

In many developing countries like Indonesia, CSR management is still weak due to the insignificant role of government agencies, NGOs, standards of implementation, systems of appeal and CSR implementation complaint system.⁸⁶⁸ Therefore, the government should strengthen the role of each party especially NGOs and other CSR managing and implementing agencies so that its implementation can get better, systematic, and sustainable.

In addition to the publication of technical guidelines and instructions for the implementation of environment-based CSR, other measures taken to implement better mandatory CSR programme in Indonesia are by publishing good corporate governance (GCG) principles and the release of companies' annual report. These steps are still voluntary for companies so a standard mechanism needs to be figured out in guarding the better implementation of mandatory CSR programme in Indonesia.

Mandatory CSR policies need to be consistently and accountably conducted by central and local government in order to carry out the mandate of the law and the decision of the Constitutional Court on judicial review on Article 74 of the mandatory CSR legal provision. The formulation of various CSR-related policies should be based on the mandatory legal provision as

⁸⁶⁸ Melody Kemp, *Corporate Social Responsibility in Indonesia: Quixotic Dream of Confident Expectation?*, [Corporate Codes of Conduct No.11, 2001], 16.

stated on the Act No.40/2007 on Limited Company Liability and the verdict of the Constitutional Court.⁸⁶⁹

Technical guidance of the environmental CSR based programme was stipulated on the technical guidance in which has been passed by the Ministry of Environment. The formulation of the policy is intended to guide the implementation of CSR programme to be more systematic, integrated and sustainable in Indonesia, especially in the environment-based programme. As for the government, the environmental CSR guidelines will help to provide complete and accurate information regarding the implementation of environmental CSR programmes and to cooperate with other groups when necessary.

Further, for the community, it provides a space for their participation in the implementation of environmental CSR programmes in their regions.⁸⁷⁰ CSR guidelines should be drawn up in a codified form of CSR guidelines covering all aspects of social, environmental, economic empowerment, rewards and punishment. Hence, it should also covers about complaint mechanism, factual verification mechanism against corporate's CSR reports, monitoring mechanism, evaluation and controlling procedures on CSR programme, and CSR reporting mechanism. The codification will facilitate the relevant stakeholders in learning and following the rules contained in the CSR guidelines.

⁸⁶⁹Ibid

⁸⁷⁰ Minister of Environment Affairs Republic of Indonesia, *Manual on Technical Guidance of the Environmental CSR Implementation*, [Jakarta, Ministry of Environment Affairs Republic of Indonesia, 2010], 3.

Due to lack of codification of the CSR-related regulations, then it confuses relevant governmental offices, companies and beneficiaries in the implementation of mandatory CSR programmes. Hence, less of socialization and information dissemination on CSR mandatory legal provision for the people, companies and governments due to lack of reference sources. As a matter of fact, many companies themselves do not understand and comprehend on the mandatory CSR legal provision.

Moreover, there is a lack of commitment from each company's shareholders to implement mandatory CSR programmes. Therefore, if the codification of mandatory CSR policy can be conducted, it can be used as a guide for companies to run the programme properly and for other relevant stakeholders to conduct initiative surveillance process.

Usually companies will only implement environment-friendly or socially-responsible behavior if it benefits them.⁸⁷¹ Therefore, there is a need for sincerity and strong commitment from them to make CSR a part of their companies' long-term strategy. Sincerity and commitment are two abstract (2) things that can not be scientifically measured. Therefore, a clear mechanism is necessary to measure the level of sincerity and the company's commitment to implement better, integrated and sustainable CSR programmes.

Hence, the prevalence of various products of policies containing general principles, general and technical guidelines, government regulation and local regulation on CSR implementation are absolutely necessary in order to provide

⁸⁷¹ Dilek Cetindamar & Kristoffer Husoy, Corporate Social Responsibility Practices and Environmentally Responsible Behavior: The Case of the United Nations Global Compact, [Journal of Business Ethics, 2007], 4.

legal certainty for all parties. It will really helpful for the government itself, local community and especially the companies in implementing CSR programmes in Indonesia to align with expectations of the society and legislation in force.

7.6 Tax Reduction Policy for Mandatory CSR Programme in Indonesia

Tax reduction policy is one of the most awaited by the companies in implementing mandatory CSR programmes in Indonesia. They expect the government to provide tax reduction policies for companies that have well-implemented CSR programmes. Further, another constraints for implementing mandatory CSR is no single effective, transparent and accountable mechanism of supervision, control and report for mandatory CSR mechanism in Indonesia.

In addition, the company needs a wider tax reduction policy and Directorate General of Taxes has passed a policy regarding the tax reduction.⁸⁷² Unfortunately, the companies need more competitive and attractive tax reduction policy from the government.

As a matter of fact, mandatory CSR reporting mechanism is not clear yet to this day despite the fact that mandatory CSR policy has been imposed since 2007. Approximately six (6) years since the implementation of mandatory CSR reporting mechanism, it is still unclear which government agencies are responsible for receiving the reports, what will be done to them once received, how is the factual verification mechanism for them, who is involved in the

⁸⁷² Government Regulation No. 93/2010 on Charity for Natural Disaster Recovery, Research and Development, Educational Facilities, Sport Development, and Social Infrastructures Development can be decuted from Bruto Revenue.

factual verification team and when the publication and dissemination of the report is made public.

All these questions are still raised today and remain unreplied. In fact, based on the data acquired from inspection to several ministries, it was found that the Ministry of Enterprise, the Ministry of Social Affairs and the Ministry of Environment did not even have their own standard mechanism of supervision and control to measure the level of compliance in the implementation of mandatory CSR programme.

Further, they have not possessed a standard mechanism for mandatory CSR programme report because an enterprise just voluntarily submits its annual CSR programme report to each of the relevant ministries. Companies are not even legally required to submit an annual report of the CSR programmes to each relevant ministry.

Many unresolved issues regarding the implementation of the government's policy of mandatory CSR also made the government is reluctant to issue a tax reduction policy for companies that have well-implemented CSR programmes. Although in fact, these issues are also under the responsibility of the ministry of law as government representative in preparing and issuing clear and definite policies for the implementation of mandatory CSR programmes in Indonesia.

This tax reduction policy stipulated in the legislation and regulation includes the reduction of taxes on the following activities;

1. Assistance to national natural disaster.
2. Donation to research and development in Indonesia
3. Assistance for social infrastructure development costs

4. Donation of educational facilities.⁸⁷³

Some of the above items are activities that obtain a company a tax deduction scheme from the government.⁸⁷⁴ However, it can still "*operates*" by conducting only those four types of activities and then claims that the activities are its CSR programme in order to obtain the tax reduction scheme from the government.

Actually, the four activities are of company's charity and therefore the company is still far from the real implementation of mandatory CSR programme, which actually should be sustainable. Although some portion of the CSR programme is indeed charity, the percentage is limited. There is no firm and real provision in the legislation that stipulates the percentage limit of charity in mandatory CSR programmes.

A number of NGO activists stated that employers' demand regarding tax deductions in the implementation of mandatory CSR programme is a form of entrepreneurs' indulgence. They should actually focus more on the preparation and implementation of mandatory CSR strategy rather than asking for tax relief from the government. The demand of tax relief indicates the company's lack of seriousness in implementing mandatory CSR programmes.

According to Siti Maemunah, who agreed on the mandatory CSR clause in the Act No.40/2007 on Limited Company Liability, so far there has been no clear commitment from the company to involve the community since the negotiation stage of investment plan up to the stage of granting mining

⁸⁷³ Article 6 clause (1) paragraph i, j, k, l of Act No. 36/2008 on Income Tax (the Fourth Amendment of Act No.7/1983 on Income Tax).

⁸⁷⁴ Ibid

royalties and implementation of CSR programmes for communities around the mining area.⁸⁷⁵

In line with the JATAM NGO activist, former Minister of Social Affairs of the Republic of Indonesia, Bachtiar Chamsjah also said that the government would be cautious in providing tax incentives for companies that implement CSR programmes because the government itself did not know exactly whether the cost for CSR will be included in the production cost since that can affect the selling price of goods in the market.

The economy observer Saparini Hendri said that tax incentives would be burdensome because the government would reduce government revenue from the tax sector. In fact, the only mainstay of the country's income is from the tax sector. Further, tax reduction may be granted if the government has changed the paradigm of tax as an instrument to provide incentives or dissincentives to the business sector.

Entrepreneurs, especially the Indonesian Chamber of Commerce and Industry (*Kamar Dagang dan Industri/KADIN*) expected that the government will provide tax incentives to companies that implement CSR programmes in Indonesia. The chamber considers that CSR mandatory legal provision contained in the Act No.40/2007 on Limited Company Liability will financially burden their companies and would undermine the investment climate in Indonesia because there are too many rules imposed by the government to the companies.

⁸⁷⁵*Op. Cit.*, Siti Maimunah, Aminuddin A. Kirom, Tracy Glynn, etc, *Tambang dan Pelanggaran Hak Asasi Manusia: Kasus-kasus Pertambangan di Indonesia 2004-2005*, [Jakarta, Jaringan Advokasi Tambang, 2007], 22.

Pros and cons between employers' associations, governments, economists and NGOs regarding the tax reduction policy for the implementation of CSR programmes in Indonesia is a form of dynamics and complexity of the CSR issue itself. Government as final decision makers should really listen to the various inputs from various parties, especially the CSR stakeholders, before making a decision for the administration of the tax reduction scheme.

The government should improve the organizational structure of CSR implementation in Indonesia and clarify the mechanism of supervision and control of CSR programmes.⁸⁷⁶ Hence, clarify its report, reward and punishment mechanism to reinforce CSR programme and to clarify the mechanism of verification of its factual statements and determine which government agency is to serve as a leading ministry/agency in the implementation of mandatory CSR programme.

If all of the profanity issues have been addressed, the government can make decision on the administration of the tax reduction scheme. Indeed, if some of the above issues can not be resolved, the tax incentive scheme administered by the government could trigger the occurrence of irregularities, falsification of data and reports, and corruption. But if a good CSR governance has been developed, the government no longer has to worry when granting a tax incentive scheme for companies with good CSR programme implementation track record.

Even in such developed countries as the United States, tax has a significant role in providing economic stimulus for social sector. Large companies in the United States will be granted huge tax incentives if supporting the programmes

⁸⁷⁶Ibid

implemented by NGOs. The tax incentive will encourage strategic partnerships between companies, governments and NGOs in building social structures in society through programmes with positive, broad and sustainable impact.

In addition to the Act on income tax, the government has also issued a policy on tax incentives for the national disaster relief programmes, the development of social infrastructure, research and development activities, and the development and construction of educational facilities in the form of government regulations.⁸⁷⁷

The regulations stipulate that companies implementing the above-mentioned programmes will be granted a tax deduction from the government up to a certain maximum amount.⁸⁷⁸ The specified maximum amount is limited by 5% (five percent) per year and if the donation given exceeds the threshold the government would only reduce the tax by 5% while the rest is charged on the company and can not be claimed for the following year.⁸⁷⁹

Further, the tax incentives may be granted only if a company meets the requirements, which are; the company can show the previous year's net income to tax officials, the donation does not cause the company to suffer losses and is supported by valid evidence such as receipts or evidence of donation handover, and the institution who receive the donations has a Tax Payer Identification

⁸⁷⁷ Government Regulation No.93/2010 on National Disaster Recovery Donation, Research and Development, Educational Facilities, Sports Development and Social Infrastructure Development Costs Deductible from Gross Revenue.

⁸⁷⁸ Article 1 of Government Regulation No.93/2010 on National Disaster Recovery Donation, Research and Development, Educational Facilities, Sports Development and Social Infrastructure Development Costs Deductible from Gross Revenue.

⁸⁷⁹ Article 3 of Government Regulation No.93/2010 on National Disaster Recovery Donation, Research and Development, Educational Facilities, Sports Development and Social Infrastructure Development Costs Deductible from Gross Revenue.

Number (*Nomor Pokok Wajib Pajak*/NPWP) except the agencies/institutions that are exempt in accordance with the Income Tax Act.⁸⁸⁰

Furthermore, these contributions can not invoke a tax deduction if they are donated to those who are still tied to the marital relationship,⁸⁸¹ as in the case of a husband whose company contributes to the educational foundation which is owned by his wife. This company can not request for a tax deduction on the donation because the donator and the recipient have a marital relationship.⁸⁸²

Donation for natural disaster relief, research and development, sports and educational facilities can be contributed in the form of money and/or goods, while the contribution to social infrastructures should not be money but facilities and/or infrastructures.⁸⁸³ In fact, the value of the donation that can be requested tax deduction can be calculated by using three (3) methods, namely calculating the value of the acquisition, the value of fiscal book and cost of goods sold.⁸⁸⁴

Tax deduction calculation by using the acquisition value method is used when donation is not depreciated at the time the company donates it to recipients.⁸⁸⁵ Fiscal book value method is used when the goods donated are

⁸⁸⁰Article 2 of Government Regulation No.93/2010 on National Disaster Recovery Donation, Research and Development, Educational Facilities, Sports Development and Social Infrastructure Development Costs Deductible from Gross Revenue.

⁸⁸¹Article 4 of Government Regulation No.93/2010 on National Disaster Recovery Donation, Research and Development, Educational Facilities, Sports Development and Social Infrastructure Development Costs Deductible from Gross Revenue.

⁸⁸²Article 8 of Act No. 36/2008 on Income Tax (the Fourth Amendment of Act No.7/1983 on Income Tax).

⁸⁸³Article 5 of Government Regulation No.93/2010 on National Disaster Recovery Donation, Research and Development, Educational Facilities, Sports Development and Social Infrastructure Development Costs Deductible from Gross Revenue.

⁸⁸⁴Article 6 clause (1) of Government Regulation No.93/2010 on National Disaster Recovery Donation, Research and Development, Educational Facilities, Sports Development and Social Infrastructure Development Costs Deductible from Gross Revenue.

⁸⁸⁵Ibid

already depreciated by the company at the time of donation. As for the principal amount method, it is used if the donated items are the products of the donating company itself.⁸⁸⁶

All the three methods of calculation are used to calculate the value of donation given by companies for natural disaster management, research and development, and sports and educational facilities. The method of calculation for donation in the form of social infrastructure, on the other hand, is determined based on the value or actual cost basis incurred by the company to build the social infrastructure.⁸⁸⁷

Hence, the counting mechanism for natural disaster relief, research and development, sports and educational facilities is different from that of social infrastructure donation. The difference is due to the fact that the social infrastructure donation is not of mobile donation while the donation of natural disaster relief, research and development, sports and educational facilities are of mobile one.

The contributor must record all forms of donations given so that any form of donation given can be reported and used to request for a reduction in taxes from the state.⁸⁸⁸ A good and transparent recording system is also required to determine the value of tax deductions to be granted to a company.⁸⁸⁹ However, there is no specific provision on whether all statements and tax reduction requests filed by the company will be re-verified by tax authorities or not.

⁸⁸⁶Ibid.

⁸⁸⁷Article 6 clause (2) of Government Regulation No.93/2010 on National Disaster Recovery Donation, Research and Development, Educational Facilities, Sports Development and Social Infrastructure Development Costs Deductible from Gross Revenue.

⁸⁸⁸ Article 7 of Government Regulation No.93/2010 on National Disaster Recovery Donation, Research and Development, Educational Facilities, Sports Development and Social Infrastructure Development Costs Deductible from Gross Revenue.

⁸⁸⁹Ibid

Provisions on factual verification are still not stipulated in the the government regulation. Perhaps, the Directorate General of Taxation only administratively receives and examines the documents of assistance handover without verifying the factual truth of form, value and amount of the donation given.

In addition to the contributor obligation to record and report the amount of the contribution, the donation recipients, especially natural disaster relief agencies or bodies, are required to make a report of receipt and distribution of the donations they receive to the Directorate General of Taxation each quarter.⁸⁹⁰ Afterwards, report of the donation for research and development, sports and educational facilities, and social infrastructure is submitted at the end of the donation year to the Directorate General of Taxation.⁸⁹¹

Unlike for the institution receiving natural disaster relief assistance with a Tax Payer Identification Number (NPWP), the amount of donation received is attached in the financial report when submitting annual income tax notice the year the donation accepted.⁸⁹²

Aside from the tax incentives given to the four (4) types of donation, the Indonesian government through the Decree of the Ministry of Finance of the Republic of Indonesia also has issued several policies on tax reduction or customs elimination on some types of goods from oil and gas business activities in Indonesia. The issuance of a number of tax deduction and the

⁸⁹⁰ Article 8 clause (1) of Government Regulation No.93/2010 on National Disaster Recovery Donation, Research and Development, Educational Facilities, Sports Development and Social Infrastructure Development Costs Deductible from Gross Revenue.

⁸⁹¹ Article 8 clause (2) of Government Regulation No.93/2010 on National Disaster Recovery Donation, Research and Development, Educational Facilities, Sports Development and Social Infrastructure Development Costs Deductible from Gross Revenue.

⁸⁹² Article 8 clause (3) of Government Regulation No.93/2010 on National Disaster Recovery Donation, Research and Development, Educational Facilities, Sports Development and Social Infrastructure Development Costs Deductible from Gross Revenue.

elimination of import duties show the Indonesian government 's commitment to attracting investors to the oil and gas industries in Indonesia.

Some of the policies consist of a policy of import duty exemption on raw materials of upstream oil, gas and geothermal industries,⁸⁹³ import duty exemption on certain raw materials for large industries,⁸⁹⁴ and indirect cost allocation reimbursable by the government⁸⁹⁵ and value added tax charged on the government on the import of goods for upstream oil, natural gas and geothermal exploration.⁸⁹⁶ Furthermore, the government has also issued Government Regulation on Cost Recovery in the oil and gas industries to open ways for investors to operate in Indonesia.⁸⁹⁷

In the cost recovery policy oil and gas contractor must apply for the approval of the work plan and budget to the Head of Indonesian Special Task Force for Upstream Oil and Gas Business (*SKK Migas*).⁸⁹⁸ The budget to be approved will include routine and project expenses,⁸⁹⁹ while the cost of business operation include a oil and gas exploration and exploitation costs and other expenses.⁹⁰⁰

The exploration cost includes 3 (three) components namely, first, drilling cost consisting of exploration and development drilling costs, second,

⁸⁹³Ministry of Finance Regulation Republic of Indonesia No. 177/PMK.011/2007 on Free Import Tax for Upstream Oil, Gas and Geothermal Industries.

⁸⁹⁴Ministry of Finance Regulation Republic of Indonesia No. 41/PMK.011/2007 Free Import Tax Facility for Materials and Certain Part of Big Equipment Assembling by Big Equipment Industries.

⁸⁹⁵Ministry of Finance Regulation Republic of Indonesia No. 256/PMK.011/2011 on Indirect Cost Recovery in Oil and Gas Profit Sharing Calculation and Income Tax for Oil and Gas Contractor.

⁸⁹⁶Ministry of Finance Regulation No. 178/PMK.011/2007 on Value Added Tax Covered by Government for Imported Goods for Oil, Gas and Geothermal Exploration Industries.

⁸⁹⁷Government Regulation No. 79/2010 on Cost Recovery and Income Tax for Upstream Oil and Gas Industry.

⁸⁹⁸Article 5 clause (3) of Government Regulation No. 79/2010 on Cost Recovery and Income Tax for Upstream Oil and Gas Industry.

⁸⁹⁹Article 5 clause (2) of Government Regulation No. 79/2010 on Cost Recovery and Income Tax for Upstream Oil and Gas Industry.

⁹⁰⁰Article 11 clause (1) of Government Regulation No. 79/2010 on Cost Recovery and Income Tax for Upstream Oil and Gas Industry.

geological and geophysical costs consisting of the cost of geological studies and geophysical research, third, general and administrative expenses in exploration activities, and fourth, the cost of depreciation.⁹⁰¹

The cost of exploitation includes several cost components, namely, first, direct production costs for oil and gas; second, gas processing costs; third, utility costs consisting of production and tool maintenance costs as well as steam, water and electricity costs; fourth, general and administrative expenses during the exploitation; and fifth, depreciation costs.⁹⁰²

The general and administrative expenses for the exploration and exploitation activities consist of administrative and financial costs, personnel costs, materials service costs, transportation expenses, general office expenses, indirect taxes, local taxes and levies.⁹⁰³

Further, there are other cost components which consists of cost for gas transportation from production point to delivery point, and the cost of post-operative upstream business activities.⁹⁰⁴ All components of the operating expenses including the exploration and exploitation costs and other expenses will be reimbursed by the government after the exploration of oil and natural gas has commercially produced oil or gas.⁹⁰⁵

On the contrary, if oil or gas exploration failed in the commercial production of oil or gas the loss of the operational cost is borne entirely by the

⁹⁰¹ Article 11 clause (2) of Government Regulation No. 79/2010 on Cost Recovery and Income Tax for Upstream Oil and Gas Industry.

⁹⁰² Article 11 clause (3) of Government Regulation No. 79/2010 on Cost Recovery and Income Tax for Upstream Oil and Gas Industry.

⁹⁰³ Article 11 clause (4) of Government Regulation No. 79/2010 on Cost Recovery and Income Tax for Upstream Oil and Gas Industry.

⁹⁰⁴ Article 11 clause (5) of Government Regulation No. 79/2010 on Cost Recovery and Income Tax for Upstream Oil and Gas Industry.

⁹⁰⁵ Article 7 clause (1) of Government Regulation No. 79/2010 on Cost Recovery and Income Tax for Upstream Oil and Gas Industry.

contractor.⁹⁰⁶ If an area of oil or gas operation can produce oil or gas products commercially, the status of the commercial production is stipulated by the Minister of Energy and Mineral Resources.⁹⁰⁷

All these operating costs, however, can only be reimbursed by the government if they meet certain conditions, namely; they are incurred for directly oil-related business activities in Indonesia with reasonable price and no indication of special relationship as stipulated in the Income Tax Act. The petroleum business is conducted by practicing acceptable business and engineering values; and the petroleum business is based on the work and budget plan approved by the Head of SKK Migas.⁹⁰⁸

There are still some requirements to be met in order for the operating cost of oil-related business activities to be reimbursed by the government as stipulated by Article 12 paragraph (1) letter of Government Regulation No. 79/2010 on Cost Recovery and Income Tax for the Upstream Oil and Gas Industry. These requirements are;

1. Depreciation costs for equipment and items that will become state properties,
2. The direct costs of the head office of oil and gas contractor whose work can not be executed by the Indonesian agency, and is not routine in nature,
3. Costs for rewards/bonus given to workers in accordance with the legislation of taxation affairs,

⁹⁰⁶Article 7 clause (3) of Government Regulation No. 79/2010 on Cost Recovery and Income Tax for Upstream Oil and Gas Industry.

⁹⁰⁷Article 7 clause (2) of Government Regulation No. 79/2010 on Cost Recovery and Income Tax for Upstream Oil and Gas Industry.

⁹⁰⁸Article 12 clause (1) of Government Regulation No. 79/2010 on Cost Recovery and Income Tax for Upstream Oil and Gas Industry.

4. Cost of natural disaster relief donation given on behalf of the Indonesian government based on the provisions of the legislation of taxation affairs,
5. Costs incurred for the community capacity building and environment preservation during exploration
6. Expenditure cost for central office on the condition that it is used to support oil and gas business in Indonesia, the office operating costs have been included in the consolidated financial statement and audited with the reasons for its allocation, and the magnitude of such cost does not exceed the limit set by the Regulation of the Ministry of Finance.⁹⁰⁹

In addition to the reimbursable costs already listed, there are other costs that can not be reimbursed by the government, namely;⁹¹⁰

1. Costs incurred for personal benefit of workers, managers, oil and gas contractors and shareholders,
2. The reserve cost for contractor's business activities,
3. Assets donated,
4. Administrative sanctions imposed on contractors such as interest, penalties for late payment of taxes or other obligation, and compensation in the execution of criminal sanctions in accordance with the legislation.
5. Depreciation cost of goods and tools that will not be state properties used for exploration and exploitation operations,
6. Payments of incentive, bonuses, pensions, insurance premiums for foreign workers', administrators', and shareholders' self-interests.

⁹⁰⁹Article 12 clause (2) of Government Regulation No. 79/2010 on Cost Recovery and Income Tax for Upstream Oil and Gas Industry.

⁹¹⁰Article 13 of Government Regulation No. 79/2010 on Cost Recovery and Income Tax for Upstream Oil and Gas Industry.

7. The cost of foreign workers who do not meet the plan procedures for foreign workers or are without working permit.
8. The cost of legal counsel that are not directly related to the implementation of the oil business,
9. The cost of tax consultant,
10. Marketing cost of oil and gas entitled to contractor, except for the cost of oil and gas marketing approved by SKK Migas,
11. Representation cost of any galas on any behalf and form except for the representation cost accompanied by a nominative list of beneficiaries and their Taxpayer Identification Number (NPWP),
12. Environment and community development costs during the exploitation,
13. The cost of technical training for foreign workers,
14. The cost of merger, acquisition or transfer of contractor rights in oil and gas cooperation contract,
15. Cost of loan interest,
16. Employee income tax borne by the contractor and other types of taxes.
17. Procurement of goods and services not in accordance with the principles of fairness and good engineering or exceeding 10 % expenditure authorization,
18. Material surplus due to improper planning and purchase,
19. The book value and asset operation costs already used but not operable due to contractor's negligence,
20. Costs of transaction detrimental to the state, the procurement of goods and services without proper tender process stipulated by the laws except in certain cases, and other costs incurred in violation of laws and regulations.

21. Bonuses paid to the government,
22. Costs incurred prior to the signing of contract,
23. Incentive cost for interest recovery, and
24. Commercial audit costs.

Considering the above costs reimbursed by the government, actually oil and gas contractor has had sufficient fund to carry out CSR activities as required in Article 74 of Act No.40/2007 on Limited Company Liability. Moreover, specifically for oil and gas companies, fund for community capacity building and environment development during the exploration stage is included in the list of expenses reimbursed by the government, or in other words, the community development and environmental fund is borne by the government. Considering such condition, there should be no further objection or refusal from oil and gas companies in Indonesia to implement mandatory CSR policy as elaborated in Article 74 of Act No.40/2007 on Limited Company Liability.

Given some provisions on cost recovery as stipulated in government regulations, it is increasingly clear that the Indonesian government has been providing various adequate facilities for oil and gas companies operating in Indonesia regarding tax reduction and incentives. The tax incentives especially for import duty exemption on certain items not available or not manufactured in Indonesia for oil and gas business operation.

Therefore, the oil and gas companies themselves actually do not intend to implement the policy of mandatory CSR legal provision in Indonesia and are always looking for excuses to avoid the obligation to implement mandatory CSR programmes. Any costs with tax reduction and incentives of import duty exemption actually have been very clearly stipulated in the existing policies.

Government, communities and NGOs need to continue to encourage both domestic and foreign oil and gas companies in Indonesia to carry out their social and environmental obligation in order to meet their legal obligations in accordance with ActNo.27/2007 on Investment and Act No.40/2007 on Limited Company Liability.

The government should intensively supervise the implementation of CSR mandatory legal provision to run in line with the expectation of the legislators. The description above makes it clear that tax incentives have been granted by the government to the oil and gas companies although it is necessary to repair and improve the policies of such tax incentives.

Business enterprises concern that mandatory CSR policy would make them less competitive due to the increased production cost and would cause rise in prices of their products. Then, it would dampen investors' interest to invest in Indonesia, especially for companies engaged in the oil and gas sector. They actually have to allocate a large number of fund for implementing CSR programmes within the framework of the implementation of Article 74 of Act No.40/2007 on Limited Company Liability.

In fact, the government, in this case the Directorate General of Taxation, and companies granted tax deduction and tax-free import incentives never disclosed publicly the wide range of facilities they receive from the government. Similarly, government did not provide access for the public to obtain information regarding the tax privilege received by the companies.

Transparency is one of the principles that must be upheld either by the Government or the company itself so that the public does not have a negative bias against them. Without information disclosure anarchy and demonstration

will take place because people have lost their confidence and do not know where to find information.

In the implementation of CSR programmes, actually fund spent by oil and gas companies in the exploration stage will be reimbursed by the government. Unfortunately, in reality none of the oil and gas companies publicly disclose information that they have the fund to finance CSR programme at the exploration stage and it is refundable by the government. In fact none of the oil and gas companies implement CSR programmes in the exploration phase on the grounds that they have not benefited from their business activities yet.

Therefore, mandatory CSR legal provision is one of the government's strategies to improve the companies' social responsiveness. Further, it would enhance harmony both the people and companies in the protection and preservation of the environment, economic empowerment and social care. At last, tax reduction incentives package issued by the government may encourage the companies in Indonesia especially those engaged in the natural resource business sector to implement mandatory CSR programme align with the mandate of Article 74 of Act No.40/2007 on Limited Company Liability.

7.7. Conclusion

The government should provide appropriate policies to enhance the implementation of mandatory CSR in Indonesia. Policies clarity is an important strategy to implement the mandatory CSR well implemented. Further, stagnation of mandatory CSR policy in Indonesia due to unclear policies from the government itself. There should be a standard guidelines on

mandatory CSR and the establishment of permanent and independent surveillance body.

The government has passed government regulation on CSR, unfortunately the policy did not meet the basic requirement to fulfill the mandatory CSR legal provision. Mean while, there are some ministries are conducting CSR activities based on their respective ministries core functions. It is not a good signal to enhance mandatory CSR legal provision. Afterwards, there are also different implementation strategy between SOEs and private companies which is SOEs implements PKBL programme, even though at the same time they also implement mandatory CSR programme in accordance with Article 74 of Act No.40/2007.

At last but not least, environmental aspect is one of the most important aspects for mandatory CSR. Even, there are two more aspects are also important in which social and economic empowerment. The three things should be done simultaneously and at once. Finally, tax incentives should be given by the government for companies are implementing good mandatory CSR programmes because “*stick*” and “*carrot*” policies are still relevant to encourage the companies obey the rules and regulations on mandatory CSR legal provision in Indonesia.

CHAPTER EIGHT

CONCLUSION AND RECOMMENDATION

8.1 Conclusion

Although many parties either from the ministries, practitioners, academics or companies themselves are supporting the enactment of Article 74 of Act No. 40/2007 on Limited Company Liability, but there is some others especially from business associations and business enterprises who rejected either directly or indirectly related to the enactment of CSR mandatory legal provision. However, those who rejected the enactment of the Article 74 are also predominantly from practitioners, academics, and business associations. It seems there is divided opinion between some academics and practitioners and the others.

Since the beginning, there are some business associations rejected the enactment of Article 74 of Act No. 40/2007 such as the Indonesian Chamber of Commerce and Industry (KADIN), the Indonesian Business Women Association (IWAPI), Indonesian Young Entrepreneurs Association (IWAPI) and the Entrepreneurs Association of Indonesia (APINDO). In addition, the rejection of the enactment of Article 74 also comes from the Ministry of Environment of the Republic of Indonesia. The Ministry is the only state institution that formally disagrees with the enactment of the mandatory legal provision.

Based on previous findings and discussion, it seen that mandatory CSR in Indonesia has become a positive rule. Even though, there is still different opinion in the stage of its implementation between business associations or companies group and the community as its beneficiaries. Government officials

are also divided into two groups, one group supported mandatory CSR and the other group does not support mandatory CSR. Those are support mandatory CSR is officials from constitutional court, ministry of cooperatives, small and medium enterprise, ministry of energy and mineral resources, ministry of home affairs, law and human rights ministry and state-owned company ministry.

Meanwhile, officials from environmental ministry and social affairs ministry do not agree with the provision mandatory CSR. They are keen on supporting voluntary CSR. Hence, there are some ministries such as environmental ministry, social affairs ministry and domestic affairs ministry produce and release a number of regulations, manuals or standards on CSR. It is sometimes confusing CSR stakeholders because the policies are frequently overlapping between one and another.

Mandatory CSR is a nontraditional way for implementing CSR programmes. The traditional way involves the programme being implemented voluntarily. Then, evidence-based situations took place whereby massive environmental destruction occurred in several countries. The destruction caused climate change, global warming, nature instability, loss of biodiversity resources, loss of indigenous people's livelihood sources, and other disasters such as landslide and extreme flood. The concern of securing environment from destruction and of protecting biodiversity are not only the concern of a particular state and society itself but also the concern of business enterprises. At this point, based on the principle of fairness and equality, the party causing the damages will be more responsible for recovery.

Therefore, business enterprises must exercise greater responsibility to take care of the environment around their business operations. The mandatory CSR

mechanism is fairer than the carbon trade mechanism in terms of protecting the environment from destructions and of securing the rights of indigenous people because the mandatory CSR mechanism places the burden of protecting the environment on business enterprises. The carbon trade mechanism, on the other hand, not only puts the burden on the community and state but also makes reserve forests the commodity of trading.

Currently, Indonesia is implementing 2 (two) types of CSR policies: voluntary CSR and mandatory CSR. Voluntary CSR policy is implemented for businesses that deal with non-natural resources, such as manufacturers, banking industries, and other services business enterprises. Whereas mandatory CSR policy is intended for companies whose core business relates to natural resources.

The legal substance of mandatory CSR policy should be enhanced by passing relevant policies and regulations to strengthen and implement the mandatory CSR legal provision. The government must remind all CSR stakeholders that the mandatory CSR legal provision does not imply that the government intends to control the CSR programmes of Indonesian companies dealing with mining, oil, gas, and other related natural resources. Hence to avoid any prejudice, the message must be clearly and publicly accessed by all CSR stakeholders.

Further, the establishment of a legal CSR structure is also necessary. With the structure, specific and powerful CSR agencies may better support the implementation of mandatory CSR programmes in Indonesia. Yet currently there is no specific government's surveillance body or agency responsible for drafting the executing regulations of mandatory CSR, and for supervising and

evaluating the programmes in Indonesia. In fact, all the processes are still scattered in different government offices and ministries. However, it needs a mandatory CSR surveillance body which under direct supervision of the President Republic of Indonesia or at least has a status as the same level with ministry body.

CSR should be seen as a good willingness of a business enterprise to build a long-term partnership with its relevant stakeholders. Hence the society should also should be taught that no more cash money assistance will be provided by companies who already have a CSR scheme to adapt with the society's best interest. The culture can be shifted slowly if the legal substance and legal structure of CSR in Indonesia are clearly made available in practice.

It is also necessary that the CSR policies are synchronized and harmonized immediately because clear CSR policies may better support the implementation of CSR programmes. Recently the CSR policies have been drafted by sectoral ministries particularly those related to social, environmental, and economic empowerments. Also currently there are several national Acts and sectoral regulations related to CSR programmes, which are as follows:

1. Company Liability Act Number 40/2007
2. Constitutional Court Verdict Number 533/PUU-VI/2008 on Mandatory CSR
3. Environmental Management and Protection Act Number 32/2009
4. Investment Act Number 25/2007
5. State Owned Company Act Number Number 19/2003
6. Oil and Gas Act Number 22/2001
7. Micro, Small and Medium Scale Enterprise Act Number 20/2008

8. Social Prosperity Act Number 11/2009
9. Coal and Minerals Mining Act Number 4/2009
10. Forestry Act Number 19/2004
11. Water Resources Act Number 7/2004
12. Governing Aceh Act Number 11/2006
13. Government Regulation Number 93/2010 on National Disaster Donation, Research and Development Donation, Educational Facility Donation, Sport Development Donation, and Social Infrastructure Development Expenses (can be deducted from Bruto Revenue).
14. Government Regulation Number 47/2012 on Corporate Environmental and Social Responsibility

Further, international organizations have also passed several guidelines on social responsibility, but the guidelines are voluntary in nature. Many companies in Indonesia have been utilizing these guidelines as manuals or guidance in implementing their CSR programmes. Some consulting firms have also offered voluntarily CSR training for CSR officers from the companies. Some of the international voluntary guidelines are as follows:

1. Organization for Economic Co-operation and Development Guidelines for Multinational Enterprises
2. The 10 (Ten) Principles of the United Nations Global Compact
3. The United Nations Guiding Principles on Business and Human Rights
4. The ILO Tripartite Declarations of Principles on Multinational Enterprises and Social Policy
5. The ISO 26000 Guidance Standard on Social Responsibility

All the above guidelines have been utilized by companies in Indonesia as a guidance to implement their CSR programmes. Unfortunately, there is yet any specific government's office or ministry that is responsible to conduct surveillance and supervision tasks to measure the performance level of CSR programmes implemented by those companies in the field.

Hence there is a need to mandate a special national agency to supervise, monitor, provide guidance, and evaluate the CSR programmes implemented by those companies. A surveillance and monitoring body is needed to ensure that all companies meet the minimum level of accountability and transparency principles while implementing the CSR programmes.

The authority of the surveillance and monitoring body should cover both types of CSR methods either in voluntary or mandatory mode. Otherwise, the accountability and transparency principles may still be questioned. The CSR national body or CSR surveillance body may involve CSR technical experts with experience in conducting the supervision, monitoring, and evaluation of such programme, as required by the law.

8.2 Recommendations

The pro and contra of enacting Article 74 will persist if there is no initiative from an executive body to maintain the implementation of mandatory CSR programmes in Indonesia. In this case, the executive body is the President. Further, the implementation of such a programme should not overlap other programmes of certain ministries. For business enterprises to not feel the legal provision as a burden, the local government should not make CSR funds as a

source of local revenue (PAD) by issuing new regulations that may result in disharmony between the society and the business enterprises.

Indeed, in the initial discussion of the Bill draft, the government (the executives) is the one who did not agree with the inclusion of Article 74 into the mandatory CSR legal provision. This explains why the implementation of Article 74 is stagnant: The article is an “illegitimate child” whose “birth” was unwanted by the government.

The existence of mandatory CSR guidelines which is an original product of Indonesia is essential. It is needed as guidance for successful implementation of the programme. There is an urgent need for the government to pass these guidelines partly due to the large potential of mobilizing CSR funds, stakeholders complexity related to CSR issues, and the diverse interpretations of CSR itself.

The absence of a standard guideline may cause fraud and the misuse of the CSR funds. In some cases, the business enterprises claimed that they have disbursed the CSR funds for funding some projects, but the funded activities were not classified as CSR programmes and the beneficiaries were not well identified. Such cases may persistently occur in the absence of clear and explicit references.

The only legal solution to countering environmental threat is by implementing mandatory CSR in all developing countries. The mechanism will improve the legal responsibility of business enterprises in order for them to be more socially and environmentally responsible. The following recommendations can be made to improve the development of mandatory CSR development in Indonesia;

8.2.1. Recommendation One: Philosophical Rationale Behind The Enactment of Mandatory Corporate Social Responsibility Legal Provision

Based on some findings above, it was found that philosophical rationale behind the enactment of mandatory CSR legal provision is due to environmental disaster that have occurred in some areas in Indonesia. Further, there was a significant social pressure from the local community in which the extractive industries are doing their businesses activities to be more socially and environmentally responsible. Nevertheless, since the beginning of discussion of Limited Company Liability Bill, there was a different view between the government and member of the House of Representative on mandatory CSR legal provision. In one side, the Government represented the interest of business associations, business leaders and companies insisted on rejecting the legal provision.

In the contrary, the members of the parliament insisted on inserting the legal provision to the bill in order to be legally bounded to all the citizen including the companies. At last, the Bill was stipulated and officially passed by the parliament with Article 74 which is require all companies to implement CSR programmes. In other words, CSR becomes a legal responsibility of the companies. Finally, the implementation of legal provision has been getting slow because of minor political will from the government to comprehensively implement it.

Mandatory CSR legal provision was approved and passed by Indonesian House of Representative. The provision is based on some evidence of business enterprises' negligence in protecting and remedying the environmental

conditions around their business operations. Facts pointed that some business enterprises had caused environmental damages from their business operations.

Lastly, the philosophical rationale of enacting the legal provision is not just limited to preserve the nature and to ensure the sustainability of the natural resources but also to empower economic's situation of the local community and to strengthen social cohesion and harmony between the local community and the companies.

8.2.2. Recommendation Two: Mandatory Corporate Social Responsibility Laws, Regulations, Guidelines and Policies in Indonesia

Mandatory CSR laws, regulations, guidelines and policies in Indonesia are scattered in some different laws and regulations. Currently, there has been released a government regulation on CSR but the existing government regulation on CSR has not fulfilled yet the major problems in the implementation of the mandatory CSR legal provision. Further, extractive industries and other companies that are exploiting natural resources are utilizing one of or several international voluntary guidelines on CSR rather than national mandatory CSR guidelines.

In addition, the sub-national government is also trying to pass policies on CSR to mobilize CSR funds for various motives. If there is no clear policy from the central government to adjust the current policies on CSR, then the implementation of the mandatory CSR will be delayed.

However, it is necessary to have a codification of all separated laws, regulations, guidelines and policies into a single policy to enhance the implementation of the mandatory CSR legal provision in Indonesia. At last, the central government is encouraged to restructure and revise the government

regulation on CSR to accommodate more inputs and feedback from a wider spectrum of CSR stakeholders in Indonesia.

At last, The legal sanctions for non-compliance of CSR provisions should be strengthened and with the introduction of criminal sanctions. The existing administrative penalty is not sufficient to enforce the law and regulations of CSR. It is also required a standard on business and human rights practices that fits Indonesia's context. It can be used as a manual for conducting businesses that respect human rights standard. The legal enforcement of administrative and criminal codes is necessary because some companies are neglectful in implementing mandatory CSR legal provision.

8.2.3. Recommendation Three: Mandatory Corporate Social Responsibility Surveillance Body in Indonesia

The absence of permanent and independent surveillance body on mandatory CSR in Indonesia is decreasing the level of transparency and accountability on the implementation of mandatory CSR programmes. A special surveillance body has not yet been established until now. Therefore, the jurisdiction and liabilities of surveillance body also become unclear. For SOEs, internal government's surveillance body may conduct monitoring and evaluation regarding the implementation of CSR programmes because the SOEs have source of funding from the government budget. Afterwards, external supervisory agency is also allowed to supervise, to monitor and to evaluate CSR funds have been disbursed by the SOEs.

Further, it becomes difficult when the internal government's surveillance body or external surveillance body are going to supervise, to monitor or to evaluate the implementation of CSR programmes have been implemented by

private companies. They are not authorized by the law to conduct supervisory, monitoring and evaluation activities towards private companies. Therefore, the establishment of permanent, transparent and independent mandatory CSR surveillance body in Indonesia is essential to increase transparency and accountability performances of mandatory CSR programmes have been implemented by either SOEs or private companies in Indonesia.

In addition, an independent and powerful CSR surveillance agency is required for a better supervision, monitoring, and evaluation tasks concerning the implementation of provision 74 on CSR and other standard of CSR practices. This agency will develop policies, manual, and guidance for the strategic implementation of mandatory CSR legal provision in Indonesia.

However, It will also conduct (1) community needs and impact assessments on the provision, (2) routine monitoring and evaluation on CSR implementation, and (3) encourage international cooperation with other institutions or agencies on the strengthening of CSR policies in Indonesia. At last, the CSR surveillance agency might be created under direct supervision of the President Republic of Indonesia or at least the status is at the same level with ministry body.

8.2.4. Recommendation Four: Indonesia's Mandatory CSR Manual

The government should provide appropriate policies to enhance the implementation of mandatory CSR in Indonesia. Policies clarity is an important strategy to implement the mandatory CSR well implemented. Further, stagnation of mandatory CSR policy in Indonesia due to unclear policies from the government itself. There should be a standard guidelines on

mandatory CSR and the establishment of permanent and independent surveillance body.

The government has passed government regulation on CSR, unfortunately the policy did not meet the basic requirement to fulfill the mandatory CSR legal provision. Mean while, there are some ministries are conducting CSR activities based on their respective ministries core functions. It is not a good signal to enhance mandatory CSR legal provision. Afterwards, there are also different implementation strategy between SOEs and private companies which is SOEs implements PKBL programme, even though at the same time they also implement mandatory CSR programme in accordance with Article 74 of Act No.40/2007.

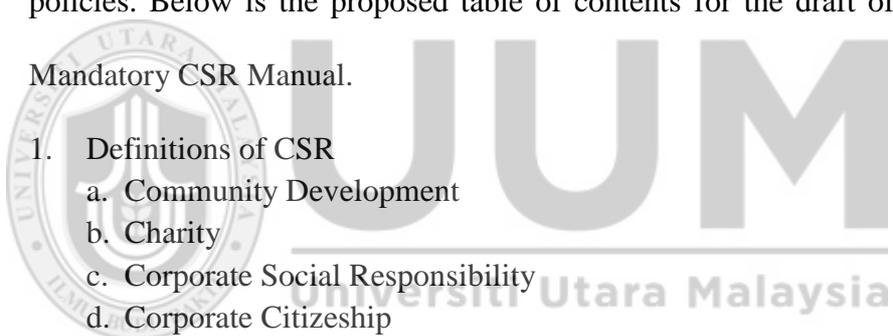
However, environmental aspect is one of the most important aspects for mandatory CSR. Even, there are two more aspects are also important in which social and economic empowerment. The three things should be done simultaneously and at once. Finally, tax incentives should be given by the government for companies are implementing good mandatory CSR programmes because “*stick*” and “*carrot*” policies are still relevant to encourage the companies obey the rules and regulations on mandatory CSR legal provision in Indonesia.

Lastly, the government of Indonesia is encouraged to draft and pass Indonesia’s Mandatory CSR Manual for the implementation and guidance of mandatory CSR legal provision. Based on the findings the draft should include the following aspects: allocation of CSR funds, beneficiaries recruitment strategies, method of project’s implementation, CSOs involvement, monitoring and evaluation procedures and reporting procedures. Further, the draft of the

manual should be discussed with CSR relevant stakeholders in advance through Focus Group Discussion (FGD), workshops, or any other means of socialization.

The codification is necessary because since the enactment of the mandatory CSR legal provision on 2007 there has been no specific manual to guide the companies in implementing the provision. In turn some companies developed their own internal policies and guidance to implement their own CSR programmes and some others have been referring to a number of international guidance CSR and human rights principles.

Additionally, there are also companies who did not have any internal CSR policies. Below is the proposed table of contents for the draft of Indonesia's Mandatory CSR Manual.

- 
1. Definitions of CSR
 - a. Community Development
 - b. Charity
 - c. Corporate Social Responsibility
 - d. Corporate Citizeship
 - e. Sustainability
 - f. Social Investment
 2. Principles of CSR Project
 - a. Transparent
 - b. Accessible
 - c. Implementable
 - d. Accountable
 - e. Relevancy
 3. Types CSR Projects
 - a. Societal Project
 - b. Environmental Project
 - c. Economic Empowerment Project
 4. Qualification of CSR Organizational Body within Company
 - a. Specific CSR terminology within the organizational chart
 - b. Number of personnel
 5. Selection of Beneficiaries
 - a. Beneficiaries Criteria
 1. Main beneficiaries

2. Non-main beneficiaries
 - b. Beneficiaries Selection and Approval Method
6. Budgeting Allocation
 - a. Amount of CSR budget allocation from private and state owned company
 - b. Criteria of budget allocation from private and state owned company
 - c. Lump sump financing mechanism
 - d. At cost financing mechanism
 - e. Cost sharing financing mechanism
7. CSR Surveillance Body
 - a. Policies and regulation function
 - b. Coordination function
 - c. Supervisory function
 - d. Investigative function
8. Independent CSR Evaluator
 - a. Basic requirement of independent CSR evaluator
 - b. Listed independent evaluator
9. Non-Governmental Organization Involvement Mechanism
 - a. Criteria of Non-Governmental Organization
 - b. Certified NGOs
10. CSR Public Private Partnership Mechanism
 - a. Company with company
 - b. Company with NGOs
 - c. Company with foundation
 - d. Company with higher education institution
11. Coordination Mechanism with Government Bodies
 - a. Coordination on Assessment Phase
 1. Coordination with relevant ministries
 - a. Monthly coordination
 - b. Quarter coordination
 - c. Semester coordination
 - d. Annual coordination
 2. Coordination with local government
 - a. Monthly coordination
 - b. Quarter coordination
 - c. Semester coordination
 - d. Annual coordination
 - b. Coordination on Implementation Phase
 1. Coordination with relevant ministries
 - a. Monthly coordination
 - b. Quarter coordination
 - c. Semester coordination
 - d. Annual coordination
 2. Coordination with local government

- a. Monthly coordination
 - b. Quarter coordination
 - c. Semester coordination
 - d. Annual coordination
- c. Coordination on Evaluation Phase
 - 1. Coordination with ministries
 - a. Monthly coordination
 - b. Quarter coordination
 - c. Semester coordination
 - d. Annual coordination
 - 2. Coordination with local government
 - a. Monthly coordination
 - b. Quarter coordination
 - c. Semester coordination
 - d. Annual coordination
- 12. Types of CSR Implementation Strategy
 - a. Self implementation by the company
 - b. Joint implementation with relevant NGOs
 - c. Joint Implementation with relevant foundation
 - d. Joint implementation with higher education institution
- 13. Indonesia CSR Index
 - a. Quarter CSR Index
 - b. Semester CSR Index
 - c. Annual CSR Index
- 14. CSR Auditor and Assesor
 - a. Basic requirement of CSR Auditor and Assesor
 - b. Training
 - c. Certification of CSR Auditor and Assesor
- 15. Monitoring Mechanism
 - a. Quarter Monitoring
 - b. Semester Monitoring
 - c. Annual Monitoring
- 16. Reporting Mechanism
 - a. Monthly Reporting
 - 1. Narrative Reporting
 - 2. Financial Reporting
 - b. Quarter Reporting
 - 1. Narrative Reporting
 - 2. Financial Reporting
 - c. Semester Reporting
 - 1. Narrative Reporting
 - 2. Financial Reporting
 - d. Annual Reporting
 - 1. Narrative Reporting

- 2. Financial Reporting
- 17. Evaluation Mechanism
 - a. Semester Evaluation
 - b. Annual Evaluation
- 18. Sustainability of CSR Project
 - a. Short term financing, i.e CSR budget of a company
 - b. Middle term financing, i.e specific financial support from the government.
 - c. Long term financing, i.e soft loan from banking institution or other financial institution.
- 19. CSR Complaint Handling Mechanism
 - a. Internal complaint handling mechanism
 - b. External complaint handling mechanism
- 20. Awards and Recognition
 - a. Basic requirement of Awards and Recognition
 - b. Awards and Recognition Submission Procedures
 - c. Benefits of Awards and Recognition
 - 1. Tax reduction
 - 2. Import cost exemption
- 21. Legal Sanctions
 - a. Administrative Sanctions
 - b. Private Sanctions
 - c. Criminal Sanctions

8.3 Proposed Further Research

The current research reports the evolvement of CSR policy and yet the stagnation of the mandatory CSR legal provision within the Indonesian legal system. The study recommends that a mandatory CSR manual be drafted as a guideline for implementing the policy in Indonesia. Future researchers in this area are encouraged to further explore guidelines of mandatory CSR coordination, CSR monitoring, and CSR reporting. Other researchers are also suggested to conduct further studies on other related subjects in the area of mandatory CSR policies.

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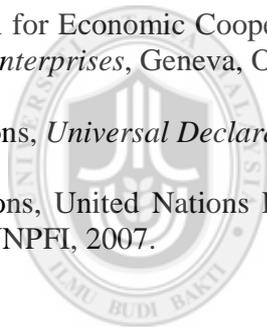
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