NEW INDONESIAN REGULATION ON SUSTAINABLE FINANCE AN IMPORTANT STEP IN ADDRESSING THE ROLE OF BANKS AND INVESTORS IN FOREST DESTRUCTION AND HUMAN RIGHTS ABUSES

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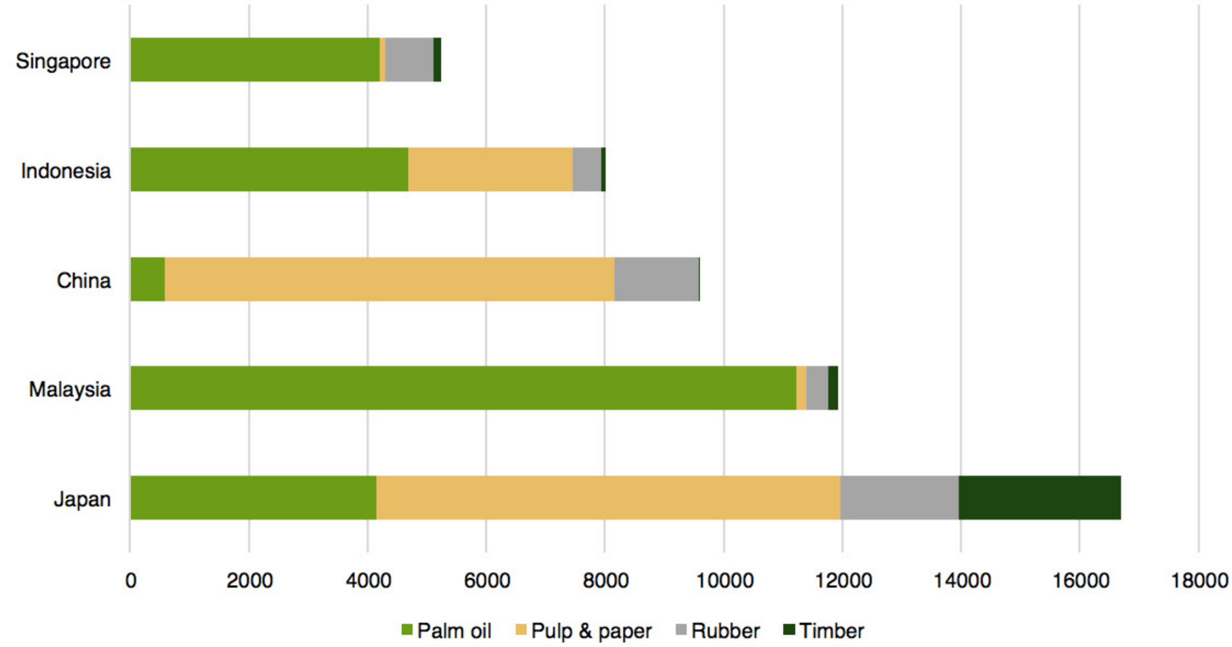
In July 2017, the Indonesian financial services authority (OJK) published a new Regulation on Sustainable Finance (POJK)[1] as a continuation of their Roadmap for Sustainable Finance, which was launched in December 2014. Indonesia is one of just a handful of countries to have a regulation on sustainable finance. The POJK is a welcome and important step in addressing the role of banks and investors in financing forest destruction and human rights abuses in Indonesia.

Research by RAN, TuK and Profundo, available on forestsandfinance.org, found that between 2010-2016 financial institutions provided more than 71 billion USD in loans and underwriting services to 183 companies engaged in tropical forest-risk commodities (palm oil, pulp & paper, rubber & timber) in Southeast Asia – with many of these companies operating in Indonesia. Financiers from Japan, Malaysia, China, Indonesia and Singapore provided approximately 75% of loans and underwriting services to these companies, with Indonesian financial institutions contributing over 11% (8 billion USD).

Figure 1 Loans & underwriting services to tropical deforestation risk companies (2010-2016, million USD)



Source: Forests & Finance (2017, June), “Explore the data”, online: forestsandfinance.org, viewed in August 2017.

Many of the financiers from these countries, and in particular those from Indonesia, Malaysia and Singapore, do not have publicly available policies or due diligence systems to mitigate the negative impacts of companies operating in the tropical forest commodity sector.[2] Given the major role of Indonesian financiers, their lack of forest sector policies and the fact that Indonesian communities and forests are most impacted by this finance,[3] this new regulation is welcome.

Key opportunities of the POJK include:

- The POJK makes it clear that promoting balance between social, economic and environmental factors is essential to achieving sustainable, stable and inclusive development.
- The POJK recognizes Law 32 2009 on Environmental Protection and Management, mandating the development of an environmentally sound financial system.
- The POJK applies to all financial services institutions, to issuer companies and public companies.
- The POJK requires financial institutions to develop a Sustainable Finance Action Plan (RAKB) and a Sustainability Report. The POJK sets out minimum criteria for both outputs, as well as a timeline for the development of them. The RAKB should cover the following aspects: the development of sustainable finance products and services; internal capacity development; organizational adjustments; risk management; governance and standard operating procedures that are consistent with the principles of sustainable finance (more details can be found in attachment 1 of the POJK). The RAKB must be communicated to shareholders and staff at all levels of the organization. The Sustainability Report must be submitted to the OJK on time and it must be made public.
- Financial Institutions with Corporate Social Responsibility Programs are required to allocate a proportion of funds from this program to support sustainable finance activities. The allocation itself must be set out in the RAKB, and implementation must be reported on in the sustainability report.
- The POJK establishes incentives for financial institutions applying sustainable finance effectively.

While the POJK is a welcome move by the OJK, the following improvements are needed to ensure the regulation is successful:

- Financial institutions should be required to develop their own policies on sustainable finance, to ensure institutional support for the regulation.
- Sanctions for non-compliance are all administrative in nature, either in the form of reprimands or written warnings. To ensure the regulation is effectively implemented by financial institutions, stronger sanctions for non-compliance are needed.

A multi-stakeholder consultation process is required is to ensure this new regulation is improved and successfully implemented and to prevent the devastating impacts associated with tropical forest-sector finance.

[1]The original regulation in Bahasa Indonesia is available in here. The elucidation of the regulation is available in English here, Attachment I here, and Attachement II here (unofficial translations)
[2]See Forests & Finance Policy Matrix, 2016
[3]See Every Investor Has A Responsibility, 2017

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