ARMA Update: 13 December 2021
(English Version)

ESG and Climate Change Update: Sustainable Investment Guideline

In light with the developing efforts towards reaching net zero emission, the Ministry of Investment/Indonesia Investment Coordinating Board (*Kementerian Investasi/Badan Koordinasi Penanaman Modal* or "**BKPM**") launched the Sustainable Investment Guideline during the G20 event in Bali which was held last month. This guideline is intended to be a reference for business actors, investors, and policymakers regarding sustainable investment which has been growing significantly over the last decade.

This ARMA Update will cover the concept of sustainable investment as well as the indicators of sustainable investment that may be developed by business actors and prioritized by investors, as described in BKPM's Sustainable Investment Guideline.

Sustainable Investment & Business

The Sustainable Investment Guideline provides multiple definitions to provide a better understanding as to what the definition of sustainable investment is. Under sustainable investment, investors do not only consider financial returns of their investments but also the economic, social, and environmental impacts. The Global Investors for Sustainable Development or GSID Alliance defines it as the mobilization of capital to generate positive contribution to sustainable development, whether it be in the form of products, services, or activities based on the sustainable development goals parameters through impact investing or investing strategies towards environmental, social, and governance ("**ESG**") aspects.

Business actors shall have a business strategy that provides the business' information and its impact towards ESG aspects. This business strategy may be used by investors as a reference to determine how business actors can achieve their goals whilst assessing its feasibility and capability of dealing with business challengers and risks, especially in the ESG aspects.

Aspects and Indicators for Sustainable Investment

The Sustainable Investment Guideline provides the how-to for companies or business actors to determine their sustainability status. The guideline serves to be a reference for business actors who want to disclose data or information regarding what are the economic and ESG impacts that have been achieved as well as what transformation that will be made in the future.

Sustainable Investment			
Economic	**Environmental**	**Social**	**Governance**
•Financial Accountability •Local Supplier Partnership •ESG Financing •Product Innovation	•Emission Measurement •Emission Reduction •Energy Efficiency •Water Efficiency •Raw Materials •Waste Management •High Conservation Value and High Carbon Stock •Restoration and Rehabilitation	•Gender, Diversity, and Inclusion •Decent Work •Consumer Protection •Community Empowerment and Human Rights Protection	•Sustainable Governance •Anti-Corruption and Grievance Mechanism

First, business actors should determine the economic and ESG impacts of their business operations as well as which aspect that should be improved in the future. Then, the business actors are to determine the prioritized business impacts and the corrective measures that shall be taken. To do this, the Sustainable Investment Guideline lays out the following aspects which can be accounted for business actors to disclose data and information for their reports or portfolio for sustainable investment.

A. Economic Aspect

Business actors should consider financial performance to ensure long-term viability as well as provide the relevant financial statements to report their economic performance, which includes the following indicators:

1. **<u>Financial Accountability</u>**: Business actors must provide adequate financial reporting that consist of financial statements, balance sheets, and income statements for the report of the company's economic performance.

2. **<u>Local Supplier Partnership</u>**: Business actors, especially local micro, small, medium enterprises ("**MSMEs**"), shall collaborate with local suppliers to encourage economic empowerment.

3. **<u>Corporate Financing to Support ESG Performance</u>**: Business actors shall specifically contribute to activities that benefit ESG aspects.

4. **<u>Product Innovations to Support ESG</u>**: Business actors may carry out product research and development gradually to support other ESG aspects.

B. Environmental Aspect

The environmental aspects include indicators to minimize the negative environmental impacts that may arise as a result of a business actor's activities. The indicators included as the company's environmental actions are as follows:

1. **Emission Measurement**: Business actors are encouraged to reduce their carbon footprint, especially by reducing the usage of non-renewable energy through emission reduction, whether it be direct emission such as from power plant generation and product-based emission, or indirect emission such as from the company's upstream and downstream supply chains.

2. **Emission Reduction**: Business actors may set targets to reduce emissions from company activities through emission reduction activities and identifying the potential risks if such targets are not met.

3. **Energy Efficiency**: Business actors may report on their energy efficiency actions such as reducing or transitioning away from non-renewable energy to renewable resources and identifying the mitigated risks.

4. **Water Use Efficiency**: Business actors may implement efficiency on water usage, keeping in mind that clean water remains a challenge for many community groups.

5. **Eco-Friendly Raw Materials**: Business actors may consider using recycled or reused materials to support sustainability goals in the process of their business activities.

6. **Waste Management**: Business actors may implement waste management strategies such as recycling or reusing materials for their production cycle.

7. **High Conservation Value and High Carbon Stock**: Business actors may strive to maintain and conserve biodiversity, to protect the environment that is affected by the company's activities.

8. **Restoration and Rehabilitation**: Business actors may seek to carry out restoration and rehabilitation activities on land affected by the company's activities and help improve its environmental functions.

C. Social Aspect

The social aspects include indicators to guarantee the minimization of negative societal impacts including to its employees and customer protection, which are as follows:

1. **Gender Equality, Diversity, and Inclusion**: Business actors are encouraged to ensure women's representation at all levels of management to assure women's

participation in business operations and decision-making. Further, business actors may empower vulnerable groups who are socially, economically, and culturally marginalized by providing them access to decent work and create tolerance, recognition, and fair treatment. Business actors are also encouraged to diversify age group representations.

2. **Decent Work**: Business actors are to provide remuneration in accordance with the prevailing regulations to ensure employee welfare and provide training and education programs to empower and improve employees' skills.

3. **Consumer Protection**: Business actors must protect consumers from risks of data leakage that may harm them. Further, business actors must ensure adequate product information that are in line with the regulations and comply to the required certification in accordance with product needs.

4. **Community Empowerment and Human Rights Protection**: Business actors may have empowerment programs with local communities, including local entrepreneurs and MSMEs. Further, business actors must ensure that children are free from exploitation and free from hazardous work, as well as ensuring decision making involves indigenous groups that are affected by the business activities.

D. Good Governance

Business actors shall ensure that sustainable principles are in place and monitored by the company's management in its implementation, which includes the following indicators:

1. **Sustainable Governance**: Business actors may provide an adequate organizational structure along with the roles and responsibilities given to ensure proper implementation of ESG and economic aspects.

2. **Anti-Corruption and Grievance Mechanism**: Business actors must assure that anti-corruption procedures are in place and understood by company personnel as well as provide mechanism for grievance and complaint supervision for internal use of the company.

ARMA Law Commentary

The Sustainable Investment Guideline is not only the embodiment of the government's focus on sustainable investment as outlined in Law No. 25 of 2007 concerning Investment and Presidential Regulation No. 16 of 2012 concerning the General Plan of Investment, but also provides support towards Indonesia's aim to achieve its Nationally Determined Contribution under the Paris Agreement. The environmental aspects outlined in the Sustainable Investment Guideline, such as emission measurement and reduction, high conservation value and carbon stock, as well as restoration and rehabilitation, conforms with the spirit of reducing emissions and seeking nature-based solutions as newly regulated in the Presidential Regulation No. 98 of 2021 concerning the Implementation of Carbon Economic Value for Achieving Nationally Determined Contribution Targets and Control of Greenhouse Gas Emissions in National Development and the Ministry of Environment and Forestry Regulation No. 21 of 2022 concerning the Guidelines of Carbon Economic Value Implementation.

The document provides a reference of indicators which may be used by business actors, investors, as well as the government. However, it's usage is not mandatory for a company's ESG disclosure, but rather serves as a voluntary instrument to identify and improve a company's ESG aspects. Thus, to maximize the purpose of the Sustainable Investment Guideline, business actors' willingness and awareness towards a more sustainable business is key. Without the propose legal basis to implement the Sustainable Investment Guideline, the ESG information disclosure system for the development of sustainable investment still has room for improvement and optimalization.

***

Please get in touch with Rudi Bachtiar (rudi.bachtiar@arma-law.com) and Salsabila Hana Safira (salsabila.safira@arma-law.com) for further information.