

REGULATING CORPORATE SOCIAL RESPONSIBILITY FOR STATE OWNED LIMITED LIABILITY IN INDONESIA

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ABSTRACT

Corporate Social Responsibility (CSR) is an action that tries to redistribute benefits from business to the affected community and environment. However, it consists of proliferation of complex and unclear approaches. Therefore, this concept is subject to many interpretations. One may see this as a marketing tool while others may see it as a moral duty to the future generations. Whilst its implementation depends on each company's vision, government can take part in this movement by creating regulation and providing the necessary support system. State-Owned Limited Liability is one type of state-owned enterprises that is obliged to implement CSR. However, it is faced with two regulations that are perceived to have contradicting orientations, those are maximizing profit and achieving sustainable development. Whereas, Fuller mentions that contradicting rules will not achieve their goal. In the end, using statutory and conceptual approaches, this normative research concludes that both CSR regulations can coexist. Although companies are exposed to more costs, but the benefits will profit community and environment.

Keywords: corporate social responsibility, sustainable development, social justice, limited liability, Indonesia

INTRODUCTION

Corporate Social Responsibility (CSR) can be defined as “a company’s commitment to minimizing or eliminating any harmful effects and maximizing its long-run beneficial impact on society” (Mohr *et al.*, 2001: 47). It is inferred that business’ fundamental responsibility is not only to make profit and expand the business but also obey the law, operate within the legal framework, respect the rights of others, and meet the expectation of what is right, just, and fair. They also need to contribute and support the broader community by improving their quality of life (Carroll, 1995; Snider and Martin, 2003). According to Garriga and Melé (2004: 53-65), there are four theories that classify the implementation of CSR program. They are the instrumental, political, integrative, and ethical theories that include business’s obligation to “pursue profits, accept social obligations, grow its business, and embed ethical values” respectively (Brown and Forster, 2012: 302).

Traditionally, CSR is seen as an investment for economic objectives. Rather than being viewed as a mere cost, CSR is implemented to maximize its shareholders’ value by promotion and enhancing companies’ reputation, therefore it looks trustworthy and people will consume their products and/or services in the future. CSR can also be considered as a cause-related marketing that is a “process of formulating and implementing marketing activities that are characterized by an offer from the firm to contribute a specified amount to a designated cause when customers engage in revenue-providing exchanges that satisfy organizational and individual objectives.” Its ultimate goal is to enhance company’s revenues and sales by building a brand and customer relationship through the association with the social responsibility or ethical dimension (Garriga and Melé, 2004: 53). Since it is considered to serve same goal of promotion, thus Kotler and Lee (2005) suggest that CSR can be used to reduce companies’ operational costs by switching promotion costs to CSR costs. According to Husted and Allen (2000), CSR is an approach of allocating resources to achieve long-term social objectives and create a competitive advantage. By investing in philanthropic activities correlated to their areas, companies can create greater social values than individual donors or government. It is because the firm has the knowledge and resources to better understanding on how to solve some problems related to their area, and thus it “can have a powerful effect on the cluster competitiveness and the performance of all its constituents companies” (Porter and Kramer, 2002: 60-61). As more global citizens put emphasize on the ethical relationship between business and society, more firms tend to use CSR to express the right thing and to achieve a good society. To balance all of its stakeholders’ interest, firms can adopt the normative stakeholder theory. This approach focuses on how to integrate social demands, where managers bear a fiduciary relationship to its stakeholders (suppliers, customers, employees, local communities), not only confined exclusively to its stockholders (Freeman, 1984: xx). Stakeholders must be viewed as persons or groups of persons with legitimate interests in procedural and substantive aspects of the corporate activity and their interests are of intrinsic value (that is, each group has their own interests) (Donaldson and Preston, 1995: 67). Under this theory, a socially responsible firm is expected to simultaneously giving attention to the legitimate interests of all appropriate stakeholders.

A more societal value-based concept that is more popular is “sustainable development.” This approach seeks to “meet the needs for the present without compromising the ability to meet the future generation to meet their own needs” (World Commission on Environment and Development, 1987: 8). It will require an integration of social, environmental, and economic considerations to make long-term balanced judgments (World Business Council for Sustainable Development, 2000: 2) and it will be a process of achieving human development in an inclusive, connected, prudent, and secure manner (Gladwin, *et al.*, 1995: 876). This

approach keeps reminding firms to create a consistent sustainable living for society, environment, and economic dimensions through value creation (Wheeler, *et al.*, 2003: 17). At this stage, firms are expected to shift company's ultimate goal from just pursuing profit, to prospering society and preserving environment (Shrivastava, 2005; Stead and Stead, 2000) with its custom-made process as long as it can meet organization's aims, strategy, and appropriate response to the circumstances in which the organization operates (Van Marrewijk and Werre, 2003).

Most CSRs will fail when companies do not fully integrate CSR into their business models; because it remains a mere strategic to enhance companies' image rather than serving as a core component of the companies' business operations. This phenomenon is particularly apparent in developing countries, such as Indonesia, whose government oversight on companies is weak or nonexistent (Slack, 2012: 179-180). Companies are often required to obtain a 'social license to operate' from the local communities. If the projects are not accepted, it will not be sustainable and no amount of future CSR programs is going to overcome the lack of acceptance and trust (Slack, 2012: 182). Hill (2001: 32) mentions that if corporation do not respond to this pressures, "society could place increasing costs on unsustainable business practices, and customers may not choose to purchase associated products and services. Ultimately, this process may alienate the company from the rest of society, resulting in reduced reputation, increased costs, and decreasing shareholder value through erosion of its license to operate." Such acceptance is important because communities will have to bear any risks that may arise from the companies' operation, such as odor pollution, cardiac symptoms, lung cancer, leukemia, as well as pollution of the aquatic environment (Luginaah, *et al.*, 2000: 1165; Luginaah, *et al.*, 2002: 55; Wake, 2005: 131; Yang, *et al.*, 2000: 39; Barregard, *et al.*, 2009: 989).

Whilst CSR is commonly perceived as a commitment to respecting environmental and providing benefits to local communities sustainably, Indonesia has not decided the standard of what is expected from CSR. It also faces three major challenges in implementing its CSR regulation: (1) lack of competent managers to run the program, (2) a high percentage of low-income families, and (3) a weak legal system (Hill, 1996). The implementation of CSR requires long-term vision and commitment from business managers while Indonesia has few trained managers in the area. The situation does not improve because there is no adequate formal education on the subject and most big businesses only promote people with political or family connections (Faulkner, 1995). Second challenge is a high percentage of low-income families. When most people are still struggling to afford basic necessities, they are likely to spend their money to buy the most affordable products rather than support socially responsible companies, despite their high involvement in CSR activities (Arli and Lasmono, 2010: 49). This is an opposite finding of consumer perception research in developed countries, where most consumers are willing to buy products whose companies have more CSR involvement (Creyer, 1997). The third and the most deterrent of CSR implementation is Indonesia's weak legal system, both structurally and legislatively. The government is perceived negatively because of bribery and endemic culture of corruption that is causing a widespread cynicism for officials' dishonesty (Kemp, 2001; Alatas, 1999). Even Henderson and Kuncoro (2004: 1) once said, "Bribes by firms in Indonesia arise principally from regulations – licenses and levies – imposed by local government officials." To further protect the business, many large enterprises are willing to have politicians on their board of directors, or create a 'conglomerates,' that is a well-connected groups of business linked to political elites and large state-owned enterprises (SOEs), which are bureaucratically protected by the government power and patronage (Kemp, 2001: 2). With such arrangement, consumers are less likely to believe that companies will put legal, ethical, and philanthropic aspects before their economics obligations.

Prior to the 2007 Law Number 40 on Limited Liability, Indonesia's norms regarding CSR provides boundaries regarding what companies should or should not do but not accompanied by strong law enforcement mechanism to hold corporation responsible. There is excessive overlap among different laws that causes in legal uncertainties regarding substance, additional administrative costs, and bureaucracy. The absence of operational standards encourages the adoption of international standards adapted to national context (Koestoer, 2007). It also relies on company's voluntary engagement and only adopted by multinational or large corporations. The notion of CSR is more developed in natural resources business sector and manufacturing industry as opposed to the service industry. They can be carried out by individual corporations or in cooperation with Non-Governmental Organizations (NGOs) or public institutions; with primary concern in charity, education, research, health, and natural disaster assistance, and less cause towards environment, security, human rights, and other social issues. The poor reception of CSR in Indonesia is further caused by a perception that CSR is a western philanthropic, cause-related marketing, or public relations concept that represents a net cost for the corporation (Wiwoho, 2009: 4-5, 7-9).

Upon enactment of the 2007 Law Number 40 on Corporate Law, there has been a lengthy discussion related to Article 74. The debate was centered on who should bear this obligation, whether it is only borne by certain types or all types including various smaller enterprises that were not subject to corporate law, such as a family-owned corporation with no legal status and separated liability, or service-oriented corporations such as banking or insurance. After six Parliamentary hearings with 23 institutions representing society, it was decided that the application of CSR be limited to companies who have impact on natural resources. This Article 74 plays a significant role in institutionalizing CSR in Indonesia. The mandatory nature enforces companies to carry out the CSR, and it enhances the reception and implementation in Indonesia. It also requires businesses to integrate CSR into its internal policy and the mandatory nature serves as a preventive mechanism to keep companies from only 'circling' the money (Waagstein, 2010: 461).

Scholars have long argued that companies have ethical and moral obligations to society that, while not required, are expected (Carroll, 2004). In Indonesia, State-owned enterprise or SOE is one type of companies that is a subject to this expectation. SOEs can be in the form of *Perum (Perusahaan Umum)* or *Persero (Perusahaan Perseroan)*. The former is a public service company wholly owned by government, whose main purpose is to provide goods and/or services to the public as well as pursuing profits. The latter is a type of SOE whose main goal is to gain profit and contribute to government revenue, and it can be a public company or 100% government-owned. Since it is also classified as a limited liability/company, therefore it is a subject under two

different regulations, i.e. the 2007 Law Number 40 on Limited Liability and the 2003 Law Number 19 on State-Owned Enterprise. With each regulation governs their own CSR principles, this overlap inevitably affects the CSR program in a State-Owned Limited Liability. Moreover, these two regulations do not outline on how CSR should be done; therefore it can create confusion during the implementation. Accordingly, this normative research paper will use statutory and conceptual approaches to provide insights into (1) whether the regulation of CSR for state-owned limited liability can effectively coexist by examining the orientation, subject, source of fund, allocation, and the CSR programs.

REGULATION OF CORPORATE SOCIAL RESPONSIBILITY FOR STATE-OWNED LIMITED LIABILITY IN INDONESIA

Since a state-owned limited liability falls into two category, therefore it is a subject under two different regulations, namely the 2007 Law Number 40 on Limited Liability and the 2003 Law Number 19 on State-Owned Enterprise. Both cover the foundation, responsibility of board of directors, business outline, as well as the corporate social responsibility guidance. To determine whether both regulations can coexist, this paper will consider several components including the orientation, subject, source of fund, allocation, and the CSR programs.

Article 74 on the former states that:

1. Companies doing business in the field of and/or in relation to natural resources must put into practice Environmental and Social Responsibility.
2. The Environmental and Social Responsibility contemplated in paragraph (1) 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 as contemplated in paragraph (1) 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.

Examined together with the 2012 Government Regulation Number 12 on Environmental and Social Responsibility on Limited Liability, the subject of this CSR obligation is limited liability working in natural resources field. The program is carried out by the Board of Directors and funded from the company's cost that has been approved by the General Meeting or Board of Commissioners. The allocated amount is only based on decency and fairness, which is vague and subject to interpretation. Related regulations also do not specify what kind of programs should be conducted, therefore the implementation will be vary across companies. Because the background of a limited liability establishment is for business purposes and to make maximum profits, it is only natural that management will budget CSR funds as minimal as possible to reduce costs. Since there is prescribed programs need to be carried out, company can choose activities that are considered cheap and do not hinder profit maximization. Based on this analysis, it can be inferred that the CSR arrangement in Limited Liability Law is consistent with instrumental theory or profit oriented orientation, in which CSR is implemented solely to fulfil regulatory obligations, rather than internal awareness or desires.

The corporate social responsibility concept for State-Owned Enterprises is governed by the State-Owned Enterprises Ministry Regulation's PER-02/MBU/07/2017 on Partnership Program and Community Development Program on State-Owned Enterprises. Briefly, this rule points out how CSR can be done through a partnership program and community development program. The former includes programs aiming to improve Small and Medium Enterprises (SMEs) quality called 'Fostered Partners' through a maximum loan of Rp 200 million per partner. This loan can be used for additional working capital, buying new assets and inventories, as well as enhancing short-term cash flows. Administration cost is charged at 3% per annum and interest calculation method is either another 3% per annum or profit sharing from 10:90 up to 50:50 for SOEs and SMEs. The SMEs must satisfy certain requirements to obtain such funding, namely maximum net wealth of Rp 500 million, excluding land and work place building, or maximum yearly sales of Rp 2,500 million. They must be Indonesian citizens owned and not a subsidiary company or affiliated to a medium or big companies. It can be proprietary or non-legal enterprise that has operated for more than 6 (six) months and with potential future. This program is targeting those who are considered "not bankable" yet. Should the SOEs opt not to run the partnership program themselves, they can give grants to another SOEs in financial sector. The latter is a program to empower community through aids for natural disaster, education, health improvement, infrastructure, religious facilities, and for nature preservation. To fund these programs, companies can use a maximum of 2% of net profit after tax for each program respectively, or considered this as an operational cost. Specifically for partnership program, companies can also use the pervious year's allocated fund, administration costs, interests from savings and deposits, and grants from other SOEs if any. While community development program can also use its own allocated fund and savings interest. Both programs can be carried out by the individual enterprises, in partnership with other enterprises, subsidiary or affiliated company, and even an appointed third party. Partnership and community development program is an innovation to reduce society's dependency on SOEs aid in the future (Dasgupta and Beard, 2007: 229-230) with the SOEs as the facilitators, and the programs are designed by themselves to conform with their specific circumstances. By having an independent economy, community should have been able to meet their own needs and yet still giving opportunity for the next generations to meet their own need later in the future. Therefore, it is interpreted that Indonesia's State-Owned Enterprises Ministry Regulation PER-02/MBU/07/2017 on Partnership Program and Community Development Program State-Owned Enterprises is consistent with the sustainable development theory.

According to Fuller, contradicting rules shall not achieve its goal. The settings of both regulations show that State-Owned Limited Liability should allocate CSR as a cost yet put aside some portion of its profit for another program with similar goal. This arrangement definitely hurts the profit and hinders the profit maximization goal. Theoretically, these regulations contradict each other and therefore shall not achieve its consecutive goals. However, it is must be noted that State-Owned Limited Liability is a government owned, and serving the need of community and environment is also government's goal. Therefore, on this basis,

these regulations should not be seen as contradicting but rather helping government to realizing the distribution of benefits to people.

CONCLUSION

Currently, the State-Owned Limited Liability is a subject of two regulations that treat CSR differently. Implicitly, both try to aim for the same goal of distribution of benefits to improve community and environmental living condition. Despite their different settings and orientation, these regulations can coexist and actually complement each other. Partnership Program and Community Development Program should be seen as a part of CSR program rather than another burden for the company. Yet, company should make a further cost and benefit analysis to make sure that profit is attained satisfactorily whilst doing good things for society and environment.

The issue in the 2007 Law is the term “companies doing business in relation of natural resources” that covers companies who do not manage or exploit natural resources but its business activities may impact on the functional capacity of natural resources. The wording “natural resources” is ambiguous as it can refer to “natural environment” such as forests and aquatic area, or to the general quality of human life. Government should provide a clearer guidance on which companies are expected to run the CSR program, as well as improving inspection and enforcement of related CSR regulations. They could encourage companies to partner with NGOs for capacity building and directions as well as providing more information on disclosing CSR performances. Most importantly, government should give examples on how CSR should be done, starting from the government departments and state-owned enterprises. Further research could analyze on how is CSR practice in Indonesia and build an ideal CSR model that can be used by firms in Indonesia.

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