Stakeholder Engagement to Ensure Sustainability in Infrastructure Development in Oil and Gas Industries

First Author Name: Alizar Anwar
First Author Company: IAP2 Indonesia Affiliate
First Author Address: Jl. Mampang Prapatan VIII Kompleks Bappenas No. 53
First Author City, State, Country: Jakarta 12790, DKI, Indonesia
Fax: +62 21 7989548
E-mail: alizar.anwar@iap2indonesia.or.id

Second Author Name: Muhammad Subhan
Second Author Company: IAP2 Indonesia Affiliate
Second Author Address: Jl. Mampang Prapatan VIII Kompleks Bappenas No. 53
Second Author City, State, Country: Jakarta 12790, DKI, Indonesia
Fax: +62 21 7989548
E-mail: muhammad subhan@yahoo.com

Third Author Name: Aldi Muhammad Alizar
Third Author Company: IAP2 Indonesia Affiliate
Third Author Address: Jl. Mampang Prapatan VIII Kompleks Bappenas No. 53
Third Author City, State, Country: Jakarta 12790, DKI, Indonesia
Fax: +62 21 7989548
E-mail: aldi.alizar@gmail.com

ABSTRACT

The economic development in Asia, including the Middle East, in recent years has taken place quite rapidly. Goldman Sachs gives a new nickname - growth markets - for the four countries with the highest economic growth rates in the world, Mexico, Indonesia, South Korea and Turkey. Higher economic growth is stimulating more foreign direct investment into these countries. It is important that this fast economic growth must be in balance with social development and environmental sustainability. The Brundtland Report emphasized that sustainability is a three-legged stool of people, planet, and profit. The balance of these three aspects ensures business growth and sustainable development.

Generally speaking, current conditions are not balanced caused by low capacity of local governments and local communities in adapting to the rhythm and pace of economic growth. The result is the emergence of the various conflicts that pose the risk of a negative reputation for companies and their negative impacts on social life. This imbalance can actually be addressed together and sustained by building a better understanding of the companies, especially at the strategic level. There are six steps to be taken as follows:

1. To analyze main source of the conflict and its subsequent impacts;
2. To identify the financial, social, and environmental risks of the oil and gas company operations.
3. To analyze the gaps that occur between the capacity of local governments and communities with that of the company;
4. To understand the gap between the capacity of the third-party sustainability standards that exist

in the international environment, such as the IFC Performance Standards, UN Global Compact, the Equator Principles, ILO Conventions, ICMM (International Council for Metal and Mining), IPIECA (International Petroleum Industry Environmental Conservation Association) and so on;

5. To better understand the relevant stakeholders who direct and indirect impacts on the issues.
6. To promote the stakeholder engagement and public relation strategy to ensure the sustainability of company operations.

These steps are very influential in planning the company's CSR programs that are environmentally friendly and socially responsible, a situation that can create profit to the company and provide benefit to the society. The paper will discuss stakeholder engagement to ensure sustainability in infrastructure development in Oil and Gas Industries.

Table of Contents

1. Introduction

1.1. Growth Market

The economic development in Asia, including the Middle East, in recent years has taken place quite rapidly. Goldman Sachs gives a new nickname - growth markets - for the four countries with the highest economic growth rates in the world, Mexico, Indonesia, South Korea and Turkey.

1.2. Asian miracle

The last three countries mentioned above are in Asia that in the last two decades has enjoyed high growth rate due to rapid industrialization. The Asian miracle refers to the relatively rapid industrialization and development of previously backward Asian nations into developed and sophisticated societies. Signs of the growth included domination of key industries by companies based in Asia, as well as high employment rates alongside explosive economic growth rates.

1.3. Growth rate

Goldman-Sachs furthermore described that a significant transformation of the global economy is well under way. Growth market economies will be the driver of the world economy in the coming decade.

Higher economic growth is stimulating more foreign direct investment into these countries. It is important that this fast economic growth must be in balance with social development and environmental sustainability.

1.4. Issues

The Brundtland Report emphasized that sustainability is a three-legged stool of people, planet, and profit. People means social welfare, improved quality of live; planet means environment protection to ensure sustainability, and profit means doing business that creates profit for the shareholders. The balance of these three aspects ensures business growth and sustainable development.

Globalization and the lack of development in the public sector in serving society has stimulated the increasing role of the private sector in development, particularly in the area where the company operates, ranging from poverty alleviation to nature conservation. It is the company's strategy to address stakeholders' welfare by being socially responsible; this is primarily due to pressure from employees and the public. The company is considered socially responsible if it can create profits for shareholders, and create positive influence on stakeholders, including customers, suppliers, employees, and society. The activities engaged by the company in dealing with various social issues in the project area where it operates, both individually and collectively, are known as Corporate Social Responsibility (CSR).

Corporate Social Responsibility is program that provides a lot of contributions in solving social problems in various sectors, such as job opportunities, health, education, economy, and the environment. CSR can improve the spirit of togetherness among different communities. However, the implementation of the CSR program still face some obstacles, among others, socialization of the program has not been well programmed. Another barrier is uncertainty about laws and regulations that governs CSR.

2. Current Conditions

2.1. CSR in developing countries

The basic understanding of CSR will be the same both in the developed and in developing countries. The basic concept is, in addition to seeking profit, the company must care about people and environment. For developing countries, what are desirable are areas that need interventions. The main challenge is in the areas that can support communities to improve their livelihood. Therefore, the way the companies provide CSR programs are driven by the needs of the community. The best way to accommodate this is to collaborate with the government and with civil society Organizations or NGOs. This is the so-called public-private partnership, and become a model that is appropriate for developing countries.

In developing countries and that includes Indonesia, current condition is not balanced because of low capacity of local governments and local communities in adapting to the rhythm and pace of economic growth. The result is the emergence of the various conflicts that pose the risk of a negative reputation for companies due to negative impacts that occurs in society. This imbalance can actually be addressed by building a better understanding among stakeholders, initiating from companies internally, especially at the strategic level. If not, this will result in weak implementation of CSR program.

2.2. CSR in Indonesia

With a population of 260 million and over 13% still live below poverty line and nearly halve of the population earn less than $2 per day, CSR and the concept of public-private partnership is very constructive to Indonesia. In any province where a company operates, they need to collaborate with the local government to ensure that the company's CSR programs suit the needs of the community. In addition, the company should work with NGOs that have good relationship with grass root to facilitate communication with the public, and also to understand what are the issues that evolve in the community that need help.

Many examples of the implementation of CSR in Indonesia are engaged in education and health to support government programs in those sectors including construction of their infrastructures. There are also programs that aim to improve economic welfare of the community. In addition, CSR also support initiatives in environmental conservation to safeguard sustainable development. CSR significantly support the government because, due to lack of available fund, the government cannot satisfy the needs of the community. However, in some cases, the local government makes appeal to the company in the form of pressure. This situation is obviously detrimental to the investment climate in Indonesia.

2.2.1 Legal Aspect

Law 40/2007 concerning Limited Liability Companies regulates the establishment of corporations as legal entities, their responsibilities, and their dissolution. One of the features of this law is the inclusion of CSR in Article 74, which states 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. 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 regulation.
4. Further provisions regarding Environmental and Social Responsibility shall be stipulated by Government Regulation.

The implementing regulations derived from Article 74 of Law 40/2007 are required to fulfill social and environmental responsibilities. Government regulation No 47/2012 about Social and Environmental Responsibility of Limited Liability Companies specifically addresses the relevant issues of CSR, as generally applicable to Indonesian companies. GR 47/2012 stipulates that all companies that manage or use natural resources are required to bear a social and environmental responsibility and should be in harmony and balance with surroundings and the local society according to the values, norms, culture of the society.

In Oil and Gas industries, however, the regulations that governs the obligation of implementing similar to CSR programs have long been enacted, both for upstream and downstream industries.

In the contract of upstream oil and gas industry, the company is required to stipulate the implementation of CSR. The obligation to implement a CSR program is based on Article 26 of Government Regulation Number 35 of 2004 as amended several times into Government Regulation Number 55 of 2009 concerning upstream business activity in the oil and gas industry, which states that the company is obliged to provide a minimum provision in the contract, to accommodate impact of the project toward people and environment. The company is required to allocate part of its annual budget to develop the environment and respect rights of indigenous societies.

In the contract of downstream oil and gas industry, the company, which is engaged in the processing, transporting, storage and/or general commerce of downstream business activity is required to ensure health and safety, environmental management and development of society. The clause is enacted in the Ministry of Energy and Natural Resources Regulation Number 0007 of 2005 concerning terms and guidelines of the business license implementation in downstream business activity in the oil and gas industry. However, there is no further elaboration as to what the requirements are for the company in terms of developing the society, and the amount the company is expected to put aside in its budget to assist with developing the society is not stipulated.

In the period prior to the issuance of the laws and regulations, the company carrying out CSR programs based on their own initiative or followed the direction from its head quarter if it was a multinational company.

2.2.2. Low Local Government Capacity

As explained earlier, another important issue that could hamper the successful implementation of CSR programs is legal issues that overlap. Many regulations overlap with each other and the different interpretations that can impact the absence of legal uncertainty in the field. Institutionally, at the government level closest to the people, although there are divisions or departments that are responsible for CSR program implementation, but they lack of capacity in the field of CSR, including in public participation. Public participation is key to the success of CSR program in the sense that it can empower the community to participate actively in the CSR programs. Therefore, we can conclude that the capacity of local governments should be enhanced to increase its role in the success of CSR programs.

2.2.3. Low Capacity of Local Community

Since two decades ago, CSR becomes an important issue, especially in his role in empowering communities and in protecting the environment. CSR programs provide many contributions in solving social problems in terms of job creation, health, education, commercial activity, and environment. The program becomes strategic and more helpful to society because of the limited government funds for infrastructure development. Moreover, implementation of CSR programs is able to nurture a spirit of solidarity in communities.

However, the application of this program experienced problems due to lack of socialization that gives impact on the lack of community participation in the program implementation. In fact participation is an important element to support CSR programs aim at improving the livelihood of the society. By involving public to participate in CSR programs, processes in decision making problem solving will become more effective.

The Law No. 40/2007 that outlines the guidelines on CSR has made strong public position. Public must be informed that they play a key role in CSR. People need to be encouraged to participate in CSR program to improve their livelihood and to protect the environment. The communities needs support to convey their messages, and are encouraged to play a key role in decision-making and problem solving processes that affect them. Facilitations may be required to make them able to communicate with other stakeholders, particularly with companies and local governments. Facilitation is needed because it can ensure that CSR programs achieve expected results that benefit society and protect the environment. The facilitations and communications with other stakeholders is to guide all stakeholders to arrive at same perception in interpreting CSR which otherwise still varied. Fostering community is not only aimed at meeting the needs of the community with health, education, sanitation facilities, and commercial activity, but also invited the public to participate in environmental protection programs. In this context, community empowerment will involve NGOs.

2.2.4. Impact to Companies

CSR and good corporate governance principles are like two sides of a coin. Both are equally important and cannot be separated. One of the four principles of good corporate governance is the responsibility, while the other three are fairness, transparency, and accountability. There is a fundamental difference between principle of responsibility and the three other principles. The other three principles of good corporate governance mentioned earlier is in the interest of the shareholders of the company; it is a shareholder driven concept. For example, equal treatment of minority shareholders (fairness), reporting detailed information and financial statements on time (transparency), and the function of shareholders, commissioners, and directors (accountability). In the concept of responsibility, significant emphasis is given to corporate stakeholders. Here the company is required to pay attention to the stakeholders, creating added value of products and services for corporate stakeholders and to maintain continuity of the value added created. Therefore, the principle of responsibility here is intended to reflect stakeholder driven concept.

Stakeholders can be defined as parties interested in the existence of a company. These include employees, customers, consumers, suppliers, communities and the environment, including the government as a regulator. The difference in the company's business will make the company apply different priority stakeholders.

2.2.5. Challenges Ahead

Although some of CSR activities have resulted to positive impact to the communities, the overall implementation of CSR program is still considered weak. At least there are two things that trigger weak implementation of CSR in Indonesia.

First, lack of understanding of CSR. The understanding of CSR as a concept is still weak and in most of the cases, inconsistent. CSR is often seen as a Western concept that is associated with philanthropic activities, as part of a marketing program, or public relations. As a result of this common misperception is that CSR is often included in the net cost, not as investments, resulting in many companies are reluctant to incorporate CSR program into their company policy.

Second, it concerns with social and legal problems. Weak legal enforcement, corruption, and excessive overlap in regulations are common problems in all sectors, including business. This situation affects legal certainty, increased administrative expenses and prolongs bureaucracy. In addition, there are also problems with lack of operational standards in the area of community and business development or corporate governance. To overcome the lack of standards, the lead company uses international standards from its head quarters for use in Indonesia. By using international standards as part of the company's policy to fill in the blanks on the absence of a national standard, in some cases, can be conflicting, resulting in lack of legal certainty. An example is the British Petroleum (BP) Tangguh project in Papua. In this case, BP is committed to hiring local people to be hired as security personnel but it was a conflict with government policy that obliges security guard by military personnel in locations that are vulnerable to the threat of Indonesia as a unitary state.

Therefore, it can be concluded that the two major problems mentioned above give the signal that CSR issues is multi facet because of political issues, cultural differences, and lack of understanding and skills in CSR conception.

3. Closing the Gaps

Poor implementation of CSR program creates gaps that are potentially can be source of conflicts. Measures need to be taken to close the gaps. There are six steps to be taken as follows:

1. To analyze main source of the conflict and its subsequent impacts;

There are at least two sources that can lead to conflict, namely:

- From the legal aspect, legal uncertainty, overlapping regulations, weak law enforcement can cause problems in the project site. In addition, as the impact of the overlapping regulatory and bureaucracy will cause high cost economy.
- From the social aspect, resource conflicts can occur if CSR programs are not well targeted, in the sense that the programs do not fit with what the community needed. The project site where the oil company operates generally located in a remote location where the level of social development is still at a low stage. Infrastructure available scarce Usually, the event may not be available at all, such as schools, health facility, electricity, roads, drinking water and sanitation.

Conflicts may occur when development approaches do not pay attention to local culture. Mistakes in the approach can fuel conflict and this can be detrimental to the project due to the cost associated with recovering the situation back to normal.

Government of Indonesia through the Ministry of Environment already have adequate regulation to assess the environmental impact, health and safety and social on a variety of projects and investments in Indonesia. Law 32/2009 regarding protection and management of the environment supported by government regulation 27/2012 regarding environmental permits provide clear guidance to investors in conducting a study on the mechanism of the implementation of the Environmental Impact Assessment (EIA).

In the policy and regulatory environment, there are guidelines and instruments for assessing conflicts, risks and social impacts as well as environmental and health and safety. In general, the measures undertaken are as follows: (i) determine the terms of reference, (ii) collect baseline data and information, (iii) data processing, (iv) assessing the impact and (vi) monitoring plan and governance. And at the time to implement at all stages, it is important to involve the relevant stakeholders.

2. To identify the financial, social, and environmental risks of the oil and gas company operations.

Impact assessment is a study to understand the effect that the project generated during pre-construction, construction and post-construction. While risk assessment is a study conducted to understand the risks that result from business activities in the pre-construction, construction and post-construction.

Social risks consists of four major components, as follows:

(i) Stakeholders, which are directly and indirectly related to the sustainability of the business. Stakeholders usually categorized into four, namely: government, affected communities, the private sector (small-medium enterprises and public) and civil society (such as non-governmental organizations-NGOs, mass media, mass organizations and others);
(ii) Issues, these are concerns that occur in the communities resulting from many effects including the company's business activities and operations. Examples are environmental issues, social and cultural, and resources;
(iii) Perception, is the understanding accepted by stakeholders resulting from the knowledge of a single or series of activities by the company;
(iv) Events, is a single or series of events caused by the behavior of companies and communities. Examples are demonstration events, mass media and networking activities between actors.

Examples of risks that may occur, among others:

- Delay in the implementation of the project would hurt the company, and also the disadvantageous for the government;
- The existence of a social gap between migrant and Indigenous population could lead to social inequality; and,
- Environment if not maintained will have a negative impact on the company in the long run because it is not sustainable.

Other social aspects that can lead to conflict is when people are not invited to participate in any decision that affect the community, for example in road construction, construction of buildings for social and public facilities, and health and sanitation facilities.

3. To analyze the gaps that occurs between the capacity of local governments and communities with the company;

One of the effects is the presence of gaps is due to differences in capacity among stakeholders. Not all stakeholders understand the technical and non-technical aspects of oil and gas investments in Indonesia. Such differences may pose risks and negative impact on the investment climate. Various parties should immediately transform the situation into a positive and appropriate atmosphere.

An analysis of the capacity of stakeholders can be done through the study of stakeholders using a variety of instruments available. One of them is by analyzing:

a) power and the effect (influence);
b) the power, influence and legitimacy;
c) the role and responsibilities and performance plans of each stakeholder;

4. To understand the gap between the capacity of the third-party sustainability standards that exist in the international environment, such as the IFC Performance Standards, UN Global Compact, the Equator Principles, ILO Conventions, ICMM (International Council for Metal and Mining), IPIECA (International Petroleum Industry Environmental Conservation Association) and so on;

Investment in Indonesia is currently very much influenced by a variety of investment performance framework generated by the multilateral financial, bilateral and commercial institutions, such as the International Finance Corporations (IFC), the Asian Development Bank (ADB) and the Banks, which are members of the Equator Principles. Investment performance framework that they developed is related to aspects of environmental, health, safety and social (EHSS).

The background of the standard implementation of EHSS performance is the increased awareness of the world's leaders together to implement the concept of sustainable development. If not, the Earth's limited capacity to bear the burden of investment will impact negatively on the welfare, safety, public health and the environment.

EHSS performance standards have not been fully understood by the various oil and gas investors in Indonesia. Therefore, it is necessary to analyze the gaps (gap analysis) between what has been done by the company with what is required by the investor.

5. To better understand the relevant stakeholders that have direct and indirect impacts on the issues.

Among the stakeholders are the people who are affected by project activities either directly or indirectly. If there is an issue or a problem that requires a decision, they may play a role, depending on their affinity to decision making process and decision made. They may be participating in decision making, participating in planning process for decision-making, or serves as advisor, or reviewers. But for those who do not want to get too involved they may be as observers or not even involved in the process at all.

Therefore it is necessary to identify the stakeholders and analyzed the level of their participation as a member of community or public, in resolving issues or in making decisions. The planning for public participation basically consists of five steps:

a) internal gain commitment
b) learn from the public
c) select the level of participation
d) define the decision process and participation objectives

e) design of the public participation plan

The levels of public impact in the decision-making processes may range from inform, consult, involve, collaborate, and empower. To inform the public means to provide the public with balanced and objective information to assist them in understanding the problems, alternatives, opportunities and/or solutions. To consult the public is to obtain public feedback on analysis, alternatives and/or decisions. Involving the public means to work directly with the public throughout the process to ensure that public concerns and aspirations are consistently understood and considered. Collaboration with the public is to partner with the public in each aspect of the decision including the development of alternatives and the identification of the preferred solution. Lastly, by Empowering the public is to place final decision-making in the hands of the public.

6. To promote the stakeholder engagement and public relation strategy to ensure the sustainability of company operations.

Stakeholder engagement and public relation strategy is based on effective communication. Specifically the strategy to build positive relationship with the public should consider two things:

a) to provide the public with the information they need to participate in the meaningful way; and,
b) to communicate to the public how their input affect the decision.

4. Conclusions

Rapidly growing economies, particularly in Asia, including the Middle East provide a positive climate as more investment to countries in the region. To maintain sustainable development and improvement of people's welfare, economic growth must be balanced with social development and environmental conservation.

In developing countries, by taking the case of Indonesia, although the framework legislation is quite comprehensive in the field of CSR, but the fact remains that there is still an imbalance: the economy is growing rapidly, but the progress is not accompanied by efforts in the field of social development and environmental conservation balanced so prone to trigger social conflict. This in turn can reduce a company's reputation to be detrimental to the company in question.

The imbalance of this development can be overcome if the company creates an understanding at strategic level internally. By doing six steps as outlined in the previous chapter, companies can formulate CSR programs that are environmentally friendly and socially justifiable, so as to develop the balance of the three main pillars of sustainability into the construction of the project that is profitable for the company, provide the public welfare, and ensure sustainability development.

References

Waagstein, P. R.: The Mandatory Corporate Social Responsibility in Indonesia:Problems and Implications (Journal of Business Ethics (2011) 98:455-466).

Crawford, P., Editor: International Association of Public Participation, 2010, State of the Practice Report, Core Values Award Nominees, , http://www.iap2.org

International Finance Corporation: 'Stakeholder Engagement and the Board: Integrating Best Governance Practices', Global Corporate Governance Forum, 2009.

International Finance Corporation: 'Stakeholder Engagement, A Good Practice Handbook for Companies Doing Business in Emerging Market', 2007.

Hohnen, P., and Jason Potts (Editor): 'Corporate Social Responsibility, An Implementation Guide for Business', International Institute for Sustainable Development, (2007), Winnipeg, Manitoba, http://www.iisd.org/pdf/2007/csr_guide.pdf

Kemp, M.: 'Corporate Social Responsibility in Indonesia, Quixotic Draem or Confident Expectation?', Technology, Business and Society Programme Paper Number 6 December 2001, United Nations Research Institute for Social Development.

Koestoer, Y. T.: Corporate Social Responsibility in Indonesia, Building internal corporate values to address challenges in CSR implementation, www.aseanfoundation.org/**Yanti**+**Koestoer** (un-dated)

Kan, R.: 'Corporate Social Responsibility: address Indonesia', http://www.pa-international.org/pa_csr2/update_Corporate_social_responsibility_address_Indonesia.htm (un-dated)

Juniarto, C. B. J. H., and Andika D.J.H. Juniarto: Corporate Social Responsibility regulation in Indonesia, www.ibanet.org/Article/Detail.aspx?ArticleUid=103427a1-0313... (un-dated)