

Entering the Carbon Trading Era in Indonesia

Amid mounting concerns over climate change, Indonesia is poised to enter a new era of carbon trading with the imminent implementation of a newly passed regulation, scheduled to take effect from September 2023.

The Financial Services Authority (*Otoritas Jasa Keuangan* – **OJK**) recently announced details of its highly anticipated Regulation No. 14 of 2023 on Carbon Exchange (“**POJK 14/2023**”), which has been designated by the Ministry of Law and Human Rights but is yet to be publicly unveiled.

This new regulation finally sets out a clear roadmap for carbon trading in Indonesia through a dedicated carbon exchange. Businesses are hopeful it will herald a new era of carbon trading in the country, dispelling the uncertainty that persisted despite the enactment of carbon trading provisions back in 2021.

Counting the days before POJK 14/2023 is made available publicly, here are some pointers on Indonesia’s current regulatory framework on carbon trading.

Indonesia’s Commitment

Since the enactment of Law No. 16 of 2016 on the Ratification of the Paris Agreement to the United Nations Framework Convention on Climate Change (effective as of 25 October 2016), Indonesia has consistently demonstrated its commitment to addressing climate change. However, the outcomes are yet to yield substantial environmental improvements.

In 2022, Indonesia submitted its enhanced National Determined Contribution (“**ENDC**”) to the United Nations Framework Convention on Climate Change.[1] This enhancement underscores

Indonesia's commitment to unconditionally reduce greenhouse gasses emissions by 29% to 31.89% by 2030, with the potential to further increase this reduction to 43.2% with international support by 2030.

To fulfill the objectives of the submitted ENDC, the Indonesian government has provided gateways and avenues for businesses to actively participate in reducing greenhouse gas emission. This has been achieved by enacting regulations on emissions and carbon, including measures related to carbon trading and monetization of carbon emissions across various ministerial sectors. These measures are generally set out under Presidential Regulation No. 98 of 2021 on the Implementation of Carbon Economic Value to Achieve Nationally Determined Contribution Targets and Control Over Greenhouse Gas Emissions in relation to National Development ("**PR 98/2021**"), as well as Minister of Environment and Forestry ("**MOEF**") Regulation No. 21 of 2022 on the Implementation of Carbon Economic Value ("**MOEF 21/2022**").

FAQ 1: How is carbon trading conducted in Indonesia?

As outlined in MOEF 21/2022, carbon trading in Indonesia can operate domestically and internationally through two primary methods: (i) emissions trading and (ii) emissions offsetting.

These mechanisms can be conducted using either direct trading or a carbon exchange platform.

General Provisions on Carbon Trading in Indonesia

Carbon trading is a market-based mechanism aimed at reducing greenhouse emissions by facilitating the purchase and sale of carbon units, as defined in MOEF 21/2021. Each carbon unit, corresponding to one metric ton of carbon dioxide, serves as tangible evidence of ownership and is documented through certificates or technical endorsement. These units are recorded in the National Registry System for Climate Change Control (*Sistem Registri Nasional Pengendalian Perubahan Iklim* – "**SRN-PPI**").

For participation in carbon trading, whether domestically or internationally, the following requirements must be met:

- a. Compliance with the Carbon Trading roadmap.
- b. Provision of emissions reduction reserves (buffers).
- c. Cross-sector carbon trading, which must be in the form of a Greenhouse Gas (*Gas Rumah Kaca* – "**GRK**") Emission Reduction Certificate (*Sertifikat Pengurangan Emisi*) ("**SPE-GRK**").

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The SPE-GRK is issued by the MOEF through the Directorate General for Climate Change Control. It serves as proof of emission reduction achieved by businesses and/or activities that have undergone measurement, reporting and verification processes. The certificate is recorded in the SRN-PPI, documented by unique numbers and/or registry codes.

Emission Offsetting

Emission Offsetting is only applicable for companies that fulfill the following conditions:

(i) They lack an Emissions Cap (*Batas atas Emisi GRK*) and instead adhere to a baseline and emissions reduction target determined by the MOEF or relevant provincial government.

(ii) They have an emissions surplus or deficit in accordance with the GRK Emissions Baseline

Companies in these categories must also obtain an SPE-GRK to carry out emission offsetting. In certain scenarios, it is also possible to rely on certificates issued by other accreditation agencies that are equivalent to SPE-GRK and can be used for emission offsetting.

International Carbon Trading

MOEF21/2022 allows for collaboration between domestic and overseas businesses for international carbon trading, upon approval from the MOEF. This cooperation with offshore entities aligns with Indonesia’s commitment to fulfilling its Nationally Determined Contribution (NDC).

The requirements for conducting international carbon trading (in addition to the general provisions above) are as follows:

(i) Implementation is permitted once the relevant minister^[3] formulates and submits plans and strategies aimed at achieving the specific sector and sub-sector NDC goals.

(ii) Attainment of NDC targets in designated sub-sectors or sub-sub-sectors for international carbon trading.

(iii) Acquisition of official authorization from the MOEF.

Upon close scrutiny of these requirements, it becomes apparent that despite the provisions made in the existing regulation for international carbon trading, the present stance treats such endeavors as a prospect that might not be realized in the near future. This is due to

Indonesia's present distance from achieving its NDC mentioned in item (ii) above. However, numerous news outlets have highlighted the Indonesian government's assertion that foreign parties are welcome to engage in carbon trading, with international transactions subject to authorization from the relevant authority. Evidently, this matter still warrants further observation.

Indonesian Carbon Exchange: What to Expect

POJK 14/2023 is expected to cover the licensing mechanism for the carbon exchange market organizer, mentioned under Law No. 4 of 2023 on the Development and Strengthening of the Financial Sector ("**Law 4/2023**"). From the general framework of the draft regulation presented by the OJK, POJK 14/2023 may also include provisions on the management structure of the market organizer, including its shareholding composition, board of directors, and board of commissioners.

The Indonesia Stock Exchange ("**IDX**") reportedly developed a carbon exchange earlier this year and has been awaiting the enactment of the OJK regulation on the carbon exchange to satisfy licensing requirements. It remains unclear whether the carbon exchange will be part of the IDX or if an entirely new entity established. Various news outlets indicate the IDX is planning to provide four distinct features within the carbon exchange framework: auction, regular trading, negotiation market, and marketplace. However, the actual implementation of these features hinges on the forthcoming POJK 14/2023, as this regulation will also govern operational aspects of the carbon market. This includes support for market infrastructure, service users, as well as transaction mechanisms including completion procedures within the carbon exchange platform.

POJK 14/2023 is also expected to include consumer protection provisions, which are anticipated to offer benefits to businesses that will use the carbon exchange as a means to engage in carbon trading.

FAQ 2: How are voluntary carbon credits treated in Indonesia?

There are no explicit references to voluntary carbon credits under the existing carbon-related regulations in Indonesia. MOEF 21/2022 only provides that emission reduction certificates issued by other certification agencies may be declared equivalent to an SPE-GRK through a cooperative mutual recognition arrangement with the MOEF. Therefore, GRK Emission Reduction Certificates issued outside Indonesia can be used for carbon trading in Indonesia, but they must first be registered and included in the mutual acknowledgment scheme along with their supporting data in the SRN-PPI.

Note that companies that register their carbon units in the SRN-PPI system must also provide information on the voluntary credits standard to be registered in the system. Such standards include the Voluntary Carbon Standard (VCS), Joint Crediting Mechanism (JDM), and the Clean Development Mechanism (CDM).

Carbon Trading in Ministerial Sectors

The Indonesian government has been issuing ministerial regulations related to the monetization of carbon emissions through carbon trading in certain sectors. These regulations include:

- (i) Minister of Energy and Mineral Resources (“**MEMR**”) Regulation No. 16 of 2022 on the Procedures for the Implementation of Carbon Economic Value in the Power Plant Subsector (“**MEMR 16/2022**”).
- (ii) MOEF Regulation No. 7 of 2023 on the Procedures of Carbon Trading in the Forestry Sector (“**MOEF 7/2023**”).

For further details on these regulations, please refer to our advisory on MEMR 16/2022 [here](#).

In relation to carbon trading in forestry sector, MOEF 7/2023 states that such trading is limited to holders of specific forestry licenses, including the Forest Utilization Business License (PBPH), Social Forest Management Approval, or management rights over forest areas (*hak pengelolaan*).^[4] This implies that the “ownership” of carbon units is tied to the company holding the relevant license, as mentioned in MOEF 7/2023.

MOEF 7/2023 also sets out a clear framework for determining the maximum amount of carbon units (beyond the NDC surplus) that can be traded internationally, including a formula for calculation.

Carbon Trading and Tax Allowance

Under Law No. 7 of 2021 on the Harmonization of Tax Regulations (“**Law 7/2021**”), the government can impose a carbon tax on companies that emit carbon waste, as a means of mitigating climate change. This carbon tax is set at minimum Rp30 per kilogram. The carbon tax is applicable in two scenarios:

(i) When purchasing goods containing carbon.

(ii) At the end of the calendar year during which activities producing a certain level of carbon emissions occurred.

However, under Law 7/2021, businesses that engage in carbon trading can benefit from a carbon tax reduction and leniency concerning their other carbon tax obligations. Nevertheless, the Ministry of Finance is yet to issue a regulation on this carbon tax allowance.

Concluding Remarks

While carbon trading is an established international concept, it is only now being adopted in Indonesia. In the coming years, the Indonesian government is expected to issue more carbon trading regulations at the ministerial level to cover all sectors. For now, the OJK’s new implementing regulation needs to be closely observed, especially on how it will play out in practice.

[1] (2022) Enhanced Nationally Determined Contribution Republic of Indonesia - UNFCCC. Available at: https://unfccc.int/sites/default/files/NDC/2022-09/23.09.2022_Enhanced%20NDC%20Indonesia.pdf (Accessed: 09 August 2023).

[2] GRK Emissions Baseline is the estimation of emission levels and projections of GRK in identified sectors or activities within determined periods without policy interventions and/or mitigation technologies.

[3] “Relevant Minister” is the minister who is the coordinator of the sector/sub-sector in carbon trading (there are six sectors: energy, waste, industrial processes and product use, agriculture, forestry, and/or other sectors) in accordance with the development of science and technology.

[4] Article 7 (1) of MOEF 7/2023.

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