

ROLES FOR ISLAMIC BUSINESS ETHICS IN THE ENVIRONMENTAL, SOCIAL, AND GOVERNANCE CONCEPT

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Abstract

The purpose of this study, which used a descriptive qualitative method with library research, is to (1) understand the role of Islamic law, ethics, and business principles in the implementation of the Environmental, Social, and Governance (ESG) concept in financial institutions. (2) Outlining the benefits of Islamic law, ethics, and business principles in the application of the ESG concept in financial institutions. The study's findings indicate that (1) Islamic law, ethics, and business principles should be applied in the implementation of the ESG concept to identifying sustainable development goals and enhancing the efficiency of financial services while ensuring the longevity of financial institutions. (2) Providing a framework for the organization's financial strategy in starting a business based on financial principles and creating products with social and environmental considerations. The implications of this research include the application of Islamic law, ethics, and business principles to the ESG framework at the World Bank, which is expected can strengthen government programs in the area of sustainable development goals (SDGs). The novelty in this research refers to the use of flexible Islamic economic principles and ethics that are oriented to the environmental and social needs of modern societies.

Keywords: *Environmental Social and Governance (ESG), Sustainable Development, Financial Institutions.*

مستخلص البحث

الغرض من هذا البحث، الذي استخدم المنهج الكيفي الوصفي مع البحث المكتبي، هو (1) فهم دور الشريعة الإسلامية والأخلاق ومبادئ الأعمال في تطبيق مفهوم البيئة والمجتمع والحوكمة في المؤسسات المالية. (2) تحديد فوائد الشريعة الإسلامية والأخلاقيات ومبادئ الأعمال في تطبيق مفهوم البيئة والمجتمع والحوكمة في المؤسسات المالية. تشير النتائج التي توصلت إليها الدراسة إلى ما يلي: (1) ضرورة تطبيق الشريعة الإسلامية والأخلاق ومبادئ الأعمال في تطبيق مفهوم البيئة والمجتمع والحوكمة في المؤسسات المالية لتحديد أهداف التنمية المستدامة وتعزيز كفاءة الخدمات المالية مع ضمان استمرارية المؤسسات المالية. (2) توفير إطار عمل للاستراتيجية المالية للمؤسسة في بدء عمل تجاري قائم على المبادئ المالية وابتكار منتجات ذات اعتبارات اجتماعية وبيئية. وتشمل الآثار المترتبة على هذا البحث تطبيق الشريعة الإسلامية والأخلاقيات ومبادئ الأعمال التجارية على إطار العمل البيئي والاجتماعي والحوكمة في البنك الدولي، والذي من المتوقع



أن يعزز البرامج الحكومية في مجال أهداف التنمية المستدامة. وتشير الجادة في هذا البحث إلى استخدام مبادئ وأخلاقيات الاقتصاد الإسلامي المرنة والموجهة للاحتياجات البيئية والاجتماعية للمجتمعات الحديثة. الكلمات المفتاحية: البيئة والمجتمع والحوكمة والتنمية المستدامة والمؤسسات المالية.

INTRODUCTION

The tendencies and phenomena of global warming, environmental damage, poverty, unemployment, and other social problems trigger companies operating in a country contributing to climate change.

As a form of role in sustainable development, companies are expected to publicly report on economic, environmental, and social impacts in an annual report to be submitted to stakeholders. This report is considered important as a measure of the sustainability and ethical impact of companies, in order to make investment decisions for investors.¹

In Indonesia, the obligation to submit sustainability reports to financial services institutions, issuers, and public companies is implemented gradually. The Financial Services Authority (FAT) through Regulation No. 51/POJK.03/2017 requires the submission of such reports to the issuer with medium assets in the fiscal year 2022, to the issuer with small asset in the financial year 2024, and to the banking group of the General Bank based on Enterprise Activities (LAB) 3, LAB 4, and against foreign banks has been carried out in fiscal year 2019. The Indonesian Stock Exchange (BEI) is also taking the initiative to require by 2022 all companies listed in the EIB to report sustainability.

Managing the form of corporate concern for the environment in society well can boost the performance of financial institutions so that in turn has important implications for corporate executives, environmental activists, policymakers, and regulators according to insights taken from the theory of agency, resource dependence, stakeholders, and legitimacy.²

In order to maintain national economic growth and ensure long-term financial stability and strengthening economic resilience, responsible and sustainable business practices need to be promoted by financial institutions in the form of a real change of attitude and action towards environmental and social issues. Based on the above background, a commitment to the application of business principles and ethics is required to improve the performance of the financial institutions

¹ Goncalves, A, & Silva, C.(2021), Looking for Sustainability scoring in apparel: A review on environmental footprint, social impacts and transparency, *Energies*, 14 (11), p. 3032.

² Nguyen, T. H., Elmagrhi, M. H., Ntim, C. G., & Wu, Y. (2021). Environmental performance, sustainability, governance and financial performance: Evidence from heavily polluting industries in China. *Business Strategy and the Environment*, 30 (5), pp. 213–2331.

industry in Indonesia through the implementation of Environmental, Social and Governance (ESG) in a planned, measurable, and sustainable manner. Therefore, the writing of this paper aims to show how the implementation of ESG business in improving the financial performance of companies in Indonesia.

Environmental Social and Governance (ESG)

ESG disclosures are tools used to measure progress by disclosing information on the impact of an organization's environmental, social, and governance practices, where disclosure is non-financial in order to evaluate the company's performance over the course of its operational activities as well as its impact.³

ESG is a corporate standard in conducting investment activities where integration and implementation of corporate policies in line with the concept of environmental concerns, social, and governance with environmental criteria includes several things such as energy consumption, waste, pollution, conservation of natural resources and treatment of flora and fauna. The criteria of governance cover all forms of good and sustainable management carried out by the internal company.

ESG can also be understood as an attempt to disclose non-economic information through a policy of disclosure of responsibility for environmental, social, and governance activities aimed at improving the trust, value and performance of companies from a public perspective.

Operational Performance

Improving profitability through disclosure of non-financial information to stakeholders will then be able to provide the investor's attraction to invest capital into the company in the form of investment. So the role of ESG is as a tool for gaining legitimacy, increasing the confidence of the public and stakeholders of the company as well as improving the working capital and the company's operations.

Business Ethics Business ethics is a common term used to indicate the ethical behaviour of a manager or employee of an organization as well as to maintain the loyalty of stakeholders in making company decisions and in solving company issues because of all decisions.⁴

As a moral thinking, always think about what should be done and what should not be done then business ethics as a reflection, highlighting and evaluating well the badness of people's behavior in the sense of considering what can and shouldn't be done, among other things can show

³ Ghazali, A., & Zulmaita, Z. (2022). *Pengaruh Pengungkapan Environmental, Social, and Governance (ESG) Terhadap Tingkat Profitabilitas Perusahaan (Studi pada Perusahaan Sektor Infrastruktur yang Terdaftar di Bursa Efek Indonesia)*. p. 3.

⁴ Inu Kencana Syafie, *Pengantar Filsafat*, Refika Aditama, Bandung, Desember 2004, p. 17.

attitude and say honestly, openly, transparently, should not cheat or commit fraud in his/her enterprise/business.

METHOD

Research is an attempt to understand literary phenomena systematically. Literature and phenomenology are closely related.⁵ Seeing the character of the problems raised using the method of qualitative research, where qualitational research is not presented in numeric form, but in word form.

Corresponding to the nature of the qualitatively approach, where the method emphasizes analysis on data descriptively that are written words observed, by observing and analyzing the study of the role of management and business in creating a sustainable, sustainable unity.

Library research is the type of research that is carried out by reading, exploring and studying books and sources of writing that are closely related to the issues discussed.⁶

As for the approach used in the writing and writing of this is a conceptual approach in this section carried out an examination of the concepts and theories used based on the existing literature. The process of data analysis has basically begun to work since the data collection was carried out and worked intensively. Analysis involves data presentation and interpretation performed qualitatively conceptually. Context relates to things that relate to the structure of the work, while construction is the building of the concept of analysis. The construction is the framework for the analysis.⁷

RESULTS AND DISCUSSION

Research that shows the application of Environmental Social and Governance (ESG) has been applied to many companies in both Indonesia and other countries.

It is important in Environmental, Social and Governance (ESG) disclosures to Corporate Performance because of its influence on the operational performance and market performance of large corporations. However, sometimes Environmental, Social, and Governance (ESG) do not affect the financial performance of companies.⁸ Such research revealed partially or individually that the independent variables described by environmental, social, and governance disclosures had no

⁵ Endraswara, S. (2021). *Metodologi Penelitian Fenomenologi Sastra*.

⁶ Zed, M. (2008). *Metode penelitian kepustakaan*. Yayasan Pustaka Obor Indonesia.

⁷ Rahayu, Y. S., & Naja, C. D. (2023). Penerapan Artificial Intelligence Sebagai Inovasi di Era Disrupsi dalam Mengurangi Resiko Lembaga Keuangan Mikro Syariah. *WADLAH*, 7 (2).

⁸ Nisa, A. Z., Titisari, K. H., & Masitoh, E. (2023). Pengaruh Pengungkapan Environmental, Social, dan Governance terhadap Kinerja Perusahaan. *Al-Kharaj: Jurnal Ekonomi, Keuangan & Bisnis Syariah*, 5(5), pp. 2400–2411.

influence on the rate of profitability projected by ROA and ROIC. But the three variables simultaneously, influenced moderate significance on the profitability rate of the company.⁹

It is also important in the implementation of ESG (Environmental, Social, and Governance) to know the perception of Generation Z towards Investment in Jakarta Islamic Index, where financial literacy, subjective norms, and attitude have a significant influence on investment interests based on Environmental, Social, and governance. (ESG). But religiousness failed to moderate gen z's interest in investing in the Jakarta Islamic Index (JII).¹⁰

The results of the study on “Environmental performance, sustainability, governance and financial performance: Evidence from heavily polluting industries in China” show that average, board size and board meetings are linked positively to the environmental performance of Chinese companies, while board independence and gender diversity have a positive relationship to the performance of China's corporate environment, but the relationship is not significant to the corporate performance. Our further evidence suggests that the internal governance mechanisms studied have varying moderating effects on the relationship between financial performance and environmental performance. The findings have important implications for corporate executives, environmental activists, policymakers, and regulators.¹¹

The implementation of Sustainable Finance is carried out using the following principles: (1) the principles of responsible investment, (2) sustainable business strategies and practices, (3) social and environmental risk management, (4) governance, (5) informative communication, (6) inclusive, (7) priority sector development, (8) coordination and collaboration.

As for the implementation of Sustainable Finance, it is an Action Plan that is structured on the following priorities: (1) Development of sustainable financial products and/or services, including enhanced portfolios of financing, investments or placement in financial instruments or projects in line with the application of sustained finance, (2) Development of internal capacity of financial services institutions, (3) adjustment of organizational, risk management, governance, and/or standard operating procedures in accordance with the principles – implementing sustainable finance.

⁹ Ghazali, A., & Zulmaita, Z. (2022). *Pengaruh Pengungkapan Environmental, Social, and Governance (ESG) Terhadap Tingkat Profitabilitas Perusahaan (Studi pada Perusahaan Sektor Infrastruktur yang Terdaftar di Bursa Efek Indonesia)*. 3.

¹⁰ Azhar, J. A., Kadua, N. C. P., & Safitri, R. D. (2023). Analisis Persepsi Generasi Z Terhadap Investasi Berbasis ESG (Environmental, Social, and Governance) di Jakarta Islamic Index. *Journal of Business Management and Islamic Banking*, 2 (1), pp. 77–94.

¹¹ Nguyen, T. H., Elmaghri, M. H., Ntim, C. G., & Wu, Y. (2021). Environmental performance, sustainability, governance and financial performance: Evidence from heavily polluting industries in China. *Business Strategy and the Environment*, 30 (5), pp. 2313–2331.

CONCLUSION

Interested parties can study corporate behavior and policies, especially governance, social, and environmental issues that cannot be assessed with regular financial analysis, by incorporating ESG variables into the investment process. As a result, more and more investors are allocating their capital to contribute to the creation of a world that is more ethical, more environmentally friendly and clean.

It is expected, companies - civil society agencies and government to enhance cooperation to ensure the successful integration of the implementation of ethics of business, environment, social and governance in the financial institutions in Indonesia well.

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