



Project Information Document/ Identification/Concept Stage (PID)

Concept Stage | Date Prepared/Updated: 22-Dec-2021 | Report No: PIDC253474



BASIC INFORMATION

A. Basic Project Data

Project ID	Parent Project ID (if any)	Environmental and Social Risk Classification	Project Name
P177773		Moderate	Indonesia Implementation Support for Carbon Pricing Instruments
Region	Country	Date PID Prepared	Estimated Date of Approval
EAST ASIA AND PACIFIC	Indonesia	22-Dec-2021	
Financing Instrument	Borrower(s)	Implementing Agency	
Investment Project Financing	Coordinating Ministry for Economic Affairs, Ministry of Environment and Forestry (MOEF)	Coordinating Ministry for Maritime and Investment (CMMAI)	

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PROJECT FINANCING DATA (US\$, Millions)

SUMMARY

Total Project Cost	5.00
Total Financing	5.00
Financing Gap	0.00

DETAILS

Non-World Bank Group Financing

Trust Funds	5.00
Partnership for Market Implementation Facility	5.00

B. Introduction and Context

Country Context

Indonesia is the world’s largest archipelago country comprising over 13,500 islands covering an area of 8.3 million km² with a land territory of 1.9 million km². Indonesia’s total population reached 270 million people in 2020, rising by 14% over the past decade. Approximately 60% of the population lives in coastal areas which are more vulnerable to the impacts of climate change. In 2019, Indonesia recorded the highest frequency of



hydrometeorology disasters in its history, more than double than in 2010. At the same time, Indonesia's GHG annual emissions places the country amongst the ten largest GHG emitters in the world, with a steady increase of annual emissions. Awareness of its vulnerability to climate change impacts and contribution to global emissions has encouraged Indonesia to actively participate in global efforts to combat climate change.

In 2018, Indonesia's total GHG emissions were estimated at approximately 1.6 Giga tonCO₂e, two times more than in 2010. The forestry and land use (FOLU) sector was the main contributor of GHG emissions with 44% of the total GHG emissions in 2018, followed by energy (36%), agriculture (8%), waste (8%) and industrial processes (4%). From 2010-2018, the compound annual growth rate of GHG emissions by sector was energy (3.5%), IPPU (6.4%), Agriculture (2.5%), FOLU (24.6%), and waste (4.7%). Indonesia's GHG emissions are projected to reach 2.8 Giga tonCO₂e in 2030 under a business-as-usual (BAU) scenario. Post-2020, the energy sector is projected to be the main contributor of GHG emission surpassing the FOLU sector.

The Government of Indonesia (GoI) has ratified the Paris Agreement through Law 16 of 2016 and submitted its first NDC in 2016 with commitments to reduce emissions to 29% with its own resources and 41% with international assistance by 2030, in comparison to a business-as-usual scenario. To achieve the ambitious NDC commitment, the government has prepared a set of policies and instruments, and aligned the NDC with the mid-term development plan (RPJMN) for 2020-2024, where emissions reductions have been included as development targets. The RPJMN for 2020-2024 constitutes Indonesia's first low carbon development plan and includes an economy-wide mitigation target of 27.3% relative to a business-as-usual scenario by 2024. GoI has also issued Government Regulation No 46/2017 on Environmental Economic Instruments. Moreover, the GoI has finalized Presidential Regulation 78/2021 on Carbon Economic Valuation and Law 7/2021 on Tax Regulation/Harmonization, which set out the basis for carbon pricing instruments (including carbon taxation) in Indonesia. The Government of Indonesia is also currently finalizing a *Presidential Regulation on Purchasing Price for Renewable Energy Generation*, which will facilitate private sector involvement in Indonesia's low carbon development trajectory

The government has made continuous efforts to increase GHG mitigation efforts in the FOLU and energy sectors, as these sectors have been identified as main contributors of GHG emissions in the country. In these two sectors, the GoI has planned to reduce 811 million GHG emissions compared to BAU scenario in 2030, accounting for more than 97% of the total GHG emission reduction target. The main GHG mitigation efforts in the energy sector are increasing renewable energy penetration, the use of clean coal technology, fuel switching in the transportation sector, and demand-side management. While the main efforts in the forestry sectors are REDD+, peatland restoration, and degraded land rehabilitation.

Sectoral and Institutional Context

Introducing a price on carbon plays an important role to support the transition to the decarbonization pathway envisaged by the RPJMN and to contribute to meeting the NDC mitigation objectives. A Presidential Regulation (Perpres) on Carbon Pricing (*Presidential Regulation 98/2021 on Carbon Economic Valuation*) was recently finalized and issued in October 2021, which supplements the 2017 regulation on Environmental Economic Instruments. The Presidential Regulation provides a framework regulation on the envisaged carbon pricing policy mix, general institutional arrangements to advance the carbon pricing agenda, and main



principles to guide design and operation of carbon pricing instruments; the design of each instrument remains left to the ministries/government agencies with specific mandate.

To familiarize stakeholders with the concept of domestic carbon pricing, pilot programs for crediting and cap-and-trade mechanisms have been established through the Ministry of Environment and Forestry (MOEF) and the Ministry of Energy and Mineral Resources (MEMR), respectively. In March 2021, Indonesia launched an trial emissions trading scheme (ETS) focused on the power generation sector. The first trial period is scheduled to run until the end of September 2021. The pilot will aim to familiarize stakeholders with carbon pricing concepts, in particular, ETS and offsets. In 2020, the Government also piloted a domestic carbon credit mechanism, known as the Indonesia Certified Emission Reduction (ICER) initiative.

The Government of Indonesia, through the Coordinating Ministry for Maritime and Investment (CMMAI), the Coordinating Ministry for Economic Affairs (CMEA), and the Ministry of Environment and Forestry (MOEF), sought assistance from the World Bank's Partnership for Market Implementation (PMI) to consolidate the assessment and support the implementation of its envisaged carbon pricing policy mix. The primary focus is to support the design and gradual implementation of the domestic emissions trading system (ETS), and a domestic offset program, including its compatibility with international carbon trade under Article 6.

The implementation of technical assistance (TA) activities pertaining the emission trading system instrument will be led by the Ministry of Energy and Mineral Resources (MEMR), while the analytical work related to Carbon Tax instrument will be coordinated with the Ministry of Finance (MOF), and the TA activities pertaining the GHG Crediting instrument will be led by Ministry of Environment and Forestry (MOEF). Each of the leading technical ministries will work in collaboration with other relevant ministries/agencies, and these activities will be monitored and coordinated by the Coordinating Ministry for Maritime Affairs and Investment (CMMAI) with support from the Coordinating Ministry for Economic Affairs (CMEA).

Relationship to CPF

The proposed activity is fully aligned with the World Bank's Country Partnership Framework (CPF) 2021 - 2025 for Indonesia approved by the Board in May 2021. The proposed activity is also aligned with the heightened emphasis on Climate Change as a cross cutting themes in the CPF, including the World Bank's Climate Change Action Plan.

C. Project Development Objective(s)

Proposed Development Objective(s)

To assist the Government of Indonesia's in the development, piloting and implementation of domestic carbon pricing instruments.



Key Results

The following results are expected from the project:

1. Informing discussions on national carbon pricing policy mix with technical assessments and international best practices
2. Designing options for national emission trading system (ETS) and domestic GHG crediting/offset program to inform the GoI's decisions
3. Enhancing human and institutional capacity, and piloting activities to support operationalization of the ETS and domestic offset program.

D. Preliminary Description

Activities/Components

The PMI will assist the Government of Indonesia through the first PMI program window (Window 1: Implementation Support) as Indonesia has shown demonstrated political commitment for the implementation of carbon pricing instruments, and 'readiness' in terms of domestic capacity and institutional architecture, and are ready to move to the next level of implementation. The support package will focus on strengthening domestic implementation capacity, strengthening legislative and policy review functions, scaling and expanding to new sectors, and other activities.

The envisaged work streams for PMI technical assistance, as identified in Indonesia's PMI Expression of Interest (EOI, endorsed by the PMI governing body in July 2021) includes the following areas:

Support design and implementation of a domestic cap-and-trade program (domestic emissions trading system/ETS)

- *National ETS design options.* Build on the existing pilot in power sector and take into consideration the requirements to implement a national multi sector ETS, the scope of PMI support could comprise works on developing agreed design of national ETS, e.g. sectoral scope, coverage, ETS rules and guidelines, etc. Support to upgrade the MRV readiness level of other sectors not covered by the previous PMR program but would be included in the national ETS is also seek in this stream, for example for textile, ceramic, and forestry.
- *ETS policy development.* In parallel with reaching the agreement on national ETS design, PMI support is expected to assist related policy works such as development of national ETS regulation(s) as derivative of the foreseen presidential regulation on carbon pricing, GHG emissions cap regulations in the relevant ministries, policy dialogues and assessments, etc.
- *ETS market infrastructure.* A working national ETS will require robust and reliable market infrastructure to ensure its integrity and effectiveness. This stream would include activities to develop integrated registry system that linked together existing sectoral systems as well as to support development of ETS units' secondary market.



- *Piloting and operationalization.* Drawing on lessons learned from the current pilot in power sector, support the preparation of national ETS pilot program, with a view of launching operation of a national ETS by 2025..

Support development and implementation of the domestic GHG offset program

- *Technical advisory to domestic offset program design.* Key building blocks of Indonesia's domestic GHG offset program have been developed to date; however, there are important instrument design gaps pertaining program governance, regulatory system, methodological guidance, for example, procedural and methodological guidance for the inclusion of GHG offset project activities from different economic sectors.
- *Domestic offset policy development.* A domestic crediting scheme alone is not sufficient to scale-up mitigation actions but has to be accompanied by a sound strategy to stimulate domestic demand for carbon credits and to access emerging international voluntary demand. The project will support policy assessment work to facilitate coherent and sound development of GHG offset policy frameworks, in a manner that optimizes domestic offset demand and supports long-term decarbonization objectives in Indonesia.
- *Assessment of compatibility with Article 6/international carbon markets.* Indonesia welcomes voluntary cooperation to scale up climate change mitigation that involves international transfer of mitigation outcomes. The program will support Indonesia to assess and ensure compatibility of its domestic offset program with ITMOs-related cooperation under Article 6 of the UN Paris Agreement (ITMO: international transferred mitigation outcomes).

Review of Indonesia's carbon pricing policy mix: interaction with the (planned) national carbon tax

- *Carbon tax policy review.* Indonesia is getting ready to introduce a fuel-based carbon tax as part of the 2021 tax code reform. The program would support modelling and upstream analytical work to assess carbon pricing impacts, addressing aspects such as mitigation outcomes and effectiveness in changing behavior; distributional and just transition concerns, considerations related to carbon leakage, impacts on domestic energy prices and competitiveness.
- *Policy interaction with existing and planned policy instruments, including the ETS program.* Identification and assessment of interactions with other existing policies and instruments affecting climate policy objectives. Review interaction with subsidies in the targeted sectors that may have a negative impact on effectiveness of the carbon pricing policy, e.g., fossil fuel subsidies. Similarly, review existing policies and instruments that would complement on the effectiveness of carbon policy objectives, such as existing incentives, subsidies or other fiscal or policy levers which mobilize investments and stimulate clean technology and market innovation.

Cross-cutting activities: enabling environment for carbon pricing and markets



- *Communication, stakeholder engagement, capacity building for domestic carbon pricing.* Proposed cross-cutting activities to support the PMI country program, covering capacity development, stakeholder engagement, communications and knowledge management. [MCR1]

Environmental and Social Standards Relevance

E. Relevant Standards

ESS Standards

Relevance

ESS 1	Assessment and Management of Environmental and Social Risks and Impacts	Relevant
ESS 10	Stakeholder Engagement and Information Disclosure	Relevant
ESS 2	Labor and Working Conditions	Relevant
ESS 3	Resource Efficiency and Pollution Prevention and Management	Relevant
ESS 4	Community Health and Safety	Not Currently Relevant
ESS 5	Land Acquisition, Restrictions on Land Use and Involuntary Resettlement	Not Currently Relevant
ESS 6	Biodiversity Conservation and Sustainable Management of Living Natural Resources	Not Currently Relevant
ESS 7	Indigenous Peoples/Sub-Saharan African Historically Underserved Traditional Local Communities	Not Currently Relevant
ESS 8	Cultural Heritage	Not Currently Relevant
ESS 9	Financial Intermediaries	Not Currently Relevant

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Legal Operational Policies

Safeguard Policies	Triggered	Explanation (Optional)
Projects on International Waterways OP 7.50	No	The project is not located in any international waterways, and does not finance any activities that may impact such waterways.
Projects in Disputed Areas OP 7.60	No	This project is not located in disputed areas (as per definition of OP 7.60)

Summary of Screening of Environmental and Social Risks and Impacts

The overall environmental and social rating is Moderate and intends to support achievement of long term positive impacts to the environment particularly on reducing GHG emissions and energy consumption, and support sustainable development. The project support for the development of the ETS, carbon offsets and carbon tax schemes will provide market incentives for GHG emitters to reduce emissions and energy consumption which leads to positive environmental impacts of mitigating climate change and maintaining and/or enhancing carbon sinks. ESS1 on Assessment and Management of Environmental and Social Risks and Impacts, ESS2 Labor and Working Conditions, ESS3 on Resource Efficiency and Pollution Prevention and



Management, and ESS10 on Stakeholder Engagement and Information Disclosure were assessed as applicable for the proposed operation. Both environmental and social risks ratings are moderate due to potential adverse downstream impacts are likely when the carbon pricing instruments assessed and delivered by the TA are implemented in the future by other funding sources which stimulate GHG emissions reductions actions/projects carried out in the sectors covered by these instruments (ETS; offset program). These potential downstream impacts are not known at this stage and will be further screened during preparation of the Terms of References for the TAs. A stakeholder engagement plan (SEP) will be developed to promote broad stakeholder engagement and participation in the design and implementation of the ETS, domestic GHG offset program as well as policy level discussions on environment for carbon pricing and markets overall through meaningful consultation. The relatively low risks associated with the labor and working conditions of project workers will be addressed through fit-for-purpose Labor Management Procedures (LMP) complying with the requirements of ESS2 (including with regards to prevention of child and forced labor, management of Occupational Health and Safety (OHS), fair and equal opportunity for hiring process and pay, and workers grievance mechanisms). A capacity building plan on ESF, TOR and appointment of an E&S Focal Point will be agreed with the implementing agency, and incorporated into the ESCP. The TOR for the E&S Focal Point will define the responsibilities for the overall environmental and social management oversight and ES risk screening of TAs, satisfactory to the World Bank. At the current stage, the ES focal point is planned to be appointed at the CMMAI as the coordinating implementing agency. The SEP, LMP, ESCP and TOR E&S Focal Point will be prepared by the CMMAI prior to appraisal.

CONTACT POINT

World Bank

Contact :	Andre Rodrigues de Aquino	Title :	Senior Environmental Specialis
Telephone No :	5781+3218 /	Email :	
Contact :	Habib Nasser Rab	Title :	Lead Economist
Telephone No :	5781+3077 /	Email :	
Contact :	Marcos Xavier Castro Rodriguez	Title :	Senior Environmental Specialis
Telephone No :	5220+32238 /	Email :	

Borrower/Client/Recipient

Borrower :	Coordinating Ministry for Economic Affairs		
Contact :	Dida Gardera	Title :	Assistant Deputy for Agro, Pharmacy, and Tourism
Telephone No :	6221-3500901	Email :	gardera@ekon.go.id
Borrower :	Ministry of Environment and Forestry (MOEF)		



Contact :	Wahyu Marjaka	Title :	Director of Sectoral and Regional Resource Mobilization, Dir
Telephone No :	6221-858-0110	Email :	wmarjaka@menlhk.go.id

Implementing Agencies

Implementing Agency : Coordinating Ministry for Maritime and Investment (CMMAI)

Contact :	Kus Prisetiahadi	Title :	Assistant Deputy for Climate Change and Disaster Management
Telephone No :	622123951100	Email :	kus.prisetiahadi@maritim.go.id

FOR MORE INFORMATION CONTACT

The World Bank
1818 H Street, NW
Washington, D.C. 20433
Telephone: (202) 473-1000
Web: <http://www.worldbank.org/projects>

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