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The Legal Framework for OJK Supervision in Preventing Greenwashing Practices in Sustainable Finance Products in the Banking Sector

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Abstract

This research analyzes the legal construction of Financial Services Authority supervision in preventing greenwashing practices in sustainable finance products within Indonesia's banking sector. Normative legal research methods with statute and conceptual approaches examine the synchronization of regulations related to sustainable finance supervision. The findings reveal that POJK Number 51/POJK.03/2017 lacks comprehensive green taxonomy and rigorous verification mechanisms for sustainability claims. The Financial Services Authority's supervisory powers remain suboptimal due to absent specific technical standards, limited capacity in environmental, social, and governance risk assessment, and weak administrative sanction enforcement. Greenwashing practices manifest through report narrative manipulation and inconsistent financing classifications. This research recommends establishing an Indonesian green taxonomy with clear technical criteria, revising POJK 51/2017 to include granular disclosure obligations and independent verification mechanisms, strengthening supervisory capacity through specialized human resource development and technology utilization, and providing fiscal incentives to encourage genuine portfolio transformation toward sustainable economic activities.

INTRODUCTION

The shift in the global economic development paradigm toward sustainability has accelerated the growth of green financial instruments, particularly sustainable finance, which has become a key priority in Indonesia's financial sector. The Financial Services Authority (OJK), as the regulator and supervisor of the financial services sector, has issued OJK Regulation No. 51/POJK.03/2017 concerning the Implementation of Sustainable Finance as a legal framework for integrating environmental, social, and governance (ESG) principles into the banking industry. This regulation reflects Indonesia's commitment to sustainable development as outlined in Presidential Regulation No. 18 of 2020 on the 2020–2024 National Medium-Term Development Plan.[1] he development of sustainable financing in Indonesia continues to grow, with total sustainable banking financing reaching Rp 2.347 trillion in 2023, an increase of 12.8 percent from the previous year.[2]

However, the rapid expansion of sustainable finance has also led to the emergence of greenwashing practices, defined as misleading claims regarding the environmental benefits of financial products without sufficient substantive evidence. This issue has become a major concern for global regulators, as highlighted by the International Organization of Securities Commissions, which identifies greenwashing as a systemic risk that can undermine investor confidence and distort capital allocation.[3] In Indonesia, indications of greenwashing are reflected in the classification of conventional financing as sustainable without clear sustainability assessment criteria, as well as the lack of transparency in reporting environmental impacts. Empirical findings suggest that approximately 37 percent of sustainable financial products in Southeast Asia are at risk of greenwashing due to weak verification and supervisory mechanisms.[4]

From a legal perspective, greenwashing practices may constitute misleading information that violates Article 8 of Law No. 8 of 1999 on Consumer Protection and undermines the principle of transparency in financial regulation.[5] Such practices not only harm consumers and investors but also generate broader systemic risks, including the

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[1] Ministry of National Development Planning, "Presidential Regulation (PERPRES) No. 18 of 2020 on the 2020–2024 National Medium-Term Development Plan," 2020, 1–7.
[2] Financial Services Authority, "Indonesian Banking Statistics 2024," Jakarta: OJK, 2024,
[3] Gabriela Figueiredo Dias, "Sustainability and Sustainable Finance: A Regulator's Perspective and Beyond BT - The Palgrave Handbook of ESG and Corporate Governance," ed. Paulo Câmara and Filipe Morais (Cham: Springer International Publishing, 2022), 217–29.
[4] Ting Pan and Boqiang Lin, "Research on the Mechanism of Improving the Energy-Saving Effect of Green Credit Policy: Green Washing Behavior and Financial Supervision," *Energy* 327 (2025): 136485.
[5] Law of the Republic of Indonesia, "No. 8 of 1999 on Consumer Protection," Law No. 8 of 1999, no. 8 (1999): 1–19.

misallocation of economic resources, the failure to achieve emission reduction targets, and the erosion of public trust in sustainable financial instruments.[6] Globally, investor losses linked to greenwashing in ESG-related financial products are estimated to reach USD 500 billion, demonstrating the urgency of strengthening regulatory oversight and enforcement mechanisms.[7]

Despite the existence of POJK No. 51/POJK.03/2017, the current regulatory framework remains insufficient to effectively prevent greenwashing practices. The regulation does not provide a clear and operational definition of sustainable finance, nor does it establish a comprehensive green taxonomy with measurable technical criteria. Furthermore, it does not impose mandatory ex ante verification mechanisms to substantiate sustainability claims, and its disclosure requirements remain general without standardized and quantifiable indicators. These weaknesses indicate the existence of significant regulatory gaps that may enable greenwashing practices to persist. In comparison, the European Union has developed the EU Taxonomy Regulation and the Sustainable Finance Disclosure Regulation, which provide detailed technical criteria and standardized disclosure obligations to ensure the credibility of sustainability claims.[8] Meanwhile, financial regulators in Singapore have introduced comprehensive guidelines that emphasize substantiation of claims, impact reporting standards, and independent third-party verification mechanisms.[9]

Based on the above issues, this study focuses on three main legal questions. First, to what extent is the current regulatory framework governing OJK supervision adequate to prevent greenwashing practices in the banking sector? Second, what regulatory gaps and institutional limitations contribute to the persistence of greenwashing practices? Third, what legal reforms are necessary to strengthen the supervisory framework in order to effectively prevent greenwashing?[10]

This study aims to analyze the adequacy of the existing legal framework, identify its regulatory and institutional weaknesses, and propose legal reforms to enhance the effectiveness of OJK supervision in preventing greenwashing practices. The analysis is based on theories of legal supervision, particularly the distinction between preventive

[6] Dirk A. Zetzsche and Linn Anker-Sørensen, *Regulating Sustainable Finance in the Dark*, *European Business Organization Law Review*, vol. 23 (Springer International Publishing, 2022.
[7] Marco Bodellini, "Greenwashing and the Misapplication of Articles 8 and 9 of the Sustainable Finance Disclosure Regulation," *ERA Forum* 24, no. 1 (2023): 27–42.
[8] G Aras, *Sustainable Finance for Sustainable Development: Regulations, Theory and Practice*, Finance, Governance and Sustainability (Taylor & Francis, 2024).
[9] Félix E. Mezzanotte, "Persuasion and Deterrence: Enforcing Sustainable Finance Provisions," *Law and Financial Markets Review*, 2025, 1–24.
[10] Laws of the Republic of Indonesia, "Law No. 21 of 2011 on the Financial Services Authority," 2011, 24.

and repressive mechanisms, as well as disclosure-based regulation and responsive regulation, which emphasize proportional and risk-based supervision. In the context of sustainable finance, these theoretical approaches underline the importance of clear classification standards, robust reporting mechanisms, and verifiable sustainability claims as prerequisites for effective regulatory oversight.[11]

METHODS

The research method employed is a normative legal research method utilizing statutory, conceptual, and comparative approaches to analyze the legal framework governing the oversight of sustainable financing and the prevention of greenwashing practices. The statutory approach is used to examine the synchronization and harmonization of laws and regulations related to sustainable finance oversight, particularly Law No. 21 of 2011 on the Financial Services Authority, Financial Services Authority regulations regarding sustainable finance and consumer protection, as well as technical regulations on banking governance and risk management. The conceptual approach is applied to analyze legal concepts relevant to the prevention of greenwashing, including disclosure-based regulation, transparency, and risk-based supervision, as analytical tools to assess the adequacy of the regulatory framework. The analysis is conducted through a normative evaluation using gap analysis, which identifies discrepancies between existing legal provisions and the regulatory requirements necessary to prevent greenwashing practices, based on parameters such as the clarity of sustainability definitions, the existence of verification mechanisms, the adequacy and measurability of disclosure obligations, and the effectiveness of enforcement mechanisms, including administrative sanctions. In addition, a comparative regulatory approach is employed by referring to best practices from comparative jurisdictions as benchmarks for evaluating Indonesia's regulatory framework. The primary legal materials used include Law No. 21 of 2011 on the Financial Services Authority, Financial Services Authority regulations regarding sustainable finance and consumer protection, as well as technical regulations on banking governance and risk management. Secondary legal materials, such as academic literature, scientific journals, research reports from international institutions, and best practices from comparative jurisdictions, were used to enrich the analysis.[12] egal data was collected through literature reviews and

[11] Romain Berrou, Philippe Dessertine, and Marco Migliorelli, "An Overview of Green Finance BT - The Rise of Green Finance in Europe: Opportunities and Challenges for Issuers, Investors and Marketplaces," ed. Marco Migliorelli and Philippe Dessertine (Cham: Springer International Publishing, 2022), 3–29.
[12] Law of the Republic of Indonesia, "Law No. 21 of 2011 on the Financial Services Authority".

documentation, while the analysis was conducted qualitatively using systematic and teleological interpretation methods to determine the legislative rationale behind existing legal provisions and identify regulatory gaps within the framework of oversight aimed at preventing greenwashing.

The significance of this research lies in its contribution to the development of administrative law, particularly regarding the oversight of the financial services sector, as well as in providing legal policy recommendations to strengthen the regulatory framework for sustainable finance in Indonesia. The urgency of this research is increasing in line with Indonesia's target to achieve net-zero emissions by 2060, which requires the mobilization of sustainable financing on a massive scale, a goal that can only be realized if there is market confidence in the integrity of sustainable financing products.[13] Previous research on sustainable finance supervision in Indonesia has been limited to the general implementation of the Financial Services Authority's (OJK) Sustainable Finance Regulation, while specific studies on mechanisms to prevent greenwashing and the effectiveness of the OJK's supervisory authority remain scarce. Consequently, this study is expected to fill this gap and provide a comprehensive legal perspective. Thus, this study is not only academically relevant but also has practical implications for strengthening the governance of sustainable finance and providing legal protection for stakeholders within Indonesia's sustainable finance ecosystem.[14]

RESULT AND DISCUSSION

1. Regulatory Gaps in the Current Framework

The regulatory framework for sustainable finance in Indonesia is fundamentally anchored in Law No. 21 of 2011 on the Financial Services Authority, which grants the Otoritas Jasa Keuangan (OJK) broad authority to regulate and supervise activities within the financial services sector, including the banking industry.[15] This authority is further operationalized through the issuance of POJK No. 51/POJK.03/2017 on the Implementation of Sustainable Finance for Financial Services Institutions, Issuers, and Public Companies, which serves as the primary regulatory instrument for integrating

[13] Simona Galletta et al., "A PRISMA Systematic Review of Greenwashing in the Banking Industry: A Call for Action," *Research in International Business and Finance* 69 (2024): 102262.
[14] Shruti Sharma et al., "Sustainable Banking Practices: Impact, Challenges and Opportunities," *E3S Web of Conferences* 556 (2024), https://doi.org/10.1051/e3sconf/202455601031.
[15] Julius Adi Chandra, Rian Sacipto, and Muktiono Muktiono, ""Analysis of the Government's Role in Greenwashing Practices Within ESG-Based Sustainable Financial Investment Strategies," Panorama Hukum Journal 7, no. 2 (2022): 138–46.

environmental, social, and governance (ESG) principles into financial activities.[16] This regulation requires all financial institutions to develop a sustainable finance action plan that covers governance, social and environmental risk management, as well as reporting and transparency.[17]

However, from a normative legal perspective, the existing regulatory framework exhibits significant structural weaknesses that limit its effectiveness in preventing greenwashing practices. One of the primary issues lies in the absence of a clear and operational definition of "sustainable finance" within POJK No. 51/POJK.03/2017.[18] he regulation formulates sustainability principles in broad and general terms without providing measurable technical criteria or sector-specific benchmarks.[19] As a result, financial institutions retain wide interpretative discretion in classifying financing activities as sustainable, which creates a definitional gap that may be exploited to justify labeling conventional financing as "green" without substantive environmental assessment.[20]

In addition to this definitional ambiguity, the regulatory framework does not impose mandatory ex ante verification mechanisms to substantiate sustainability claims. Although financial institutions are required to implement sustainable finance principles, there is no explicit obligation to conduct independent validation or third-party verification prior to the issuance of sustainability labels.[21] This normative omission weakens the credibility of sustainability claims and increases the likelihood of greenwashing, as claims can be made based on internal assessments without external scrutiny.[22]

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[16] Ahmad Sutanto, Wita Juwita Ermawati, and Lukytawati Anggraeni, "Assessing the Impact of Sustainable Finance Regulation on Bank Risk: Evidence from Indonesia Using a Difference-in-Differences Approach," *Journal of Accounting and Strategic Finance* 8, no. 2 (2025): 209–34.
[17] Risna Kartika and Andini Grace Tinia, "Faktor-Faktor Yang Mempengaruhi Adopsi Green Finance Pada Perbankan Di Indonesia," *Accountability: Journal of Economic Sciences* 17, no. 2 (2025): 17–27.
[18] Financial Services Authority Regulation No. 51/POJK.03/2017, "Financial Services Authority Regulation No. 51/POJK.03/2017 on the Implementation of Sustainable Finance for Financial Services Institutions, Issuers, and Public Companies," Financial Services Authority, 2017, 1–15, https://peraturan.bpk.go.id/Details/129651/peraturan-ojk-no-51pojk032017-tahun-2017.
[19] Iman Prihandono and Dewi S. Yuniarti, "Indonesia's Sustainability Reporting Standard: What Needs to Be Improved?" *Associate Professor at the Faculty of Law* 7, no. 1 (2023): 1–23.
[20] Widia Yuliyansa and Anggun Okta Fitri, "Environmentally Conscious Islamic Banking: An Analysis of the Opportunities and Challenges of Green Banking," Academic Media Journal *(Jma)* 3, no. 5 (2025): 1–9.
[21] Novi Nugrahani et al., "Determinants of Green Banking Disclosure State Banks," *Jamanika (Journal of Business Management and Entrepreneurship)* 5, no. 1 (2025): 86–100.
[22] Maharestu Setyorini and Dzikri Firmansyah Hakam, "The Impact of Green Banking Activities on Environmental Performance: A Youth-Driven Perception Study in Indonesian Financial Institutions," *Journal of Risk and Financial Management* 18, no. 10 (2025).

Furthermore, the disclosure regime under POJK No. 51/POJK.03/2017 lacks sufficient precision and standardization. While the regulation requires sustainability reporting, it does not establish uniform, measurable, and comparable indicators for assessing environmental impact or ESG performance.[23] The absence of standardized disclosure metrics enables financial institutions to rely on narrative-based reporting, which may obscure material information and facilitate selective disclosure practices. Consequently, sustainability reports may fail to provide an accurate representation of the actual environmental impact of financed activities.[24]

Another critical weakness concerns the absence of explicit legal provisions addressing greenwashing and the lack of proportionate administrative sanctions for misleading sustainability claims.[25] Although OJK possesses general enforcement powers, the regulatory framework does not clearly define what constitutes greenwashing nor specify the legal consequences for such conduct.[26] This lack of normative clarity creates enforcement difficulties and reduces the deterrent effect of supervisory mechanisms, as regulatory authorities face challenges in identifying, proving, and sanctioning misleading sustainability practices.[27]

Developments such as the Sustainable Finance Roadmap Phase II (2021–2025) demonstrate regulatory commitment to strengthening the implementation of ESG principles, particularly through initiatives in governance, data development, and capacity building. However, these policy instruments remain largely programmatic and do not sufficiently address the underlying normative deficiencies in the existing regulatory framework, particularly with regard to enforceable standards and verification mechanisms.

A comparative analysis with international regulatory frameworks further highlights these shortcomings. The European Union, through the EU Taxonomy Regulation, has established detailed technical screening criteria that define sustainable economic activities based on scientific benchmarks. Similarly, Singapore has developed regulatory

[23] Reny Dany Merliyana, "The Role of Governance and Regulation in Shaping ESG Disclosure Quality," *Summa : Journal of Accounting and Tax* 2, no. 3 (2024): 89–100.
[24] Agne Sneideriene and Renata Legenzova, "Greenwashing Prevention in Environmental, Social, and Governance (ESG) Disclosures: A Bibliometric Analysis," *Research in International Business and Finance* 74 (2025): 102720.
[25] Dadan Ramdhan, "The Role of ESG Disclosure in Attracting Sustainable Investment in Indonesia's Capital Market," *RIGGS: Journal of Artificial Intelligence and Digital Business* 4, no. 3 (2025): 3384–93.
[26] Rhea Proudi Siagian, Pandu Prahara Arista, and Yossi Naswa Faradila, "Green Investment or Greenwashing ? Foreign Investment in Indonesia ' s Renewable Energy Sector," *Liberatica*, 2025, 23–33.
[27] Amrie Firmansyah and Adelia Puspitasari, "Sustainable Finance and Green Banking Disclosure: Unlocking Firm Value Potential," *Riset* 7, no. 1 (2025): 172–90.

guidelines that emphasize substantiation of sustainability claims, standardized impact reporting, and mandatory independent verification. These frameworks illustrate a more advanced regulatory approach that combines definitional clarity, robust disclosure requirements, and enforceable verification mechanisms, thereby reducing the risk of greenwashing.

In light of the above analysis, it can be concluded that the current regulatory framework governing OJK supervision of sustainable finance remains insufficient to effectively prevent greenwashing practices. The absence of clear definitions, verification requirements, standardized disclosure mechanisms, and enforceable sanctions constitutes a set of interrelated regulatory gaps that undermine the integrity of sustainable finance in Indonesia. Addressing these deficiencies requires not only policy development but also the formulation of more precise, technical, and enforceable legal norms within the regulatory framework.

2. Greenwashing Practices in Sustainable Finance Products in the Indonesian Banking Sector

Greenwashing practices in the Indonesian banking sector manifest as a discrepancy between sustainability claims and the actual substance of financing activities. In practice, these practices are reflected in the classification of financing as sustainable based on administrative or formal criteria, without a substantive assessment of environmental impact or ESG performance.[28] This indicates that sustainability labeling is often not grounded in verifiable and measurable standards, but rather in interpretative flexibility arising from the absence of clear regulatory benchmarks.[29]

From a normative legal perspective, the emergence of greenwashing is closely linked to the deficiencies in the regulatory framework, particularly the lack of precise definitions, verification requirements, and standardized disclosure mechanisms. In the absence of clear legal obligations to substantiate sustainability claims, financial institutions are able to construct sustainability narratives that are not necessarily supported by objective data. This results in a form of regulatory arbitrage, where compliance is achieved formally but not substantively, thereby undermining the integrity of sustainable finance.[30]

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[28] Radi Mugisana, Eneng Nurdiana Septifani, and Laras Angelia Nirwana Sari, "Greenwashing in ESG Disclosure: A Systematic Literature Review through Theoritical and Bibliometric Anaylisis," *Wahana Accounting Journal* 20, no. 2 (2025): 157–70.

[29] Galletta et al., "A PRISMA Systematic Review of Greenwashing in the Banking Industry: A Call for Action."

[30] Yehezkiel Benaya Nanlohi et al., "Examining 'Greenwashing' Behind the Hype of ESG: A Case Study of Retail Investors' Perceptions and Experiences Regarding the Implementation of Corporate ESG Practices in

The practice of greenwashing is further reinforced by the reliance on narrative-based sustainability reporting.[31] Financial institutions frequently employ broad and non-quantifiable language in sustainability reports, emphasizing commitments and policies rather than measurable outcomes.[32] Without mandatory quantitative indicators or independent verification, such disclosures create information asymmetry between financial institutions and stakeholders, particularly investors and consumers, who rely on these reports in making decisions.[33]

From a legal standpoint, greenwashing practices may constitute misleading information that violates the principle of transparency in financial regulation and consumer protection norms.[34] However, the absence of explicit legal definitions and evidentiary standards for greenwashing complicates enforcement.[35] Regulators face difficulties in distinguishing between permissible interpretation and misleading claims, particularly in cases where sustainability assertions are framed in general or qualitative terms.[36]

The systemic impact of greenwashing practices extends beyond individual transactions and affects the integrity of the financial system as a whole. Misleading sustainability claims may lead to the misallocation of financial resources, where capital is directed toward activities that do not contribute to environmental objectives.[37] This not only undermines investor confidence but also hampers the achievement of broader policy goals, including emission reduction targets and the transition to a sustainable economy.[38]

Moreover, the lack of transparency in the use of sustainable financing funds and the absence of periodic impact assessment requirements further exacerbate greenwashing

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Indonesia Following the Latest Regulations," Anggaran: Journal of Economics and Accounting 3, no. 2 (2025): 53–61.

[31] Sneideriene and Legenzova, "Greenwashing Prevention in Environmental, Social, and Governance (ESG) Disclosures: A Bibliometric Analysis."

[32] Ramdhan, "The Role of ESG Disclosure in Attracting Sustainable Investment in Indonesia's Capital Market."

[33] Siagian, Arista, and Faradila, "Green Investment or Greenwashing ? Foreign Investment in Indonesia ' s Renewable Energy Sector."

[34] Yehezkiel Benaya Nanlohi et al.. Behind the ESG Hype: A Case Study on Retail Investors' Perceptions and Experiences Regarding the Implementation of Corporate ESG Practices in Indonesia Following the Latest Regulations."

[35] Merliyana, "The Role of Governance and Regulation in Shaping ESG Disclosure Quality."

[36] Sneideriene and Legenzova, "Greenwashing Prevention in Environmental, Social, and Governance (ESG) Disclosures: A Bibliometric Analysis."

[37] Firmansyah and Puspitasari, "Sustainable Finance and Green Banking Disclosure: Unlocking Firm Value Potential."

[38] Siagian, Arista, and Faradila, "Green Investment or Greenwashing ? Foreign Investment in Indonesia ' s Renewable Energy Sector."

risks. Without mechanisms to track and verify the actual environmental outcomes of financed projects, sustainability claims remain largely untested, allowing discrepancies between commitments and implementation to persist.

In this context, greenwashing should not be viewed merely as an ethical issue, but as a legal and regulatory problem arising from normative gaps and institutional limitations. The persistence of such practices demonstrates that the current supervisory framework is insufficient to ensure the credibility of sustainability claims. Therefore, addressing greenwashing requires not only strengthening regulatory provisions, but also enhancing the capacity of supervisory institutions and improving the quality of sustainability data and verification mechanisms.

3. Analysis of the Financial Services Authority's Supervisory Powers in Preventing Greenwashing

The supervisory authority of the Financial Services Authority (OJK) in preventing greenwashing practices is derived from Law No. 21 of 2011, which grants the institution broad powers to regulate, supervise, and enforce compliance within the financial services sector.[39] These powers encompass regulatory functions in establishing legal norms, supervisory functions in ensuring compliance, and enforcement functions in imposing administrative sanctions. In the context of sustainable finance, such authority should theoretically enable OJK to prevent misleading sustainability claims and ensure the integrity of financial products.[40]

However, from a normative legal perspective, the effectiveness of these supervisory powers is contingent upon the availability of clear and operational legal standards. [41] As identified in the previous analysis, the absence of precise definitions of sustainable finance, mandatory verification mechanisms, and standardized disclosure requirements significantly limits the ability of OJK to exercise its supervisory authority effectively.[42] Without clear normative benchmarks, supervision becomes interpretative and reactive rather than preventive and rule-based.[43]

In the domain of preventive supervision, OJK possesses the authority to formulate technical standards related to ESG risk assessment, sustainability classification, and

[39] Julius Adi Chandra, Rian Sacipto, and Muktiono Muktiono, ""Analysis of the Government's Role in Greenwashing Practices Within ESG-Based Sustainable Financial Investment Strategies," Panorama Hukum Journal 7, no. 2 (2022): 138–46."
[40] Prihandono and Yuniarti, "Indonesia's Sustainability Reporting Standard: What Needs to Be Improved?.
[41] Sutanto, Ermawati, and Anggraeni, "Assessing the Impact of Sustainable Finance Regulation on Bank Risk: Evidence from Indonesia Using a Difference-in-Differences Approach."
[42] Nugrahani et al., "Determinants of Green Banking Disclosure State Banks."
[43] Setyorini and Hakam, "The Impact of Green Banking Activities on Environmental Performance: A Youth-Driven Perception Study in Indonesian Financial Institutions."

reporting obligations.[44] However, the current regulatory framework does not translate this authority into detailed and enforceable technical rules. The absence of binding standards on sustainability verification and classification weakens the preventive function of supervision, as financial institutions are not required to meet specific, measurable criteria before labeling their financial products as sustainable.[45]

Furthermore, the implementation of risk-based supervision in sustainable finance remains constrained by institutional limitations. Although OJK conducts both off-site monitoring through periodic reports and on-site inspections, the effectiveness of these mechanisms is limited by the lack of reliable ESG data and the absence of standardized reporting frameworks.[46] As a result, supervisory assessments often rely on information provided by financial institutions themselves, without sufficient independent verification, thereby reducing the accuracy and credibility of supervisory outcomes.[47]

From an enforcement perspective, OJK has the authority to impose administrative sanctions, including written warnings, business restrictions, suspension of activities, and revocation of licenses, as stipulated under the applicable legal framework. However, in practice, enforcement related to sustainability reporting and greenwashing remains limited. This is primarily due to the absence of explicit legal provisions defining greenwashing and the lack of clear evidentiary standards for determining misleading sustainability claims. Consequently, regulators face significant challenges in proving violations and applying sanctions proportionately.[48]

Another critical limitation lies in the institutional capacity of the supervisory authority. The assessment of ESG risks and sustainability claims requires interdisciplinary expertise, including environmental science, data analysis, and financial risk management. The current shortage of specialized human resources within the supervisory framework limits the ability of OJK to conduct substantive evaluations of sustainability claims, thereby weakening both preventive and repressive supervisory functions.

Comparative analysis with other jurisdictions demonstrates that effective supervision of sustainable finance requires a combination of detailed regulatory standards and robust

[44] Yuliyansa and Fitri, "Environmentally Conscious Islamic Banking: An Analysis of the Opportunities and Challenges of Green Banking."
[45] Mugisana, Eneng Nurdiana Septifani, and Laras Angelia Nirwana Sari, "Greenwashing in ESG Disclosure: A Systematic Literature Review through Theoritical and Bibliometric Anaylisis."
[46] Merliyana, "The Role of Governance and Regulation in Shaping ESG Disclosure Quality."
[47] Ramdhan, "The Role of ESG Disclosure in Attracting Sustainable Investment in Indonesia's Capital Market."
[48] Prihandono and Yuniarti, "Indonesia's Sustainability Reporting Standard: What Needs to Be Improved?.

institutional capacity. Regulatory authorities in developed jurisdictions have adopted proactive supervisory approaches, including mandatory due diligence, standardized disclosure requirements, and external assurance mechanisms. These practices highlight the gap between formal authority and practical effectiveness in the Indonesian context.

In light of the above analysis, it can be concluded that although OJK possesses broad supervisory authority, the effectiveness of such authority in preventing greenwashing is significantly constrained by normative deficiencies and institutional limitations. The lack of clear legal standards, limited data reliability, weak enforcement mechanisms, and insufficient supervisory capacity collectively undermine the ability of OJK to ensure the credibility of sustainable finance practices. Therefore, strengthening supervisory effectiveness requires not only regulatory reform but also institutional capacity building and the development of robust verification mechanisms.

4. Challenges in Implementing Sustainable Finance Oversight and Greenwashing Risks

The implementation of sustainable finance oversight in Indonesia faces a fundamental challenge in the form of regulatory fragmentation, which leads to inconsistencies in sustainability reporting and assessment standards across industrial sectors.[49] The absence of a comprehensive and legally binding green taxonomy has led financial institutions to use different definitions and criteria when classifying sustainable financing, which in turn hinders data comparability and complicates the oversight process. This situation is exacerbated by the limited technical capacity of banking institutions to conduct accurate environmental impact assessments of the projects they finance.[50]

The second challenge relates to the limited quality and availability of reliable ESG data to support financing decision-making and sustainability performance evaluations.[51] The majority of companies in Indonesia, particularly micro, small, and medium-sized enterprises—which constitute the primary segment of bank financing—do not yet have standardized environmental reporting systems, making it difficult for banks to verify borrowers' sustainability practices. The lack of transparency in supply chains and the absence of independent certification for environmentally friendly products further complicate efforts to prevent greenwashing at the operational level.[52]

[49] Ramdhan, "The Role of ESG Disclosure in Attracting Sustainable Investment in Indonesia's Capital Market."
[50] Kartika and Tinia, "Factors Influencing the Adoption of Green Finance in the Banking Sector in Indonesia."
[51] Prihandono and Yuniarti, "Indonesia's Sustainability Reporting Standard: What Needs to Be Improved?
[52] Nugrahani et al., "Determinants of Green Banking Disclosure State Banks."

From the perspective of the banking sector's internal governance structure, the implementation of sustainable finance has not yet been fully integrated into business processes and strategic decision-making.[53] Many banks treat sustainable finance as a compliance function separate from their core business, so their commitment to sustainability is not reflected in their credit allocation policies and risk management strategies. Empirical research shows that small banks and state-owned banks experienced a higher increase in risk following the implementation of POJK 51/2017 due to limited capacity to assess green credit risk.[54]

The fourth challenge relates to the dilemma between short-term profitability and long-term sustainability faced by banking institutions.[55] Financing for sustainable projects often requires longer payback periods and involves higher technological risks compared to conventional financing, so banks tend to be conservative in allocating green loans, especially under conditions of liquidity stress. The lack of adequate fiscal incentives and government risk-sharing mechanisms for sustainable financing leads banks to prefer labeling conventional financing as green financing rather than actually transforming their portfolios.[56]

The systemic risks associated with greenwashing are increasing as the market for green bonds and sustainability-linked loans grows to a significant size within Indonesia's financial system. If the majority of sustainable financial instruments turn out not to meet genuine sustainability criteria, a bubble could form in the green finance market, ultimately leading to investor losses and a loss of confidence in sustainable financial instruments as a whole.[57] Therefore, strengthening independent oversight and verification mechanisms is crucial to mitigating these systemic risks.[58]

5. Recommendations for Strengthening the Legal Framework for Oversight to Prevent Greenwashing

Strengthening the legal framework for OJK oversight to prevent greenwashing practices requires comprehensive regulatory reform through the development of an

[53] Setyorini and Hakam, "The Impact of Green Banking Activities on Environmental Performance: A Youth-Driven Perception Study in Indonesian Financial Institutions."
[54] Yuliyansa and Fitri, "Environmentally Conscious Islamic Banking: An Analysis of the Opportunities and Challenges of Green Banking."
[55] Mugisana, Eneng Nurdiana Septifani, and Laras Angelia Nirwana Sari, "Greenwashing in ESG Disclosure: A Systematic Literature Review through Theoritical and Bibliometric Anaylisis."
[56] Sneideriene and Legenzova, "Greenwashing Prevention in Environmental, Social, and Governance (ESG) Disclosures: A Bibliometric Analysis."
[57] Merliyana, "The Role of Governance and Regulation in Shaping ESG Disclosure Quality."
[58] Siagian, Arista, and Faradila, "Green Investment or Greenwashing ? Foreign Investment in Indonesia ' s Renewable Energy Sector."

Indonesian green taxonomy that provides clear and measurable technical definitions of sustainable economic activities.[59] The taxonomy must be developed based on credible scientific methodologies and aligned with international standards such as the EU Taxonomy and the ASEAN Taxonomy for Sustainable Finance to facilitate cross-border investment flows. Establishing specific technical criteria for each economic sector will reduce the scope for interpretation that could be exploited for greenwashing practices.[60]

The second recommendation concerns strengthening disclosure and transparency requirements through the adoption of harmonized and legally binding sustainability reporting standards.[61] The OJK needs to revise POJK No. 51/POJK.03/2017 to include more granular disclosure requirements covering sustainability assessment methodologies, quantitative data on environmental impacts, and mechanisms for monitoring the use of sustainable financing funds. Adopting international reporting frameworks such as the Task Force on Climate-related Financial Disclosures (TCFD) and the Global Reporting Initiative (GRI) can enhance the comparability and credibility of sustainability reporting by banks in Indonesia.[62]

Strengthening independent verification and assurance mechanisms is a crucial element in preventing greenwashing.[63] The OJK needs to establish regulations requiring financial institutions to undergo external verification by accredited third-party assessors of their sustainability reports and green financing claims. A certification mechanism for green bonds and sustainable-linked loans conducted by independent bodies with technical expertise in ESG assessment will enhance investor confidence and prevent misleading information.[64]

From a law enforcement perspective, there is a need to strengthen administrative sanctions to make them more stringent and proportionate in response to violations of sustainability reporting obligations and greenwashing practices.[65] The OJK needs to formulate implementing regulations that explicitly define the elements of greenwashing

[59] Chandra, Rian Sacipto, and Muktiono, "Analysis of the Government's Role in Greenwashing Practices Within ESG-Based Sustainable Financial Investment Strategies."
[60] Prihandono and Yuniarti, "Indonesia's Sustainability Reporting Standard: What Needs to Be Improved?
[61] Ramdhan, "The Role of ESG Disclosure in Attracting Sustainable Investment in Indonesia's Capital Market."
[62] Sutanto, Ermawati, and Anggraeni, "Assessing the Impact of Sustainable Finance Regulation on Bank Risk: Evidence from Indonesia Using a Difference-in-Differences Approach."
[63] Setyorini and Hakam, "The Impact of Green Banking Activities on Environmental Performance: A Youth-Driven Perception Study in Indonesian Financial Institutions."
[64] Yuliyansa and Fitri, "Environmentally Conscious Islamic Banking: An Analysis of the Opportunities and Challenges of Green Banking."
[65] Mugisana, Eneng Nurdiana Septifani, and Laras Angelia Nirwana Sari, "Greenwashing in ESG Disclosure: A Systematic Literature Review through Theoritical and Bibliometric Anaylisis."

and establish a graduated system of sanctions ranging from written warnings, administrative fines, and restrictions on business activities to the revocation of licenses for systematic violations that harm the public interest. The publication of sanctions against violators is also necessary to serve as a deterrent and enhance public accountability.[66]

Finally, strengthening the OJK's supervisory capacity requires investment in the development of human resources with specialized expertise in ESG risk assessment, environmental impact analysis, and methodologies for verifying sustainability claims.[67] Collaboration with international organizations and financial supervisory authorities in other jurisdictions can facilitate the transfer of knowledge and the adoption of best practices in sustainable financial supervision. Additionally, the use of technologies such as artificial intelligence and big data analytics can enhance the efficiency of supervisory processes through the automated detection of patterns indicative of greenwashing practices in sustainability reporting.[68]

CONCLUSION

This study finds that the legal framework governing the supervision of sustainable finance by the Otoritas Jasa Keuangan (OJK) remains insufficient to effectively prevent greenwashing practices in Indonesia's banking sector. The absence of a comprehensive green taxonomy, the lack of mandatory verification mechanisms, and weak disclosure standards create significant regulatory gaps that allow misleading sustainability claims to persist. In addition, the effectiveness of OJK's supervisory authority is constrained by limited ESG assessment capacity and the lack of clear and enforceable legal standards, resulting in weak implementation of both preventive and repressive supervisory functions.

From a normative perspective, these findings highlight the need for a shift from a principle-based regulatory approach toward a more rule-based framework supported by measurable standards and enforceable obligations. Strengthening legal certainty through the development of a binding green taxonomy, the implementation of independent verification mechanisms, and the establishment of proportionate administrative sanctions is essential to enhance the credibility of sustainable finance. These measures are

[66] Merliyana, "The Role of Governance and Regulation in Shaping ESG Disclosure Quality."
[67] Firmansyah and Puspitasari, "Sustainable Finance and Green Banking Disclosure: Unlocking Firm Value Potential."
[68] Sneideriene and Legenzova, "Greenwashing Prevention in Environmental, Social, and Governance (ESG) Disclosures: A Bibliometric Analysis."

crucial not only to prevent greenwashing practices but also to ensure that financial resource allocation genuinely contributes to achieving sustainable development goals and Indonesia's carbon neutrality target.

This study is limited by its normative legal approach without empirical validation, its focus on the banking sector, and the absence of in-depth cross-jurisdictional analysis. Future research is therefore recommended to incorporate empirical methods, expand sectoral coverage, and conduct comparative studies to evaluate the effectiveness of regulatory reforms in preventing greenwashing practices.

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