



Legal Issues Surrounding Financial Technology Industry in Indonesia

Dona Budi Kharisma^a, Jamal Wiwoho^b, Pujiyono^c, ^{a,b,c}Faculty of Law, Universitas Sebelas Maret (UNS) Surakarta, Indonesia, Email: [donabudikharisma@staff.uns.ac.id](mailto:^adonabudikharisma@staff.uns.ac.id)

Financial Technology (FinTech) industry in Indonesia has seen a rapid growth. In 2019, the value of Indonesia's digital economy reached USD 40 billion. As of early 2020, Indonesia Financial Services Authority (OJK) has 161 fintech companies registered and licensed to operate under its supervision. Data from Bank of Indonesia (BI) recorded 51 payment companies in Indonesia, the majority of which offer peer-to-peer lending, digital payment, and crowdfunding services. Despite this growth, a clear legal framework is still absent in the industry. As of today, it is regulated with the Regulation of the Financial Services Authority (POJK) but has not been regulated in the Indonesian Law. As secondary legislation, POJK has a weaker legal power. This results in several significant flaws in the industry's legal certainty and consumer protection. This article aims at elaborating various legal issues surrounding Indonesia's fintech industry and at constructing a legal framework that can propel the growth of the digital economy and strengthen consumer protection in Indonesia.

Key words: *legal issues; financial technology*

Introduction

Digital technology has brought about massive changes in financial services. Innovations have been made to improve service time, ease of access, efficiency, and effectiveness in the industry. The amalgamation of financial services and technology birthed the term "financial technology" or fintech.

Kelvin Leong and Anna Sung define fintech as "any innovative ideas that improve financial service processes by proposing technology solutions according to different business situations, while the ideas could also lead to new business models or even new businesses" (Kelvin Leong & Anna Sung, 2018:75). Bank of Indonesia Regulation number 19/12/PBI/2017 on the Implementation of Financial Technologies which defines fintech as "the use of technology in a financial system that produces new products, services, technologies, and/or business

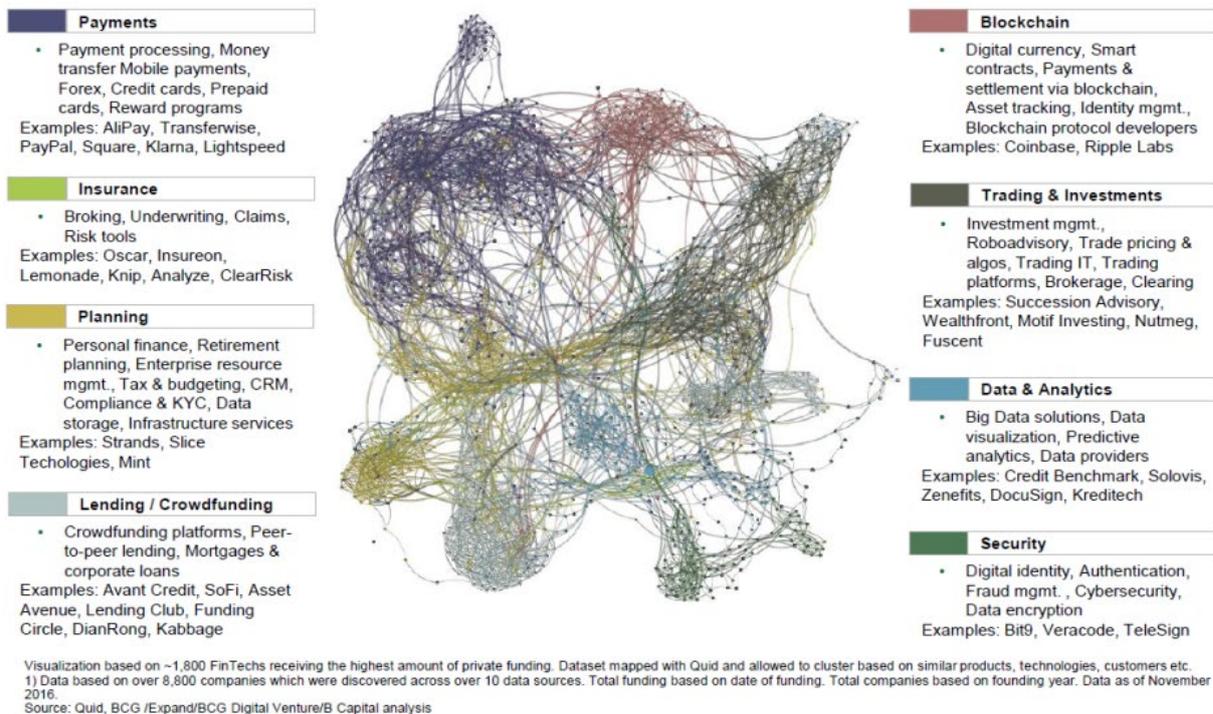
frameworks that can affect the stability of the monetary system, financial system, and/or the efficiency, stability, security, and reliability of payment systems.”

There are at least two key elements in fintech: innovative business models and new technologies. The first element is reflected in the way fintech companies offer more than one specific, automated online financial products and services. Through the internet, fintech companies provide various financial services otherwise found in traditional banking, brokerage, and investment management services. Fintech allows the emergence of equity crowdfunding platforms offering stocks, peer-to-peer lending providing easier access to loans, and Robo-advisors giving automated investment management advice. Fintech also relies heavily on the use of new technologies such as cognitive computing, machine learning, artificial intelligence, and distributed ledger technologies (DLT). It has created direct changes in the monetary and financial services (IOSCO, 2017: 4) (Svetlana Saksonova & Irina Kuzmina-Merlino, 2017: 962).

Fintech can be mapped across eight categories: payments, insurance, planning, lending/crowdfunding, blockchain, trading and investments, data and analytics, and security (A. Fraile Carmona et al, 2018: 11). Figure 1 illustrates the fintech landscape.

Figure 1. Fintech Landscape (IOSCO, 2017: 4-5)

The global FinTech landscape can be mapped across 8 broad categories



The Indonesian fintech industry ranked 47th globally. The value of the Indonesian digital economy in 2019 reached USD40 billion, or approximately IDR568 trillion. Indonesia’s e-commerce in 2019 reached a value of USD20.9 billion (approximately IDR308 trillion). The

large population of the country—placing fourth globally only after China, USA, and India and as the 16th world’s largest economies—also contributes to the rapid growth of fintech. The Internet penetration rate in Indonesia is quite high, reaching 65.3% of the total population, which means that 171 million people in the country use the internet (Wimboh Santoso, 2020).

With fintech’s huge economic potential, however, comes potential high risks (Dona Budi Kharisma & AL Sentot Sudarwanto, 2020: 1735). Its growth is disrupted by the surge of illegal companies, system failures, misinformation, transaction errors, data security concerns, implementation of know-your-customer (KYC) principles, a high interest rate, exoneration clauses, and inappropriate customer complaint handling procedures. Without proper mitigation, these potential high risks can have dire effects on financial stability, consumer protection, and the growth of the fintech industry itself (The Financial Stability Board (FSB), 2017: 14-15).

Fintech innovates at every step, often through a new value proposition such as flexible products (Ambar Budhisulistiyawati et al, 2020:1780) and a better way to address the challenges faced by, say, SMEs who have difficulty getting access to financing or low-income users. Fintech also makes financial services more affordable (Pujiyanti Fauziaha, 2019: 209) and accessible; Improve customer experience and accelerate usage and engagement; Build foundations — including digital identity verification for easier, collaborative customer due diligence, data sharing, and payment schemes — that can accelerate a number of financial services (Akeel Almagtome, 2019: 204).

These issues provide the background for this article, which aims at identifying various legal issues surrounding the fintech industry in Indonesia. It is important to come up with legal mitigations for stakeholders to prevent potential risks in the industry threatening monetary stability and to strengthen consumer protection regulations in Indonesia. This article will also suggest a legal framework for the country’s fintech industry as a consumer protection strategy that can also boost the growth of the digital economy in Indonesia.

Research Methods

This article is a result of normative legal research. Data were collected through literature study and document observation. The study found its juridical footing in (1) The 1945 Constitution of the Republic of Indonesia (UD NKRI 1945); (2) Law No. 8/1999 on Consumer Protection; (3) Law No. 11/2008 on Electronic Information and Transactions, as amended by Law No. 19/2016; (4) Law No. 23/1999 on the Bank of Indonesia and its updates in Law No. 6/2009; (5) Law No. 12/2011 on the Formulation of Law and Regulations, amended by Law No. 15/2019; (6) Law No. 21/2011 on the Indonesia Financial Services Authority (OJK); (7) Government Regulation in Lieu of Law No. 71/2019 on the Implementation of Electronic Systems and Transactions (PTSE); (8) POJK No.1/POJK.07/2013 on Consumer Protection in Financial Services Sector; (9) POJK No.77/POJK.01/2016 on Information Technology-based

Lending; (10) POJK No. 38/POJK.03/2016 on the Application of Risk Management in the Use of Information Technology by Commercial Banks; (11) POJK No. 13/POJK.02/2018 on Digital Financial Innovation in the Financial Services Sector; (12) POJK No. 37/POJK.04/2018 on Equity Crowdfunding; (13) PBI No.19/12/PBI/2017 on the Implementation of Financial Technology; and (14) PBI No. 20/6/PBI/2018 on Electronic Money (E-Money).

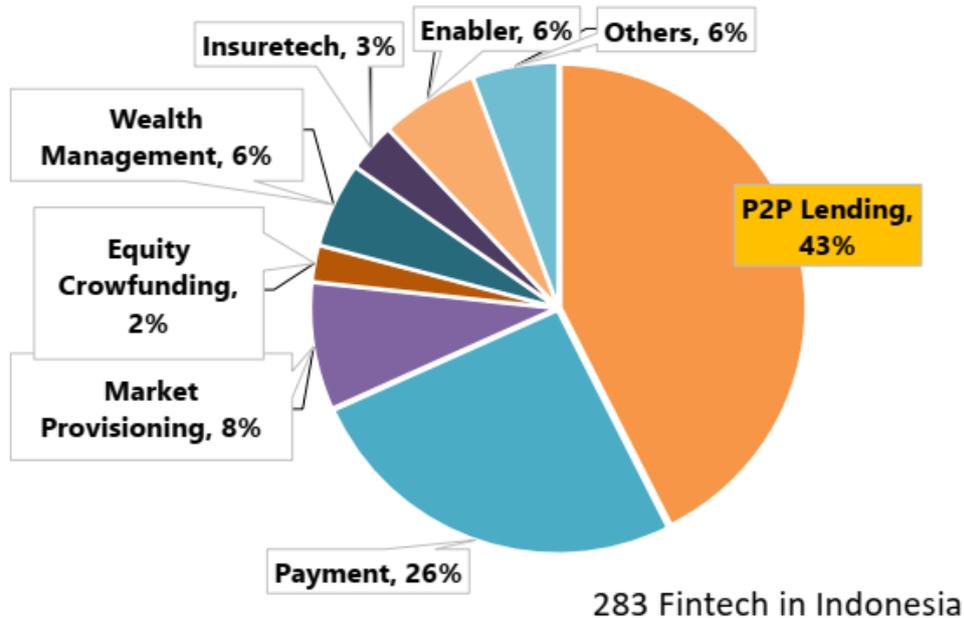
This descriptive research aims to provide a systematic, factual, and accurate description of certain features, characteristics, or factors in a particular population or region. It employs a qualitative juridical analysis based on legal interpretation, reasoning, and argumentation. This research describes issues in the regulations of the Indonesian fintech industry and analyzes the urgent need for sounder policies reviewed from philosophical, juridical, and sociological points of view. It also aims to formulate a regulatory framework for the fintech industry as a strategy to strengthen consumer protection laws and advance the growth of the digital economy in Indonesia.

Result and Discussion

1. Challenges for Fintech Industry in Indonesia

Each year, fintech companies in Indonesia see an increase in growth. In 2015-2016, the Indonesian Fintech Association (AFI) declared a 78% growth of fintech companies. As of November 2016, there were 103 startup fintech companies registered under AFI. In 2019, there were 283 fintech companies registered with OJK and BI; out of them, 43% were in the peer-to-peer lending sector, 26% in payments, 8% in market provisioning, while the rest were in equity crowdfunding, wealth management, insurtech, and many other sectors, as illustrated in Figure 2.

Figure 2. Overall Distribution of Fintech Services in Indonesia in 2019 (Wimboh Santoso, 2020)



When further categorized by the supervising authority, data from BI show that as of 2020, there are 51 fintech companies offering payments services (Bank Indonesia, 2020). Data from OJK as of February 19, 2020, also recorded 161 companies (136 registered and 25 licensed) operating with its supervision. By ownership status, 110 fintech companies run on local funds and 51 on foreign funds (OJK, 2020).

However, despite this promising growth, fintech companies in Indonesia face various challenges. **First**, the potential and development of Fintech in Indonesia needs to be supported by a strong and clear legal framework. In addition to overcoming the legal vacuum, the Fintech Law provides legal certainty and becomes a means of legal protection for consumers, investors and business people. This is because Indonesia is the 4th most populous country in the world after China, America and India, which are included in the World's 16th largest economy. Indonesia's population has a fairly high internet penetration, 171 million people, or 65.3% of the Indonesian population who use internet connections. Indonesia's Fintech Industry occupies position 47 in the World. The value of Indonesia's digital economy in 2019 will reach USD 40 Billion or approximately equivalent to 586 Trillion Rupiah. E-Commerce value in Indonesia in 2019 has reached USD 20.9 Billion or approximately equivalent to 308 Trillion Rupiah. In 2019 Fintech had registered 283 in the OJK and BI.

The second challenge is the large number of disputes in the industry. As of February 2019, Jakarta Legal Aid Institute (LBH) had received approximately 3,000 customer complaints related to fintech. The Indonesian Joint Funding Fintech Association (AFPI) had also received 426 complaints reporting 510 p2p platforms throughout January to March 2019. The majority

of the complaints reported the lack of sufficient and transparent information given by companies about the whole lending process, such as information about the interest rates and administration fees. The charging and billing process for these fees is reported to involve various criminal offenses including defamation, fraud, intimidation, the spread of personal and private information, even sexual harassment (Hukumonline, 2020).

The third issue is the surge in illegal fintech practices. Data from the Investment Alert Task Force (Satgas Waspada Investasi) recorded 2,018 illegal p2p lending companies, 472 illegal investment companies, and 69 illegal mortgage lenders (Wimboh Santoso, 2020). If these issues are left unattended, consumer protection in Indonesia could collapse. Improper fintech business management increases liquidity risks and could even lead to a financial crisis.

2. Legal Vacuum Surrounding the Fintech Industry in Indonesia

The Indonesian Law has specifically regulated most financial industries in the country, but the fintech industry has yet to have its own set of rules. They are Law on Capital Market (No. 8/1995), Law on Banking (No. 7.1992, amended in No. 10/1998), and Law on Insurance (No. 40/2014). The Law on Bank of Indonesia, Law on Banking, and Law on OJK have yet to touch upon the intricacies of the fintech industry. This legal vacuum surrounding the Indonesian fintech industry is a situation the government needs to address promptly. The best step is to construct a national Law on Fintech that ensures the industry's legal certainty and strengthens existing consumer protection regulations.

Today, existing regulations on the Indonesian fintech industry are issued in the Bank of Indonesia Regulations (PBI) and Indonesia Financial Services Authority Regulations (POJK). Some of them are (1) PBI No.19/12/PBI/2017 on the Implementation of Financial Technology; (2) PBI No. 20/6/PBI/2018 on E-Money; (3) POJK No. 77/POJK.01/2016 on Information Technology-based Lending; (4) POJK No. 13/POJK.02/2018 on Digital Financial Innovation in the Financial Services Sector; (5) POJK No. 37/POJK.04/2018 on Equity Crowdfunding.

Regulations issued by the Bank of Indonesia and Indonesia Financial Services Authority covering the fintech business have significant weaknesses, due to their position as secondary legislation. **The first weakness** is that PBI and POJK cannot stipulate criminal provisions. Despite having a permanent, recognized, and a legally binding existence, PBI and POJK cannot contain criminal provisions, as stated in Articles 8 and 15 of Law No. 12/2011 on the Formulation of Law and Regulations. This means that these regulations cannot resolve illegal practices and criminal offenses of fintech companies even though they are registered with and licensed by BI or OJK. This is why the government needs to formulate a law on fintech that also covers criminal provisions to resolve these issues.

The second weakness is that the establishment of POJK and PBI has no element of people's sovereignty. POJK and PBI were formed unilaterally by OJK and BI based on their authority without involving political infrastructure. In contrast to the Law established by the Parliament and the Government as representatives of the people who do have legislative rights so that the elements of people's sovereignty are fulfilled. The involvement of political infrastructure as the embodiment of the elements of popular sovereignty is important so that the material content of the legislation formed is more comprehensive and in line with the legal needs of the community.

Financial Service Authority establishes a policy that every financial services sector has one *LAPS*. This institution is needed if the dispute resolution agreement is not reached between the consumer and the *LJK*. In line with the characteristics and developments in the financial services sector that are ever-fast, dynamic, and full of innovation, *LAPS* in the financial services sector requires fast, low-cost procedures (Marzukia, 2020: 172-173), and with an objective, relevant, and fair outcome. The settlement of disputes through these institutions is confidential so that each party is more comfortable in performing the dispute resolution process and does not take a long time because it is designed by avoiding procedural and administrative slowness (Ikhsan, Arfan, 2019: 159-171).

The third weakness is that without a sound law on fintech, the industry, as a part of the digital economy ecosystem of Indonesia, lacks risk mitigation procedures. Law on fintech that stipulates risk mitigation strategies need to be formulated alongside the existing infrastructures, financial literacy, surveillance, consumer protection, and licensing and supervision regulations. Indonesia needs a law on fintech that can provide legal protection for the government, involved authorities, private companies, and consumers to oversee make sure that the fintech industry in Indonesia is going in the right direction, creating a stable and ever-growing digital economy.

An effort to strengthen all the involved authorities should aim to prevent systemic risks and manage the financial crisis so that the national economy remains at sustainable growth. Law on fintech should lay down the rights and responsibilities of all the involved institutions as a form of supervision. Indonesia needs a legal foundation that regulates the coordination between agencies and involved parties, prevent as well as manage a crisis that may arise from liquidity and solvability problems that the fintech business might face.

3. The Absence of Alternative Dispute Resolution (ADR) Agency in the Fintech Sector

In fintech industry, disputes have a high potential of occurring. The number of complaints about fintech services reflects the frequency of disputes surrounding the industry. This demands a detailed and effective dispute resolution mechanism. However, dispute resolution efforts through litigation processes have some significant weaknesses; the process is lengthy and expensive. There is also the issue of 'judicial mafia' in the Indonesian court. The



government needs to come up with a quicker, more accessible, just, efficient, discrete mechanism.

Non-litigation processes are in line with the current development and innovation in financial services. From an economic standpoint, a dispute settlement process designed to be quick and affordable benefits all the parties involved. Skilled, arbitrary mediators in ADR agencies will be able to ensure that the process is carried out in the justest, most objective, and relevant manner. A non-litigation process also guarantees the privacy and discretion of the involved parties, appealing to the “discrete” and “private” nature of business. Parties in dispute do not have to worry about the risks of defamation or leaked personal information, allowing for a more effective and unhindered settlement process.

In the Indonesian financial service sector, there are six existing alternative dispute resolution agencies: (1) Indonesia Insurance Mediation and Arbitration Agency (BMAI); (2) Indonesia Capital Market Arbitration Agency (BAPMI); (3) Indonesia Pension Fund Mediation Agency (BMDP); (4) Indonesia Alternative Banking Dispute Resolution Agency (LAPSPI); (5) Indonesia Loan Company Arbitration and Mediation Agency (BAMPPI); and (6) Indonesia Funding and Pawnbroker Mediation Agency.

The establishment of ADR agencies is an effort to strengthen existing consumer protection procedures. They facilitate dispute resolution for consumers of banking and financial services (Dona Budi K, 2019: 213). The source of regulation for these agencies is POJK No.1/POJK.07/2014 on Alternative Dispute Resolution Agencies in the Financial Service Sector (POJK LAPS). In the regulation, it is stated that ADR agencies are formed to facilitate a quick, affordable, just, and efficient dispute resolution between the financial service company and the consumer. ADR agencies work by the principles of accessibility, independence, fairness, efficiency, and effectiveness.

ADR agencies specifically meant to meet the needs and emerging issues in the Indonesian fintech sector are still absent. From a sociological point of view, the rapid growth and significant potential of the country’s fintech industry, the high number of disputes that follow, and consumers’ need for a quick, easy, fair, efficient, and discreet dispute resolution mechanisms are enough reason for the formation of ADR agencies specifically meant for the industry. Facilitating dispute resolution and warranting consumer protection are responsibilities that the government needs to fulfill.

Disputes in fintech services require dispute resolution mechanisms that are easy, fast, fair, efficient and confidential. This is in line with technological developments and financial service innovations. From the economic side, the dispute resolution process that is designed quickly and at low cost will be very beneficial for the parties. In addition, the settlement completed through LAPS is carried out by mediators and arbiter who have expertise, so that they can

produce fair, objective and relevant decisions. Dispute resolution outside the court also guarantees the confidentiality of the parties. The nature of secrecy is identical to the nature of "privacy" in business law. The parties to the dispute are still maintained their good name in the business world so that each party to the dispute is more comfortable in carrying out the settlement process.

The legal basis for the establishment of LAPS in the Fintech industrial sector originates in Article 28D paragraph (1) of The 1945 Constitution of the Republic of Indonesia (UD NKRI 1945). Article 28D paragraph (1) affirms that: Everyone has the right to recognition, guarantee, protection, and certainty of legal justice and equal treatment before the law . In business interactions between consumers and Fintech organizers, the potential for dispute is inevitable. As consumers, there are often differences in understanding of a product, on the one hand from the side of the organizer Fintech often does not heed the provisions of consumer protection laws. Therefore, to facilitate the differences in understanding, LAPS is needed so that public trust is maintained and digital economic value continues to increase. Thus, the formation of the Fintech LAPS is a form of constitutional mandate that must be realized immediately.

Law No. 30/1999 on Arbitration and Alternative Dispute Resolution (Arbitration Law and APS) also forms the legal basis for the establishment of LAPS in the Fintech industrial sector. LAPS is an alternative dispute resolution mechanism mandated in the Arbitration Law and APS. Article 1 point 10 of the Arbitration Law and the APS defines an alternative dispute resolution as a dispute resolution agency or dissent through a procedure agreed by the parties, namely settlement outside the court by means of consultation, negotiation, mediation, conciliation, or expert judgment. In principle, disputes or civil dissent can be resolved by the parties through alternative dispute resolution based on good faith by ruling out litigation settlement in the District Court.

The rapid growth and huge potential of fintech in Indonesia have to be supported by agencies that can carry out dispute resolution through non-litigation processes. Not only will these agencies strengthen the existing efforts in ensuring consumer protection, but they will also increase the public's trust in the industry, as well as provide legal protection for consumers, investors, and fintech companies. Indonesia's huge potential in the fintech industry, as the world's fourth-largest economy, furthered by the country's high rate of internet penetration, will propel the country's economy into new heights if managed and regulated properly. This is why ADR agencies for the fintech industry is crucial in ensuring consumer protection, conduciveness of business, the climate of investment in Indonesia.

Conclusion

The lack of national law governing the fintech industry in Indonesia is an urgent issue that can seriously affect the growth of the digital economy ecosystem. Moreover, the absence of



alternative legal aid agencies that focus on resolving fintech-related disputes is also a pressing matter in consumer protection efforts. These problems result in legal uncertainty and flawed consumer protection laws that greatly encumber the development of the Indonesian fintech industry. Therefore, the Indonesian government needs to issue a sound regulatory framework, i.e. Law on Fintech, as well as establish an alternative agency for dispute resolution dedicated for the fintech sector for a more conducive and secure digital economy that can contribute more to the growth of Indonesia's financial market and economy.



REFERENCES

Book and Journal

- Almagtomea, Akeel, et al. "The Integration between Financial Sustainability and Accountability in Higher Education Institutions: An Exploratory Case Study." *International Journal of Innovation, Creativity and Change (IJICC)*, Volume 8, Issue 2, (2019), page 204.
- A. Fraile Carmona, A. González-Quel Lombardo, R. Rivera Pastor, Tarín Quirós, Villar García, Ramos Muñoz, Castejón Martín, Competition issues in the Area of Financial Technology (Fintech), Directorate General For Internal Policies Policy Department a: Economic And Scientific Policy, European Parliament, Juli 2018.
- Ambar Budhisulistiyawati, Dona Budi Kharisma, and Anjar Sri Ciptorukmi Nugraheni, The Role Of Cooperatives In Indonesian Creative Economy, *International Journal of Advanced Science and Technology* Vol. 29, No. 4, 2020.
- Dona Budi Kharisma, Meneropong Masa Depan LAPSPI Dalam Penyelesaian Sengketa Perbankan di Indonesia, *Buletin Hukum Kebanksentralan*. Volume 16, Nomor 2, Juli - Desember 2019.
- Dona Budi Kharisma and AL Sentot Sudarwanto, Market Trader Cooperatives (MTCS) as The Center of Food Commodity Distribution at Traditional Markets, *International Journal of Advanced Science and Technology* Vol. 29, No. 4, 2020.
- Kelvin Leong and Anna Sung, Fintech (Financial Technology): What is It and How to Use Technologies to Create Business Value in Fintech Way?, *International Journal of Innovation, Management and Technology*, Vol. 9, No. 2, April 2018.
- Marzukia, Marzuki, and Nurdin Nurdinb. "The Influence of Halal Product Expectation, Social Environment, and Fiqih Knowledge on Intention to Use Shariah Financial Technology Products." *International Journal of Innovation, Creativity and Change*, Volume 13, Issue 1, (2020), page. 172-173
- Ikhsan, Arfan, "The Effect of Islamic Work Ethics and Organisational Cultural Motivation on OCB and Employee Performance at Bank Aceh Syariah". *International Journal of Innovation, Creativity and Change (IJICC)*, Volume 9, Issue 4, (2019). page. 159-171.
- International Organization of Securities Commissions (IOSCO), IOSCO Research Report on Financial Technologies (Fintech), 2017.
- Fauziaha, Pujiyanti, and Ratna Candra Sarib. "The Development of a Financial Literacy Questionnaire for Early Childhood." *International Journal of Innovation, Creativity and Change (IJICC)*, Volume 7, Issue 7, (2019), page. 209
- Svetlana Saksonova and Irina Kuzmina-Merlino, Fintech as Financial Innovation – The Possibilities and Problems of Implementation, *European Research Studies Journal* Volume XX, Issue 3A, 201



Wimboh Santoso Ketua Dewan Komisioner OJK, Fintech and The Future of Finance, Presented at the International Fintech and The Future of Finance Seminar at Sebelas Maret University Surakarta, Thursday, 12 March 2020.

Internet

Data on Providers of Financial Technology that have registered at Bank Indonesia, accessed at <https://www.bi.go.id/id/sistem-pembayaran/fintech/Pengumuman-Penyelenggara/Contents/default.aspx> access date April 25, 2020, 6:13.

Directorate of Fintech Regulation, Licensing and Supervision of the Financial Services Authority (OJK), Profile and Development of Fintech Lending in Indonesia, February 2020 Data. Accessed at <https://www.ojk.go.id/id/kanal/iknb/data-dan-statistik/fintech/Documents/Perkembangan%20Fintech%20Lending%20Periode%20Februari%202020.pdf> access date April 25, 2020, 06: 40.

Fintech Legal Developments and Issues, accessed at <https://www.hukumonline.com/berita/baca/lt5c9b2221dcb1c/perkembangan-dan-permasalahan-hukum-fintech/> access date 25 April 2020, at 10:22.