

# Model of business activities of microfinance institutions in Indonesia

Etty Mulyati<sup>1</sup> and Nun Harieti<sup>2</sup>

<sup>1</sup> Padjadjaran University. Faculty of Law, Bandung 40132, Indonesia  
Email: ettymulyati@gmail.com

<sup>2</sup> Padjadjaran University. Faculty of Law, Bandung 40132, Indonesia  
Email: nunharieti@gmail.com

**Abstract.** Micro Finance Institutions as non-bank financial institutions are growing very rapidly in Indonesia. A very large number and scope of business in villages/sub-districts and sub-districts or districts can play a role in an inclusive financial program. The existence of micro finance institutions operation helps to expand employment, improve the welfare, and improve the economy and productivity of the people, especially low-income communities. The problem is how to model the business activities of micro finance institutions in Indonesia. This research will use normative juridical approach method, with analytical descriptive research specification. In an effort to provide financial services, which are intended for low-income communities who do not have access to bank financial institutions, micro finance institutions can bridge the problems of micro business access to capital needed in business development. Micro finance institutions have a different character from the other financial sector businesses, because it is not solely intended for profit. Micro finance institutions business activities can be done with a conventional or sharia model, including loan/financing for micro enterprises for capital needs in business development and management of deposits in an effort to bring awareness to the community's fond of saving. Besides, micro finance institutions can also provide consulting services for the purpose of business development for community empowerment. To provide legal certainty for the micro finance institutions service to the user community, micro finance institutions are regulated in micro finance institutions. Laws, according to the law the micro finance institutions, must be a legal entity of the Cooperative or Limited Liability Company. Fostering, regulating, and supervising and licensing of micro finance institutions are performed by the Financial Services Authority.

**Keyword:** Micro Finance Institutions, micro business, Financial Services Authority

## 1. Introduction

Implementation of economic development in addition to aiming to increase national income, is also aimed at accelerating job growth and reduction of unemployment rate so that it can solve the problem of poverty. Development in the economic field has an impact on the development of business in Indonesia: big business, medium business, small business, and especially micro business. Micro-enterprises are the most influential sectors to the development of national economy and provide broad economic services to the community. The function and role of small-scale enterprises is very large in the economic activities of the community, including: Provision of goods and services; Employment; Equity of added value added for regional products; and Increasing standard of living (1).

Graph of business deployment in Indonesia stated that UMKM dominates 99.75 percent, and only 0.19 percent of it is a large-scale business. The dominance of micro business scale is 83.27 percent as many as 18.933 million business and 15,81 percent small business (2). Bank Indonesia notes some of the strategic roles of the small business, among them: 1) the large number and is present in every sector of the economy, 2) the huge potential in employment as every investment in the small business sector can create more employment opportunities than the same investment in the business Medium / large, and 3) the ability to utilize local raw materials and produce goods and services needed by the community at an affordable price (3).

In order to encourage the empowerment of micro enterprises, comprehensive support from financial institutions is required. To overcome the constraints of access to finance to formal financial institutions, the community has grown and developed many non-bank financial institutions that conduct business development services and community empowerment activities, either established by the government or the community. These institutions are known as Micro Finance Institutions (MFIs). MFI is a profit-motivated institution that is also a social-motivated, whose activities are more community development without disregarding its role as a financial intermediary institution (4). As an institution that has a function as an intermediary, MFI also conducts savings and loans activities, which aside from providing loans is also required to provide awareness of savings to the community, especially low income people (4). The existence of this MFI provides a good impact to the community doing micro business, helping to increase economic empowerment and community productivity in developing its business activities. The MFI is an effort to provide financial services, especially savings, loan or financing management, and other financial services intended for poor and low-income families who do not have access to commercial banks (5).

In order to provide a strong legal basis and legal certainty over the operationalization of MFIs, Law No. 1 Year 2013 has been enacted on Microfinance Institutions (MFI Act). The need for MFI legislation, considering the Banking Law, stipulates that any party engaging in fund raising activities from the public in the form of savings must first obtain a business license as a Commercial Bank or Rural Bank from the Management of Bank Indonesia (now the authority of the Financial Services Authority), unless the activities of collecting funds from such public are governed by a separate law.

Institutions that run the MFI's business are numerous but not yet incorporated and do not yet have a business license, as mandated in the MFI's Law. A large and diverse number of different types of MFI services as well as a wide range of business areas. The problem is how to model business activities and regulate and supervise MFIs in Indonesia.

## **2. Methodology**

Approach method used is normative juridical approach method, which includes research of positive law inventory, research on law principles and law research in concrete, systematic research of law, research of law history and comparison of law (6). This research examines the data of the library or secondary data obtained from libraries and related institutions that are competent with this research. As normative legal research, research on secondary data is in the form of primary legal materials, secondary law materials, and tertiary legal materials (7). This research will examine about the legal aspects of the model of MFI activities in Indonesia, especially on legal issues that have been identified.

## **3. Findings**

MFIs have a different character from other financial sector businesses. The presence of MFIs is not only for profit, but also increases the income and welfare of the people and helps to increase economic empowerment and productivity of the community by facilitating the poor and low income people, especially micro businesses. This is seen through the type of MFI business activities that include loans or financing in micro-scale enterprises, savings management, and business development consulting services that estuary of all is community empowerment. In its development MFIs may also engage in fee-based business activities as long as they do not conflict with the provisions of legislation in the financial services sector. MFIs conducting business based on Sharia Principles can manage the social funds and the virtues of zakat, infaq, alms and waqfs in accordance with applicable laws and regulations. Bookkeeping on the management of social and benevolent funds is done separately, from savings accumulation activities and disbursement of Financing which is the main activity of the MFI concerned.

The MFI must have a business license from OJK, subject to the following minimum requirements: Organizational structure and management; Capital; Ownership; And Feasibility of the

work plan. In addition, the provision of business licenses for institutions that have operated before the MFI Act with the inauguration of the MFI. The institutions that are required to obtain business licenses through Inauguration as MFIs to OJK are: Village Bank, Village Lumbung, Market Bank, Employee Bank, Village Credit Board (BKD), Kecamatan Credit Board (BKK), Small People Business Credit (KURK), Sub-district Credit Agencies (LPK), Village Production Work Banks (BPR), Baitul Maal wa Tamwil (BMT), Baitul Tamwil Muhammadiyah (BTM), and / or other equivalent institutions which have been established and have been operating prior to the enactment of the MFI Act, and have not obtained a business license under applicable laws and regulations. OJK provides an additional grace period, as well as providing convenience such as applying for a non-cash initial capital deposit. As of early February 2016, there have been 34 MFIs already licensed. The number increased significantly because on January 8, 2016 newly registered 20, MFIs are entirely in the form of cooperative legal entities.

While Lembaga Perkreditan Desa and Lumbung Pitih Nagari and similar institutions that have existed before the MFI Act apply, are declared to be recognized based on customary law and not subject to MFI Law. Considering that an adat village is an autonomous government entity, it is feared that this regulation will reduce the authority of indigenous villages in the management of their financial institutions. The form of an MFI's Legal Entity is a Cooperative or Limited Liability Company (PT), and the ownership of an MFI may only be owned by an Indonesian Citizen, a Village-Owned Enterprise, Regency / City Government; And / or Cooperatives. MFIs are prohibited to be owned directly or indirectly, by foreign nationals and / or entities that are partly or wholly owned by foreign nationals or foreign business entities. MFI supervision, regulation and supervision is conducted by OJK. Guidance and supervision is delegated to the Regency / City Government. In the framework of the implementation of supervisory and supervisory functions, OJK may conduct examination of MFIs and OJKs may conduct direct examination of MFIs individually or jointly with District / City Government or other designated parties.

The scope of the business area of an MFI is located within one village / sub-district, sub-district, or district / municipality area according to the business scale of each MFI. The MFI's business scale is determined on the basis of the borrower or financing customer distribution, i.e. the MFI that has the business scale of the village / kelurahan if providing loans or financing to the population in 1 (one) village / kelurahan; and MFIs have the scale of the kecamatan business if they provide loans or financing to the population in 2 (two) villages / kelurahan or more in 1 (one) same sub district; MFIs have district / city business scale if they provide Loans or Financing to residents in 2 (two) sub-districts or more within 1 (one) same regency / municipality. An MFI intending to expand its business territory is obliged to adjust its business license in accordance with the scope of the new business area.

The capital to establish an MFI consists of paid up capital for an MFI or a principal savings, mandatory savings, and a grant for an MFI with a legal entity cooperative. The amount of paid up capital or principal savings, mandatory savings, and MFI grants is set at least: 50,000,000.00 (fifty million rupiahs), for an MFI within the scope of the village / kelurahan business area; 100,000,000.00 (one hundred million rupiahs), for an MFI with coverage of the kecamatan business area; Or Rp 500,000,000.00 (five hundred million rupiahs), for an MFI with coverage of the district / city business area. At least 50% must be used for working capital.

The MFI is obliged to transform into a rural credit bank or sharia financing bank when conducting business activities in excess of 1 (one) regency / municipality in which the MFI's position, or an MFI has an Equity of at least 5 (five) times of the minimum paid up capital requirement of the RB or SRB. In accordance with the provisions of laws and regulations, and the amount of third party funds in the form of deposits collected in the last 1 (one) year at least 25 (twenty five) times of minimum paid up capital requirement of RB or SRB in accordance with the provisions of legislation.

MFIs may be dissolved, in the event that the MFI's effort does not solve the liquidity and solvency problems in the MFI's business, the OJK will revoke the MFI's business license and instruct the MFI Board to immediately hold a general meeting of shareholders or member meetings to dissolve the legal entity MFI and form a liquidation team. The liquidation team is tasked with completing the rights and obligations of the MFI. Dissolution of the MFI's legal entity, the formation of a liquidation team, and the settlement of rights and obligations are carried out in accordance with the legislation. The liquidation team shall submit a report on the progress of liquidation implementation to OJK at least 1 (one) time in 6 (six) months. It will also report the implementation of liquidation to shareholders or members, and OJK, no later than 3 (three) months from the date of completion of the liquidation exercise.

In the framework of the implementation of supervisory and supervisory functions, OJK may conduct an Examination of MFIs and Direct Investigation of MFIs individually or jointly with District / City Government or other appointed parties. Any MFI that violates the terms may be liable to: Fines of money; Written warning; Suspension of business; Dismissing the board of directors or the board of the MFI and subsequently appointing and appointing a temporary replacement until the General Meeting of Shareholders or Meeting of Cooperative Members appoints a permanent replacement with OJK approval; Or revocation of business license. The imposition of such administrative sanctions is in accordance with the level of violations committed by the MFI.

#### 4. Conclusion

In an effort to provide financial services, which are intended for low-income communities who do not have access to bank financial institutions. MFIs can bridge the problems of micro-enterprise access to capital needed in business development. MFIs have a different character from other financial sector businesses, because they are not solely aimed at making a profit. MFI business activities can be done in a conventional or sharia-based manner, including loans / financing in a micro-scale enterprise for capital needs in business development, and savings management as an effort to provide awareness to the public to enjoy saving, while the MFI also provides business development consultancy services. The goal is community empowerment. To provide legal certainty for the MFI service user community, MFI institutions are regulated in MFI Laws, according to the law the MFI must be a legal entity of the Cooperative or Limited Liability Company. The supervision, arrangement, and supervision and permission of MFIs is done by OJK. If conducting business activities beyond a regency / municipality territory or having met the requirements stipulated in the Financial Services Authority Regulation, the MFI shall transform into a Rural Bank (BPR).

#### 5. References

- [1] Sumitro S 2003 *Analisis Ekonomi Jawa Barat* (Bandung: Unpad Press) p 270
- [2] Statistics Center Indonesia *Statistic of Indonesia*
- [3] Bank Indonesia 2001 *Sejarah Peranan Bank Indonesia dalam Pengembangan Usaha Kecil* (Jakarta: Biro Kredit, Bank Indonesia)
- [4] Baskara I G K 2013 Lembaga Keuangan Mikro di Indonesia *J Bul Stud Ekon.* **18** (2) 115.
- [5] Arsyad L 2008 *Lembaga Keuangan Mikro, Institusi, Kinerja dan Sustainabilitas* (Yogyakarta: Andi) p 1
- [6] Soemitro R H 1990 *Metodelogi Penelitian Hukum dan Jurimetri* (Jakarta: Ghalia Indonesia) p 9-10
- [7] Soekanto S and Mamudji S 2006 *Penelitian Hukum Normatif suatu Tinjauan Singkat* (Jakarta: Rajawali) p 13-14

Reproduced with permission of copyright owner. Further reproduction prohibited without permission.