

# Application of Equity Crowdfunding as an Alternative to MSME Business Funding in Indonesia

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DOI: <https://dx.doi.org/10.47772/IJRISS.2023.701037>

Received: 13 September 2023; Revised: 25 September 2023; Accepted: 29 September 2023; Published: 30 October 2023

## ABSTRACT

During the Covid 19 pandemic that hit Indonesia, the development of MSMEs increased by 60%. This business growth was also followed by a reduction in business in the retail sector due to a lack of business capital and difficulties in applying for credit capital loans through banks or other financial institutions, both through sharia and conventional. Financial technology provides fresh air for MSMEs in providing fast capital assistance. Equity crowdfunding as fintech is very numerous and growing in Indonesia, this is due to the ease of the fast and efficient funding process for MSME business actors. Equity crowdfunding also requires supervision by the Financial Services Authority which is useful for protecting investors as providers of funds through crowdfunding.

**Keywords:** Equity Crowdfunding, MSME Business Funding, Indonesia.

## INTRODUCTION

The era of globalization has brought changes in various aspects of human life, including social, economic, cultural and technological. These changes occur as a result of an increase in human needs that encourage entrepreneurs to innovate in their businesses so they can compete with other businesses. One way to encourage the superiority of their products is that entrepreneurs must be able to create creative, innovative and effective products for the community.[1]

The Covid 19 pandemic emerged in Indonesia resulting in a decline in economic growth in Indonesia. However, since the emergence of the MSME business, it has become one of the driving forces in the wheels of the Indonesian economy at that time.[2] The contribution of the MSME sector to the economy in Indonesia at that time grew to 60.3%.[3] This was also followed by the absorption of domestic workers by MSMEs of around 97.22%.[4]

The period of the Covid 19 pandemic was also felt by MSME players which resulted in business closures. This is due to the sluggish purchasing power of the public and the lack of business capital for MSMEs, so information technology-based crowdfunding services are one of the capital solutions for MSMEs during the COVID 19 pandemic.[5] Crowdfunding has provided fresh air for MSMEs because it can help provide business capital quickly and require various requirements to help develop their business, unlike through conventional banking or financing or sharia financing.[6]

The One form of crowdfunding that is currently developing is equity crowdfunding. Regulations regarding equity crowdfunding services are contained in POJK 37/2018. This service is carried out through an information technology-based stock offering (shared crowdfunding). Share-based crowdfunding as referred to in Article 1 (1) POJK 37/2018 explains that information technology-based stock offerings are carried out by issuers that provide stock offering services to sell shares directly to investors through the capital market.

The Financial Services Authority in POJK 37/2018 provides opportunities for MSME entrepreneurs to develop their businesses through a crowdfunding implementation platform that helps MSMEs in providing

their capital and this implementation is supervised by OJK. Based on this background, the authors are interested in discussing the implementation of POJK 37/2018 in relation to equity crowdfunding activities and analyzing the impact of crowdfunding regulations on the digitization of MSMEs in Indonesia.

## RESULTS

### Implementation of Crowdfunding According to POJK 37/2018

The development of information technology is growing very rapidly at this time in Indonesia. There are various factors that influence technological development, one of which is technological innovation in the financial sector, known as financial technology or fintech. Fintech is a technology in the financial system that produces new business services and can have an impact on the efficiency, smoothness, security and reliability of the payment system. The use of financial technology in financial services is changing conventional business systems into digital business systems that have the advantage of providing practical services in the financial sector by facilitating payments, financing with a remote system and can be done in seconds.

In Indonesia, the Fintech industry sector is starting to develop and is recognized by all ages. The development of the Fintech industry sector began with the emergence of new investment instruments for MSME small and medium enterprises, especially Equity Crowdfunding (“ECF”) and has been upgraded to Securities Crowdfunding (“SCF”).

Small and medium enterprises are considered as one of the pillars of the Indonesian economy, because the existence of MSMEs is a solution to solving problems due to high unemployment rates and mass reductions in employees in companies caused by the Covid 19 Pandemic. Regulations regarding MSMEs are regulated and protected in Law No. 20 of 2008 concerning Micro, Small and Medium Enterprises (UU UMKM). MSME development in Indonesia faces two main obstacles, namely capital and marketing difficulties.

Many MSMEs members cannot develop their business due to lack of finance. MSME’s access to capital for financing relies more on the crowdfunding sector. The government as a state organization should provide infrastructure to develop the businesses of MSME members through capital accumulation that can be used for the process of developing the MSME business unit.

Article 7 of Law No. 20 of 2008 states that the state and local governments provide support to foster a business climate for small and medium enterprises, one of which is through the funding aspect by providing capital facilities to SMEs through banking credit institutions or conventional and sharia financing institutions.

In fact, not all MSMEs can access sources of financing through banking credit institutions or conventional and sharia financing institutions due to the inability of MSMEs to meet some of the requirements put forward. One of the binding conditions is collateral, which is a common obstacle for every economic sector that wants to obtain credit loans in the banking sector or conventional and sharia financing institutions.

The provisions for capital in crowdfunding to help capitalize MSMEs are contained in POJK Number 37 / Pojk.04 / 2018 concerning Crowdfunding Services through Information Technology-Based Stock Offerings (Equity Crowdfunding). Crowdfunding organizers are required to be Indonesian legal entities that provide, manage and operate crowdfunding services as an alternative in financing for MSMEs.

The capital obtained by MSMEs is not the capital that has been determined in the MSME law, namely through conventional or sharia banking or financial institutions. MSMEs also have the possibility to develop their business capital by offering shares on the crowdfunding platform provided by the hosting company.

Capital development can be done through banking facilities or financial institutions, capital development through crowdfunding platforms must also meet the requirements set by the OJK.

The requirements that must be met by SME owners, as stipulated in Article 6 of the OJK Regulation concerning Equity Fundraising by issuers are legal entities in the form of limited liability companies offering their shares through equity crowdfunding providers. The issuer is a company in the form of a limited liability company which must be in the form of an open limited liability company, which must have shares that are traded on the capital market and the company has assets of more than Rp. 10,000,000,000.- (ten billion Rupiah) excluding land and buildings.

### **The Role of Crowdfunding in the Digitalization of MSMEs**

Indonesia's digital commercial transactions in e-commerce occupy the top position compared to other countries with growth reaching 78%.<sup>[7]</sup> The acceleration of innovation in the technology sector is driving the transformation of businesses in Indonesia towards digital, better known as financial technology ("fintech"). This transformation occurs in order to achieve a practical business and provide speed of access for economic actors to reach a wider market, and more economical operational costs. The potential of the fintech industry as crowdfunding in applying technology functions to connect parties seeking funds (publishers) and potential investors so as to facilitate communication between parties as well as the fundraising process itself.<sup>[8]</sup>

Information technology-based crowdfunding arrangements in Indonesia apply a digital-based registration mechanism to optimize the trust of crowdfunding participants. This is based on the fact that MSMEs have a higher level of risk than companies. Article 7 paragraph (1) POJK No. 57 of 2020 concerning Securities Offerings Through Information Technology-Based Crowdfunding Services states that issuers are required to pocket a license by registering their business entity through the organizer's website which has been integrated online.

Registration of an equity crowdfunding business requires the issuer to fill in information and documents regarding the business entity, such as the business structure, desired offer structure, type and number of securities issued, prospectus or business plan and projected income. Issuers have an obligation to publish financial reports that are prepared at least based on micro, small and medium entity financial accounting standards to administrators, OJK, and the public in order to monitor the realization of the use of funds.

This procedure is intended to assess the legal aspects of issuer operations carried out by operators to ensure the interests of investors between stakeholders as a means of communication within the electronic Know Your Customer (eKYC) system to optimize control over the identity of participating investors.

The obligation to publish financial reports digitally for publishers required by POJK 57/2020 is a medium for MSMEs to gain administrative management and business development skills digitally. The application of IT-based crowdfunding which functions to increase MSMEs' knowledge in the IT ecosystem to contribute to the digitalization of MSMEs, among other things, is through audit trails or track records according to Article 71 POJK 57/2020. The audit track record is useful as a business portfolio consideration when you want to access financing services or offer larger securities, such as an IPO on the capital market.<sup>[9]</sup>

Crowdfunding executant according to Article 1 point 5 POJK 57/2020, namely Indonesian legal entities that organize and operate crowdfunding, require a licensing application no later than ninety days in fulfilling requests according to Article 13 POJK 16/2021 in the form of a photocopy of the deed of establishment of a legal entity, a photocopy of the deed of amendment to the last articles of association that has been authorized or approved by the competent authority, shareholder data, data of the board of directors and

board of commissioners, organizational structure of the organizer, operational guidelines, work plan for the first 1 year, proof of readiness of the electronic system and data on the organizer's operational activities, standard operating procedures, photocopy of the organizer's taxpayer identification number, agreements with custodian banks and storage and settlement institutions, statement letters of responsible parties, recommendations from associations recognized by the financial services authority. Qualified the requirements as a crowdfunding executant if it qualify Article 11 POJK 57/2020, having a capital of at least 2,500,000,000 (two billion five hundred million rupiah) when applying for a license.

Crowdfunding can be chosen as an alternative solution in obtaining capital to advance the development of MSMEs. Some of the advantages obtained by MSMEs include the non-existent collateral obligations to obtain funding. Fundraising companies only need to offer shares in their company as a form of compensation for the investment provided by investors. The investor will also get benefit in the form of income in accordance with the amount of shares listed during the crowdfunding process. In addition, it is easy to access the online platform on the Securities Crowdfunding service anywhere and anytime. So that companies and investors can monitor the progress of Crowdfunding carried out[10]

Securities crowdfunding also does not have a requirement for a business owner to have a large company scale and capital owners do not have to put their money in large amounts. This crowdfunding investment registration scheme also does not go through a difficult process so that even the most ordinary people will easily understand and can actively contribute to the empowerment of MSMEs in Indonesia.[11]

Another advantage is that despite being able to access a wide range of investors, the process is more simplified and shorter from the entrepreneur's point of view. Compared to traditional sources of capital, contracts in crowdfunding are relatively simple, the process is shorter, and it can reach a wider range of investors.[12]

Besides the benefits of using crowdfunding in funding MSMEs, there is another factor in filling the capital gap for entrepreneurs that can increase competitiveness among capital providers, which also increases the competitiveness of small businesses due to lower costs. Crowdfunding, by meeting the demand of new ventures for capital, can enable financial markets to improve their efficiency.[13]

Security Crowdfunding is often chosen as an alternative to conventional bank lending. There are several reasons for this. The emergence of crowdfunding is due to economic and technological developments. These factors include: the tightening of bank lending following the global financial crisis of 2007-2008, which was followed by a worldwide economic downturn, and the availability of systems provided by 'Web 2.0'. Since the financial crisis of 2007-2008, capital constraints and the importance of stimulating and funding newly established MSMEs have been a subject of discussion for policy makers, the financial industry, and relevant professionals.[14]

The selection of equity crowdfunding has the potential to provide cheaper funding compared to conventional sources (in this case banks). Armour and Enriques found that the costs associated with complying with securities laws to conduct an initial public offering were estimated to be between €1 million (A\$1.6 million) and €2.3 million (A\$3.7 million).<sup>127</sup> While most startups cannot access capital from regulated markets, entrepreneurs can use crowdfunding as an alternative to meet unmet capital needs.[15]

In crowdfunding, funding platforms typically invite each member of the crowd to invest a small amount of money, rather than raising a large amount of capital from a few sophisticated investors. This structure means that everyone is theoretically eligible to invest and makes it the most inclusive method of raising capital, compared to conventional funding sources. Some authors refer to it as 'democratized access to investment opportunities', to describe the broad participatory inclusiveness of crowdfunding.[16]

In one of the lecture series of the virtual summer program "International Week (iWeek) 2022 held by the

faculty of economics and business at Gadjah Mada University with expert speaker Dr. Konstantinos Sedaris from Southampton University, United Kingdom who mentioned that there are a number of advantages that MSMEs can get from crowdfunding funding, for example crowdfunding allows more control for projects than when seeking financial support through banks or venture capital.[\[17\]](#)

Security Crowdfunding is indeed considered an alternative means of meeting the capital needed by MSMEs, but keep in mind that Security Crowdfunding also has drawbacks that need to be considered. Equity crowdfunding also has undesirable risks such as investment default/failure, fraudulent platform closure, lack of investment liquidity (making it difficult for investors to exit), cyberattacks, and lack of transparency. Investing in equity crowdfunding is considered illiquid as a secondary market for this type of investment is unlikely to exist for practical reasons. The amount of securities issued in an equity crowdfunding offering is most likely too small to be transacted on a secondary market. Therefore, the fall out strategy for investing in equity crowdfunding is acquisitions.[\[18\]](#)

Investors as buyers of funds through Crowdfunding Services have certainly seen various positive and negative values through various views in funding umkm. Investor confidence to invest in umkm can be seen from the financial statements used to predict the return and risk of a given investment. Through these reports, investors can be more careful in making decisions to invest. If the performance of umkm is satisfactory, then investors can have more confidence in the ability to generate financial benefits. Crowdfunding can be done by various parties and does not have to be in a large amount, which is a plus point for investors. However, in its implementation, investors must also be prepared to accept several risks that will occur in the future such as loss of investor privacy, fraud or default which has the potential to lose some or all of the money invested.[\[19\]](#)

Crowdfunding arrangements in digitizing MSMEs play a role as digitizing MSMEs in developing their business, so the implementation of POJK 57/2020 is in line with the government's vision of accelerating the digitization of the Indonesian economy, as stated in Presidential Regulation No. 7 of 2017 concerning the Roadmap for the 2017-2019 Electronic-Based National Trade System (E-commerce Roadmap) (SPNBE 2017/2019) in order to expand and improve the economic activities of the Indonesian people to become more efficient and also contribute to the digitalization of MSMEs, both in administrative and business aspects. The integration of the crowdfunding system as a visionary view of future government programs is also expected to provide further support to business owners to develop their businesses under expert guidance and direction provided by the government.[\[20\]](#)

## CONCLUSION

Crowdfunding is an alternative method of capital for MSMEs during the COVID-19 pandemic. This happens because the time for applying for capital loans to banks and financing institutions is very long and there is an obligation to provide credit guarantees. In the implementation of Crowdfunding, there are advantages, one of which is that the process is simpler and shorter, and the amount of investment is not fixed. Crowdfunding disadvantages such as default or investment failure. Investor confidence to invest in umkm can be seen from the financial statements used to predict the return and risk on the investment given. If the performance of umkm is satisfactory, then investors can have more confidence in the ability to generate financial returns. Crowdfunding regulations in Indonesia are overseen by the OJK by issuing POJK 37/2018 which was replaced with POJK 57/2020 and partially amended with POJK 16/2021 bringing positive changes to crowdfunding in Indonesia, especially access for MSMEs.

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