Supervision and Regulation of Microfinance Institutions in Indonesia

Contents

- FSA Indonesia (OJK)
- MFIs in Indonesia
- MFIs Regulations
- Challenges
Indonesia
Financial Services Authority
(Otoritas Jasa Keuangan – OJK)
Establishment of OJK

Capital Market & Non-Banking Supervision (Ministry of Finance)

Banking Supervision (Bank Indonesia)

Act No. 21 of Year 2011

Integrated Supervision
OJK has a vision to become a trustworthy monitoring institution that oversees financial services industry, in order to protect the interests of consumers and public, and to be able to bring about the financial services industry into becoming a pillar of national economy with global competitiveness as well as capability to promote public prosperity.

To realize the convening of all activities in financial sector so that they are managed regularly, fairly, transparently, and accountably.

To protect the interests of consumers and public.

To realize a sustainable and stable financial system.
Financial Services Supervised by OJK

- BANKS
- CAPITAL MARKET
- INSURANCE COMPANIES
- PENSION FUNDS
- FINANCE COMPANIES
- OTHER FINANCIAL INSTITUTIONS
- NON-BANK

- Pawnbroker Companies
- Credit Guarantee Companies
- Indonesia Exim Bank
- Secondary Mortgage Company
- Other financial institutions being declared by laws and regulations as under supervision of OJK
- (Nonbank) Microfinance Institutions
Microfinance Institutions in Indonesia
## MSMEs & Big Enterprises

<table>
<thead>
<tr>
<th></th>
<th>2011</th>
<th>2012</th>
<th>2013</th>
</tr>
</thead>
<tbody>
<tr>
<td>Micro</td>
<td>54,559,969</td>
<td>55,856,176</td>
<td>57,189,393</td>
</tr>
<tr>
<td>Small</td>
<td>602,195</td>
<td>629,418</td>
<td>654,222</td>
</tr>
<tr>
<td>Medium</td>
<td>44,280</td>
<td>48,997</td>
<td>52,106</td>
</tr>
<tr>
<td>Big</td>
<td>4,952</td>
<td>4,968</td>
<td>5,066</td>
</tr>
</tbody>
</table>

Source: Ministry of Cooperatives & SMEs
## Informal MFIs

<table>
<thead>
<tr>
<th></th>
<th></th>
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</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Government</td>
<td>Parliament</td>
</tr>
<tr>
<td>Initiated by community/NGO</td>
<td>1,250</td>
<td>24,392</td>
</tr>
<tr>
<td>Unable to transform into rural banks in 1997</td>
<td>6,241</td>
<td>6,971</td>
</tr>
<tr>
<td>Government programs</td>
<td>90,659</td>
<td>606,475</td>
</tr>
<tr>
<td>Total</td>
<td>98,150</td>
<td>637,838</td>
</tr>
</tbody>
</table>

Sources: ProFI GTZ, National Team of MFI Bill, OJK

* Based on MFI Act, OJK must conduct survey and collect data of informal MFIs until Jan 2017. The survey is in coordination with Ministry of Home Affairs and Ministry of Cooperatives & SMEs, and supported by Regional Governments (Province/City) and Bank Rakyat Indonesia.
Example of Informal MFIs

National Program of Community Empowerment (PNPM)

- Umbrella program for poverty alleviation based on community empowerment
- Terminated in December 2014
- Program for village community: total revolving fund was IDR 10.7 trillion spread over 5,300 subdistricts

Sources: National Team for the Acceleration of Poverty Alleviation, Ministry of Development Planning

Subdistrict Credit Agency (BKK) in Central Java

- Established by the Provincial Government of Central Java
- In 1992-1997 few of them were transformed into rural banks, but the majority failed
- After being merged in 2014, there were 29 BKK and 131 branch offices, with total assets IDR 1.88 trillion. Now they are in the process of becoming rural banks

Source: Provincial Government of Central Java
(Nonbank) MFIs Regulations
Amendment of Banking Act:
- Any parties conducting activities of collecting funds from the public in the form of Deposits shall previously obtain an operating license as a Commercial Bank or a Rural Bank from the Chairmen of Bank Indonesia, except the concerned activities of collecting funds from the public is stipulated in a separate act.
- Informal MFIs shall be granted the status of Rural Bank pursuant to this Act after the requirements and procedures to be stipulated in a Government Regulation are fulfilled.
- Gov’t Regulation: Deadline for informal MFIs to apply for licensing of rural bank was 30th October 1997.

Joint Decree of Bank Indonesia, Ministry of Finance, Ministry of Home Affairs, and Ministry of Cooperatives & SME: Strategies of Empowering MFIs
- Survey and educate informal MFIs
- Transform informal MFIs into rural banks, cooperatives, or village-owned business entities.
- Provide capacity building for those rural banks, cooperatives and village-owned business entities.

Only a fraction of informal MFIs met the requirements of becoming rural bank. Many others continued to operate under Cooperative Act, Provincial Regulation, local customary law or even without proper regulation/licensing.

- Establishment of OJK (FSA Indonesia)
- Enactment of MFI Act

MFI Act has been effective since Jan 2015.
Regulation Framework

Legal Basis

Act No. 1 of 2013 on Microfinance Institutions

Government Regulation

No. 89 of 2014 on Lending Rate and Coverage of Business Area

OJK Regulations

• No. 12 of 2014 amended by No. 61 of 2015 on Business License and Institutional Aspects of (Nonbank) MFIs

• No. 13 of 2014 amended by No. 62 of 2015 on Business Activities of (Nonbank) MFIs

• No. 14 of 2014 on Supervision of (Nonbank) MFIs
Business Activities of (Nonbank) MFIs

Besides operating business as explained above, (nonbank) MFIs may also conduct fee-based activities, as long as they are not contradictory to the prevailing laws and regulations in the financial sector.

Sharia MFIs may manage social funds in the form of zakat, infaq, shodaqoh, and waqaf according to the provision of laws and regulations.
Limited Liability Company:
The share of the company at least of 60% shall be owned by City/County Governments or village-owned business entities. The remaining share may be owned by Indonesian citizen and/or cooperatives.

* (Nonbank) MFI is prohibited being owned, either directly or indirectly, by foreign nationals and/or business entities whether in part or in whole owned by foreign citizens or foreign corporations.

<table>
<thead>
<tr>
<th>Coverage Area</th>
<th>Minimum Paid Capital</th>
</tr>
</thead>
<tbody>
<tr>
<td>Village</td>
<td>IDR 50 million</td>
</tr>
<tr>
<td>Subdistrict</td>
<td>IDR 100 million</td>
</tr>
<tr>
<td>City/County/District</td>
<td>IDR 500 million</td>
</tr>
</tbody>
</table>
Licensing Mechanism of (Nonbank) MFIs

New entities

Paid capital in the form of time deposit

Operating entities

Paid capital in the form of net equity

While the application documents are incomplete but net equity meets the requirement, OJK grants temporary license for 2 years to complete the application
MFI Deposit Insurance

Group of (Nonbank) MFIs → MFI Deposit Insurance

Regional Government

Central Government

Regional Government

Group of (Nonbank) MFIs

Group of (Nonbank) MFIs

Regional Government
Supervision of (Nonbank) MFIs

Ministry of Home Affairs and Ministry of Cooperatives & SMEs

Coordination

OJK
Ultimate supervisor of (nonbank) MFIs

Supervision

Delegated to

City/County/District Government

Another appointed party, in case of local government is not ready
Supervisory Regulations

Offsite supervision

Onsite supervision

Reporting & publishing financial report

Consumer protection

Reporting lending rate

KYC compliance

MFI
Criteria:
• MFI conducts business activities in excess of 1 (one) county/city in which MFI is located; or
• Equity is at least 5x of minimum capital requirement of rural bank and total deposits is at least 25x of minimum capital requirement of rural bank.
Challenges
## Work Plan of MFI Policies

<table>
<thead>
<tr>
<th>Policies</th>
<th>Status</th>
</tr>
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<tbody>
<tr>
<td>Survey and educate the informal MFIs*</td>
<td>On going</td>
</tr>
<tr>
<td>Transform the informal MFIs into (nonbank) MFIs, cooperatives, or village-owned business entities*</td>
<td>On going</td>
</tr>
<tr>
<td>Assist, regulate, and supervise (nonbank) MFIs</td>
<td>Gradually implemented</td>
</tr>
<tr>
<td>Empower (nonbank) MFIs:</td>
<td></td>
</tr>
<tr>
<td>– Linkage program with other financial institutions</td>
<td>Will be implemented (medium term)</td>
</tr>
<tr>
<td>– APEX of MFIs</td>
<td>Will be implemented (long term)</td>
</tr>
<tr>
<td>– MFIs deposit insurance</td>
<td>Will be implemented (long term)</td>
</tr>
</tbody>
</table>

* In coordination with Ministry of Home Affairs; Ministry of Cooperatives & SMEs; Ministry of Villages, Underdeveloped Regions & Transmigration; and Regional Governments (Province/City).
Why do MFIs have to be formalized & supervised?

- To legalize deposit taking activities
- To protect depositors
- To ensure sustainability of MFIs
- To raise credibility of MFIs
- To enable synergy between MFIs, other formal institutions, and MSMEs development programs
Transform the informal MFIs into formal entities

a. Internal factors

- Lack of skilled human resources
- Reluctant to be licensed & supervised

Key strategy:
clear guidance & intensive assistance
Challenges

b. External factors

- Many related laws & regulations (MSMEs Act, Cooperatives Act, Limited Liability Company Act, Village Act, Regional Government Act, etc). Example: legal issue on ownership of revolving fund
- Many stakeholders

Key strategy:
consultation, coordination & harmonization
Thank You