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Brief Overview on P2P Lending from the Regulatory Perspective in Indonesia and a Sneak Peek into the Draft New Regulations of Information Technology Based Collective Funding Services.

Bank of Indonesia classifies Financial Technology (fintech) into several categories i.e lending, financing, and capital funding. Some of the popular ones in Indonesia are Information Technology-Based Lending Services or known as Peer-to-Peer Lending ("**P2P Lending**") and Information Technology-Based Fundraising or known as crowdfunding ("**Crowdfunding**"). For those who are unaware, we note that they may confuse P2P Lending and Crowdfunding as the same, but they are 2 (two) different funding arrangements.

P2P Lending is considered as a simple, convenient, and fast borrowing and lending services, while also offering competitive interest rate. These traits make P2P Lending services become one of the more popular alternatives for borrowing and lending than banks, because of the stricter requirements and longer process for applying financing from banks.

P2P Lending activity is regulated under the Financial Services Authority ("**OJK**" – *Otoritas Jasa Keuangan*) since 2016 pursuant to OJK Regulation Number 77/POJK.01/2016 on Information Technology-Based Lending Services which was enacted on 29 September 2016 ("**P2P Lending Regulation**"). However, in November 2020, OJK has issued the draft of new P2P Lending regulation on the Information Technology-Based Collective Funding Services to complement and amend several noteworthy provisions such as licensing provisions and capital requirements for P2P Lending business/services ("**Draft New P2P Lending Regulation**").

In this newsletter, we will explain a brief overview on regulatory perspective on the differences between P2P Lending and Crowdfunding with a focus on

P2P Lending Regulation in Indonesia and a sneak peek on some of the notable differences the Draft New P2P Lending Regulation has in comparison with the current P2P Lending Regulation.

A. General Overview on P2P Lending and Crowdfunding and Types of P2P Lending

Under Bank Indonesia Regulation Number 19/12/PBI/2017 of 2017 on Financial Technology Provider, P2P Lending falls under the category of lending, financing, and capital funding, along with Crowdfunding. The general differences between P2P Lending and Crowdfunding are:

Differences	P2P Lending	Crowdfunding
Type	Lending service Providers	Fundraising services Providers
Provider purpose	Bridging the Lender and the Borrower through its platform (web-based and/or app-based) to facilitate lending services between the parties (for consumptive and/or productive purposes).	- Gathering investor to fund a certain business (equity-based Crowdfunding / reward-based Crowdfunding); - Could be used for fundraising in helping victims of disaster and other humanitarian aid (donation-based Crowdfunding).
Reward	Interest from lending amount to the Borrower	Part of Shares (equity-based Crowdfunding) or other form such as the business product (reward-based Crowdfunding – for example: Kickstarter).

P2P Lending in practice is comprised of 2 (two) types namely P2P Lending productive (they are focused for facilitating the financing of business sector such as Micro, Small and Medium Enterprises (UMKM – *Usaha Mikro, Kecil dan Menengah*)) and P2P Lending consumptive (focused on retail sectors for facilitating financing for consumptive purposes such as online shopping through e-commerce). Current P2P Lending Regulation does not regulate these types differently; they just emerged by practice in Indonesia. However, the Draft New P2P Lending Regulation makes the distinction between P2P Lending Productive and P2P Lending Multipurpose. It is interesting to note that the Draft New P2P Lending Regulation requires any P2P Lending Provider to obtain OJK approval if it intends to change its business model (including changing its business sector target).

Under P2P Lending Regulation, the following may participate in P2P Lending services:

1. Borrower

A Borrower may be an individual and/or legal entity from and domiciled in Indonesia.

2. Lender

A Lender may be an individual, legal entity, business entity whether from Indonesia or offshore and/or international institution.

3. P2P Lending Provider (“Provider”)

The party providing, managing and operating the marketplace and P2P Lending system bridging the parties above. A Provider may be a legal entity in the form of limited liability company or cooperatives. Foreign citizen and/or foreign legal entity may hold the shares ownership of a Provider in Indonesia provided that the shares ownership is directly or indirectly up to 85% (eighty five percent).

It is also interesting to note that in P2P Lending Regulation, there are 2 (two) stages of licensing process that must be followed by a Provider i.e registration stage and licensing process. In both stages, the Provider must provide the required documents and submit it to the OJK. The difference is registration must be done before applying the P2P Lending business license. After the Provider is registered with the OJK, they must apply the business license within 1 (one) year. The registered Provider is also required to increase its capital when it applies for its business license to the OJK. If after 1 (one) year and the registered Provider does not apply for the business license, then the registration will no longer be valid and they will not be able to re-register under the same Provider. However, since 2020 OJK issued a moratorium of not accepting registrations for new Provider because of its unprecedented rapid growth rate in Indonesia while the regulatory framework still needs to be patched to ensure firm protection for the users.

B. OJK Draft New on P2P Lending in Indonesia

On November 2020, OJK socialized the Draft New P2P Lending Regulation for P2P Lending in Indonesia and requested public comments on the draft. It is important to note that this is still a draft and is highly likely be subject to change in the final version, but we believe it is interesting to see the potential key changes the Draft New P2P Lending Regulation will bring to the space. With that in mind, the following are some of the notable differences between the current P2P Lending Regulation and Draft New P2P Lending Regulation:

Differences	P2P Lending Regulation	Draft New P2P Lending Regulation
P2P Lending Type	No distinction is made. However, in practice the market segment of the Providers is comprised of Providers for productive lending purpose and consumptive lending purpose.	- Distinction is made between productive lending purpose and multipurpose lending. - Productive lending: Provider focusing on facilitating business related loan for producing goods and/or services. - Multipurpose: Provider focusing on facilitating loan for consumptive purpose and not for a business/productive purpose. - Approval from OJK is necessary if Provider intends to change its business model (e.g. from productive lending to multipurpose lending).
Business License	Licensing process is comprised of 2 (two) stages namely registration stage and licensing process. Provider who has completed registration stage must apply for business license within 1 (one) year and must satisfy the licensing requirement (e.g. capital injection (since the capital requirement is different from registration stage and licensing process)).	The registration stage is no longer applied. There is only 1 (one) licensing process.

Capital	- Paid up capital of Provider in the form of a limited liability company is at least Rp 1.000.000.000,- (one billion rupiah) at the time of registration. - Capital of Provider in the form of a cooperatives is at least Rp 1.000.000.000,- (one billion rupiah) at the time of registration. - At the time of applying for licensing process, Provider must have minimum capital Rp 2.500.000.000,- (two billion five hundred million rupiah).	- Paid up capital of Provider in the form of a limited liability company is at least Rp 15.000.000.000,- (fifteen billion rupiah) at the time of applying for the license. - Capital of Provider in the form of a cooperatives minimum Rp 15.000.000.000,- (fifteen billion rupiah) at the time of applying for the license. - The capital must be fully paid up at the time of the establishment.
Shareholders Business Activities	Not specified.	If the shareholder is a foreign legal entity, it is required to operate in the financial services sector.
Lending Total Limit	OJK may from time to time review the lending total limit on P2P Lending which currently is Rp 2.000.000.000,- (two billion rupiah).	OJK has removed its right to review the total limit meaning the total limit is fixed at Rp 2.000.000.000,- (two billion rupiah).
Changes of Provider's Shareholders	OJK approval is required without specifying the conditions to meet to obtain such approval.	OJK added certain conditions for change of shareholders, among others, that the existing shareholder may not sell its share ownership in the Provider within 3 (three) years from the issuance date of Provider' license or approval from OJK on change of (previous) shareholder.

From the comparison above we can see that the differences are quite significant. Existing Provider and those who are planning to start a business as a Provider are encouraged to pay attention on the prospective new provisions/requirements of Draft New P2P Lending Regulation, for example:

1. **New acquisition/shareholding related requirements.** As mentioned above:

- If the shareholder is a foreign legal entity, it must operate in the **financial services sector**. Since the current P2P Lending Regulation does not impose this requirement, if the Draft New P2P Lending Regulation is enacted, there may be major restructuring/adjustments ahead for the existing Providers whose shareholders are foreign entity and do not operate in financial sector (i.e. shares divestment may be in order); and
- The existing shareholder of a Provider may not sell its shares in the Provider within 3 (three) years since the issuance date of the Provider's license or the date of OJK's approval for change of (previous) shareholding ("**Divestment Condition**"). Unless a leniency is granted by OJK, this requirement seems to conflict with 1.a above because (if condition 1.a above is met) a divestment is required to comply but on the other hand, divestment may not be carried out if the Divestment Condition is not met.

2. **New Capital Requirements.** The new capital requirements of IDR 15 billion in comparison to the previous IDR 1 billion and IDR 2.5 billion requirements is a steep change and would require existing Providers to inject significantly more capital into the business.

C. Legal Perspective to be Considered in P2P Lending

1. Legality of the Provider

The fast growing of illegal fintech requires Lender to be smart in determining a good Provider and prospective Borrower they may lend to. For example, the Lender must ensure that the Provider has obtained registration or license from OJK. It will help the Lender to ensure that the Provider they will use has the legality from OJK, is supervised by OJK and complies with the Standard Operating Procedure (SOP) determined by OJK. With these in place, it is expected that the prospective borrowers eligible to be displayed in the Provider's platform have gone through strict selection.

2. Delay of Payment or Default by Borrower

The Lender is often faced with the risk of default from Borrower. OJK also disclaims that all risks arising from lending activity on application or platform of the Provider that are not caused by an error or failure of the Provider system are not the responsibility of the Provider and must be borne by the Lender.

In other words, default of the Borrower still needs to be resolved by civil procedural law with the Lender without involvement from the Provider. Furthermore, even though the creditor is secured, the difficulty in selling the security or the diminishing value of the security is one of the risks of lending. In relation to this, the Indonesian Joint Funding Fintech Association (AFPI – *Asosiasi Fintech Pendanaan Bersama Indonesia*) has also taken a supportive measure by creating a Fintech Data Center system. This system may be accessed by the Provider to carry out fraud risk assessments, late repayments of loan, and check the track record of Borrowers registered in the Fintech Data Center system. Through the Fintech Data Center system, the Provider would also be able to identify if a Borrower uses more than one P2P Lending platform so the Fintech Data Center system can work as a tool to mitigate the risk of potential bad borrowers in the Provider' platform and provide additional protection to the Lenders.

The above is brief overview on P2P Lending in Indonesia and more importantly some noteworthy points on the potential upcoming changes that will be brought by the Draft New P2P Lending Regulation. However, currently there is no estimate on when the Draft New P2P Lending Regulation will be enacted. The above is presented for information purpose only and particularly on the draft regulation, there is always a possibility that there are changes made in the final version of the new regulation which may/may not affect the validity of the information presented above.

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