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LEGAL PROTECTION FOR CONSUMERS IN EQUITY-BASED CROWDFUNDING ACTIVITIES IN INDONESIA

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ABSTRACT

Financial Technology has developed very rapidly in recent years. Among the products of its creation is crowdfunding. Crowdfunding itself is defined as the practice of funding a project or business by collecting small amounts of money from large numbers of people, and usually via the internet. One form of crowdfunding that is currently in demand in several parts of the world is Equity-based Crowdfunding. Equity-based crowdfunding is a funding transaction in which a fundraising company offers a share of shares in the company as compensation for the investment made through the platform, namely the website. There is no regulation on this activity in Indonesia. However, if the future constitution regarding this matter will be made, one thing that should be emphasized will be consumer protection. Regulators, in this case, must provide protection by considering the nature and purpose of crowdfunding itself to make it easier for new companies to raise funds without going through a mechanism that consumes a high value at a fairly long process.

Keywords: Equity-based crowdfunding, public offering, Consumer Protection, stocks.

INTRODUCTION

Globalization makes technology an important part of human life. The internet is not only a source of information or communication media but can also facilitate the financial needs of its users. In line with technological developments, the financial sector is also developing to be more practical and modern. One proof of the adjustment of the financial sector with technological developments is Financial Technology, or commonly known as "Fintech" which

means a company that provides financial services, therefore fintech aims to become a means for financial transactions carried out by the public, among which is Crowdfunding, one of the products that is currently in demand. Crowdfunding itself is defined as the practice of funding a project or business by collecting small amounts of money from large numbers of people, and usually via the internet. According to De Buysere, who took part in the making of Crowdfunding regulations in Europe, crowdfunding is a collective effort of many people who build and pool their resources to support activities initiated by a person or organization. This is usually done through the internet. Individual projects and businesses are financed with small contributions from large numbers of people, allowing innovators, entrepreneurs and business owners to use their social media to raise capital. The main idealism of crowdfunding is that the community funds what the community wants. In this context, the community or “crowd” is represented by internet users in general and in particular by users of social media and other social networking sites.

In recent years, a type of crowdfunding called Equity-based Crowdfunding has become a very important funding alternative for companies, especially for start-ups, and the volume is increasing every year. Equity-based Crowdfunding is a form of financing where entrepreneurs open funding via the internet, which is expected to attract investors to provide funding. Equity-based crowdfunding provides an opportunity for entrepreneurs to offer shares from their companies to investors as a form of funding. Entrepreneurs can still carry out these activities through angel investors or someone who uses their money to provide capital to start-up companies and gets a reward in the form of a percentage of ownership shares of the company⁵ and venture capitalists or companies investing in start-ups.⁶ However, with Equity-based Crowdfunding, companies and community can do it through an intermediary crowdfunding platform.

The crowdfunding system has developed greatly in various countries, while in Indonesia, Equity-based crowdfunding is just beginning to be developed. Loan-based crowdfunding has already been established, causing it to be operated based on a certain regulation. However, Equity-based Crowdfunding is still uncommon to people in Indonesia because there are no regulations to facilitate its mechanism.

Considering that Equity-based Crowdfunding is a share sale transaction that is not carried out as in the Stock Exchange because it involves companies that are not yet public, information disclosure must still be done because it is the only way to make this activity safe and long lasting to protect investors from loss or fraud. Information disclosure in public offerings in Indonesia has been regulated. Yet, considering that the regulations on Equity-based crowdfunding have not been made, it is necessary to take into account how the disclosure of information is appropriate to protect consumers in this activity.

The protection of consumers then becomes interesting for further review because regulators in this case must balance the tightness of protection with the nature and purpose of crowdfunding itself, which is none other than to make it easier for new companies to raise funds without going through a mechanism

that is quite fund-consuming at a fairly long time. However, in Indonesia, there seems to be no clarity regarding the form of further requirements or protection against equity-based crowdfunding activities.

Based on this, the authors are interested in further research on what equity-based crowdfunding is and how its regulation is applied in America, Britain and Malaysia. The authors also intended on making comparisons of protection for consumers (investors), especially in information disclosure in the regulatory regimes of Equity-based crowdfunding activities for the three countries listed above. The authors will also analyze the possibility of implementing the arrangement of Equity-based Crowdfunding activities in Indonesia. This study aims to determine what the characteristics of equity-based crowdfunding are and to find out what legal protection can be provided to consumers in their activities in equity-based crowdfunding as well as to examine the possibility of its implementation in Indonesia. Hence, this study is expected to be able to contribute knowledge regarding legal protection for consumers in their activities through equity-based crowdfunding and can overcome the uncertainty in society regarding the importance of legal protection in the crowdfunding activities.

RESEARCH METHODS

This study is written based on the normative juridical method, which regards the discovery of legal rules, legal principles, and appropriate legal doctrines. In this case the authors refer to the legal rules that apply in the United States, United Kingdom, and Malaysia. The approach method used in conducting this research in order to obtain problem solving is the Statute Approach, Conceptual Approach and Comparative Approach. The primary legal material in this research is in the form of applicable laws and regulations and has something to do with the title and the formulation of the problem to be discussed. There is also secondary legal material consisting of scholar's opinions in literature books on law, particularly consumer protection law, capital market law and investment law, business entity law, information law and electronic transactions, lecture notes, scientific papers, articles from printed media any internet whose substance is related to the problems that will be discussed in this thesis. The collection of legal materials is carried out by means of library research which is intended to obtain legal material in both primary and secondary forms. The legal material is then analyzed to obtain answers to the formulation of the problem, so that the results of the discussion can be accounted for systematically.

RESULTS AND DISCUSSION

Before Equity-based Crowdfunding began to be developed, a mechanism called the Sharing Economy had developed which connected consumers with people who had goods or services to sell and rent through an online platform (Sharing Economy Platforms, nd). The Sharing Economy itself is a social economic ecosystem built from human resources and shared capital (Somers et al., 2018). This can include the creation, production, distribution, trade, or joint consumption of products and services by various parties and organizations (Matofska, 2016). As time goes by, it is realized that the people who create this

value - who usually use their own resources, are often not compensated in the form of value or long-term ownership even though they are the pioneers of the company's success, finally now the Sharing Economy is starting to expand to share in financial value. In a later stage, the value can be distributed where it is formed. Consumers, employees, and users can become owners of a community member, benefiting when the company is profitable. Starting from this, the idea emerged that any company could support a community to invest, which finally emerged through Equity Crowdfunding (Sundararajan, 2016).

The crowdfunding model that has recently sprung up in various parts of the world is Equity-based Crowdfunding. Investors in this type of crowdfunding will become shareholders of a fundraising company (issuer) and therefore receive rights from a shareholder based on the provisions of the applicable laws and regulations. This mechanism allows small and medium-sized companies to offer their shares to the public by avoiding the large costs that will arise from the public offering process (Smith, 2014). However, in this activity, it is still required for every company that wants to register on the platform and open fundraising already in the form of a Limited Liability Company, because in this stage there will be due diligence, where information disclosure is required regarding the company's articles of association and legal position. The types of shares that are invested in this activity are ordinary shares or shares by giving voting rights at shareholder meetings, receiving dividends, preemptive rights, and liabilities in the form of corporate risk in accordance with the number of shares (votes) owned. In this equity-based crowdfunding transaction, the relationship between issuers and intermediaries and between investors and intermediaries is the consumer for intermediaries. Here, a membership agreement occurs, in which the issuer and investor have signed an agreement to use the services of intermediaries. Meanwhile, between an issuer and an investor, a share purchase agreement regulates the relationship between the two as a seller and a buyer.

Later, the money received from investors will be held by the company with a separate trust account at the financial institution. Money is deposited in the trust account first to minimize fraud and make it easier for issuers, when the campaign is successful, the money given by investors will be transferred to the issuer and shares will be issued, and vice versa when the campaign does not reach the target amount, the funds will be returned to investors.

After the agreement between shareholders and related parties is carried out, the money in the trust account will be transferred to the Issuer. Meanwhile, in the event that the offer fails or when the profit sharing payment is withdrawn during the cooling off period, the company will, within 14 working days, return the profit sharing payment to the Investor without interest and after deducting transaction costs. If there is an oversubscription (fundraising gets more than the maximum amount proposed) then the company can close its bid, increase the maximum amount submitted (by consulting the Issuer first,) or continue to accept offers that will be reconsidered whether to accept or reject after cooling off period. The company will be given the power to access the funds given by

the Investor and deposited in the trust account in accordance with the terms and conditions of the agreement.

In America, the flow of activities in Equity-based Crowdfunding on each platform is almost the same. Taking a source from a platform in America called Seedinvest, from an investor's point of view what you have to do is first register at Seedinvest then enter your personal data on your investment experience and investment interest. There are two institutions that monitor and oversee the implementation of equity-based crowdfunding. The Securities Exchange and Commission (SEC), which created an exemption arrangement for equity-based crowdfunding, closely monitors the fundraising process subject to anti-fraud provisions even though filing requirements in the United States are very flexible. There is also the Federal Trade Commission (FTC), which is a consumer protection organization established under the Federal Trade Commission Act of 2014, which also plays a proactive role in protecting equity-based crowdfunding activities.

In its Equity-based Crowdfunding activities, the United States has made special regulations to support funding for small businesses (Green, 2014). This regulation paved the way for companies to use crowdfunding to find stocks that were not previously allowed. From the laws that existed at the time, several new crowdfunding equity platforms were starting to take shape. This regulation specifically regulates only issuers and intermediaries (broker or funding portal). The new regulations allow non-accredited investors to buy shares of startups via crowdfunding platforms. Four years after the effort to establish this online platform was carried out, business owners can now apply for and receive investments from non accredited investors through the online platform.

In Title III JOBS Act (Jumpstart Our Business Startups Act) specifically in the Securities Act Section 4A (b) (1) consumer protection which is regulated only in terms of information disclosure for Issuers. The financial statement requirements are based on the quantity bid and sold subject to the crowdfunding regulations in the previous 12 month period. For Issuers who sell shares for the first time in accordance with the Crowdfunding regulations: Financial reports that have been reviewed by an independent Public Accountant, unless there is a financial report that has been reviewed by an Independent Auditor. For offers that have not been completed or discontinued, the Issuer can submit a Change Form to explain any changes, additions, or updates to information. Issuer must provide updates on its progress to meet the target number of bids within 5 (five) working days after reaching 50% and 100% of the target number of bids.

Information disclosure in the United States is the most appropriate way to reduce risk in equity-based crowdfunding activities. Intermediaries are required by law to adopt policies to reduce fraud in bidding through their platforms. Anti-fraud measures that can be taken are conducting background checks on the company and also examining related parties such as founders and directors, as well as closing access to the issuer if there are signs of fraud. There also explained that to better protect privacy, the platform cannot pay or compensate promoters, seekers, or prospect makers for providing a broker or funding

platform with the personal identifiable information of each potential investor via e-mail list (Cunningham, 2016). Its purpose is to prevent third parties from obtaining information to sell to other portals and also avoid spam.

Crowdcube is an Equity-based Crowdfunding platform that is fairly successful in the UK, this year Crowdcube users have reached half a million and £ 310 million has been invested through this platform (Hurst, 2018). Given the potential for loss, equity-based crowdfunding is called a high risk investment. Thus, the UK made a regulation on investment called the Financial Conduct Authority. All transactions related to investment must be authorized by the FCA both online and offline (Okhrimenko, 2018).

In the UK, consumer protection in equity-based crowdfunding is a major concern. Equity-based crowdfunding in the UK is under the FSMA where retail investors must be protected under consumer protection principles. The Financial Services Compensation Scheme (FSCS) and The Financial Ombudsman Services (FOS) are the main authorities protecting consumers. FSCS deals with the portion of the compensation fund which covers investment losses caused by fraud. Both FSCS and FOS are government dependent and are funded by fees collected from registered members of the FCA.

FCA emphasizes the importance of protection for investors by focusing on the company (Gunawan & Wahyuni, 2014). Because as surveyed by Nesta and the University of Cambridge in 2014, 62% of investors in equity-based crowdfunding qualify them as retail investors who have no prior investment experience (C. Smith, 2015). Companies must provide accurate information for investors, in a comprehensive form, so that investors can adequately understand the nature and risks of this investment, and so that investors in making investment decisions really know enough information.

Currently FCA is opening a "call for input" or input on a "review" of crowdfunding regulations so that investors can carry out this activity safely. FCA ensures that it will provide adequate protection for investors against the risk of losing money when seeking funding through failed equity-based crowdfunding platforms, as well as against crimes such as fraud.

Of all the countries that are members of ASEAN, Malaysia is the first and only country that has its own regulation regarding Equity-based Crowdfunding (Cheah, 2015). The regulation of Equity-based Crowdfunding in Malaysia is mainly guided by the Guidelines on Regulation of Markets under Section 34 of the Capital Market and Services Act ("Guideline 34") which was issued on 11 February 2015 (Lee, 2015).

In Malaysia, the form of protection provided is also about disclosure of information provided by each party involved in equity-based crowdfunding. When an issuer makes an offer, it does not have to be obliged to be approved by SCM, besides that the issuer is exempted from the obligation to issue a prospectus as stipulated in Article 212 jo. Article 232 of the 2007 CMSA.

However, this does not mean that the issuer is exempt from the responsibility of disclosing information. Malaysia also provides consumer protection in the form of data protection in which Guidelines 34 Article 11 paragraph (5) letter j requires ECF Operators to maintain the privacy of information on the platform in accordance with the Personal Data Protection Act 2010.

So far, the Equity-based Crowdfunding Platform or Equity-based Crowdfunding Operators are only required to register their Website with the Security and Exchange Commission, there are no special requirements for the Equity-based Crowdfunding Platform or Operators to disclose information as regulated and in Malaysia.

In Indonesia, special arrangements relating to equity-based crowdfunding have not been regulated. Although Equity-based Crowdfunding is a platform for investing, under regulation in the US, UK and Malaysia, Investors are treated as consumers, especially retail investors or non-accredited investors. Whereas in Indonesia, consumers, according to article 1 number 2 of Law Number 8 of 1999 concerning consumer protection are defined as every person who uses goods and or services available in society, whether for the interests of themselves, their families, other people, or other living things.

The regulations that must be made for issuers are the need to review the regulations regarding who can be allowed to become issuers in Equity-based Crowdfunding activities. This is under the consideration that those who become issuers in Equity-based Crowdfunding activities are not the same as ordinary issuers who have to go through long procedures to do a public offering. It should be noted that although the Business Entity Law does not explicitly prohibit the activity of offering closed Company shares to the public, this activity will be classified as a “public offering” activity in the Capital Market Law, so it should be interpreted that private companies are prohibited from engaging in this activity. In this case, it is hoped that the Company will no longer be obliged to change its status to a Public Company. The Financial Services Authority Regulation Number 53/POJK.04/2017 concerning Registration Statements in Public Offerings can be used as a reference, however regarding the obligation to disclose information, it needs to be accommodated so that private companies can continue the share offering without having to be burdened by the obligation to disclose information given to publicly listed companies.

CONCLUSION

It can be concluded that the obstacles to equity-based crowdfunding activities can be easily overcome, considering that peer-to-peer lending activities are developing in Indonesia. The biggest challenge regards the legal framework that is not yet available as well as provisions that “allow” this activity to be carried out, as those two factors seem to limit the potential of this method. However, according to the authors, it cannot be said that equity crowdfunding activities are prohibited by the provisions of the prevailing laws and regulations.

Implementation of equity-based crowdfunding activities in Indonesia currently does not have specific regulations. Therefore, it is necessary to formulate appropriate regulations to accommodate entrepreneurs and investors and prevent the impact of legal uncertainty that tends to harm the parties involved. The Consumer Protection Law can only be used as a basis for this activity, however, to implement equity-based crowdfunding there are regulations that can be used as a reference for now, namely Capital Market and Financial Institution Supervisory Agency Regulation IX.A.5, Financial Services Authority Regulation Number 53/POJK.04/2017, Financial Services Authority Regulation Number 77/POJK. 01/2016, Information and Electronic Transaction Law and Indonesia Bank Regulation No. 19/12/PBI/2017. Apart from these laws, there is still a need for regulations regarding the definition of who consumers are in this activity so that there is proper protection to the parties involved.

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