



# Light-Touch Regulation to Optimize the Startup and MSME Ecosystem in Indonesia

Dwi Ratna Indri Hapsari<sup>1</sup>, Nur Putri Hidayah<sup>2</sup>

<sup>1, 2</sup> Faculty of Law, University of Muhammadiyah Malang, Malang, Indonesia

*dwiratna@umm.ac.id\**

**Abstract.** Startup is a newly business entity based on digital technology which is currently a novel development to provide alternative solutions to problems and ease the burden of modern life. Almost the same as Micro, small, and emerging businesses (MSME) in Indonesia experience problems in terms of access to capital. Apart from that, the complexity of business licensing procedures, regulations and unclear institutions that regulate startup and MSMEs in Indonesia fail even before they develop. This research aims to restore regulations in Indonesia in the field of startup and MSMEs. The research method employed is normative legal research with a statute- and conceptual-based approach. From the study's findings, it can be concluded that the Light Touch Regulation in the field of startup and MSMEs is expected to improve the startup and MSMEs ecosystem, such as ease of business trials, legal protection for new entrepreneurs, access to financing, or protection of intellectual property as has been proven implemented by several countries such as America, Japan, Germany, Swiss, South Korean, etc.

**Keywords:** Startup, Regulation, SME

## 1 Introduction

Currently, the progress of information technology continues to develop throughout all sectors, one of which is the digital revolution which brings us all towards the technological era or known as industry 4.0 (Zulkarnain & Andini, 2021). The internet serves as the primary support for the production process in the modern period of the fourth industrial revolution. Each object is equipped with technological devices assisted by sensors that are able to communicate independently with information technology systems. Convenience is one of the many reasons for technological developments to be easily accepted by society. With the existence of industry 4.0, every human activity has been helped by advances in technology, so that it can be done anywhere and anytime.

Industry 4.0 (Rahmatullah et al., 2022) is expanding in step with the expansion of Indonesia's creative industry which has begun to move towards a digital economy, namely with the emergence of various technology based startups, in Indonesia itself

startups have a crucial role in the development of Micro, Small, and Medium-Sized Enterprises (MSMEs).

MSMEs are an essential component of the populace's economy, which is strategically positioned to realize a more just, developed, and balanced national economic system. To accomplish this, the national economy is being implemented with a focus on creating an economic system that is pro-people's economy, equitable, trustworthy, just, accountable, transparent, and competitive in both the regional and global markets. MSMEs must be developed in order to expand their potential and involvement in achieving economic growth in order to establish this economic democracy (Zia, 2020).

The government should give empowerment (priority and partiality) the attention it deserves (through strategy and policies). MSMEs are seen as a group of business units that should be integrated into the business world nationally, which will later be able to increase the cost of living and competitiveness. The simplicity of regulation in conducting business activities is one area where MSMEs, which are the pioneers of entrepreneurial processes, require more attentive attention (Arliman S, 2017). The existence of MSMEs will become a stabilizer for the Indonesian economy because MSMEs are able to live in the midst of large businesses and can increase productivity with more productive workforce. In addition, MSMEs can also help large businesses, such as supplying raw materials, components and other needed materials to be processed by large businesses into products or goods that have high value (Aliyah, 2022).

MSMEs are strategically positioned to play a key role in establishing a fair and expanding national economic framework. By creating a favorable environment, offering business opportunities, support, protection, and as much business development as possible, MSME empowerment is carried out in a comprehensive, ideal, and sustainable way. This increases the position, role, and potential of MSMEs in achieving economic growth, equity, and raising people's incomes, as well as in creating jobs, reducing poverty, and other goals. The facts show that the job opportunities created by the MSME group are far more than the workforce that can be absorbed by large businesses. Therefore, it is hoped that MSMEs will continue to play an optimal role in efforts to tackle unemployment, whose number tends to increase every year.

Indonesia offers a lot of potential for the growth of MSMEs and startups. This sector, as previously mentioned, is considered an important economic driver (Tubagus, 2016), creating new jobs and being able to encourage innovation. MSMEs and startups have a lot of room to develop in Indonesia. The way startups work can be judged from sales figures on E-Commerce and the value of Financial Technology (Fintech) transactions(Njatrijani, 2019).

However, in recent years, there have been challenges and obstacles in optimizing the growth and development of startups and the MSME ecosystem in Indonesia. One of the obstacles faced is complicated and convoluted regulations. Excessive regulatory burdens and complex bureaucracies can become barriers to growth and innovation. Therefore, it is very important to consider a lighter and adaptive regulatory approach that can encourage the development of the startup and MSMEs ecosystem in Indonesia.

The MSME problem is complicated by a number of factors, including structural imbalances in resource allocation and control, the state's ambivalence in supporting efforts to develop the people's economy through industrialization policies and development strategies, an oligopolistic market structure, and relatively poor performance on traditional issues (human resources or human resources, capital and access to financial institutions, technology, management, marketing and information), the prevalence of distortions and contradictions in development-related policies.

Quoting the opinion of Matsuhiko Hayashi in Masnut Tiurmaida Malau said that in his research results he stated that the problem in the development of MSMEs in Indonesia was that there was no implementation process that was in line with government policies and was precisely caused by the bureaucratic system and the domestic political-economic situation which was not conducive (Malau, 2014).

The concept of Light-touch regulation offers an alternative to heavy, rigid and complicated regulatory approaches. In the context of startups and MSMEs, this approach can then provide wider space for business actors, encourage innovation and facilitate a more streamlined business process. However, the application of light touch regulation in the Indonesian context still requires more in-depth research.

Singapore, the United States and the United Kingdom have previously implemented light-touch regulations to support the growth of startups and MSMEs(PD et al., 2021). the experiences of these major countries can assist in formulating relevant policy recommendations for Indonesia. The application of the right Light-touch regulation can increase the potential for startups and MSMEs to grow optimally. Efficient and measurable regulations can create a conducive environment for the development of innovation, investment and access to markets which in turn can drive economic growth and create new jobs.

Based on this background, this article will discuss how the concepts and principles of light touch regulation can be applied in the context of regulations for start-ups and the MSME ecosystem in Indonesia and how light-touch regulation can help overcome the obstacles and challenges faced by startups and MSMEs in Indonesia.

## 2. Method

This study employs a doctrinal or normative method of legal inquiry. The statutory approach and the conceptual approach are used in the study methodology (Marzuki, 2008). The statutory method is implemented by reviewing all statutory provisions pertaining to the issue under investigation (Soekanto, 2015). Primary legal materials and secondary legal materials are the sources of law that are employed. To understand the laws and rules pertaining to the issue, use Primary Legal Materials. whereas secondary legal materials are found in books, journal papers, etc. Library research is the method used to gather legal resources, and qualitative analysis is the method used to evaluate legal information (Moleong, 2006) analysis techniques.

## 2 Result and Discussion

### 2.1 Concepts and Principles of Light-Touch Regulation in the Context of Regulations for Startups and MSMEs

The idea and methodology behind light-touch regulation (Kelly, 2014) can be applied in the context of regulation for startups and MSMEs in Indonesia in several ways, one of which is by trimming (Putra & Kurniawati, 2020) regulations that are deemed unnecessary or redundant. The government can evaluate existing regulations and identify requirements that are no longer relevant or are too burdensome for startups and MSMEs (Saputra, 2015). Excessive regulatory trimming can help reduce the cost, time, and effort required to comply with administrative requirements.

Identifying unnecessary regulations regarding startups and MSMEs in Indonesia can involve evaluating existing regulations and identifying requirements that are either too onerous or no longer relevant (Nuryasman & Wiweko, 2001). Some examples of regulations that might be considered for trimming or simplifying are as follows:

- 1) Excessive licensing requirements, some business sectors are still burdened by complicated licensing requirements. For example, licensing procedures that take a long time to obtain business licenses, building permits, or certain operational permits.
- 2) Unrealistic minimum capital requirements, some business sectors have high capital requirements to set up a business. This requirement can be an obstacle for startups and MSMEs who have limited resources. Evaluation can be carried out to review the minimum capital requirements and ensure that these requirements are realistic according to the characteristics of different business sectors and business scales.
- 3) Complex tax regulations, a complicated tax system can be a burden for startups and MSMEs. Evaluations can be carried out to clarify tax requirements, simplify reporting procedures and introduce tax policies that are simpler and in accordance with the needs of small-scale businesses.
- 4) Excessive financial reporting requirements, administrative burdens related to financial reporting requirements can also burden startups and MSMEs. Evaluations can be done to assess the actual need for certain financial statements, such as simplifying financial statement requirements or making allowances for smaller business sizes.
- 5) Complex labour provisions, complex labour regulations can affect flexibility in the use of labour and expenditure costs. Evaluation can be carried out to review excessive labour requirements or provide exceptions for startups and MSMEs with smaller business scales.

The use of the principle of proportional risk also needs to be applied by the government in light-touch regulation efforts. This is by taking into account the level of risk associated with startup businesses and MSMEs in determining the level of regula-

tion needed. Lighter regulations can be applied to businesses with lower risks while businesses with higher risks can be subject to more stringent regulations (Yang, 2016). This can allow startups and MSMEs to focus on important aspects related to the risks they face.

The government can encourage the principles of trust and transparency between regulators and business people by building more open and communicative relationships. Regulators can provide clear and measurable guidance to startups and MSMEs regarding regulatory requirements. This transparency allows businesses to understand regulatory expectations and ensure easier compliance.

Light-touch regulation can encourage a regulatory approach that is adaptive to changes in the business and technology environment. The government can regularly evaluate regulations and update policies according to industry developments and the needs of startups (Assyifa et al., 2021) and MSMEs. The adaptive approach allows businesses to innovate and adapt quickly without being constrained by outdated regulations. In addition, strengthening supervision and effective law enforcement is urgently needed. Although light-touch regulation reduces overregulation it is important to ensure effective oversight and enforcement. Regulators need to ensure that existing regulations are properly enforced to prevent violations that could harm stakeholders. Effective supervision and law enforcement can provide legal certainty, protect consumers (Hapsari & Kurniawan, 2020), and build trust in the startup and MSME ecosystem.

## **2.2 Barriers and Challenges to the Light-touch Regulation regarding Startups and MSMEs in Indonesia**

Identification of regulations related to startups and MSMEs (Zia, 2020) in Indonesia covers various aspects related to business establishment, operations and development. Some of these regulations include:

1. 1. The Micro, Small and Medium-Sized Enterprises (MSMEs) Law No. 20 of 2008; this law provides a legal basis for the protection and development of MSMEs in Indonesia. This regulation regulates definitions, criteria and policies related to MSMEs including access to financing, technical guidance and administrative facilities
2. The Law Regarding Limited Liability Companies No. 40 of 2007;
3. Limited Liability Companies (Persero) are governed by Government Regulation No. 39 of 2014, which governs their establishment, administration, and management that play a role in supporting the startup ecosystem in Indonesia;
4. Financial Services Authority (OJK) regulations related to Peer to peer (P2P) lending, OJK issued this regulation as the basis for funding access rules for startups and MSMEs;
5. Regulations of the Financial Services Authority (OJK) regarding Crowdfunding;

## 6. Financial Services Authority (OJK) regulations regarding Financial Technology which regulate payment gateways, P2P lending and e-money.

In fact, apart from providing legal certainty, regulations that are too complex have a separate impact on the growth of startups and MSMEs. Reducing excessive regulatory burdens and complicated bureaucracy can provide greater space for businesses to develop their business. By reducing the number of regulations that startups and MSMEs have to comply with, they will be more focused on core business activities. It can also reduce the time, effort and cost required to comply with excessive regulations, thereby increasing operational efficiency and competitiveness. For example, the Omnibus Law concept's Law Number 11 of 2020 concerning Job Creation does not yet regulate startups. As a result, the startup licensing process is still complicated and lengthy. For example, startups engaged in fintech (Krisnadi, 2016) are still facing a lengthy licensing process, namely a total of 13 (thirteen) ministries or government agencies that must be passed in the licensing process. In addition, startup actors must have 14 (fourteen) documents or business licenses from the process of establishing a Limited Liability Company to special sector permits. This process is a licensing process that must be passed by startups that have complex business fields such as transportation, food and shopping, digital payments, investment, and telemedicine (Khairisma, 2021).

The complexity of the bureaucracy related to the process of establishing a company, licensing, and business administration in Indonesia often involves complicated procedures and takes a relatively long time. The number of steps, requirements and documents needed can slow down business processes and burden entrepreneurs, especially for those who are just starting a business.

Some of the regulations mentioned above are only a few related regulations and in fact there are many more various regulations and regulatory bodies. Indonesia has a variety of regulations governing various aspects of business, both at the national and regional levels. The Ministry, the Financial Services Authority (OJK), the Commodity Futures Trading Supervisory Agency (Bappebti), and other regulatory organizations also have the power to enact numerous rules and specifications. This can cause confusion and difficulties for startups and MSMEs in understanding and fulfilling the applicable requirements.

The complicated tax system is also a challenge for startups and MSMEs in Indonesia. Complex taxation requirements and frequently changing regulations can make it difficult for entrepreneurs to understand their tax obligations and fulfil them properly (Wardoyo & Hapsari, 2023). This can increase the cost and time required for tax purposes.

A lighter regulatory approach for startups and MSMEs can provide greater freedom and convenience to develop and test new ideas (Zulkarnain & Andini, 2021). Business actors can experiment more in creating innovative products and services without being burdened by rigid regulatory requirements. Light-touch regulation facilitates the process of innovation and creativity needed to face competition and meet the needs of a growing market(Hapsari et al., 2021). In addition, lighter regulations can enable startups and MSMEs to carry out their business processes more quickly. Simple procedures and more measurable requirements allow startups and MSMEs to

start their operations more efficiently, reducing time constraints that can slow down growth. The fast and easy process can also increase the attractiveness of potential investors and partners(Ratna Indri Hapsari & Pratama, 2022).

### 3 Conclusion

Light touch regulation can help increase access for startups and MSMEs to financing. By reducing the requirements and limitations associated with regulations, startups and MSMEs become more attractive to investors and financial institutions. Ease in the regulatory process can speed up the process of completing financial transactions and minimize legal risks so that it can increase opportunities to obtain the financing needed for business growth and expansion.

Clear and measurable light-touch regulation can help improve compliance of business actors with regulations. Under lighter regulatory conditions, startups and MSMEs are better able to understand and meet the set requirements. This helps reduce the risk of accidental violations of the law and strengthens the confidence investors, business partners and consumers have in their business.

The application of light-touch regulation in Indonesia must still pay attention to the protection of public interests, such as aspects of security, consumer rights and environmental protection. This approach should be based on a careful evaluation of the positive impacts and risks that may arise, as well as involving relevant stakeholders to achieve a steady balance between freedom of business and consumer protection(Saravistha & Sancaya, 2022).

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