



This policy brief was prepared by obtaining input from the Digital Economic Ecosystem Webinar Series I with several stakeholders in the e-commerce sector in Indonesia organized by CSIS Indonesia and various previous studies. The public discussion was attended by representatives from the government, namely the Coordinating Ministry for Economic Affairs and the Ministry of Trade. In addition, the discussion was also attended by representatives from the e-commerce industry and digital platforms, namely the Indonesian E-Commerce Association (idEA) and Facebook Indonesia. This policy brief aims to provide reviews related to discussions and provide policy recommendations related to e-commerce regulations so that regulations are made by technological innovation to encourage the growth of the e-commerce industry in Indonesia.

CSIS Policy Brief

Department of Economics

E-Commerce Development and Regulation in Indonesia

Yose Rizal Damuri

Kepala Departemen Ekonomi, CSIS Indonesia

yose.rizal@csis.or.id

Adinova Fauri

Peneliti Departemen Ekonomi, CSIS Indonesia

adinova.fauri@csis.or.id

Dandy Rafitrandi

Peneliti Departemen Ekonomi, CSIS Indonesia

dandy.rafitrandi@csis.or.id

Foreword

In this advanced era of technology, commonly known as the Industrial Revolution 4.0, the transformation of economic activities ranging from daily household transactions to creating new business models, has improved the supply chain's efficiency. Innovation and digitalization can significantly increase multi-sector productivity and further include the society into a more inclusive economy. Bain and Company stated that Indonesia's digital industry contribution reached USD 44 Billion in 2020 and is expected to rise to USD 124 Billion in 2025¹. One of the main contributors to the digital industry growth in Indonesia is E-Commerce. With the growing number of internet

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users and more entrepreneurs migrate their businesses to e-commerce platforms, Indonesia is on its way to witness robust e-commerce growth. Therefore, it is pivotal for the government to strategize its policy not to disrupt the technological progress but to facilitate it. This policy brief then formulated to review e-commerce advancements in Indonesia along with the policy framework that has been prepared by the government and provide policy recommendation that is in line with the upswing of innovation.

E-Commerce Advancement in Indonesia

The e-commerce industry has taken quite a stride in Indonesia with the growing innovation in technology and the ever-increasing use of the internet. Looking at the data provided by Bank Indonesia, e-commerce transactions had been valued at Rp 265 Trillion in 2019, a high amount compared to the numbers in 2018 (Rp 146 Trillion) and 2017 (Rp 80 Trillion). This surge in transaction value was boosted by greater internet access coverage and raising the number of consumers involved in this electronic trade. Bain & Company noted that the number of Indonesian consumers in online platforms reached 137 million people. On top of that, We Are Social survey also found that 96% of internet users in Indonesia had used e-commerce to look for products or services.²

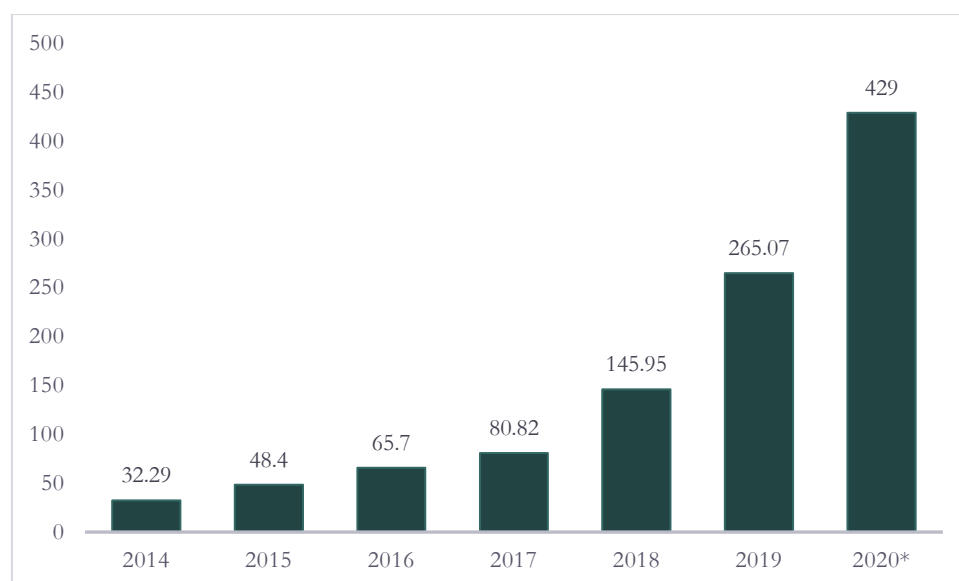
The valued transaction in e-commerce and the number of consumers in Indonesia certainly is an understatement. The data has yet to capture the number of transactions happening in social media, showing a growing electronic commerce trend. With a massive user base and time spent on social media, it has become a unique way for businesses to market their products. The National Socioeconomic Survey/*Susenas* (2017) data shows that internet users' most significant Indonesian activity is within social media platforms (79%). A survey conducted by ISEAS also observed that 13.5% of respondents had purchased goods through social media in 2017 which is higher than those who purchased goods in e-commerce platforms (7%).³ This positive trend of transactions in both platforms must be utilized to accelerate the digital economy growth in Indonesia.

¹Facebook and Bain & Company, "Digital Consumers of Tomorrow, Here Today," Insights, August 06 2020, <https://www.bain.com/insights/digital-consumers-of-tomorrow-here-today/>.

²Kataadata, "96% Pengguna Internet di Indonesia Pernah Menggunakan E-Commerce," September 2019, <https://databoks.katadata.co.id/datapublish/2019/12/03/96-pengguna-internet-di-indonesia-pernah-gunakan-e-commerce>.

³ISEAS – Yusof Ishak Institute, Indonesia National Survey Project (INSP), 2017, dalam Yose Rizal Damuri, "E-commerce in Indonesia: The Rise of Online Commerce and its Impact on Firms' Performance and Consumers," CSIS Working Paper (Jakarta: CSIS Indonesia, 2020).

Figure 1. Transaction Value of E-Commerce in Indonesia (2014-2020) in Trillion Rupiahs



Source: Bank Indonesia

BPS (2019), in a census ranging across 101 cities and regencies in Indonesia, found that only 15.08% of MSMEs that put use e-commerce as their business platform

only 15.08% of MSMEs that put use e-commerce as their business platform and the majority rationale of not migrating is due to their sense of comfort in operating their business offline. This indicates that the root challenge of digital economy development in Indonesia is not derived only from digital infrastructures, logistics, and financial supports (Damuri, 2020) and the behavior of entrepreneurs who are reluctant to change.

Looking at the distribution alone, e-commerce users in Indonesia have yet to spread evenly. *Susenas* (2017) data reveals that most entrepreneurs who utilize digital technology for their business activities are located in Java Island (68%) and thus display a lower usage of e-commerce by entrepreneurs outside Java Island. The disparity is also seen for the consumer side with 35% of e-commerce consumers located in DKI Jakarta and West Java. This data has uncovered an accessibility issue and educational gap on e-commerce that need to be addressed if the government committed to developing the digital economy in Indonesia.

Covid-19 and Digital Economy

In this time of the Covid-19 pandemic, activities requiring direct physical contact have an inherent risk of infection, consequently making the digital economy an essential factor for Indonesia's economic recovery. Along with other countries all over the world, Indonesia had its economy contracted in 2020. BPS data shows that in the 3rd quarter of 2020, Indonesia's economy is still experiencing a contraction by 3.5% *y-o-y*. However, it is recovering a bit from the previous quarter, which amounts to 5.3% *y-o-y*. Household consumption as the main foundation of Indonesia's economy also displays some improvement—especially from lower-income households.

⁴Badan Pusat Statistik (BPS), Statistik E-Commerce 2019. (Jakarta: Badan Pusat Statistik: 2019), <https://www.bps.go.id/publication/2019/12/18/fd1e96b05342e479a83917c6/statistik-e-commerce-2019.html>

Nevertheless, the same trend still cannot be seen from the middle to upper-income families which prefer to save more from this uncertain time.⁵

Amidst the current recession happening in Indonesia, it is noteworthy for the government to have a national recovery program. One of which is to use digital technology that inherently not requiring direct physical contact. The government has cooperated with banks and fintech to distribute the benefits of *Kartu Prakerja*. Bank Indonesia also stated that Rp 31.08 Billion of People's Business Credit (KUR) had been successfully allocated through banks and e-commerce by September 2020.⁶ Many other collaborative programs, such as training for MSMEs, had also been done with the expectation of accelerated digital transformation among MSMEs. Digital economy platforms—including social media—can support national recovery programs, one of many is to help distribute social assistance and stimulate demand.

With the realization of Rp 180 Trillion total transactions in e-commerce by August 2020, Bank Indonesia estimates a total transaction of Rp 429 Trillion throughout 2020.

Generally, the pandemic has greatly enhanced the digital economy industries in Indonesia.⁷ The demand for groceries in e-commerce that had significantly risen and food deliveries has balanced the transportation and travel sectors' negative growth. In a short period, the Covid-19 pandemic has effectively altered Indonesia's transaction behaviors, where direct interaction between sellers and buyers is avoided. This brings online transactions in e-commerce platforms more relevant to be done. With the realization of Rp 180 Trillion total transactions in e-commerce by August 2020, Bank Indonesia estimates a total transaction of Rp 429 Trillion throughout 2020.

Bain & Company shows a 37% increase in Indonesia's new digital consumers during this pandemic era.

The increase in e-commerce transaction value is due to a shift in consumption patterns offline to online during this pandemic. Also, Bain & Company shows a 37% increase in Indonesia's new digital consumers during this pandemic era.⁸ Furthermore, these new consumers are mostly located in non-metropolitan areas, thus enlarging and expanding e-commerce access throughout Indonesia.

The Formulation of E-commerce Regulatory Framework

Looking at the positive trend and the enormous potential, the government must play its part not only as of the regulator but also as the accelerator of Indonesia's e-commerce growth. The digital economy will become the backbone of economic development in the future. Even after the pandemic is over, digital transformation will still be an irreplaceable part of Indonesia's and global economies. Several notable considerations for the regulatory framework on e-commerce and digital economy facilitate a smooth development when formulating the regulations needed.

Flexibility and Balance between Regulation and Innovation

The first major consideration is that it will always be a challenge for the government to follow innovation and technological development. Thus, it is crucial to maintain and evaluate current or new regulations to be flexible and to complement technological innovation.

With the rapid development of technology, the e-commerce industry needs to have different types of business (B2B and B2C), which are more identical in e-commerce platform practices, and C2C

⁵ Estimasi OCE Bank Mandiri dalam Muhamad Chatib Basi, "Resesi dan Pembalikan Ekonomi", *Harian Kompas*, 11 November 2020.

⁶ Sugeng, "Peran Fintech dalam Transformasi & Pemulihan Ekonomi Nasional", disampaikan dalam Diskusi Indonesia Fintech Society, Jakarta, 9 November 2020.

⁷ Google, Temasek, Bain & Company, "E-Conomy SEA 2020: At full velocity: Resilient and Racing ahead", 2020.

⁸ Ibid

is more similar in trading practices social media) to get a *light-touch regulation*. Flexibility is the keyword to support the use of digital platforms by business actors such as MSMEs. Regulations, for example, need to provide different treatment between different business models. Business activities that directly interact with consumers can be distinguished from online transactions that do not function. With this division, it becomes clearer what individuals or companies need to comply with these e-commerce regulations. Therefore, not all business actors need to carry out the same obligations.

Many business actors on online platforms are still in the trial-and-error stage or do not operate mainly in e-commerce platforms. Thus, business actors' entry and exit will always be very high and will only become a hindrance if everyone needs to take care of licensing. Flexibility is also required in the area of taxation and other obligations. It would be beneficial for small entrepreneurs to be freed from this tax burden to provide room for them to grow first.

The purpose of regulation should be to facilitate digital economic growth, not increase entry barriers or increase business expenses.

This flexibility is also required for the development of the digital platform itself. On a small scale, start-ups may find the cost of following regulations too high. What is feared is that only companies with large capital can meet these obligations, thus stifling innovation. The purpose of regulation should be to facilitate digital economic growth, not increase entry barriers or increase business expenses.

Balance between Agendas

In economics, digital economy activities are known as the representation of a *two-sided market*. In contrast, buyers and sellers of goods and services interact through intermediaries—in this case, the digital platform—and one party's decision will determine the others' including the digital platform itself.⁹ Under this type of transaction, many parties are involved. For that reason, regulation should take into account all agendas involved.

Consumers' protection is an essential element to provide a sense of security while doing electronic media activities.

With the entire economic process in the electronic realm, regulations need to ensure consumer protection in every transaction. Thus, a suitable mechanism needs to be prepared if there is a dispute between the seller and the buyer. Consumers' protection is an essential element to provide a sense of security while doing electronic media activities. It will be tough for Indonesia to encourage the e-commerce industry's growth if there is no trust from consumers.

However, consumer protection is only one of many aspects of securities needed. The seller in the digital platform must also be given enough attention and supports. Disincentivizing regulation must be avoided at all costs because the seller's involvement in this two-sided market has made their decision a significant influence on the consumer and the platform. The platform providers must also receive supports by enabling an encouraging ecosystem.

Harmonization among Best Practices and International

The borderless nature of e-commerce gave birth to a new global challenge. Currently, there are many primary principles on digital international trade that is being spoken on many occasions. No less than 85 WTO countries have been discussing issues regarding e-commerce and other digital trade. The problems being discussed ranged from the principle and regulations on international data traffics, goods and services traffic that use digital platforms, and many other aspects. The OECD countries and other developed countries also discuss the international taxation regulatory

⁹ Marc Rysman, Journal of Economic Perspectives—Volume 23, Number 3—Summer 2009—Pages 125–143

framework on international digital activities. Moreover, the ASEAN countries had also signed an e-commerce agreement since 2018—where Indonesia is still preparing to ratify.

Regulations that are not by international principles, such as in taxation, data processing, and requirements, give rise to the possibility that Indonesia will lose international competitiveness and the potential for a large digital economy.

Thus, it is necessary for Indonesia to harmonize domestic regulations with the directions of various international agreements. It will not be profitable for Indonesia to carry out various discriminatory policies and based on protectionist sentiments, which can marginalize Indonesia in the development of the digital economy. Regulations that are not by international principles, such as in taxation, data processing, and requirements, give rise to the possibility that Indonesia will lose international competitiveness and the potential for a large digital economy.

Besides, Indonesia also needs to be more active in various international negotiations and discussions to be able to bring national interests within the framework of international regulations that are currently being discussed. Of course, the national interest that is obtained must accommodate the interests of various parties in Indonesia, not only the interests of certain parties.

Notes on Indonesia's Current E-commerce Policy Framework

Last year, the government issued a Government Regulation (PP) as a corridor for Indonesia's e-commerce development. This PP was made to provide legal certainty for trading business actors in the e-commerce industry. By definition, electronic trading business actors are being divided into domestic and foreign players. The government hopes that this legal framework will protect consumers from boosting confidence to do online shopping. This regulation is also aimed at ensuring the level playing field between online and offline business actors and generally providing legal certainty for actors and investors.

In 2017, the government issued an e-commerce *Roadmap* to provide strategic direction for the e-commerce industry in the short term to support growth. Given the rapid development over the past three years, there is a great need for an update.

The government is currently trying to create a national digital transformation strategy, which will later become broader legal protection for a more comprehensive and integrated development strategy. This strategy is essential considering that issues in the digital world continue to grow in huge stride, which yet to be accommodated in the previous e-commerce roadmap. These issues include data protection, cross-border transactions, regulation of digital goods and transactions, and digital finance (fintech and cryptocurrency).

Making a roadmap and a digital economy strategy must provide direction for e-commerce policies and regulations in Indonesia. Without a clear strategy and direction, the regulations issued will tend to be ad-hoc and may not touch the problem's root. Unfortunately, various regulations have been published before the strategy and direction has been established.

Figure 2 E-commerce Policy Framework in Indonesia

Peta Jalan E-commerce	PP 80 tahun 2019	StraNas Ekonomi Digital
<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
<input type="checkbox"/> Financing & Taxation	<input type="checkbox"/> Business Player Definition	<input type="checkbox"/> Data Protection
<input type="checkbox"/> Consumer Protection	<input type="checkbox"/> Requirement of Business Player	<input type="checkbox"/> Cross-border Transaction
<input type="checkbox"/> Education and Human Resources	<input type="checkbox"/> Business Player Obligation	<input type="checkbox"/> Digital Goods
<input type="checkbox"/> Infrastructure	<input type="checkbox"/> Electronic Advertisement	<input type="checkbox"/> SMEs
<input type="checkbox"/> Logistic	<input type="checkbox"/> Payment and Delivery	<input type="checkbox"/> Digital Financing/Fintech
<input type="checkbox"/> Cyber Security	<input type="checkbox"/> Personal Data	
	<input type="checkbox"/> Dispute Settlement	

Source: author's documentation

Licensing regulations in the e-commerce industry are stated more clearly in the Regulation of the Minister of Trade No. 50/2020 which is effective in November 2020. With an online mechanism, the procedure for business licensing has been made easier. This is in line with the digital economy idea, which is to carry economic activities without the need for direct contact. However, several things can be improved in the regulation.

The most fundamental problem of the current regulation is a business generalization, whereas many types of businesses and platforms currently exist in electronic commerce. For example, entrepreneurs have their websites, or some that utilize online trading platforms (Tokopedia, Bukalapak, Lazada), and others who use social media (Facebook, Instagram).

These platforms have significant differences. In terms of access, everyone who has an email or phone number can have a social media account and use it for economic transactions. Meanwhile, those who wish to have a stall on the online trading platform need to register first. The implication is that trading platforms can have easier control if there is a dispute between entrepreneurs and consumers. It is also easier to collect data, which is one of the government programs.

Nonetheless, the implementation of this regulation on social media platforms is arduous. The buying and selling activities on social media are more C2C in nature, and every individual can easily offer their products through their accounts. Often this buying and selling activity is merely an additional job, especially during this pandemic when they are starting to look for alternative employment.

It is also important to remember that trading activities on social media are usually limited to advertisements of products and services being traded. In contrast, the transactions themselves are carried out outside the platform. In many countries, business actors under this mechanism do not need to be burdened with various obligations like business actors on e-commerce platforms, given the difficulty of implementation and potentially burdensome business expenses. It is feared that this will even provide a disincentive to conduct trading activities on digital platforms. Marketing on social media can be an entry point for wider use of digital platforms in the future, especially for micro and small businesses.

The current regulatory framework also lacks recognition of online aggregators' role as a bridge between producers, especially small and medium industries, to access e-commerce. For many business actors, the difficulty in conducting online trading is a matter of access and ability and the trade-off between producing and carrying out marketing activities. Aggregators can provide space for business actors to focus on their products and make innovations. Simultaneously, online buying and selling activities, starting from licensing and technical use of the platform, can be left to the aggregator. Regrettably, the existing regulations impose the same rules on these aggregators, even though they have different business models.

Closing

The rapid development of e-commerce in Indonesia and its high potential to support economic recovery and development in the post-pandemic era, the government's efforts to encourage the development of e-commerce should be supported. This commitment includes creating a regulatory framework to ensure legal certainty for this fast-growing sector.

However, the principle of prudence must still be adhered to so that the regulations made are not too restrictive which can hinder the growth of e-commerce in Indonesia. It is vital for the government to always have a mindset as an accelerator and has a light touch regulation on the digital sector, rather than just focusing on licensing and regulation alone. In addition, a collaboration between the government-platforms-MSMEs needs to be encouraged so that more and more micro and small entrepreneurs can adopt this digital platform to accelerate digital transformation in Indonesia and provide protection to all users providers of digital economy platforms.

CSIS Indonesia, Pakarti Centre Building, Indonesia 10160
Tel: (62-21) 386 5532 | Fax: (62-21) 384 7517 | csis.or.id