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# **Business ethics, illegal trade practices and rise of e-commerce industry**

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## **Abstract**

This study examined the new laws related to online business in Indonesia and the extent of freedom given to foreign investors. It also discusses whether new regulations would be able to check illegal trade practices. Using a survey methodology the study identified a few issues related to e-commerce transaction in Indonesia. Findings reveal that the Indonesian online business is growing but at the cost of compromises with legal mechanisms. In conclusion, the current study has assessed the need and importance of a legal mechanism to exist within the domestic Indonesian law to prevent unethical practices in ecommerce transactions.

**Keywords:** Ethics, Online Business, Infrastructure, Law.

# Ética empresarial, prácticas de comercio ilegal y aumento de la industria del comercio electrónico

## Resumen

Este estudio examinó las nuevas leyes relacionadas con los negocios en línea en Indonesia y el grado de libertad otorgada a los inversionistas extranjeros. También analiza si las nuevas regulaciones podrían controlar las prácticas comerciales ilegales. Utilizando una metodología de encuesta, el estudio identificó algunos problemas relacionados con las transacciones de comercio electrónico en Indonesia. Los hallazgos revelan que el negocio en línea de Indonesia está creciendo, pero a costa de compromisos con mecanismos legales. En conclusión, el estudio actual ha evaluado la necesidad y la importancia de que exista un mecanismo legal dentro de la legislación nacional indonesia para evitar prácticas no éticas en las transacciones de comercio electrónico.

**Palabras clave:** Ética, Negocio Online, Infraestructura, Derecho.

## 1. INTRODUCTION

In 2014 there were only 17.14% of individuals using the internet in Indonesia, which rose to 21.98% in 2015. Indonesia was the eighth largest internet user in the world in 2015 and Internet Live Stats have estimated that Indonesia is the twelfth largest group of internet users.

Southeast Asia's digital economy (which includes a variety of segments including e-commerce, online games, and online advertising) is estimated to surge to USD \$200 billion by 2025. Indonesia's digital market is forecast to account for 40.5 percent - or USD \$81 billion - of this total market in the region aiming to call Indonesia as the Silicon Valley of Southeast Asia. With an estimated USD \$46 billion, Indonesia's e-commerce sector will contribute most to the total.

While currently, e-commerce only accounts for less than one percent (worth US\$2 billion per year) of Indonesian retail spending, analysts believe that the country's fast-growing middle class and proliferation of smartphones will soon raise that share to eight percent (worth US\$8 billion) in just a few years. If that scenario were to happen, then Indonesia's e-commerce market would be the largest in Southeast Asia. However, infrastructure remains the biggest obstacle to the online retail industry. Indonesia's quality and quantity of infrastructure development are inadequate and therefore logistic costs are very high giving rise to expensive online products. But if the government remains committed to its ambitious infrastructure development plans then the online retail business of Indonesia is in a great position to grow rapidly (Agbim and Eluka, 2018; Obodo, 2018).

Recently, the government of Indonesia started with the construction of the Palapa Ring project construction, one of the nation's priority infrastructure projects that involves a huge undersea fiber-optic cable network to secure faster broadband to the entire archipelago, including the islands of Java and Bali. Expected to be completed by

2019, the online transactions in Indonesia would cross \$3 billion this year. In addition to infrastructural and logistics reforms, the Government has also announced to open e-commerce to foreign investment. This study has chosen Indonesia to discuss the ecommerce industry for mainly two reasons: firstly, Indonesia has the 4th largest population in the world, with the largest geographical area in Southeast Asia, tends to reflect e-commerce benchmarks of other developing countries in the region. Secondly, the sheer size of the population and vast territory are good reasons for businesses in Indonesia to adopt e-commerce.

However, as commonly found in most developing countries, the adoption of e-commerce in Indonesia is still lagging behind when compared to the developed countries (Kartiwi & Macgregor, 2008). This study used a survey methodology to understand the state of ecommerce in Indonesia and how it plans to surge ahead to become the largest ecommerce player in the south Asian region. It also examined the impact of the increase of ecommerce activities on trade practices and identified such illegal unethical trends that have penetrated into the whole system. Finally, the study looked into the legal aspects and identified such elements in the Indonesia Business Law that dealt with e-commerce and which primarily stood in support of the domestic trader as compared to a foreign investor.

### *1.1. Indonesia's E-Commerce Industry*

There exist various definitions offered by several authors. Turban (2010) defined e-commerce as the process of buying, selling, transferring, or exchanging products, services, and/or information via computer networks, mostly Internet and intranets. While, Tagliavini et al. (2001), argued that any economic activity conducted via the internet can be called e-commerce. In more detail, Clarke (2005) elaborated the detailed elements of e-commerce as support services for trading... encompass(ing) inter-organizational email, directories, trading support systems for commodities, products, customized goods and services, management information, and statistical reporting systems.

Three factors have contributed to Indonesia's rapidly growing e-commerce industry: (1) demographic composition (2) rapidly rising mobile phone users as well as smartphone penetration, and (3) rising Internet penetration. Additionally, about half of the total population being below 30 years of age, the younger generations of Indonesians absorb online lifestyle much faster than compared to the older generations. There are nearly 100 million smartphones users in Indonesia and Internet penetration has reached 50 percent of the population. Most popular E-Commerce products in Indonesia are an item like clothes, shoes, footwear, bags, watches, airplane tickets, mobile phones/smartphones, vehicle accessories, cosmetics and books. However, the online retailing currently forms less than one percent of total retail business in Indonesia, it is expected online retail subsector

to expand rapidly over the next few years reaching 20 percent of total retail in Indonesia by 2020.

Indonesia has interpreted e-commerce in a manner agreeable to its people, law and existing trade practices. For this reason, therefore, e-commerce does not exist as a classified business form in its Negative Investment List. The reason is that Indonesia does not differentiate businesses based online through e-commerce methods or through brick and mortar stores in shopping malls. Moreover, with the growing online transactions, internet companies have come under much closer surveillance. A new provision has been added for all internet companies to apply for a correct business classification (KBLI) if they wish to get investment application approval (Ahmed, Umrani, Qureshi & Sarmad, 2018; Ali & Haseeb, 2019; Haseeb., 2019; Suryanto, Haseeb, & Hartani, 2018). However, in the absence of clear guidelines, internet companies are not able to decide their classification status. There are a few guidelines but not too sufficient.

### *1.2. Opening Foreign Investments*

Most internet companies in Indonesia are run by foreign nationals and therefore they look for overseas investors who can be registered for business under such classifications that would not restrict foreign ownership. Web portal classification, for instance, was used so often that BKPM started to investigate whether all of those portals actually meet the requirements and found a lot of misuses. This means

that this loophole has been closed and future investors are required to give a much more detailed investment plan in order for the Indonesia Investment Coordinating Board (BKPM) to determine the correct business classification. In this connection, in order to legalize the issue, the MOCI is expected to issue a government regulation for this sector.

Presidential Decree No. 44/2016 on the Negative Investment List issued the decree to revise the list and include those items that are currently disallowed to foreign investments. The Indonesia Investment Coordinating Board (BKPM) informed that a Law would be promulgated soon to provide 100 percent foreign investment if the minimum capital is at least IDR 100 billion (approx. USD \$7.4 million) for the establishment of an e-commerce company in Indonesia.

### *1.3. E-commerce Players in Indonesia*

In recent years, e-commerce sites have sprung up recently as Lazada.co.id, Olx.co.id, Tokopedia.com, Elevenia.com, Blibli.com, Traveloka.com, Bhineka.com, Pegipegi.com, Qoo10.com, Kaskus.com, Mataharimall.com and others. In fact, based on the rating agency website, Alexa.com, 5 of the 20 best-selling sites in Indonesia is an e-commerce site, namely: Lazada.co.id, Bukalapak.com, Onlickads.net, Tokopedia.com, and Olx.co.id. Companies like Lazada, known as the Amazon of Southeast Asia, are already operating within Indonesia. Lazada, operating since 2013 was rated as the largest B2C site in Indonesia during 2014 (taking the top spot from Amazon.



The company reportedly averages around 6.5 million views a month with Indonesians spending on average 181 minutes on their smartphones every day – the longest time in the world.

However, recently there is a flux of e-commerce players in Indonesia ranging from giants like Rakuten of Japan to local players such as Tokopedia, all of which have risen by the rapid growth of Internet access and smartphone penetration in the archipelago. Other sites operating in the country include Alibaba, with 3.9 million views/month and eBay with 2.2 million views/month. Amazon is though planning to invest into Indonesia with a physical presence. To give it a tough competition, Tokopedia, the local company and one of Indonesia's top consumer to consumer (C2C) marketplaces has reportedly received over US\$100 million in funding from venture capitalist firms like Softbank and Sequoia Capital. Such large cash injection will spur further investment into the e-commerce businesses in Indonesia.

#### *1.4. Problem Statement: Unethical Trade Practices and Absence of Legal Mechanism*

The problem started when e-commerce players in order to compete rigorously and beat the rival companies and acquire a big market share resorted to unethical practices and adopted illegal methods. A few of these include: Kosong (no stock) implying that buyers may have to rush or book in advance even though the product

may be available; Buyers could not check stock directly nor the stock availability is updated. Palsu (counterfeit), selling fake products by identical trademark or the brand name; drop shipping (collecting orders, then passing it on to another merchant), resulting in long delays in shipping or sometimes cancelling the order after a long wait; Scammers (false companies) selling goods at attractive prices that are too good to be true; several companies do not accept credit cards and prefer to receive payments in cash or through cash payment agencies; communication and transactions are not supported by the system. Payments are made without going through the payment gateway.

Besides such practices, there are indiscriminate taxes that consumers are not properly made aware of. Generally speaking, any goods bought from outside of Indonesia is subjected to taxes. The exemption is however over goods up to US\$100 (inclusive of shipping charges). Indonesia's importation tax is among the highest in the world which makes it difficult to import items. It is particularly difficult to ship in foods, drugs, and cosmetics. They require special authorization from BPOM (Badan Pengawas Obat dan Makanan – Food and Drug Inspection Agency) which allows only a limited inventory after paying the high cost of shipping and taxes. Companies like Amazon refuse to enter the Indonesian e-commerce business owing to these constraints and taxation rules, though Amazon promises the consumers to refund any excess of import duty collected.

## **2. LITERATURE REVIEW**

The Government of Indonesia announced the launching of its 14th economic policy package on 10 November 2016 under the Coordinating Economic Affairs Ministry as well as the Ministry of Communication and Information Technology. This economic policy package focuses on providing incentives for e-commerce and creative industries to support this sector, which offers significant opportunities for Indonesia's youthful and tech-savvy population. This regulatory package, which is also known as a road map for e-commerce, aims to support the development of Indonesia as a digitally focused economy. Furthermore, as Indonesia's e-commerce sector is set to reach \$130 billion in transactions by 2020, consumer protection and cyber security are also being addressed. Moreover, this new regulation will ensure that foreigners who do not meet the threshold of \$7.3 million but have a joint venture with a local partner, can only own a maximum of a 49% stake in the business (Kinasih, 2016).

E-commerce has thus changed the way a business sells, purchases or deals with its customers and suppliers but it has also changed the business perspective from production excellence to "customer intimacy" Macgregor & Vrazalic (2007) and from being agent of seller to being agent of buyer (Achrol & Kotler, 1999), and the business has shifted its focuses from physical goods to a service, information and intelligence focus (Rayport & Jaworski, 2001). As a result, the new economy era - the information era - has been created.

To be able to survive in the new economy, therefore, a business is pushed to adopt the technology. Jerry Jasinowski, President of the US National Association of Manufacturers, in the Wall Street Journal affirmed that small firms need to get in the e-commerce game or they are going to be shut out of a critical part of the marketplace (Shahalam et al., 2011; Williams et al., 2009; Daniel & Grimshaw, 2002).

### *2.1. Laws and Regulations*

In this section, evidence has been collected from the existing laws of the Indonesian government that relates to the e-commerce business and online trading involving electronic transactions and internet applications. Subsequent to amendments as proposed by the Indonesian government, it is also assumed that a few of these regulations shall also be reviewed and amended to suit the latest changes and development.

#### *i. Law No. 7 of 2014 regarding Trade (the Trade Law):*

In 2014, the Indonesian Government enacted the Trade Law, Article 66 of which provides that further provisions on trade transactions through electronic systems shall be regulated by government regulation. However, to date no draft government regulation has been issued to the public, although press reports have indicated one is under discussion, led by the Ministry of Trade (MOT) together with several stakeholders such as Ministry of Communications and Information (MOCI), the Ministry of Home Affairs, the Indonesian

Internet Services Providers Association (APJII), Bank Indonesia, the Indonesian Financial Transaction Reports and Analysis Centre (PPATK) and social media network providers. Media reports have also indicated that a draft government regulation on e-commerce is under consideration.

It contemplates three types of e-commerce transactions: (i) sellers (merchants), (ii) organizers of e-commerce transactions through electronic systems (Penyelenggara Transaksi Perdagangan Melalui Sistem Elektronik or PTPMSEs) and (iii) intermediary service organizers (Penyelenggara Sarana Perantara or PSPs). It appears that this draft of government regulations may require retail sellers and merchants to obtain certificates or licenses from the MOT to conduct e-commerce transactions. It also appears that any foreign PTPMSE that wants to enter the Indonesian market would be required to establish an Indonesian entity. Media reports have indicated that PSPs may be required to register with the MOT but it is not clear whether they also must establish Indonesian entities.

ii. Law No. 11 of 2008 regarding Electronic Information and Transactions (the ITE Law) and Government Regulation No. 82 of 2012 regarding the Implementation of Electronic Systems and Transactions (GR 82")

The ITE Law, GR 82 and various MOCI regulations implementing the ITE Law deal partly with the e-commerce sector. An e-commerce business actor is also regarded as an Electronic Systems Provider since it manages a website and stores personal data of its

customers. The law states that e-commerce website itself must be registered with the MOCI because it has a domain name. At present, there are no requirements to register or obtain a license from the MOCI for e-commerce business actors. However, investors are advised to verify licensing requirements with the MOCI before entering this business since it could regulate this sector at any time (Lee, 2019).

iii. Ministry of Communications and Information

Technology Regulation No. 82 of 2012 regarding Implementation of Electronic System and Transactions (MOCI Reg 82/2012").

Article 41 of MOCI Reg. 82/2012 states that, any business actor conducting an electronic transaction may have to be certified by a Certificate of Competence Institution. The purpose of a Certificate of Competence is to show evidence that a business actor conducting electronic trading has been assessed or audited by an authorized agency. The proof that a Certificate of Competence has been obtained is a trust mark logo on the web home page of the business actor. However, this is a compulsory requirement applicable only for electronic transaction providers for national services. This requirement is not mandatory for electronic transaction providers that are not providing any services intended for national services. Therefore, few Indonesian electronic transaction providers, and in particular ecommerce business actors, have trust mark logos on their websites (Indriastuti, 2019; Zare, 2015).

iv. Government Regulation No. 39 of 2014 regarding List of Business Fields Closed to Investment and Business Field Open, with

### Conditions to Investment (GR 39/2014")

GR 39/2014 is the Indonesian government's latest version of the Negative Investment List (the 2014 DNI). The 2014 DNI contains a list of those sectors that are closed for foreign investment or are open with restrictions. As noted above, the e-commerce business sector is presently closed to foreign investment. This is because e-commerce activities are regarded as retail activities open only for domestic investors (Yang et al., 2019; Soo et al., 2019; Kaithari et al., 2017).

### **3. CONCLUSION**

Indonesia is still in the early stages of e-government implementation or the government offering remedies linked with ecommerce transactions in the country. The delay has, of course, increased unethical practices in the country however evidence collected have shown that the government understands stakeholders' perspectives and is, therefore, looking forward to making amendments in its services and provide useful remedies to all stakeholders. The current study has assessed the need and importance of a legal mechanism to exist within the domestic Indonesian law to prevent unethical practices in e-commerce transactions. Using a survey methodology, the study identified a few issues related to e-commerce transaction in Indonesia. The study also highlighted the activities of ecommerce players in the region. It has also collected information on

the relevant laws related to e-commerce and trade practices in Indonesia.

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