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Regulating the Regulator: Improving consumer protection under a Twin Peaks regulatory framework

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A B S T R A C T

Australia is in the midst of a financial regulatory crisis. Evidence of malpractice, fraud, criminality, contempt for the law, and the abuse of consumers on an industrial scale, all while Australia's Twin Peaks regulators looked on, has come as a shocking surprise. The implications stretch well beyond Australia: they are relevant wherever the Australian 'Twin Peaks' model has been adopted or is under consideration. This article argues that the Twin Peaks model must be analysed from the perspective of regulatory design, as well as implementation. The design - the architecture of Twin Peaks - remains optimal. However the implementation - the plumbing - requires urgent reforms. Drawing on the work of notable international scholars, this article proposes a new accountability framework for the two, peak regulators, in order to enhance their efficacy. In the process of rescuing Twin Peaks from its current inadequate plumbing, consumers may expect to enjoy levels of protection commensurate with those of a developed economy possessed of rule of law.

Keywords: Twin Peaks; consumer protection, regulatory theory, financial system regulation, Sentinel, Sunshine Commission, regulatory enforcement, regulatory implementation, Australian financial services Royal Commission

Ⅰ. Introduction

This article analyses a proposed framework, the goal of which is to improve protection of consumers of financial products and services, within the Australian Twin Peaks regulatory model.

While Twin Peaks is widely regarded as the optimal model by which to regulate the financial system, and while its adoption is steadily increasing across the globe, the model's progenitor, Australia, is in the midst of a financial regulatory crisis. Consumer abuse and market misconduct in Australia has become a national emergency. As a consequence the Australian Federal government established the Australian Royal Commission of Inquiry into Misconduct in the Banking, Superannuation and Financial Services Industry[1] (hereafter 'RCI' or 'Royal Commission') in November 2017. So widespread and egregious has been the litany of misconduct, dishonesty and fraud perpetrated against consumers of financial products and services which has emerged in the first six months

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[1] Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry, "Home", Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry, 2018, accessed: 11 January, 2018.

of testimony before the Commission, that the Australian public has been left reeling. A recitation of instances of misconduct (which is primarily in the form of consumer abuse), or a description of the types of harm visited upon consumers is not within the purview of this article. Suffice it to say that even before the establishment of the RCI, the extent and gravity of consumer abuse was sufficient to deem the establishment of such a Commission a necessity. What has emerged during testimony indicates that the abuse that was known of, and which precipitated the establishment of the Commission was a mere tip. The remainder of the iceberg is still to be uncovered.

What has been of equally great concern is the evidence that has emerged of how Australia's consumer protection peak, the Australian Securities and Investments Commission (ASIC), ignored evidence of misconduct or actively colluded with regulatees, and failed consistently for over ten years to protect consumers or punish wrongdoers. It is for this reason that the current crisis may accurately be described as a 'financial regulation crisis'. What this writer describes as Australia's GF(r)C – *Great Financial (regulatory) Crisis.*

Consequently this article will focus on how to improve the efficacy of consumer protection within the Twin Peaks regulatory architecture. To that end this writer will draw upon the work of a number of leading scholars, each of whom has put forward mechanisms for enhanced oversight, and with that, the prospect of enhanced regulator efficacy. Together these mechanisms are termed a 'regulator for the regulators'.

Ⅱ. A regulator for the regulator

In the aftermath of the Global Financial Crisis (GFC) the prevailing narrative asserted that the GFC was as a result of poor market conduct and wide-scale consumer abuse (principally in the US subprime lending market). Similarly, the perceived solution appeared at first blush to require ceding more power to the regulators.[2] This narrative-cum-solution assumed that the regulators were inadequately empowered to begin with.[3] Whether this was correct requires a deeper analysis, and one which takes account of regulatory capture.

> This cannot be stressed enough. As emphasised by a vast literature, financial institutions pay virtually unlimited sums to shape financial policies, regulations and supervisory practices to serve their private interests. As emphasised by an equally vast literature, narrow political constituencies work tirelessly on tilting the financial rules of the game so as to collect a greater share of the economy's resources.[4]

Not only because a thorough investigation of the causes and possible solutions requires an investigation of all potential culprits, but more importantly, because there is existing scholarship which specifically points to the existence of capture of regulators prior to the GFC.[5] Solutions aimed at addressing capture then become relevant to an inquiry into the enhancement of Australia's Twin Peaks regime (and other, later Twin Peaks adopters), in light of the evidence of regulatory capture also in Australia, which in turn precipitated our GF(r)C.

Despite the ever-increasing body of evidence that points to the failures of our regulators, the response from the Australian Federal government was, initially at least, to provide our regulators with more power, such as the new bank executive accountability regime.[6] Again, this begs the question: was the poor performance of Australia's

[2] See for example: Treasury Laws Amendment (Banking Executive Accountability and Related Measures) Bill 2017 (Cth) 2017.

[3] See: Frederic S. Mishkin, NBER Working Paper Series, *Over the Cliff: From the Subprime to the Global Financial Crisis*, National Bureau of Economic Research No 16609 (2010); Paul G. Mahoney, Law, Economics, & Business Workshop, *Deregulation and the Subprime Crisis*, Berkley Law: Legal Scholarship Repository (2016).

[4] Ross Levine, "The governance of financial regulation: reform lessons from the recent crisis", series edited by Monetary and Economic Department, in *BIS Working Paper*, Vol. 329, Bank for International Settlements, November, 2010, p 10.

[5] Stijn Claessens & Laura Kodres, "The Regulatory Responses to the Global Financial Crisis: Some Uncomfortable Questions", in *IMF Working Paper*, no. WP/14/46, Research Department and Institute for Capacity Development, International Monetary Fund, March, 2014, p 6/12; Andrew Baker, "Restraining Regulatory Capture? Anglo-America, Crisis Politics and Trajectories of Change in Global Financial Governance", *International Affairs (Royal Institute of International Affairs 1944-)*, Vol. 86, no. 3 (May, 2010); Eric Monnet, Stefano Pagliari & Shahin Vallée, "Europe Between Financial Repression And Regulatory Capture", in *Finance & Financial Regulation*, Bruegel Working Paper 2014/08, Bruegel, July, 2014; Simon Johnson & James Kwak, *13 Bankers: The Wall Street Takeover and the Next Financial Meltdown*, 2010.

[6] *Treasury Laws Amendment (Banking Executive Accountability and Related Measures) Bill 2017 (Cth)*, 2017.

regulators a result of inadequate power and resources? Or was it as a result of inadequate enforcement of existing powers? This question is crucial, because if the cause was the latter, then providing more power to our regulators will not fix an underlying unwillingness to exercise the powers already provided. Extending more power to regulators that do not exercise the powers they already have is not a uniquely Australian response. As Barth et al state:

> Unfortunately, in the wake of the [global financial] crisis, we now seem to be lurching from one simplistic, unqualified ideology— that private markets will look after society's interests—to an equally flawed, if not more perilous, ideology—that the Guardians will always act in society's interests, so let's give them more power to do so.[7]

Evidence before the RCI, and anecdotal evidence leading up to the establishment of the RCI indicated that Australia's peak regulators, ASIC and APRA (Australian Prudential Regulation Authority) were, at best missing in action, or at worst actively colluding with dishonest, and at times criminal financial services providers.

> It's not that the Australian Securities and Investments Commission (ASIC) is in need of added muscle. It needs to grow a spine··· ASIC is the law enforcement agency that shies away from enforcement, particularly in the top end of town.[8]

Evidence abounds of serious misdeeds in the Australian financial services industry so widespread and so common, that there is a credible argument to be made that criminality, fraud, and consumer abuse has become systemic. Australia's banc assurers have rigged interest rates, repeatedly stolen from their customers – including customers who were deceased[9] - and rejected legitimate insurance claims for death and permanent disablement, including from customers who had been left paralysed;[10] despite having paid premiums, in some cases, for decades. In other cases banks foreclosed on borrowers who had never missed a payment, or had never been in arrears.[11]

> Since the financial crisis, they have forked out more than $1 billion in fines and compensation for their misdeeds. But not one senior banking executive has faced a court room for any of this.[12]

Despite being invested with the power to launch criminal and civil proceedings, for the past 15 years ASIC has instead chosen to use, almost exclusively, enforceable undertakings[13] - described as a *slap on the wrist,* replete with a *hollow threat*[14] to take stronger action if the undertaking is breached. Criticism of the manner in which these undertakings are heavily negotiated, and the comparatively small fines that are attendant thereto has been withering.[15] At other times financial service providers have simply ignored the undertakings given to ASIC, without repercussions.[16]

It is within the context of these failings that the 2014 Financial System Inquiry ('Murray Inquiry' or 'FSI')[17] recommendation for the creation of a Financial Regulator Assessment Board[18] (hereafter referred to as the 'FRAB'; 'Assessment Board'; 'Board of Assessment'; or simply as the 'Board') to oversee the regulators warrants examination.

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[7] James R. Barth, Gerard Caprio & Ross Levine, "Making the Guardians of Finance Work for Us", Chap. 8, in *Guardians of Finance: Making Regulators Work for Us*, 2012, p 211.

[8] Ian Verrender, "Banking royal commission: How ASIC went missing in action with the banks", series edited by Australian Broadcasting Corporation, in *Analysis*, Australian Broadcasting Corporation, 25 April 2018, 1:09 pm, accessed: 4 July, 2018.

[9] Emily Stewart, "Banking royal commission: How dead people can be charged bank fees", series edited by Australian Broadcasting Corporation, in *News*, Australian Broadcasting Corporation, 19 April 2018, 4:50 pm, accessed: 4 July, 2018.

[10] Dr Benjamin Koh, "The Price of Silence: by Commonwealth Bank whistleblower Dr Benjamin Koh", series edited by Michael West, in *Finance*, Michael West, 30 May, 2018 accessed: 4 July, 2018.

[11] Elizabeth Redman & Cliona O'Dowd, "Banking royal commission live: CBA may have breached ASIC Act, Hayne told", 'News', *The Australian*, 2018 at 4:43 PM.

[12] Ian Verrender, op cit.

[13] Ian Ramsay & Miranda Webster, "ASIC Enforcement Outcomes: Trends and Analysis", *Company and Securities Law Journal*, Vol. 35, no. 5 (November, 2017).

[14] Ian Verrender, op cit.

[15] Dan Ziffer, "Banking royal commission casts doubt on regulator ASIC's enforceable undertakings", series edited by Australian Broadcasting Corporation, in *News*, Australian Broadcasting Corporation, 17 May 2018, 7:48pm, accessed: 4 July, 2018.

[16] Clancy Yeates, "Funeral insurer targeting Indigenous Australians ignored court orders", 'Business', *The Sydney Morning Herald*, Business Day ed., 2018.

[17] Financial System Inquiry, "Financial System Inquiry Final Report", series edited by The Treasury of the Australian Government, The Treasury, Commonwealth Government of Australia, November, 2014.

[18] Ibid, p 239.

This recommendation forms part of an international body of scholarship aimed at enhancing regulator efficacy – a body of scholarship that dates back to the late 1800s and the contribution of Charles Francis Adams Jnr.[19]

Arguably the most developed proposal is that of Barth, Caprio and Levine.[20] Published in 2014, the authors address the failures exhibited by the regulators' prior to the GFC. Their proposal for a panel of oversight comprised a committee of experts called a 'Sentinel'.[21] Their thesis builds upon the work of Charles Adams Jnr who, observing the unfettered market power exercised by the railroad barons, argued in the late 1860s for the creation of an expert, permanent, apolitical body – a regulatory commission:

> To organize that intelligence should be the labor of a new commission, composed of such men in material life as Story was in law, Mann in education, and Bache in science. These men must study causes, point out effects, and indicate remedies.[22]

McCraw[23] christened this proposed commission a 'Sunshine Commission': 'a commission that would shed the cleansing light of disclosure on the hitherto secret affairs of business corporations'[24] to which Breger et al added: 'an impartial body of experts that would investigate, examine, and report on railroad activities but would not have enforcement power.'[25]

Informed by this scholarship, Barth et al's proposal is for an institution that would act on the public's behalf. This would entail providing informed, expert, and independent assessments of financial regulation. To that end they envisaged an authoritative institution, and independent of short-term politics; independent of the financial services industry; vested with the power to demand the information necessary for assessing and monitoring the regulators – the 'Guardians of Finance'; possessed of multidisciplinary expertise to enable it to process the information it gathers; sufficiently prominent to deliver assessments to the public and Parliament; and capable of influencing an open discussion of financial regulatory policies. Barth et al argue that these characteristics are 'necessary for improving the still seriously flawed financial regulatory institutions operating around the world today.'[26]

An institution such as this would plug a gap that the authors assert exists world-wide. They assert that the 'absence of an institution with these five traits means that the public cannot effectively evaluate financial regulation and, therefore, cannot constantly oblige the Guardians to act in the public interest.'[27]

> The Sentinel would improve the entire apparatus for writing, enacting, adapting and implementing financial regulations. … reduce the ability … to obfuscate regulatory actions … make regulators more accountable for [their] societal repercussions … reduce the probability and costliness of regulatory mistakes and supervisory failures. … the Sentinel's reports to legislators would help reduce the influence of special interests …. sole objective … to evaluate the state of financial regulation from the [public's] perspective … help inform… and… augment public influence over financial regulation.[28]

Barth et al and Levine target this new framework squarely at enhancing regulator efficacy, by providing a structure that addresses what is currently lacking:

> Successful and lasting reform requires addressing a core cause of the systemic malfunctioning of financial systems —poor governance of the Guardians of Finance.[29]

Examples exist, but are relatively rare. They include (to a limited policy-extent – that is to say limited to the function of the provision of independent expert advice, at arms-length from both the regulator and the regulatee)

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19 Adams, Jr., Charles Francis, "Boston", Vol. 106, no. 218 (January, 1868).

20 James R. Barth, Gerard Caprio & Ross Levine, op cit.

21 Ibid, p 203-232.

22 Adams, Jr., Charles Francis, op cit, p 25.

23 Thomas K. McCraw, *Prophets of Regulation: Charles Francis Adams; Louis D. Brandeis; James M. Landis; Alfred E. Kahn*, 1986.

24 Ibid, p 15.

25 Marshall J. Breger & Gary J. Edles, *Independent Agencies in the United States: Law, Structure, and Politics*, 2015, p 27. See also a proposal along similar lines for an 'Expert Review Panel': Stefano Pagliari, "How Can We Mitigate Capture in Financial Regulation?", Chap. 1.0, in *Making Good Financial Regulation. Towards a Policy Response to Regulatory Capture,* edited by Stefano Pagliari, series editor: ICFR (International Centre for Financial Regulation), 2012, p 4.

26 James R. Barth, Gerard Caprio & Ross Levine, op cit, p 204.

27 Ibid, p 203.

28 Ross Levine, op cit, 2.

29 James R. Barth, Gerard Caprio & Ross Levine, op cit, p 213.

the Inspector General of Taxation in Australia,[30] and the UK's Financial Policy Committee (UKFPC),[31] established as a Statutory Body in April 2013,[32] with binding authority over the agencies under its jurisdiction. UKFPC has been charged with looking for the next 'bombshell' that may strike the financial system, by identifying, monitoring, and acting against systemic risks.[33] Notwithstanding the scarcity of operational precedents however, and in light of the failures of the Australian regulatory responses to date, the notion of an over-arching framework of independent, expert evaluation nonetheless bears analysing.

Ⅲ. The Australian Response to regulatory failures

On 7 December 2014 the FSI released its Final Report. The Report made a number of recommendations, one of which specifically addressed the need to enhance regulator efficacy - Recommendation 27:

> Create a new Financial Regulator Assessment Board to advise Government annually on how financial regulators have implemented their mandates. Provide clearer guidance to regulators in Statements of Expectation and increase the use of performance indicators for regulator performance.

This Financial Regulator Assessment Board would provide annual reports to government on the performance of both APRA and ASIC, as well as on the Reserve Bank of Australia's regulation of the payment-system.[34] The proposed Board would analyse the regulators' performance relative to their mandates and priorities as specified in their Statements of Intent (SOIs), but not the mandates themselves.[35] In a similar vein, the proposed 'Sentinel's' ambit of responsibility would entail the provision of annual reports only, in order to prevent a blurring of the boundaries of accountability.[36] The proposed Assessment Board was more closely aimed at improving the efficacy of ASIC,[37] which had been found to be severely lacking.

> '[analysis of ASIC's performance] showed ASIC as a timid, hesitant regulator, too ready and willing to accept uncritically the assurances of a large institution that there were no grounds for ASIC's concerns or intervention.'[38]

The FSI's aim in establishing such an Assessment Board was to: 'help to ensure ASIC has the appropriate skills and culture to adopt a flexible risk-based approach to its future role. Its overall performance would also be subject to annual review by the [Assessment Board].'[39] To that end the Board was intended to provide annual, independent advice to the Federal government on the performance of the regulators,[40] and crucially, that these reports would be made public.[41] In so doing this proposal would emulate, at an ideational level, the proposal put forward by McCraw[42] that relies upon public exposure and opprobrium, as opposed to formal legislative instruments, to ensure that regulators remain true to their duty to protect the public interest. The FSI envisaged that the Assessment Board would evaluate the full gamut of regulator efficacy: how they discharge their mandates, balance competing priorities, allocate resources, and respond to challenges.[43]

In putting forward this proposal, the FSI took account of the current framework of Parliamentary oversight in Australia, but found it to be materially deficient, and inadequate to the task of monitoring the regulators, in order to ensure that they maintained a minimum level of efficacy. In particular, the occurrence of parliamentary

30 Inspector-General of Taxation (IGT), "Our Role", in *About us*, Inspector-General of Taxation (IGT), 2018, accessed: 24 July, 2018.
31 Financial Policy Committee, "Financial Policy Committee", series edited by Bank of England, in *Financial Stability*, Bank of England, 2014, accessed: 26 September, 2014.
32 *Financial Services Act* 2012 (United Kingdom).
33 Jill Treanor, "Farewell to the FSA – and the bleak legacy of the light-touch regulator", 'Business', *The Guardian/The Observer*, 2013.
34 Financial System Inquiry, op cit, p 239.
35 Ibid, p 239.
36 James R. Barth, Gerard Caprio & Ross Levine, op cit, p 217.
37 Financial System Inquiry, op cit, p 235.
38 Senate Economics References Committee, "The Performance of The Australian Securities and Investments Commission", series edited by Senate Standing Committees on Economics, in *Executive summary*, Parliament of Australia, 26 June, 2014, p xviii.
39 Financial System Inquiry, op cit, p 237.
40 Ibid, p 240.
41 Ibid, p 239.
42 See fn 23, above.
43 Financial System Inquiry, op cit, p 240.

assessments were found to be irregular; that whilst Parliament reviewed regulators' annual reports, its scrutiny was ad hoc, and often focused on particular issues or decisions, as opposed to overall regulator performance.[44] This, in combination with the complexity of the regulator's mandates, made effective monitoring of the regulators difficult. Furthermore, Parliament's review of regulators' annual reports was not supported through regular, independent assessments.[45]

Crucially, the FSI did not call for the Assessment Board to be a separate agency – doubtless in order to avoid a blurring of the boundaries of responsibilities and jurisdictional remit – but did propose that it be supported by its own secretariat, seconded from the Federal Treasury.[46] In so doing contamination between the functions of the Assessment Board and those of Treasury could be better avoided, which the FSI deemed valuable in light of Treasury's policy role as a member of Australia's Council of Financial Regulators.[47]

The FSI envisaged a Board comprised of between five and seven members, who would serve in a part-time capacity, and would bring to the Board industry and regulatory expertise, but would not be drawn from current employees of regulated entities.[48] The Board's assessments would be strictly ex post, and limited to reporting its findings to government.[49] As such the Board would be precluded both from directing the regulators, or adjudicating upon individual complaints against the regulators,[50] and nor would it be permitted to enquire into financial system regulatory policy, such as the desirability of regulators' mandates.[51] Rather it would determine if the regulator's mandates, as they stood, were being met. It would, however, replace the Financial Sector Advisory Council (FSAC). Curiously, despite the fact that FSAC would be dissolved only if a Board of Assessment was established under the FSI proposal, the Australian Federal government nonetheless announced that it would reconstitute the FSAC in 2016 to provide advice to the Australian government on, inter alia, the performance of Australia's financial system regulators, and areas in need of regulatory reform.

To be clear, this is not a de facto Financial Regulator Assessment Board, as envisaged by the FSI. Here it is of note that of the nine members of the FSAC committee, four are in banks and merchant banks, one in a non-bank financial institution (shadow bank), one in a life-assurer, two in securities issuers, and one in a funds manager. All are in executive positions in those entities (CEO, Executive Chairman, or MD).[52] This is, therefore, effectively a formally recognised peak industry lobby group.

Juxtaposed with that is the emphasis from the FSI on the need to avoid undue influence over the Board. As a result the FSI proposed reliance upon diversity in the composition of the Board, and/or a code of conduct.[53] As such these recommendations neatly reflect what was envisaged for a Sentinel by Levine:

> [T]he Sentinel would be both politically independent and independent of financial markets. Senior members would be appointed for staggered terms to limit political influence. To shield it from market influences, senior staff would be prohibited from receiving compensation from the financial sector ... create an institution in which the personal motives, ambitions, and prestige of its employees are inextricably connected to accurately assessing the impact of financial regulations on the public.[54]

The FSI proposal envisaged a Board capable of providing guidance to regulators on how to balance competing objectives, such as 'promoting competition and efficiency, maximising business certainty and minimising compliance costs.'[55] By way of example, the FSI cited that lower barriers to market entry may encourage competition and benefit consumers, but may also increase risks for consumers by allowing for the establishment of smaller, less well-capitalised, and more fragile institutions.[56] Taken

[44] Ibid, p 241.
[45] Ibid, p 241.
[46] Ibid, p 243.
[47] Ibid, p 239.
[48] Ibid, p 239.
[49] Ibid, p 235/239.
[50] Ibid, p 239.
[51] Ibid, p 245.

[52] The Honourable Kelly O'Dwyer MP, Minister for Revenue and Financial Services, "Financial Sector Advisory Council", series edited by The Treasury, Australian Government, in *Media Releases*, The Treasury, Australian Government, 6 May 2016, accessed: 25 July, 2018.
[53] Financial System Inquiry, op cit, p 239/240.
[54] Ross Levine, op cit, p 2.
[55] Financial System Inquiry, op cit, p 241.
[56] Ibid, p 242, fn 18.

together, the FSI report asserted that such a Board would 'strengthen the accountability framework governing Australia's financial sector regulators.'[57] The FSI concluded that:

> The Inquiry believes that creating a new Assessment Board to review regulator performance is the best way to address the gap it has identified in the current accountability framework. … would facilitate improved scrutiny of regulator performance without creating new agencies or compromising existing accountability …. [it is] not intended to reduce the independence of regulators in executing their statutory mandates.[58]

In light of the findings of the Senate Inquiry into the performance of ASIC,[59] handed down some five months prior to the publication of the FSI Final Report, the arguments in favour of the creation of a Financial Regulator Assessment Board were compelling. Subsequent to those developments of 2014, the arguments in favour of the establishment of a FRAB have moved beyond compelling. The Australian Federal government's failure to accept the recommendation to establish an Assessment Board – the only recommendation from the FSI which the Abbott-Turnbull government rejected[60] – has proven catastrophic, and has been instrumental in the maintenance of a regulatory framework so unfit for purpose as to have facilitated Australia's GF(r)C.

Whilst not within the scope of this paper to analyse in depth, two further seminal developments bear mentioning as great inflexion points in the collapse of the credibility of Australia's regulatory framework: one has been alluded to earlier – the RCI. The RCI has exposed a venality and at times wickedness in the conduct of our largest financial institutions.[61] As appalling as this behaviour has been, the fecklessness, timidity, indolence and ineptitude of our conduct regulator, ASIC, has been equally shocking.[62] This writer predicts that ASIC, at least in its current form, will not survive – and nor should it. In addition to its legion of other failures, too numerous and too disparate to mention here, ASIC stands accused, by this writer at least, of no-less than having undermined Australian rule of law.

The second significant inflexion point in the performance of Australia's regulators was revealed in February 2018 with the release of the Interim Report of the Australian Productivity Commission's inquiry into the financial industry.[63] The Commission concluded that Australia's financial industry has devolved into a four-bank oligopoly,[64] bereft of competition, abusive and exploitative of its customers,[65] and comprising, now, the most profitable banks in the world by return on equity.[66] The Commission

[57] Ibid, p 240.

[58] Ibid, p 244.

[59] See fn 39, above.

[60] Australian Government, "Improving Australia's Financial System, Government response to the Financial System Inquiry", series edited by The Treasury of the Australian Government, The Treasury, Commonwealth Government of Australia, 2015, p 23.

[61] See for example: Clancy Yeates, op cit; Elizabeth Redman & Cliona O'Dowd, op cit; Dr Benjamin Koh, op cit; Emily Stewart, op cit; Stephen Letts, "ANZ, NAB agree to $100 million settlement of swap rate rigging case", series edited by Australian Broadcasting Corporation, in *Analysis*, Australian Broadcasting Corporation, 10 November 2017, 3:03 pm, accessed: 20 March, 2018.

[62] John Durie, "Regulator bares its teeth", 'Feature Edition', *The Australian*, Feature Edition ed., 2016; Andrew Schmulow, "New laws on bankers behaving badly don't matter in light of ASIC inaction", 'Business & Economy', *The Conversation*, 2016 3:09 PM AEDT; Ian Ramsay & Miranda Webster, op cit; Ian Verrender, op cit; Dan Ziffer, op cit; Andrew Schmulow, "APRA and ASIC have the legal power to sack bank heads, but they need will power", 'Business & Economy', *The Conversation*, 2018, 3:25 pm.

[63] Peter Harris, Julie Abramson & Stephen King, "Competition in the Australian Financial System, Draft Report", Productivity Commission, Government of Australia, Productivity Commission, January, 2018.

[64] Ibid, p 32.

[65] Citizens Electoral Council of Australia, "APRA blatantly props up housing bubble to rescue the crooked banks", in *Media Releases*, Citizens Electoral Council of Australia, Friday, 27 April, 2018, accessed: 25 July, 2018; Stephen Letts, "Big banks get $19b benefit over rivals from financial rules", series edited by Australian Broadcasting Corporation, in *News*, Australian Broadcasting Corporation, 16 November 2016, 12:26 pm, accessed: 25 July, 2018; Bendigo and Adelaide Bank Bank of Queensland, ME Bank and Suncorp Bank, "Levelling the Playing Field", in *Financial System Inquiry*, Financial Services, Financial System Inquiry, Regional Banks Submission to the Financial System Inquiry, March, 2014; Anonymous, "Loyal bank customers exploited: Productivity Commission draft report", 8 February, 2018, accessed: 23 July, 2018; Paul Karp, "Banks are exploiting loyal customers, warns Productivity Commission", 'News/Australia', *The Guardian*, Australia edition ed., 2018 7:48 am AEDT; J Eyers, "How APRA became the regulator of choice", 'Banking & Finance', *Australian Financial Review*, 2017 at 11:00 pm; Peter Ryan, "'Four pillars' banking policy is 'ad hoc' and 'redundant', Productivity Commission warns", series edited by Australian Broadcasting Corporation, in *News*, Australian Broadcasting Corporation, 7 February 2018, 5:03am, accessed: 22 July, 2018.

[66] Anonymous, "FactCheck: do Australian banks have double the return on equity of banks in other developed economies?", *The Conversation*, 2017 12.50 pm AEST; Adam Courtenay, "Aussie banks the world's most profitable", *Your Week InFinance*, (2016), (accessed:

sheeted much of the blame for this outcome to the policies of the Australian bank regulator, APRA.[67] Under those policies Australia's big four banks (the Australia New Zealand (ANZ) Banking Group; the Commonwealth Bank; National Australia Bank (NAB); and Westpac Bank) have gone from enjoying significant market share prior to the GFC, to today, where their market share is now crushingly dominant.[68] In the process of becoming the most profitable banks in the world, Australia's banks have sapped-dry the remainder of the real economy.[69] While APRA may claim that it does not have a competition mandate, and whilst that may be true, it is also true that APRA is required to maintain regulatory neutrality.

> In performing and exercising its functions and powers, APRA is to balance the objectives of financial safety and efficiency, competition, contestability and competitive neutrality…[70]

However, its deployment of internal ratings-based models (IRBs) for the four largest of Australia's banks is but one example of a lack of regulatory neutrality – one which according to Australia's second- and third-tier banks has consistently favoured the big four in respect of their costs of funding, and which in turn has enabled the big four to gain an unassailable competitive advantage in the market.[71]

There are further examples of deep, systemic distortions that are now evident in the Australian economy, which may not be possible to rectify, and which point to serious and sustained deficiencies in the manner in which Australia's bank regulator has approached its task. Possibly the most socially disruptive of these is the increase in the price of residential property in Australia's major population centres, particularly Melbourne and Sydney. There are credible arguments that have been made that these two property markets – now of the most expensive in the world – became so as a consequence of capital adequacy rules laid down by APRA.[72] In particular, as residential property is classified as a 'tier 1' asset, the amount of capital that Australia's banks are required to retain in order to extend residential mortgages is lower than the amount of capital they are required to retain for any other kind of loan. As a consequence Australia's banks have channelled ever greater amounts of money into mortgages, and in the process activated a spiral of more money chasing ever more valuable property, leading to ever greater impetus to invest in property.[73] Indeed, residential property has, for the past twenty years at least, been Australia's slow-motion *Bitcoin*.

To be clear, these distortions to the housing market and the lack of competition have seriously eroded consume protection: in the case of competition, the provision of a fair and accessible market; in the case of the mortgages, home-ownership accessible not only to the wealthy or the very wealthy. While the FRAB, like the proposed Sentinel, would not inquire into *financial system regulatory policy*, and the concomitant regulator mandates that emanate there from, it would be empowered to evaluate a *financial system regulator's policies*, to determine whether they were well-suited to contributing to the dis-

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29 March), published electronically; cf Gaurav Sodhi, "Why Australian banks earn so much profit", *Intelligent Investor*, (2016), (accessed: 4 October), published electronically.

67 J Eyers, op cit; Citizens Electoral Council of Australia, "APRA blatantly props up housing bubble to rescue the crooked banks", (2018), (accessed: Friday, 27 April), published electronically; Stephen Letts, "Big banks get $19b benefit over rivals from financial rules", op cit.

68 Bendigo and Adelaide Bank Bank of Queensland, ME Bank and Suncorp Bank, op cit, p 2; Peter Harris, Julie Abramson & Stephen King, op cit, p 3.

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72 Gaurav Sodhi, op cit.; Citizens Electoral Council of Australia, "APRA blatantly props up housing bubble to rescue the crooked banks", op cit.

73 Stephen Letts, "Big banks get $19b benefit over rivals from financial rules", op cit.

charge of the regulator's mandate?

It should be noted also that examples of APRA's failures as a regulator and the concomitant detriment to consumers is not confined to distortions created by APRA's own internal policies. Included are implementation and enforcement failures. The RCI has heard evidence that APRA knew about misconduct, fraud and theft being committed against Superannuation members on an industrial scale - 15,000 criminal breaches at Commonwealth Bank for its failure to move default Superannuation accounts into 'MySuper' accounts,[74] which in turn attract no fees – to turning a blind-eye to 550,000 Superannuation members at various divisions of National Australia Bank being charged fees for no service – a form of theft. Remediation just for fees for no service is expected to top AUD$ 1 billion.[75] Throughout this time APRA took no legal action of any kind. To this end APRA stands accused of colluding with regulatees, not simply so that the regulated entities in question could escape past instances of consumer abuse, but that they could continue to commit abuses against their customers, on an industrial scale, within sight of the regulator, and to continue doing so for several years further, without any form of sanction. In the case of a division of Commonwealth Bank's 15,000 criminal breaches of MySuper legislation, this was allowed to continue for a further two years after the regulator first became aware of this allegedly criminal misconduct.[76]

> It is submitted that the case studies suggest that the approach of neither APRA nor ASIC to regulation of superannuation entities is sufficient to achieve specific or general deterrence. The evidence suggests that APRA is reluctant to commence court proceeding and to take public enforcement action.[77]

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Ⅳ. Conclusion

With these factors in mind it was already in 2014 important for the continued health and future prospects of the Australian economy that a framework be implemented to evaluate the performance of the financial sector regulators. This was evident at the time, thanks to the findings of the Senate Inquiry into the performance of ASIC, and it has become more evident with each passing year since.

The revelations before the RCI are of a kind that not only can they not be ignored, but they will not be ignored. Neither the current government nor a future Opposition-led government will be capable of resisting implementation, to some degree or another, of the far-reaching changes that the Australian electorate will undoubtedly demand. As a consequence the reconsideration of the proposal for the establishment of a Financial Regulator Assessment Board is more crucial than ever before. The time for that reconsideration is now.

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Encouraging Microcredit through Group Guarantee Loan Model: The Success Story of MEKAAR Program in Indonesia

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A B S T R A C T

In 2015, PT Permodalan Nasional Madani/PNM (Persero) initiated the establishment of Mekaar, a state-owned financing product targeting the pre-prosperous micro business sector. Among all the local organizations that provide microcredit service for the poor, Mekaar is considered as the nearest to the poor, since the program is targeted productive poor women with a credit amount of only IDR2 million (around US$150 in average) per person. With its unique peer-lending model, Mekaar has successfully reached more than 1,300,000 customers within two years of its establishment. The peer-lending model was originated from microcredit practice in Bangladesh; however, PT PNM has been successful in adjusting the peer-lending model with Indonesian culture and market through their Mekaar programs.

In this article, we examine how Mekaar penetrates Indonesian pre-prosperous market with ultra microfinancing. The information presented in this article is collected primarily from field observation to several Mekaar's branches and interview with the key person in those branches. First, we presented an overview of PT PNM, an Indonesian state-owned company that created Mekaar program, including its vision and mission. Then, we evaluate Mekaar's loan product and how PT PNM satisfies the funding needs for Mekaar program. We also evaluate characteristics of Mekaar's target market, Mekaar's peer lending model, and the role of Account Officer as a facilitator between the lender and the borrowers in Mekaar's case. Finally, we evaluate the impact of Mekaar's program and provide consideration related to future planning of Mekaar.

Keywords: microcredit, peer-lending, poverty

Ⅰ. Introduction

In general, the term microcredit is used to describe the small loans granted to low-income individuals who are unreachable by formal banking system. It is part of larger microfinance industry, which includes other financial products/services intended to serve low-income individuals such as micro saving, micro insurance, and other basic financial products/services for the poor. In Indonesia, where 99% of all businesses are micro, small, and medium enterprises, micro credit is very important to support the development of these businesses. For millions of Indonesia's micro and small enterprises, the commercial banking system is a closed door. Even if these business owners want to borrow from Bank, the lending regulations — which require customers to have proof of a permanent job, income and collateral- prevents them from borrowing. Most of them have no collateral to give to the bank. Hence, micro and small business owners frequently complaints that capital constraints limit their ability to grow, and microcredit emerges as a solution to solve that capital problem (The Asia Foundation, 2003).

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In the beginning of microcredit development in Indonesia, Bank Rakyat Indonesia is known as the formal financial institution that successfully extending micro credit on commercial basis (The Asia Foundation, 2003). Other than that, most small business owners can get micro credit through microfinance institutions (MFIs). It is estimated that there are more than 600.,000 microfinance institutions in Indonesia, however Indonesian Financial Services Authority still has difficulties in verify all those institutions.

One of the institutions that are considered successfully spreading microcredit throughout Indonesia is PT Permodalan Nasional Madani (PNM) through its program called Mekaar. Mekaar is established in 2015 and it has objectives to give small loans to pra-prosperous women so that they have capital to open or develop their own business. The microcredit products offered by Mekaar have quite different characteristics than the other microcredit products. For example, they offer a very small amount of loans, only IDR2 million per individual, intended to serve very poor clients. Hence, the term ultra-microcredit is often used to address Mekaar microcredit. Moreover, Mekaar clients must attend a weekly group meeting and carry out several rituals before Mekaar officers collect their weekly installment. Some of the rituals are reading Pancasila (five national principle of Indonesia), praying together according to client's religion, and reading customer's promise. Generally, the rituals are the same for all Mekaar clients across Indonesia, however, Mekaar also adjust the rituals according to the culture and language of specific region. For example, in Aceh, due to the strong Islamic culture, the clients refused to read Pancasila.

The implementation of this microcredit system proves to be successful in Indonesia. In just two years after its establishment, Mekaar shows an amazing clients growth. Now, it already has 1.26 million active clients across Indonesia, and 1.3 million if we also account for inactive clients with 0.0023% non-performing loans. PT PNM (Persero) even has a goal to reach 2 million active clients by the end of 2017. This achievement has put Mekaar into national spotlight. The distribution of Mekaar clients in various regions in Indonesia can be seen in Table 1.

This paper aims to analyze the way PT PNM implements its ultra-microcredit products[1] and how the microcredit product could successfully penetrate the poor market across Indonesia. The data obtained for this paper is the primary data obtained from interviews with the parties involved in the implementation of Mekaar and also from interviews with Mekaar clients. The secondary data is obtained from company's internal data. The paper is structured as follows: section 2 introduces the institution that creates Mekaar, including its vision and mission. After that, the analysis is conducted starting from the discussion about types of loan products offered by Mekaar and the way PT PNM (Persero) satisfies its funding needs for Mekaar program. Characteristics of Mekaar's clients will be discussed in section 4. Section 5presents the group lending system that is implemented by Mekaar. Section 6 reports organizational structure of Mekaar and how the decisional and operational level works to support the success of Mekaar program. In the last section, which

Table 1. Total of Mekaar Branches per Province

No.	Province	Total of Mekaar Branches	Number of Clients
1	Banten	51	53,464
2	Jambi	6	4,339
3	West Java	281	397,262
4	DKI Jakarta	20	26,148
5	Central Java & DI Yogyakarta	250	198,106
6	East Java	271	280,803
7	South Kalimantan	4	2,592
8	West Kalimantan	6	8,091
9	West Nusa Tenggara	35	43,370
10	East Nusa Tenggara	26	48,288
11	Papua	4	2,334
12	Maluku	3	1,901
13	South Sulawesi	21	28,757
14	West Sulawesi	5	11,323
15	Southeast Sulawesi	7	3602
16	Central Sulawesi	3	4,702
17	Aceh	26	39,311
18	North Sumatera	51	83,033
19	West Sumatera	17	21,907
20	Riau	11	7,279
21	South Sumatera	27	29,097
22	Lampung	45	66,803

[1] The authors use ultra-microcredit and Mekaar interchangeably throughout this paper

is section 7, author will provide an evaluation of Mekaar's practice in Indonesia and consideration related to future planning of Mekaar.

Ⅱ. Microfinance Industry in Indonesia

The Indonesian microfinance industry is exceptionally old, dated back to the era where Indonesia was colonized by the Dutch. The industry is very heterogonous and wide variety of financial institutions provide microfinance products for small-scale borrower in Indonesia, such as formal banks, cooperatives, microfinance institutions, and there is also an informal moneylender (loan sharks) that offers loan to the low-income people. One of the best-known player is Bank Rakyat Indonesia (BRI) with its Micro Business Division (referred as BRI Units) (Charitonenko & Afwan, 2003). The bank was established its BRI Units in 1970 and has been offering various financial products intend to serve micro segment since then. Other than BRI, there are another type of banks that also provide microloans such as Regional Development Banks (Bank Pembangunan Daerah, BPD) and Village Credit Agencies (Badan Kredit Desa, BKD).

In 2018, Bank Indonesia issued a regulation which requires Bank to have at least 20% of its loan portfolio dedicated to microloans. Furthermore, current Indonesian President, Joko Widodo (Jokowi), urges Banks to provide loans more evenly, especially to micro, small, and medium enterprise segments. This situation implies that the competition in microloans industry will be stiff in Indonesia starting from 2018, because the microfinance institutions must compete not only with other MFIs, but also with formal banks to provide microfinance products to micro entrepreneur and low-income segment. In average, the interest rate for microloans offered by Banks is 18% (per February 2017). This number is much lower than the interest rate offered by ultra-microcredits such as Mekaar, which is more than 20%. However, the higher interest rate for ultra-microcredit products is justifiable because ultra-microcredit clients do not have to provide any collateral for the MFIs and the default risk is likely higher. In the future, the interest rate for ultra-microcredit product is expected to decrease since Indonesia's Minister of Finance is committed to support the development of ultra-microcredit and is currently conducting an evaluation towards ultra-microcredit interest rate.

In addition, since 2013, Indonesian Financial Services Authority (OJK) also issued a regulation which requires microfinance institutions to have a business license and legal entity. However, until December 2017, there are only 180 entities of microfinance institutions that register themselves to Indonesian Financial Services Authority (OJK) (Indonesian Financial Services Authority, 2017). Whereas, based on the initial academic data for Micro Finance Institution Bill Draft, there are about 600,000 MFIs in Indonesia. Meanwhile, based on the re-calculation of OJK with financial institutions there are 24,000 to 25,000 MFIs spread across Indonesia. Thereby, there is no definite data regarding the number of microfinance institutions in Indonesia, and although OJK has encourage MFIs to register themselves, many of them are still unwilling to legally register their institutions to OJK.

Ⅲ. PT Permodalan Nasional Madani/PNM (Persero): Historical Background, Vision, and Missions

PT PNM is a state-owned company established by Indonesian government as part of strategic solution to increase economic equality and welfare of society through the development of access to financing and capacity building program (Ministry of State Owned Enterprises Republic of Indonesia, 2014). The company began its operation in 1999 and has a vision to become a leading financial institution in promoting sustainable value added for Micro, Small, Medium Enterprises and Cooperatives based on their principle of Good Corporate Governance (GCG). Pursuing its vision, PT PNM sets itself to work towards the achievement of four mission: (1) Carry out various efforts, related to the company's operations, to improve the feasibility of business and entrepreneurship capabilities of Micro, Small, Medium Enterprises and Cooperatives (MSMEC) people, (2) To assist Micro, Small, Medium Enterprises and Cooperatives actors in obtaining and increasing access to financing from financial institutions, both banks and non-banks which will ultimately increase MSMEC contribution in the expansion of employment and the improvement of the welfare of the community,

(3) Improve employee's creativity and productivity to achieve the best performance in the effort of developing MSMEC sector. These vision and missions then translated into several products and services including ULaMM (Micro Capital Services Unit), Mekaar (Fostering Prosperous Family), Business Capacity Development Program, Management Services, and Partnership Program with Other Institution. However, this paper will analysed further only the ultra-microcredit product of PT PNM (Persero), namely Mekaar. The rest of the paper will use the word Mekaar to represent Fostering Prosperous Family Product of PT PNM.

Ⅳ. The Product

Currently, Mekaar only offers one type of product to its clients, which is group guaranteed loans with an amount of IDR2 - 5 million per person within group. In the beginning of the cycle, all clients will be given a loan of IDR 2 millions. If the clients run their business successfully and completed their obligations properly in the first loan cycle, then they can get a subsequent larger amount of loan (second loan cycle). For each of subsequent loan cycle, PNM will give clients a lower interest rate. This policy aims to encourage clients to become a good debtor. In other words, clients will get subsequent loans with a better interest rate if they can run their business properly and proof their disciplined (e.g. attend weekly meeting, pay weekly loan installment).

Customers can choose two types of loan term that are 25 weeks or 50 weeks. With an amount of IDR2 millions of loans, the installments to be paid each week are as follows:

First cycle	
25 weeks installment	IDR90,000/ week (±US$6.75)
50 weeks installment	IDR50,000/week (±US$3.75)
Second cycle	
25 weeks installment	IDR87,600/week (±US$6.57)
50 weeks installment	IDR47,600/week (±US$3.57)

Mekaar has unique selling propositions (USP) for its loan product: 1) the clients do not have to pay installment in the first two weeks after they got the loans. This allows clients to settle their business first so that they can pay the first installment, 2) the clients do not have to pay installment in two weeks during Idul Fitri (Moslem's holy day). In Indonesia, where most of the people are moslems, the clients tend to spend more money and return to their home village to celebrate Idul Fitri with their family. Surprisingly, these simple USPs are one of the factors that attracts clients to borrow from Mekaar. They find it helpful to not have to pay loan installment during those weeks.

The loan requirements are very easy to fulfill, so these loans are suitable for the target market, which is pre-prosperous women who are mostly very poor and have no financial knowledge. Mekaar loan requirements are as follows:

a) Be aged between 18 to 55 years, because the target market is a housewife who already have or intend to open a business, then the age of the customer must be in the working age range of work.
b) Use the loan for working capital to develop a business or open a business, in other words, women of productive age who have no job/business are welcome to become Mekaar customers as long as he has the intention to open a business and have the intention to improve his life
c) Willing to attend weekly collective payments and pay weekly installment by herself, it is a testament to customer commitment to be disciplined and follow the rules set by Mekaar
d) Create a minimum group of 10 people and a maximum of 30 women in the same neighborhood, where all members must agree to be the guarantor of the other members. Mekaar does not require customers to have collateral when applying for loans, and instead there is a guarantee from the group that each member will pay off the loan. With such schemes it is evident that Mekaar has succeeded in minimizing NPLs. In fact, NPL Mekaar is said to be almost non-existent (only 0.0023%). According to the study that PT PNM conducted, group guarantee lending is effective because the customers are afraid of other group members and account officers if they do not perform their obligations to pay installments every week. In addition, further loans will be provided if the

customer has a good record on the previous loan, hence, they feel encouraged to follow the rules
e) Prospective customer may use KTP or Resi or Certificate of Domicile from local neighborhood association (rukun tetangga or RT) as a proof of identification.

Related to the funding, in the beginning, PT PNM get funding from Indonesian government to provide financing to pro-prosperous people in Indonesia through Mekaar. However, due to the success of Mekaar program, PT PNM get additional capital loan from state-owned Bank, namely Bank Mandiri, as much as IDR300 billion. In addition, Bank Mandiri is committed to provide bank accounts with an initial balance of IDR100,000 for Mekaar's customers. Bank Rakyat Indonesia (BRI) also participated to channel IDR500 billion as capital loan to PNM in 2016. As of September 2017, PNM has disbursed the amount of ±IDR2,7 billion to ± 1.3 million clients across Indonesia through its Mekaar program.

Table 2. Summary of Mekaar's Product Characteristics

Product Characteristics	Mekaar Group Guaranteed Loans
Creation date	2015
Client type	Pra-prosperous women (10 – 30 women per group)
Collateral required	Group guarantee
Loans term range	25 weeks and 50 weeks
Repayment schedule	Weekly
Loans size range	IDR2,000,000 – IDR2,500,000 (currently)
Interest rate	24% per year (1st cycle) and 19% per year (2nd cycle)

Ⅴ. Fostering Prosperous Family (Mekaar): Target Market

The target market for Mekaar is productive housewives, who live under the poverty line (pre-prosperous woman). In other words, the target market is a woman who has income of less than US$1.9 per day. Mekaar chose woman as a target market because they believe that women have bigger sense of responsibility to their family rather than men. Besides, woman is also known to have honesty and ability to manage finances within the family. Therefore, PNM strongly believes that empowering women is propelling motor to increase the income and achieve better living standards of underprivileged family.

To become Mekaar clients, women should have the following characteristics:

1. Be aged 18-55 years
2. Use the loan for working capital to develop a business or open a business
3. Have a commitment to attend weekly collective payments and deposit weekly installment by themselves

In brief, any productive underprivileged, unbanked, or poor women could apply to become Mekaar's clients as long as they have willingness to improve their lives and to follow rules specified by Mekaar.

Ⅵ. Mekaar Group Lending System

In general, the lending process should begin by reaching the potential clients. In the case of Mekaar, the account officer (loan officer of Mekaar) has responsibility to promote Mekaar through door-to-door marketing. Account officer (AO) only use Mekaar flyer as a promotion tools, they have to persuade prospective clients using a direct conversation and eventually build trust. It is not easy to convince prospective clients, who are basically uneducated women who never have a loan before. Most of them, especially those living in remote areas, are afraid to borrow. Hence, it is important for AO to build their trust from the beginning. Oftentimes, AO has to visit the house of prospective clients several times before they agreed to join and become Mekaar clients. AO has to explain that Mekaar is a loan product owned by state-owned enterprise, hence, Mekaar isnot solely aimed at seeking profit, but it is part of government commitment, through Ministry of State Owned Enterprise, to improve the welfare of Indonesian people. Most of the times, after explaining that fact, the prospective clients starting to trust Mekaar and willing to hear more explanation. In addition, prospective clients become interested with Mekaar loans after hearing that they do not have to pay the installment two weeks after the loan is disbursed and two weeks during Eid Al-Fitr.

If one prospective client agreed to become Mekaar clients, the AO will asked her to find another prospective clients and form a group consisted of 10-30 people. Typically, the one who gather members to form a group will become the leader and the members are their families or residents who live in the same area as the leader. The leaders will be responsible for dealing contracts between the group and Mekaar officer. Mekaar uses a group guaranteed system, in which all the group members are held accountable if one of their group members could not repay the loans.

After the group is formed, the prospective clients enter a prequalification stage. They will be asked to fill out a simple form, in which the prospective clients also need to get the consent from their husband in the form of signature. Then, AO will visit each of their houses and verify the prospective client's data. The data will be re-verified by the Head of Branch Office by visiting the prospective client's house. The group guaranteed loans are approved in the branch office. Once the Head of Branch Office approved the loan requests, there will be a trial period of five days, during which the Customer will be given information about Mekaar and the rituals that must be executed by the group members every week. This trial period is also a testament of prospective clients' commitment to Mekaar since they are required to attend the trial meeting for five consecutive days. If the prospective Customer is absent to attend, then the group will not be granted the loan. However, if all members of the group successfully demonstrate their commitment during the trial days, the loan will be disbursed to prospective clients one day after the trials ended.

In the 3rdweek after getting a loan, group members begin to attend meetings every week. Weekly meetings are named Weekly Collective Payments (PKM). In weekly collective payment, the client must pay the loan installment in accordance with the selected loan term (for example, if the group choose the 25 weeks term, then each member has to pay IDR90,000 per week). The loan amount and the installment amount should be the same for all group members; hence, all group members must have an agreement upon the selection of the loan term. Each group is also required to collect the solidarity money and emergency fund. If, in the future, there is a group member who cannot pay her weekly installment or did not come to the weekly meeting, then the leader of the group will use emergency fund and solidarity money to bail out that group member. The money is entrusted to the leader of the group. Then, in Weekly Collective Payments (PKM), the customer is required to perform rituals such as read a prayer (according to each member's religion), read Pancasila, and read customer promises.

Account officer will be responsible to collect the money in Weekly Collective Payments meetings. After collecting the money, the AO will calculate the money in front of all group members and all the members will act as a witness. In this case, Mekaar wants to show that they uphold the principle of transparency and they do not intend to take advantage of clients. Such simple action can build a client's trust towards the AO, and towards Mekaar as a whole.

Overall, PT PNM is not only offered a loan product for pre-prosperous women, but they also insert educational elements to their clients within the process. In each prayer, promises, and Pancasila that clients have to read each week, PT PNM indirectly wants to instill the value of honesty in doing business, discipline, and hard work. With Pancasila, the poor women are also taught to maintain harmony and mutual respect despite coming from different tribes or religions. Furthermore, Mekaar clients are also taught to save their money. In fact, currently, there are more than 300,000 Mekaar clients that has saving in Mekaar. Thus, in Mekaar, clients are prepared to become small or even medium business owners by firstly building their discipline, responsibility, and also being introduced to the banking system.

Ⅶ. The Organizational Structure

PT PNM is a state-owned company with tens of thousands of employees to support its business. PT PNM has several business units and products including Mekaar. Mekaar is managed separately under the supervision of an Executive Vice President (EVP). EVP along with portfolio manager and mentoring manager are responsible for designing Mekaar business development strategies. As for Mekaar, human resource is one of the key factors in achieving the 2 million customers target by the end of 2017. In the early stages, PT PNM put a lot of effort into setting up human resources system for Mekaar's operations in all branches from Aceh to Sorong Papua. As of September 2017, Mekaar employs 11,649 Account Officers, 1,464 Senior Account Officers and 1,137 Branch Heads and approximately 500 additional workers. The organization structure within Mekaar and the linking of decision-making process between Mekaar's officer and PNM managerial, especially in the credit lending process, are shown in the Figure 1 below.

Account officers, senior account officers, and branch heads are in charge to do day-to-day operations in each branch area. Furthermore, account officer play a vital role in the success of Mekaar program. As company's frontline employees, account officers interact directly with costumers during most of their working hours. Account officers are regarded as company's representatives that being influential in the level of customer satisfaction and engagement. Account officers are responsible for visiting loan groups in their area to conduct Weekly Collective Payment. The locations of weekly collective payment are sometimes become one of the biggest challenges faced

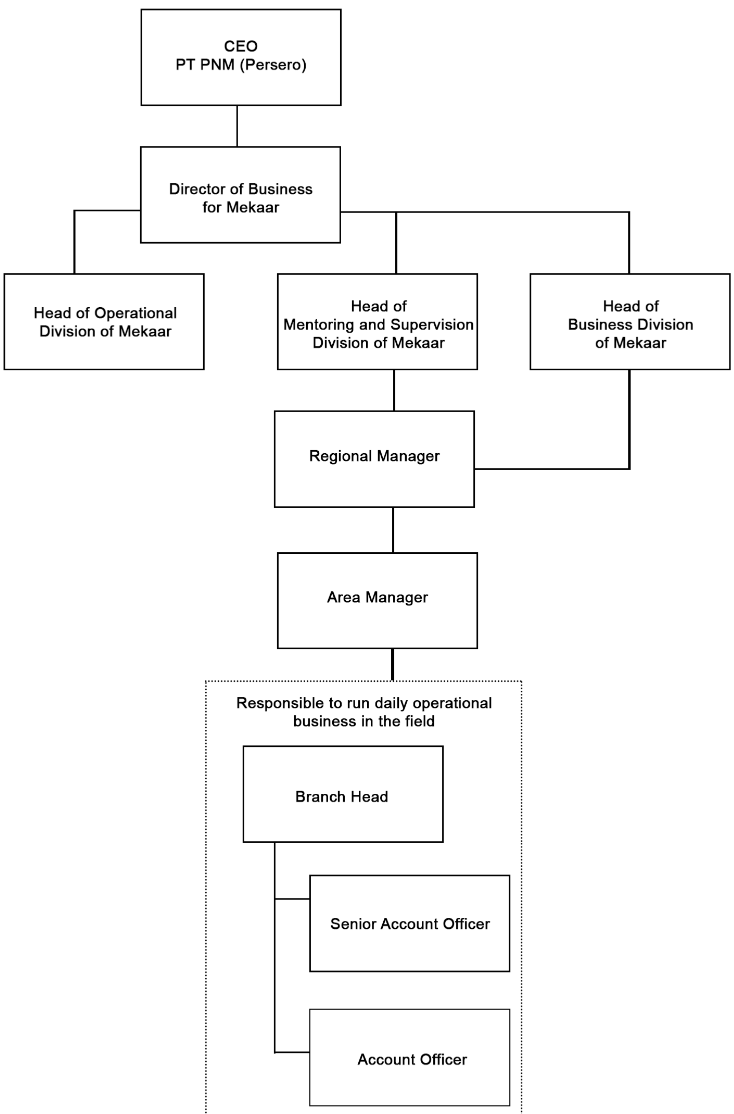

Figure 1. Mekaar Organization Structure

by account officers. Some of Mekaar branches operate in remote area and have no vehicles access, which take hours from the nearest branch.

In addition to collect the weekly payment, account officers are also assigned to recruit potential customers. The highest level of educational attainment of the account officers is high school diploma. During the employee induction period, PNM provides product knowledge and soft skills training to the newly recruited account officers. Additional necessary trainings are also provided by branch head, which are usually held on Saturday. Meanwhile, senior account officers are responsible for administering administrative matters in the branch office and the branch manager is the person who has the highest authority to make decisions regarding loan approval in his territory.

Ⅷ. Discussion

In terms of financial decision making, low income consumers have their own reasoning system (Sawady & Tescher, 2008). This segment have historical experience of being excluded from the mainstream for decades, thus, trust becaome the central issue for them when creating financial decision making. For them, intangible features such as respect, trust, safety, and sense of belonging is very important (Sawady & Tescher, 2008). For Asian customers, respect aspect was even more sensitized.Hence, low-income consumers tend to be very cautios at accepting new financial products, especially those who live in remote area and rarely touched by financial service providers (FSPs).

Furthermore, social network is crucial in the lives of this segment. They often rely on community and family networks to provide them with resources, including financial resources, for their survival. Basically, this segment has two options when it comes to fulfilling their financial needs, informal cash economy and formal financial services. However, people are usually choose the informal one because it is familiar and comfortable, and the informal lenders are usually part of their community. Furthermore, many people from low-income segments are confused by the formal financial services, some others feel rejected by the formal FSPs. We believe that the success of Mekaar in penetrating its ultra-micro credit product to more than one million customers because it was able to understand the need and behavior of low-income people and integrate those understandings in the loan products that they created.

- Trust and belonging. Mekaar lending products building trust of the clients in two ways, using internal (client’s immediate network such as family and friend) and external means (through account officer). According to our interview with clients, they were interested to join Mekaar because Mekaar is promoted by their family and/or friends. Some of them were being asked to form a group together with their family/friends, and the others were interested because they see how their family/friends improve their lives after receiving Mekaar loans. They were willing to accept Mekaar because they believe on what was recommended by their family/friends. Using this practice, Mekaar was able to increase consumer’s comfort in the product and sense of belonging. For external means, Mekaar use account officer to build client’s trust. To approach new clients, account officers (AO) used personal approach by visiting customer's residence. They visited the clients for several times, and every time, they will give explanation about Mekaar. Slowly building the trust of the clients towards account officer and Mekaar. In addition, AO should also read “AO promises”, which contains AO's commitment to always be honest and to treat consumers fairly, at every weekly meeting with clients. We believe that this practice provides a good impression, that AO also has a commitment to serve clients for the better. In low-income consumer eyes, people are the major differentiator, not a brand (Sawady & Tescher, 2008). Hence, the relationship between AO and customers is a crucial factor to build trust and sense of belonging of clients.
- Respect. Mekaar account officer were trained to treat and communicate with clients with utmost respect. Furthermore, Mekaar mostly hire account officers who are originated from the area, in fact, some of them are the child of Mekaar clients. Therefore, they know the culture in the area and able to build and maintain personal relationships with clients.
- Navigation. Mekaar is an easy to understand product, it does not need any collateral from clients, the clients only need to provide proof of identification and fill in the Mekaar form. The credit disbursement process takes only one week, the company will disburse the

money one day after the clients finished the training. Hence, for low-income consumer, this arrangement is very convenient, easy requirements and quick cash disbursement. Furthermore, account officer of Mekaar is responsible to provide clear explanation about client's responsibilities (such as attending weekly meeting) and negative consequences if clients do not fulfill their responsibilities, thus, clients will not feel betrayed because Mekaar already provide explicit information of what is expected from clients from the beginning. According to Sawady & Tescher (2008), low income consumers, who already feel swamp by the complexities of their lives, need an explicit navigation.
- Low income consumers tend to have short-term focus, hence, allowing frequent small payment has better suited them (Sawady & Tescher, 2008). Mekaar also implements the practice by offering weekly installment, rather than monthly installment, to their clients.

Formal banks usually put price (such as reducing/eliminating fees) and convenience (such as opening more branches in area where low-income consumers located) strategy as a priority when decided to serve low-income consumers (Sawady & Tescher, 2008). However, previous study by Sawady and Tescher (2008) shows that for low income consumers, emotional needs are somehow as important, or even more important, than that. Financial service providers (FSPs) need to fulfill the emotional needs because low income cconsumers proved to have quite different reasoning system when creating financial decision making. When creating their loan product, Mekaar is mindful of the characteristics of low income and was able to provide a loan product that is suitable for the poor. Therefore, focus on account design and incentive to increase lending to low income is not sufficient if FSPs decided to serve low-income consumers, FSPs also need to accomodate emotional needs and behavioral insight related to this unique segments.

Basically, Mekaar's target market is poor and unbankable women who does not have asset to be guaranteed when they take a loan. However, the average NPL of Mekaar clients is almost zero (0.0023% to be exact), very low when compared to the national NPL of 2.93% in 2016 and 3.07% by mid 2017. One of the key to Mekaar's success in pressing NPL is the group guarantee system that they implement in their loan product. This group guarantee scheme is believed to be effective to disciplined consumers, especially to come to weekly meetings. Delinquency cases are also very rare: firstly because the solidarity guarantee is applied immediately when a group member is delinquent, secondly because peer pressure assures this happens in very few cases. Group coordinators are in charge to warn their group members once the members failed to make weekly payment. An internal survey conducted by PNM suggested that the main reason group members adhere to the term of payment and willing to do all the rituals is because they are afraid they will not be included in the next loan term. In addition, the results also mentioned that most Mekaar clients feel embarrassed and afraid with their peers (e.g. other group members) if they come late to the weekly meeting and did not pay the loan on time. This shows that the mechanism of peer pressure is naturally present in Mekaar's group guarantee system. This system is also very effective in maintaining the quality of Mekaar loan.

Ⅸ. Impact of Mekaar to the Society

In measuring the performance of a microcredit program, Rosenberg (2009) proposes five basic tools which are breadth of outreach (number of clients being served), depth of outreach (how poor are the clients?), loan repayment (portfolio quality), financial sustainability (profitability), and efficiency (how well the MFI control its operating costs). Nevertheless, Mekaar has been running for only two years and some branches operate even less than a year, which makes the financial data is not readily available to calculate the aforementioned indicators related to financial performance of the Mekaar program.

Furthermore, in the donor brief published by Consultative Group to Assist the Poor (CGAP), impact of microfinance is related to measuring how financial services affect the lives of poor people (Cohen, Burjorjee, & CGAP Staff, 2003). Impact in microfinance considers income growth, asset building, and reduction of vulnerability. Other times, it also includes indicators that intend to measure multiple dimensions of poverty, such as overall household income, social improvements in health and education, and empowerment (increased self-esteem and control of household resources among women) (Cohen, Burjorjee, & CGAP

Staff, 2003). We also measure multidimensional poverty index of Mekaar clients in early 2017, and the results show that among 1382 clients that we surveyed, only 74 clients (5%) who are categorized as a multidimensional poor based on indicators set by Alkire and Foster (2007, 2011a). The respondents for this study are consumers who have been a Mekaar clients for at least 6 months.

Furthermore, we assessed the impact of Mekaar in a household level and individual level (Cohen, Burjorjee, & CGAP Staff, 2003). In a household level, Mekaar ultra-microcredit was proved to provide another source of income for the client's family. Mekaar plays a significant role in empowering women within the family economy. Prior to Mekaar's presence, the majority of Mekaar's customers were housewives and only husbands played the sole breadwinner. We conducted a survey, in which in the results show that Mekaar ultra-microcredit allows the clients to open new business and leads to an increase in their household income. The credits also increase the assets of clients; they reported an increase in their assets such as jewelry, land/ rice fields, livestock, and food stand/carts. Currently, the survey is still ongoing, therefore, we are not able to present the final results in this paper. At an individual level, Mekaar ultra microcredit are able to increase client's savings. Mekaar offering clients to save their money in Account Officer. In remote areas, the existence of formal financial institutions such as banks is rare that people are not accustomed to have saving account. Mekaar taught customers to manage their finances and set aside excess funds as savings which can be withdrawn at any time. Furthermore, looking at the number of current Mekaar consumers who almost reach 1.4 million consumers (per November 2017), we can say that this group guarantee loan has potential to give greater impact to the Indonesian poor people, especially those who live in remote area and unreachable by formal financial services. Mekaar also give a way for women empowerment, because Mekaar open an access to financial services which then leads to increase in greater choices and voice in a family for women. However, we still need to conduct a study to measure how much the impact of Mekaar to women empowerment in Indonesia, which will be our agenda in the future.

From social point of view, with their education agenda by incorporating prayer, client's promises, and Pancasila in their weekly meeting, Mekaar is indirectly attempting to alter the behavior of poor people in a positive way. First, Mekaar instill discipline value to their customers through the implementation of weekly meeting, and clients are required to attend (clients are allowed to absent from weekly meeting maximum 2 times during the loan term). Second, Mekaar is also embedding the value of honesty and working hard to customers by requiring them to read consumer promises each week. Meanwhile, regular reading of Pancasila aims to instill a sense of unity and tolerance within the community. Over time, these values are expected to be instilled inside the consumers' self. Therefore, in the long run, Mekaar has a goal to raise the status of poor people by changing their behavior.

Initially, there were a lot of Mekaar consumers who never use, or even visited, a banking institution before. These consumers are usually called unbankable segment. In Mekaar loan process, PNM attempt to familiarize this segment with banking products (e.g. savings, loans, etc), thus, these consumers are expected to become bankable in the near future. However, currently, PNM is already cooperating with several Indonesian state-owned banksto provide consumers with formal banking savings accoount. Mekaar could be seen as an agent that transform unbankable segment into bankable segment

Ⅹ. Future Opportunities for Mekaar

Based on our discussions and evaluation above, there are some strategic decisions for the future of Mekaar's program:

1. Caution against NPLs. Considering that Mekaar's clients are very poor and unsecured, Mekaar should have a prevention strategy in the event of a shock or disaster that could causes the loan to default. So far, there have not been many cases where clients cannot continue with the loan process (e.g.client's death or natural disaster). Mekaar have been working together with state owned enterprise (SOE) PT Jiwasraya (Persero), a state-owned insurance company, to cover Mekaar's clients against death risk. Nevertheless, other type risk as fire, husband's death, and natural disaster have not been included in the insurance policy. Since PT PNM wants to grow the number of their consumers, the likelihood of such things happen is higher and can cause consum-

er's inability to return the loan. Therefore, PT PNM should make risk mitigation strategies to overcome this matter.

2. For future funding, PT PNM should start considering cooperation with other state-owned companies. Under the Ministerial Regulation, State Owned Enterprises (SOEs) are required to set aside a portion of their profits for the partnerships and community development program (in Indonesia, it is known as Program Kemitraan dan Bina Lingkungan (PKBL)). Usually, in the partnership program, SOEs will channel the money to small and medium enterprises in the form of loans. But, often times, the number of NPL for this program is quite high. This is understandable because the distributing loan to SMEs is not the core business of that SOE. Given that PT PNM has expertise in distributing loans to the poor, it is expected that in the future, SOEs' PKBL money can be managed by PT PNM. This money could be treated as a source funding to increase the number of Mekaar customers across Indonesia.
3. In addition, PT PNM may also offer other microfinance products to their clients, such as micro insurance. PT PNM already has an established business process, a great amount of human resources, and market that is readily available. Accordingly, offering other microfinance products could present great opportunity for PT PNM to diversify its business.

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The Impact of Perceived Risk and Trust on Consumer Intention to Use FinTech Payment in Indonesia

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A B S T R A C T

FinTech rises as a faster, easier, and cheaper alternative to conventional financial products and services in Indonesia. The largest FinTech sub-segment in Indonesia is payment systems, representing over 30% of overall FinTech startup community. Consumer confidence and trust are essential to acquire and retain users and increase transaction volumes for FinTech companies. Therefore, in the expectation that a better understanding of factors that shape consumer behavior can promote the development of FinTech payment system, the goal of this research was to examine consumer perceived risks and trust in FinTech payment systems in Indonesia. The data generated from 175 respondents were analyzed using the Structural Equation Modeling (SEM). Using trust as the mediating variable, this research concludes that there is a significant relationship between perceived risk and intention to use Fintech payments. Perceived ease of use is also found to be the antecedent of trust. In addition to that, this study also suggests that consumer trust and intention have positive impacts on a good evaluation of FinTech payment with objective opinions on the future of FinTech payment.

Keywords: Fintech payment, perceived risk, trust, intention to use

Ⅰ. Introduction

Financial Technology, more widely known as Fintech, has been rising as one of the most discussed topics on finance in recent years. FinTech commonly defined as companies that incorporate innovative technology to improve the delivery of financial services to customers. As a result of digital disruption, FinTech offers more personalized, efficient, and user-friendly products and services compared to the traditional financial services. FinTech companies can be classified into four segments according to their business models namely financing, asset management, payment system, and other FinTechs (Dorfleitner et al., 2017). The growing role of FinTech in Indonesia happened simultaneously with rapid mobile Internet penetration growth in Indonesia. In 2016, there were 140 FinTech companies operating in Indonesia. This number had increased by 78 percent compared to the previous year (Indonesia Fintech Association, 2017). The majority of FinTech companies in Indonesia fall into the payment system segment. Since FinTech payment system is relatively new to the financial service consumer in Indonesia, it is often associated with some type of risks like security and privacy risks. The way consumer perceive risks in using FinTech payment system may influence their intention to use the services. Therefore, in the expectation that a better understanding of factors that shape consumer behavior can promote the development of FinTech payment system, the goal of this research was to examine consumer perceived risks and trust in

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FinTech payment systems in Indonesia.

Many research have been conducted to investigate the relationship between perceived risk and trust on consumer decisions to purchase products online (Hong & Cha, 2013, Ling et al., 2010; Lopez-Nicolas & Molina-Castillo, 2008, Suki & Suki, 2017). Some previous research focus on exploring consumer perceived risk and trust for online payment system (Roubah, Lowry & Hwang, 2016; Yang, Pang, Liu, Yen, and Tarn, 2015). Although the literature that examine the relationship among perceived risk, consumer trust, and intention to buy is extensive, no research has been conducted of the aforementioned variables on the intention to use FinTech payment system, particularly in Indonesia. FinTech payment system is seen as a promising alternative to conventional payment system provided by banks or other financial institutions in accelerating financial inclusion in Indonesia. Thus, it is necessary to study consumer perceived risk and trust for FinTech payment system in the Indonesian context, in which percentage of bank account ownership is still low and cash payment is highly preferred over digital payment system.

The remainder of this article is organized as follows. Section 2 discusses literature review and theoretical foundations. The methodology used in this research is described in section 3, while data analysis and results are presented in Section 4. The final section provides conclusions and implications of the study as well as direction for future research.

Ⅱ. Literature Review

A. Technology Adoption Models

Since FinTech is a combination of financial and technological product, hence it is relevant to analyze consumer intention from technology adoption models perspective. Early literature on the relationship between user beliefs, attitudes, and intentions include Theory of Reasoned Action, or TRA hereafter (Fishbein & Aizen, 1975), Theory of Planned Behavior or TPB hereafter (Aizen, 1991), and Technology Acceptance Model or TAM hereafter (Davis, 1989). TRA explains that consumer' intentions, which eventually generate their behavior, are influenced by consumers' beliefs. This study reveals that attitude (towards performing behavior) and subjective norms (to perform behavior) determine consumer behavior. TPB extends TRA by incorporating perceived behavioral controls toward performing behavior as additional factor that can generate a person's actual behavior. This theory suggests that behavior can be deliberative and planned. TAM, also an adaptation of TRA, was designed for modeling acceptance of information technology (Davis, Bagozzi, & Warshaw, 1989). TAM predicts the likelihood of a new technology being adopted based on the user's perceived usefulness and perceived ease of use of that technology.

Venkantesh, Davis, Davis, and Morris (2003) proposed the unified theory of acceptance and use of technology (UTAUT), developed from eight prominent models to explain the acceptance and use of information system and information technology innovations. The eight models consolidated by Venkantesh et al. (2003) are TRA, TAM, Motivational Model (Davis, Bagozzi, & Warshaw, 1992), TPB, Integrated Model of TAM and TPB (Taylor & Todd, 1995), Model of PC Utilization (Thompson, Higgins, & Howell, 1991), Innovation Diffusion Theory (Moore & Benbasat, 1996), and Social Cognitive Theory (Bandura, 1996). In order to explain the variance in intention, UTAUT proposes four constructs, namely: (i) performance expectancy, (ii) effort expectancy, (iii) social influence, (iv) facilitating conditions, grouping similar earlier constructs. UTAUT also explores the role of four key moderating variables: gender, age, experience, and voluntariness of use. Venkantesh, Thong, & Xu (2012) extended the UTAUT model by adding three new constructs: (i) hedonic motivation, (ii) price value, and (iii) habit, and also dropping voluntariness of use from the moderating variable lists. UTAUT has been widely used to examine user's acceptance toward mobile technologies, such as Internet banking and mobile banking in Malaysia (Tan, Chong, Loh, & Lin, 2010), and on-line banking adaption in Oman (Riffai, Grant, & Edgar, 2012).

B. Perceived Risk

Perceived risk is an uncertainty faced by the customers when considering to purchase products or services, as a result of involving their subjective assessments into the decision making process (Murphy and Enis, 1986). In the context of electronic transactions, Kim et al. (2007)

defined perceived risk as consumer's belief about the potential uncertain negative outcomes from the online transaction. There are various types of risks discussed in the marketing literatures. Jacoby & Kaplan (1972) classified seven types of risks namely financial, performance, physical, psychological, social, time and opportunity cost risk. They also introduced the overall risk measurement as the general measure when all risks are evaluated together. Overall risk is referred as total risk in this paper. Physical risk is considered to be not relevant for electronic services (e-services) because there is no physical contact between the seller and the buyer. In the case of online shopping, (Bhatnagar, Misra, and Rao, 2000) identified the three predominant risks: financial risk, product risk and information risk (security and privacy risk). More specific to risk associated to electronic payment system, Yousafzai, Pallister, & Foxall (2003) mentioned economic risk, personal risk, functional risk, and privacy risks as risk factors that determine trust for e-banking. Lopez-Nicolas & Molina-Castillo (2008) argued that technical risk, delivery risk, and service risk are relevant in the context of e-commerce. Technical risk and delivery risk are basically part of security risk, so those risk are not considered as perceived risk facets in this paper. The following table shows the description and definition of risk facets.

Based on that description above, this research propose the following hypothesis:

H1. Economic risk, functional risk, security risk, privacy risk, time risk, service risk, psychological risk, and social risk are multiple aspects of perceived total risk in FinTech payment system

C. Perceived Usefulness and Perceived Ease of Use

Perceived usefulness and perceived ease of use are derived from the Technology Acceptance Model (TAM). Davis (1989) proposed TAM to measure the quality of information system and its suitability to job requirements, therefore the acceptance and usage of information system can be predicted. Perceived usefulness is defined as the extent to which individuals believe that using a specific application system will enhance their productivity (Davis, 1989). In the case of e-commerce, Koufaris and Hampton-Sosa (2004) defined perceived usefulness as customer's subjective perception on website's function during their online shopping. Perceived Ease of Use (EOU) is defined as the degree to which a person believes that using a particular system would be free from effort (Davis, 1989). Geffen (2000) mentioned that perceived ease of use in-

Table 1. Description of Perceived Risk Facets

Perceived Risk Facet	Description
1. Economic Risk	"The potential monetary outlay associated with the initial purchase price as well as the subsequent maintenance cost of the product" (Grewal, Gotlieb, and Marmorstein,1994). Economic risk also includes the potential monetary losses because of payment sytem failure.
2. Functional Risk	Risk related to the stability and reliability of the payment system. Grewal et al., (1994) defined performance or functional risk as "the possibility of the product malfunctioning and not performing as it was designed and advertised and therefore failing to deliver the desired benefits"
3. Security Risk	The risk that the payment system or third parties are vulnerable to cyber attacks. (Penningto, Wilcox, Grover, 2003)
4. Privacy Risk	The risk that consumers' personal information being used without their permission due to negligence or illegal activities of FinTech payment system, third parties or others (Featherman and Pavlou,2003); (Veloutsou and Bian, 2008); (Yousafzai et al., 2003)
5. Time Risk	The risk of time wasted for doing research on products and services, making the bad purchasing decisions, and completing the payment process (Featherman and Pavlou,2003)
6. Service Risk	The risk that the payment systems provide low quality services (Lopez-Nicolas and Molina-Castillo, 2008)
7. Psychological Risk	The risk that the uncertainty in the payment system will have a negative effect on consumer's feeling (Featherman and Pavlou, 2003)
8. Social Risk	"Potential loss of status in one's social group as a result of adopting a product or service, looking foolish or untrendy" (Featherman and Pavlou,2003)
9. Total risk	"A general mesure of perceived risk when all criteria are evaluated together" (Featherman and Pavlou, 2003)

dicates the cognitive effort required to learn and use new information technology. In relation to e-service, Kim and Forsythe (2008) found that perceived usefulness has a positive effect toward e-service. In addition to that, Featherman, Valacich, and Wells (2006) mentioned that perceived ease of use also has negative impact on perceived risk in the e-server. Thus, this research proposed the hypotheses as follows:

H2a. There is a negative relationship between perceived usefulness and consumer perceived total risk

H2b. There is a negative relationship between perceived ease of use and consumer perceived total risk

D. Trust

Due to its business nature, consumers face certain level of inherent risk when they are engaged in e-services. The absence of physical contact and new technology adoption services raises the uncertainty of e-services compared to offline services. Trust plays important role in dealing with the uncertainty in e-services. In the presence of trust, a person gains feelings of certainty and security towards other party (Rempel, Holmes, and Zanna (1985). Hong and Cho (2011) argue trust is a significant factor that determines online purchase intentions. Furthermore, Urban, Amyx, and Lorenzon (2009) found that the biggest obstacle to consumers in doing online transaction is the lack of trust.

There are no concensus among researcher regarding the relationship between perceived risk and trust. Murkherjee and Nath (2007) investigated that online trust can reduce perceived risk in the online retailing. In contrast, some research showed different results. Chen and Barnes (2007) suggested that there is a positive relationship between perceived risk and initial trust in e-commerce. Yang et al. (2015) concluded that perceived total risk is negatively related to trust in case of online payments in China. In the context of mobile banking, Kuisma, Laukkanen, & Hiltunen (2007) studied the relationship between individual value and resistance to Internet banking. The study found that consumers prefer ATM services to Internet banking due to Internet insecurity, inefficiency, and inconvenience. Perceived risk factors such as the possibility of consumers' passwords and lack of official receipts contribute to low level of consumer trusts. Rotchanakitumnuai and Speece (2003) explain that perceived risks by corporate costumers in using Internet Banking provided by Thai banks affect trust, particularly among non-users. This research will test a hypothesized negative relationship between perceived total risk and trust.

H3. There is a negative relationship between consumer perceived total risk and trust

Previous studies have investigated the relationship between perceive usefulness and perceived ease of use and trust. Malhotra, Kim, and Agarwal (2004) argue that perceived ease of use is on of the contributing factor in building consumer trust in online shopping. Perceived usefulness and perceive ease of use in e-commerce reduce consumer's effort to control and monitor transactional process, hence increase the level of trust (Chircu, Davis, and Kauffman, 2000). Li, Hess, and Valacich (2008) mentioned perceived usefulness, perceived ease of use, and risk are elements of trust. The presence of trust has positive effect to intention to use online payments and also encourage consumers to do evaluation of online payment channels after they pick the best one. In accordance with the discussion above, this research suggest:

H4a. There is a positive relationship between perceived usefulness and trust

H4b. There is a positive relationship between perceived ease of use and trust

As a relatively new payment system alternative, consumers often compare FinTech based payment system to payment system offered by banks or other financial institutions. Yang et al. (2015) confirmed that in the case of online payment, perceived usefulness and perceived ease of use both have positive impact on comparison. As has been discussed previously, trust in e-services is positively associated with consumer intention. Thus, the positive relationship between those variables will lead to a positive evaluation towards e-services development. The conceptualizations above have directed the formation of the following hypotheses:

H5a. There is a positive relationship between perceived usefulness and comparison

H5b. There is a positive relationship between perceived ease of use and comparison

H6. There is a positive relationship between comparison and trust

H7. Perceived risk is positively related to intention to use FinTech payment system, mediated by trust

H8. Consumer trust and intention positively influence the evaluation of FinTech payment system

Ⅲ. Methodology

A. Procedure and data collection

Data were collected using an online survey and restricted to those who have used or is still using FinTech payment systems. Structured self-administered questionnaires were distributed to respondents with minimum age of 17. Convenience sampling method was used as data collection method among 176 respondents. After the data cleaning process, 175 responses were usable and one unusable response was excluded. The questionnaire was structured into three sections. First section covered respondents' demographic profile such as gender, age, monthly expenses. Second section comprised of questions detailed the independent, mediating, and dependent variables. The measurement of economic risk, functional risk, privacy risk, time risk, and psychological risk were adopted from Featherman and Pavlou (2003) and Veloutsou and Bian (2008). Last section asked respondents their experience on using FinTech payment system. Reference was made to Pennington et al. (2003) in developing items of security risk, where else questions on service risk, social risk, and psychological risk were taken from Lopez-Nicolas & Molina-Castillo (2008). Items of trust and intention were adopted from McKnight and Chervany (2002), Mayer et al. (1995), and Jarvenpaa et al. (2000). Meanwhile, the questions of comparison and evaluation were derived from Yang et al. (2015). All measurement items were measured by using a five-point Likert scale ranging from 1 (Strongly Disagree) to 5 (Strongly Agree).

B. Statistical technique

The data were analyzed using the Structural Equation Modeling (SEM) approach supported by Lisrel 8.51. SEM method is quite similar to multiple regression analysis, makes it suitable for exploratory research purposes. SEM is capable to model and estimate complex models with both latent and observed variables. Data requirements are also more relaxed in SEM, it accommodates non-normal data, small sample sizes, and formatively measured constructs (Hair, Sarstedt, Hopkins, and Kuppelwieser, 2014). This research apply a conceptual model of consumer perceived risk and trust proposed by Yang et al. (2015) as shown below:

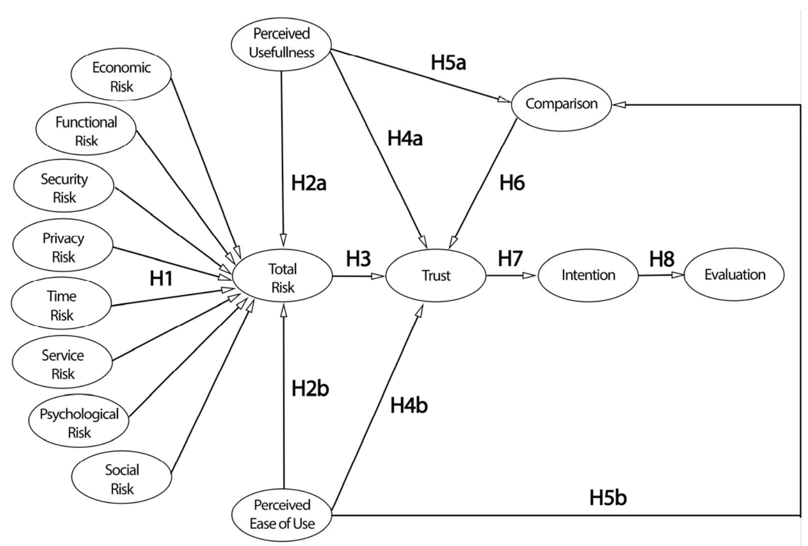

Figure 1. Research Model

Ⅳ. Data analysis and results

A. Descriptive statistics

Table 1 depicts the descriptive analysis of demographic characteristics of the respondents. Of those 175 participants in the sample, 57.7% are female and 42.3% are male. In terms of age distribution, more than half of the respondents were 35 years old and younger (84%). The remaining 16% of the respondents aged more than 36 years old. In the case of monthly income, 19.4% of the respondents spent less than Rp2 million per month, 42.9% spent between Rp2 million to 5 million per month, 20.6% spent between Rp5.000.001 to Rp10.000.000, and 17.1% spent more than Rp10 million per month.

Table 2. Sample Characteristics

Variable	Frequency	Percentage
Gender		
Female	101	57.7%
Male	74	42.3%
Age		
17-25	64	36.6%
26-30	37	21.1%
31-35	46	26.3%
36-40	20	11.4%
41-45	5	2.9%
>45	3	1.7%
Monthly expenses		
<Rp2.000.000	34	19.4%
Rp2.000.000-Rp5.000.000	75	42.9%
Rp5.000.001-Rp10.000.000	36	20.6%
Rp10.000.001-Rp15.000.000	14	8.0%
>Rp15.000.001	16	9.1%

Table 3 portrays the main purpose of consumer using FinTech payment system. The majority of the respondents (68.6%) chose FinTech payment systems to pay their transportation expenses. About 18.3% of the respondents paid their online shopping transaction via FinTech payment systems. Other purposes such as offline shopping, fund transfer, etc were chosen by less than 5% of the respondents each.

Table 3. The Main Purpose of Consumers using FinTech Payment

Variable	Frequency	Percentage
Purpose of Using		
Pay transportation expense	120	68.6%
Online store shopping	32	18.3%
Offline store shopping	8	4.6%
Fund transfer	6	3.4%
Top up phone credit	3	1.7%
Pay mandatory participation fees (universal health coverage, workers social security)	2	1.1%
Pay financial product bill (insurance, credit card, pension plan)	2	1.1%
Pay utilities bill (electricity, gas, water)	2	1.1%

B. Measurement properties

Research model was estimated using PLS-SEM approach that comprises two-stage data analysis: measurement model and structural model. The measurement model is used to test the validity and reliability of the measures. Table 4 displays the results of reliability and validity analysis. Reliability of the measurement items were examined via composite reliability (CR) and average variance extracted (AVE). Hair et al. (2009) stated that CR value has to be higher than 0.7 and the AVE should be higher than 0.5. The results showed that measurement items used in this study met all the reliability requirements. Validity was gauged by testing the standardized loading factors and t-values. Hair et al. (2014) suggested that factor loading should be greater than 0.5. Meanwhile, a research model is valid when the absolute value of the t-value is greater than or equal to 1.96 (two-sided test) and 1.65 (one-sided test). Table 4 shows that factor item for all loadings surpassed the threshold value.

Table 5 shows the goodness of fit analysis of the measurement model. This study used five indicators to test the goodness of fit namely: Chi-square and degrees of freedom, Root Mean Square Error of Approximation (RMSEA), Comparative Fit Index (CFI), Incremental Fit Index (IFI), and Goodness of Fit Index (GFI). The results for measurement model and structural model indicate a good fit to the data.

Table 4. Reliability and Validity Analysis

Variable	Items	Standardized loadings	t-values	Composite reliability	Average variance extracted
Economic Risk	ECON1	0.6	7.96	0.703127062	0.549909982
	ECON2	0.86	11.49		
Functional Risk	FUNCT1	0.61	7.54	0.731418832	0.576719577
	FUNCT2	0.58	7.19		
Security Risk	SECUR1	0.85	10.53	0.885423653	0.794733153
	SECUR2	0.93	15.32		
Privacy Risk*	PRIVACY1	1	n.a	1	1
Time Risk	TIME1	0.8	11.97	0.843338214	0.642737896
	TIME2	0.85	12.87		
	TIME3	0.75	11		
Service Risk*	SERVICE1	1	n.a	1	1
Psychological Risk	PSYCHO1	0.57	13.19	0.816316682	0.604570892
	PSYCHO2	0.86	12.69		
	PSYCHO3	0.86	14.54		
Social Risk*	SOCIAL1	1	n.a	1	1

Note: * anchor item

Table 5. Goodness of Fit Statistics

Goodness of Fit	Chi-Square (d.f.)	Chi-Square/d.f.	RMSEA	CFI	IFI	GFI
Good Model Fit		<3	<0.080	>0.9	>0.9	≈0.90
Measurement	231.12 (137)	1.69	0.06	0.95	0.95	0.88
Structural	669.70 (414)	1.62	0.06	0.92	0.92	0.81
Results		good fit	good fit	good fit	good fit	marginal fit

C. Test of the structural model

Table 6 shows the statistical results for the structural model, including standardized loadings and t-values. Based on those two indicators, all of the eight perceived risk facets had insignificant impact on total risk. Hence, H1 is not supported. The results were different from previous studies (Yang et al., 2015), which found economic, functional and privacy risk have significant affect toward total risk. This suggests that the consumers of FinTech payment system in Indonesia do not consider eight risk facets mentioned in this study when doing transactions. One possible explanation of this result is most of the respondents were 35 year and younger, commonly known as millennials. One of the most prominent characteristics of the millennials is they are digital natives. Prensky (2001) defined the younger generation, who were born between the early 1980s and the early 2000s, as the native speaker of the digital language of computers, video games and Internet. Hence, Internet-based payment systems like FinTech payment are not new thing for the digital natives. In regards to trust, Hoffmann, Lutz, and Meckel (2015) stated that unlike digital immigrants, digital native did not critically weight the risks of a transaction against its benefits.

The relationship between perceived usefulness and total risk was also found to be insignificant, thus H2a is not validated. The previous explanation about respondents' characteristics can also justify this result. As digital natives, consumers have been using computers and Internet form an early age, thus the marginal utility of using FinTech payment system may not be as high as it is for the older generations. On the other hand, statistical results confirmed that perceived ease of use have negative effect to total risk as proposed in H2b. It confirmed previous study by Featherman, Valacich, and Wells (2006), which men-

Table 6. Structural Model Statistical Results

Hypo-thesis	Path	Standardized Loadings	t-values	Results
1	Economic risk -> Total risk	1.8	0.38	H1 Not supported
	Functional risk->Total risk	-2.88	-0.38	H1 Not supported
	Security risk -> Total risk	0.83	0.32	H1 Not supported
	Privacy risk -> Total risk	0.16	0.32	H1 Not supported
	Time risk -> Total risk	0.23	0.29	H1 Not supported
	Service risk -> Total risk	0.29	0.59	H1 Not supported
	Psychological risk -> Total risk	0.51	0.35	H1 Not supported
	Social risk -> Total risk	-0.26	-0.59	H1 Not supported
2a	Perceived usefulness -> Total risk	-0.01	-0.06	H2a Not supported
2b	Perceived ease of use -> Total risk	0.77	9.38	H2b Supported
3	Total risk -> Trust	-0.03	-0.5	H3 Not supported
4a	Perceived usefulness -> Trust	0.08	-0.6	H4a Not supported
4b	Perceived ease of use -> Trust	0.49	4.49	H4b supported
5a	Perceived usefulness -> Comparison	0.22	1.64	H5a Not supported
5b	Perceived ease of use -> Comparison	0.34	2.58	H5b supported
6	Comparison -> Trust	0.47	6.16	H6 supported
7	Perceived risk moderated by Trust -> Intention	0.8	9.22	H7 supported
8	Trust and Intention -> Evaluation	0.81	13.39	H8 supported

tioned that perceived ease of use has negative effect on perceived risk in the e-server.

The result of this study is in line with Morgan and Hunt (1994) which found no relationship between perceived risk and trust. Based on the statistical results, it is shown that perceived usefulness is not an antecedent of trust as previously mentioned by Gefen, Karahanna, and Straub (2003) and Erikson, Kerem, and Nilsson (2004). The possible explanation is that during the development stage of Fintech payment system in Indonesia, the nominal amount of transaction are limited compared to traditional payment system. This may also explain the lack of effect of perceived usefulness to comparison. The limitation on amount of transaction may also cause consumer were unable to compare FinTech payment sytems to other payment systems. However, perceived ease of use indicates a positive impact on both trust and comparison. The results are persistent to previous studies by Chircu (2000) and Li (2008).

Furthermore, comparison shows a positive impact towards trust as suggested by Yang et al. (2005). This suggests that the more consumers prefer to use FinTech payment compared to any other means of payment, the higher level of trust in FinTech payment. The negative relationship between perceived risk and intention, with trust as mediating variable, were statistically significant. In line with Kim et al. (2008), which considered perceived risk as an important factor that influence purchasing decisions. Finally, consumer trust and intention are positively related to a good evaluation on FinTech payment as mentioned in Yang et al. (2015).

Ⅴ. Conclusions

This research examined the relationship between perceived risk and trust in FinTech payments in the Indonesian context. Using trust as mediating variable, this research concludes that there is no significant relationship between perceived risk and intention to use Fintech payments. Perceived ease of use is found to be the antecedent of trust in FinTech payment. In addition to that, this study also suggests that consumer trust and intention have positive impacts on a good evaluation of FinTech payment with objective opinions on the future of FinTech payment. In regard to managerial implication, the results of this study provide inputs for the FinTech companies to increase consumer intention to use FinTech payments. FinTech companies need to develop strategies to increase the perceived ease of use and build consumer trusts, hence consumers have higher intention to use FinTech payment. Most of the FinTech payment systems in Indonesia handle payment in small amount but high in frequency, daily transportation expenses, for instance. Consumer prefers to use FinTech payment system instead of other means because FinTech offers mobility and simplicity. Unlike Internet Banking or Mobile Banking that require several steps and open more than one application to complete the transaction, FinTech should make the payment steps less complicated in order to increase consumers' intention to use. FinTech companies should also emphasize the easy-to-use feature in their marketing campaign. In addition to that, this research also has policy implications with regards to financial consumer protection. The results of this study revealed that consumer perceived risks are not relevant in building trust and intention to use, which may indicates the lack of consumers' knowledge in risk embedded in FinTech products. Indonesia Financial Service Authority or OJK, as the authorized agency in charge of financial consumer protection, needs to conduct further study to examine consumers' knowledge of FinTech product risks. Low level of product knowledge could potentially lead to unfair practices against consumers.

The main limitation of this study is the small number of sample used due to limited number of potential respondents. FinTech payment is relatively new in Indonesia and only few people have used or are currently using the services. Therefore, as a recommendation for future research, larger number and more diverse sample will enrich the study of intention to use FinTech payment system. This study also shows that the relationship between common perceived risk facets (such as economic risk, security risk, etc) and total risk are not significant. The preliminary analysis regarding this finding related to demographic characteristic of the majority of the respondents. Hence, it is also suggested to explore the perceived risk facets from the digital natives perspective. Understanding the consumer behavior of different age groups is necessary to support the development of FinTech payment in Indonesia.

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Editorial Principles

1. Mission

The International Review of Financial Consumers (IRFC) aims to offer a communication platform for scholars, regulators, and practitioners to share their latest academic research on financial consumers and related public policy issues in both advanced economies and emerging market countries. All theoretical, empirical, and policy papers of relevancy are welcome, with the following as the topics to cover:

① protection for financial consumers
② business ethics of financial institutions
③ market discipline of financial industries
④ corporate social responsibility of financial institutions
⑤ renovation or innovation of law and regulations related to financial consumption
⑥ public policies for financial consumption
⑦ fair trading of financial products
⑧ dispute resolution for financial consumption
⑨ case studies of best practices for financial consumption
⑩ international comparison on any of the above topics

2. Publication schedule and contents

IRFC, the affiliated journal of the International Academy of Financial Consumers (IAFICO), will be published twice a year – April and October each year - and will pursue to be the first international academic journal focusing on the research related to financial consumers. As the contribution of financial consumption becomes increasingly important to the national economy for most countries, how to maintain an efficient and equitable financial market is an imminent issue for research. The trend of globalization and liberalization policies has reinforced the challenges in financial markets. Not only the financial instruments become more complicated and hard to understand by the public, but also the frequent changes in regulations and business practices cause confusions to the financial consumers. Consumption disputes regarding the financial products have drawn attention by the media in recent years. IRFC attempts to serve as a forum to publish and share original and innovative research, both academic and policy-oriented, on all the above issues.

3. On ethics for research

The range of research misconducts

① Misconducts related to academic research (“misconducts” hereafter) means that fabrication, falsification, plagiarism, unfair showing of papers' author, during research proposal, research performing, research report and research presentation, etc. It is as follows.

1) “Fabrication” is the intentional misrepresentation of research results by making up data or research result.

2) “Falsification” is the distortion of research contents or results by manipulating research materials, equipment and processes, or changing or omitting data or results.

3) “Plagiarism” is the appropriation of another person's ideas, processes or results, without giving appropriate approval or quotation.

4) “Self-plagiarism” is the reusing a large portion of their own previously written research.

5) “Unfair showing of papers' author” is not qualifying people, who have been contributing to research contents or results scientifically, industrially and politically, as an author without just reason, or qualifying people, who have not been contributing the same, as an author with an expression of thanks or respectful treatment.

6) Obstructing investigation about misconducts of their own or others, or harming an informant.

7) Action which is out range of usually acceptable in the course of the research.

8) Action which is suggestion, pressure or threat to others to do the above things.

4. On plagiarism

Types of plagiarism

Following two forms are defined the representative action of research misconducts (Plagiarism).

① Using the original author's idea, logic, unique terms, data, system of analysis without indicate the source.

② Indicating the source but copying the original paper's words, idea, data and so on without quotation marks.

Bylaws of the International Academy of Financial Consumers (IAFICO)

March 31, 2015
April 19, 2016

Section 1 General Provisions

Article 1 (Official Name)

The official name of this academic society shall be the "International Academy of Financial Consumers (IAFICO hereafter)".

Article 2 (Registered office and Branch offices)

The registered office is to be in Seoul, South Korea. Branch offices may be established in provincial cities in South Korea or overseas should the need arise.

Section 2 Objectives and Undertakings

Article 3 (Objectives)

* *Pending*

The IAFICO is a non-profit association aiming at promoting and developing at an international level collaboration among its members for the study of various issues relating to financial consumers, including its education, legislation, creation of best practices, supervision and policy advancement to contribute to the development of the global economy and financial market, through investigation or research into financial consumers, and other academic activities.

Article 4 (Undertakings)

The following activities shall be carried out in order to achieve the objectives of the IAFICO.
1. Publication of journal and other literature
2. Hosting of academic conferences
3. Additional undertakings corresponding to the objectives of the academic society which are deemed necessary at the board of directors meeting or the general meeting

Section 3 Membership

Article 5 (Requirements and Categories)

The IAFICO shall have following categories of membership :

① Individual member
Individual members are categorized further into a regular member or and associate member.

1. Regular member shall be a specialist in the area such as finance, consumer studies, economics, management, law, or a specialist in the area such as finance, consumer studies, economics, management, law, or education etc, and must be a full-time instructor at a domestic or overseas university, an researcher at a research institute with equivalent experience, or should hole equal credentials to those mentioned previously, and shall become its member by the approval of the board of directors. Regular members attend general meetings and may participate in discussions, hold the right to vote, and are eligible to be elected a director or other status of the IAFICO.
2. Associate members shall be divided into either a student member, who is a current domestic or overseas graduate school student, or an ordinary member, who works for a financial institution or a related organization. Associate members do not hold the right to vote and not eligible to be elected to a director or other status of IAFICO.
3. Both regular member and associate member must pay the membership fee to the IAFICO every year.
4. In the case that a decision is made by the Board of Directors to expel a member due to a violation of the objective of the society, or demeaning the society, or in the case that a member fails to pay the membership fees for two years continuously without prior notice, their membership shall be revoked.

② Institutional member
1. Institutional member

Shall be organizations related to financial consumers who do not damage the impartiality of the IAFICO subject to approval of the Board of Directors Institutional members do not hold the right to vote and are not eligible for election.

2. Institutional member must pay its membership fee to the IAFICO every year.

Section 4 Organization

Article 6 (Designation of Board of Director)

The following Directors are designated to constitute the Board Directors to run the IAFICO.

1. Chairperson
2. Vice-Chairperson
3. President
4. Vice-President
5. Ordinary Directors
6. Auditor

Article 7 (Election of Board Members and Director)

① The Chairperson, Directors, and Auditors shall be elected or dismissed at the general meeting.
② Appointment of the Directors may be entrusted to the Chairperson pursuant to the resolution of the general meeting.
③ The Vice-Chairperson, President, and Vice-President shall be appointed and dismissed by the Board of Directors.

Article 8 (General Meetings)

① General meeting shall decide following matters relating to the activities of the IAFICO.
1. Amendments to the Bylaws
2. Approval of the budget and settlement of accounts
3. Election or Dismissal of the Chairman
4. Election or dismissal of Auditors
5. Regulations concerning the duty and right of members
6. Resolutions regarding items submitted by the President or Board of Directors
7. Other important matters

② The Chairperson must call a regular general meeting at least once a year and report on the undertakings of the IAFICO. Provisional general meetings may also be held by the call of the Chairperson, or at the request of at least a quarter of current regular members, or according to the resolution of the Board of Directors.
③ At a general meeting, a quorum is formed by one third of regular members. However, regular members who are not able to participate in the general meeting in person may be represented by proxy, by entrusting a specific regular member attending the general meeting with their attendance or voting right. In this case the letter of proxy is included in the number of attendees.
④ Resolutions at the general meeting will be made according to the majority vote of the attending members who hold the right to vote.
⑤ In principle, the general meetings shall be held with face-to-face meeting, however, it may be held web-based meeting when needed.

Article 9 (Auditors)

① The auditors shall audit financial affairs, accounts and other transactions of IAFICO, shall participate in, and may speak at board meeting, and must present and auditor's report at the regular general meeting.
② There shall be two appointed auditors.
③ Auditors are elected at the general meeting.
④ And auditor shall serve a term of two years and may be reappointed.

Article 10 (Board of Directors)

① The Board of directors shall be made up of chairperson and fewer than 80 directors.
② The Board of Directors shall decide a plan of operation and establish the budget, in addition to matters on the running of IAFICO.
③ Board meeting requires a quorum of at least one third of current board members. Resolutions at the Board meeting will be made according to the majority vote of the attending members. However, board members who are not able to participate in the board meeting in person may be represented by proxy, by entrusting another specific

board member attending the board meeting with their attendance or voting right.
④ A board member shall serve a term of two years, with a possibility of serving consecutive terms.
⑤ A number of sub-committees or branches in each country or region may be set up under the Board of Directors to support the running of the IAFICO.

Article 11 (Steering Committee)

① The Board of Directors may entrust some decisions relating to the conducting of business to the Steering Committee.
② The Steering Committee shall be comprised of the Chairperson, Vice-Chairperson, President, and the heads of each subcommittee.
③ Temporary task forces may be established by the Steering Committee when necessary to run the business of the Steering Committee.

Article 12 (Chairperson)

① The Chairperson shall represent the IAFICO and chair its general meeting and board meeting.
② There shall be one appointed Chairperson who serves a term of five years.
③ In the case of an accident involving the Chairperson, the Vice-Chairperson shall complete the remaining term of office of less than one year. If it lasts longer than one year, a new Chiarperson shall be elected at the general meeting.
④ A new Chairperson should be elected at the general meeting one year prior to the end of the current Chairperson's term of office.
⑤ Should it be judged that it is difficult for the Chairperson to carry out their duty any longer, he or she may be dismissed from their post by the decision of the Board of Directors and general meeting.

Article 13 (Vice-Chairperson)

① The Vice-Chairperson shall assist the Chairperson, and serve as a member of the Board of Directors.
② The Vice-Chairperson shall serve a term of two years, or the remaining term of office of the Chairperson, whichever is shortest.
③ The Vice-Chairperson shall be elected from one of the regular members at a meeting of the Board of Directors, according to the recommendation of the Chairperson.
④ The Vice-Chairperson shall may be reappointed.

Article 14 (President)

① During its term of office, the President shall become the head of the organizing committee supervising international conferences, and serves for a term of one year. The President shall attend the board meeting as a member of the Board of Directors.
② The succeeding President shall be elected by the Board of Directors after considering their ability to organize and host the following year's conferences. The succeeding President shall also attend board meeting as a member of the Board of Directors.
③ The Board of Directors may elect the next succeeding President should the need arise. The next succeeding President

shall also attend board meeting as a member of the Board of Directors.

④ The President, succeeding President, and the following President may appoint a vice-President respectively by obtaining approval of the Board of Directors.

⑤ The appointment and dismissal of the President is decided at the board meeting.

Article 15 (Vice-President)

① A Vice-President is a member of the Board Directors and shall assist the President, supervise applicable international conferences.

② A Vice-President is recommended by the President and shall be approved by the Board of Directors.

③ Multiple Vice-Presidents may be appointed.

④ A Vice-President shall serve a term of one year, the same as the term of President.

⑤ In the event of an accident involving the President, a Vice-President shall fulfill the President's duties during the remaining term of office.

Article 16 (Editorial Board)

① The Editorial Board shall be responsible for editing of journals and other materials to be published by the IAFICO.

② The head of the Editorial Board shall be appointed by the Board of Directors, and shall serve a term of office decided by the Board of Directors.

③ The head of the Editorial Board shall be a member of the Board of Directors.

④ Additional matters concerning the running of the editorial board shall be decided separately by the Board of Directors.

Article 17 (Advisory Board and Consultants)

① The Chairperson may select individuals who could make a large contribution to the development of IAFICO, and appoint them as advisors subject to the approval of the Board of Directors.

② The Chairperson may appoint consultants subject to the approval of the Board of Directors in order to receive advice relating to all business matters of the IAFICO, such as development strategies, conferences, research plans, and research projects etc.

③ Advisors and consultants shall serve terms of one year and may be reappointed.

Section 5 Financial Affairs

Article 18 (Accounting and Revenue)

① The fiscal year of the IAFICO shall run from the 1st of January to the 31st of December each year.

② The finance required to operate the IAFICO shall be sourced from membership fees, member contributions, society participation fees, and other incomes. Related matters shall be decided by the Board of Directors or the Steering Committee.

③ Should the need arise, the IAFICO may accept sponsored research, donations or financial support from external parties in order to support the business performance of the IAFICO. The Chairperson shall report the details of these at the board meeting.
④ Chairperson should report all the donation from outside and their usage of the year at the IAFICO homepage by the end of March of the next accounting year.

Section 6 Supplementary Rules

Article 19 (Revision of the Bylaws)

① Any other matters not stipulated by this Bylaws shall be resolved by the Board of Directors.
② Revision of the Bylaws shall be carried out, by the proposition of the Board of Directors, or at least one-tenth of regular members, at a general meeting where at least one-third of the total regular members are in attendance, or at a provisional general meeting, with the agreement of at least two-thirds of current members.

Article 20 (Dissolution)

Should the IAFICO intend to be dissolved, it must be decided upon at a general meeting with the agreement of at least two-thirds of current members, and permission must also be received from the Fair Trade Commission. Except for bankruptcy, the dissolution must be registered and reported to the Ministry of Strategy and Finance within three weeks, accompanied by a certified copy of register.

Article 21 (Residual Property upon Dissolution)

Should the IAFICO be dissolved, according to article 77 of the Korean civil law, all remaining assets of IAFICO shall belong to the state, local government, or other non-profit corporations carrying similar objectives.

Additional Clause

These Bylaws shall become effective from the 1st April 2016.

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