

# The Taxation Constraints and Potential Solutions For Indonesian MSMEs

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This study aims to know the constraints of taxation that is currently faced by Indonesian Micro Small Medium Enterprises (MSMEs), and also to find out the potential solutions expected by Indonesian MSMEs. Researchers have conducted interviews and also observations to obtain the information needed in the study. The place chosen by the researchers was the UMKM exhibition located in the Jakarta and Tangerang areas. Researchers used the location of the MSME exhibition to facilitate research covering MSMEs throughout the territory of Indonesia. The results of this study indicate that most of MSMEs respondents in Indonesia do not yet have a sufficient understanding of taxation especially income tax rates for MSMEs. Until now, the main focus of Indonesian MSMEs is still limited to the area of marketing or market education. The paper suggests development of the brand image, managing the business finances and marketing as an identified solutions for MSME to survive in business.

**Key words:** *MSMEs, Taxation, Small Enterprises, Medium Enterprises.*

## 1. Introduction

The Micro Small Medium Enterprises (MSME) is one sector that plays an important role in developing the Indonesian economy (Irjayanti & Azis, 2012). The Indonesian government pays special attention to development of MSMEs and ability to compete in the global market. Various types of businesses are becoming the most influential MSME in boosting the country's economy. The current information shows that total number of MSMEs in Indonesia is over than 57million business unit and has a proportion of 99.99% in Indonesia business

unit (Kemenkop, 2018). This means that MSME can prove their existence in the Indonesian economy.

To optimise Government revenue through the MSME sector, a product must necessarily have quality and excellence in order to compete in the global market. Various products imported from abroad are flooding the Indonesian market with easily adapted by the customer. Plus, imported products are able to provide high quality products at lower prices compared to local products. Starting from the technology that is used in the product manufacturing process, to the marketing system, it can attract customer interest so that it can be said to be superior compared to local products.

With this, there are still many things that the Government evaluation materials to promote MSME in Indonesia. Both those who have internal and external issues, in terms of production and processing, marketing, human resources, design and technology, capital, and business climate (Law No. 20, 2008) have become obstacles in developing their business internationally. Other constraints such as the compliance of business actors in paying the MSME tax have also become obstacles to maximising Government revenue. Based on data from the Ministry of Cooperatives, if MSME is the largest contributor to the country's revenue for the Indonesian economy, it should be able to maximise its potential tax revenue as well (Hendri, 2016). The compliance of MSME actors depends on the knowledge of paying taxes. If they know the use of taxes and the taxes paid are managed in an orderly, efficient and responsible manner, it will be easier to maximise the potential tax revenue. Until today, the effort still has many obstacles in terms of paying taxes. Therefore, the government must help and encourage Indonesian MSME to be able to eliminate various MSME obstacles that still occur frequently in our country.

Tariffs for MSME Income Tax is regulated in (GR No. 46, 2013) with a tax rate of 1% . However, starting from July 1, 2018 (GR No. 23, 2018) is valid as a substitute for previous regulation, with a change in a tariff of 1% to 0.5% and it is final. This rate change is expected to minimise MSME tax payments which can be allocated to maximise MSME businesses or make investments and increase the resilience of the Indonesian economy. Other benefits are also expected to meet tax obligations in an easier and simpler way.

So this study aims to know the constraint of taxation that currently faced by Indonesian MSMEs and to find out the potential solutions expected by Indonesian MSMEs.

## **2. Literature Review**

### **2.1 Small medium enterprises**

According to the Law No. 20 (2008) the definition of MSMEs are: (1) Micro enterprises is a productive property of individuals and/or entities. (2) Small enterprises, are productive

economic activities that stand alone, carried out by an individual or business entity that is not a subsidiary or not branches of companies owned, controlled, or be a part either directly or indirectly from medium or large businesses. (3) Medium enterprises are productive economic activities that stand alone, carried out by individuals or entities that are not subsidiaries or branches of companies owned, controlled, or be a part either directly or indirectly with a small business or a large business with total net worth or annual sales results.

MSME has several principles to be managed: kindship, economic democracy, togetherness, efficiency with justice, sustainable, insightful environment, independence, balance progress, and unity of the national economy. MSMEs have the aim to grow and develop their businesses in the context of building a national economy based on a just economic democracy.

The following are the principles of empowering MSME according to The Law No. 20 (2008): (1) Growth of independence, togetherness and work on their own initiative. (2) Embodiment of transparent, accountable and fair public policies. (3) Development of area-based and market-oriented businesses in accordance with the competence. (4) Increasing the competitiveness. (5) Implementation of integrated planning, implementation and control.

MSME criteria contained in the Law No. 20 (2008) , namely: (1) Micro enterprises has maximum wealth of 50Million IDR, excluding land and buildings, and annual sales of 300Million IDR. (2) Small enterprises has maximum wealth of 500Million IDR, excluding land and buildings, and annual sales of 2.5Billion IDR. (3) Medium enterprises has maximum wealth of 510Billion IDR, excluding land and buildings, and annual sales of 50Billion IDR.

The MSME Sector Classification follows the International Standard Classification of All Economic Activities (ISIC) concept as follows: Agriculture, Animal Husbandry, Forestry and Fisheries; Mining and Quarrying; Processing Industry; Electricity, Gas and Clean Water; Building; Trade, Hotels and Restaurants; Transportation and Communication; Finance, Rentals and Company Services; and services.

## 2.2 Taxation for MSME

Income tax for SMEs was previously regulated in Government Regulation No. 46 (2013) with a final tax rate of 1% . But the case contents of final income tax for MSMEs are changed from a rate of 1% to 0.5%. This revision also became a substitute regulation. The President of the Republic of Indonesia, stipulated on June 8, 2018 (PP No. 23, 2018), that Income Taxes on Income from Businesses Received or Obtained by Taxpayers who have a Specific Gross Distribution and stated valid from July 1, 2018 (Kompas.com, 2018).

Government proposed the tax subject are individual taxpayer and the Agency in the form of a CV, Firm, Cooperatives or Limited companies. The final 0.5 % PPh rate has a term of 7

years, for individual taxpayer, 4 years for corporate taxpayer in the form of CV, Firm, cooperatives, and 3 years for limited companies. A taxpayer is a business actor that has a turnover of under Rp 4.8 Billion IDR in a year. The turnover count used as a reference is subject to a final PPh rate of 0.5%, which is turnover per month, and if the business turnover exceeds Rp 4.8 billion, then the same rate of 0.5% will still be imposed until the end of the tax year. Taxpayers who are not subject to this regulation are taxpayers who choose to be subject to Article 17 Income Tax, permanent establishment, taxpayer who obtain Income Tax facility, and CV or Firm formed by several taxpayer that have special expertise or submit services of the same kind as services in connection with free employment (Anon., 2018).

### 2.3 Obstacles to MSME

At present, Indonesia's MSMEs still have many obstacles such as: intense competition between businesses; access to finance; energy prices; technology; inefficient production costs; economic factors (government fiscal and monetary policy, inflation, interest rates and foreign exchange rates); management skills; processes (feasibility, difficulties and bad habits management); limited sales; and raw materials. MSME believes that intense competition is a daunting challenge that must be faced today, not only to compete with other MSME products, but also with large-scale companies. They think that the market is filled with many competitors with more power which makes it difficult for them to compete. The impact of the financial crisis is also a barrier for MSMEs in Indonesia. MSMEs are still having difficulty getting financial access from formal financial institutions to develop their business which is exacerbated by energy prices which continue to increase from year to year. Capital is also one of the factors that really makes their business grow slowly. They stated that financial institutions did not operate on their side, they found many difficulties when they tried to apply for credit financing from banks, due to complex requirements that could not be met by MSMEs (Iriyanti & Azis, 2012).

MSME obstacles and constraints can also come from internal and external factors. The following are some of the obstacles that originate from internal and external scope (Bank Indonesia, 2016): Internal (capital, human resources, law and accountability); and External (business climate is still not conducive, infrastructure and access).

## 3. Research Methods

### 3.1 The research objects

In this study, the research objects used were respondents of MSME business owners conducted at MSME exhibitions in Jakarta and Tangerang. There are 3 exhibitions which have been covered: **Pekan Raya Indonesia (PRI)** on the date of 27 September to 7 October 2018 in ICE BSD City; **Organic Green & Healthy Expo (OGH Expo)** on 10 - 14 October



2018 at Lippo Mall Puri; and the **Organic Pink Mini Festival** exhibition on October 25-28, 2018 at Ciputra Mall.

Pekan Raya Indonesia (PRI) is an indoor multiproduct exhibition with nuances of the festival and there are many exponents in it, ranging from senggol snacks, fashion, beauty and lifestyle, indie music festival, clothfest, MSME and consumer goods, furniture and home appliance, MAP club, travel and electronics, to the AEKI coffee carnival and automotive. In this exhibition, the researchers interviewed 5 respondents.

Organic Green & Healthy Expo (OGH Expo) is an annual event of the organic community in Indonesia. There are more than 300 local SME craftsmen/farmers/entrepreneurs from all over Indonesia who introduce organic products in harmony with nature. In this exhibition, researchers interviewed 9 respondents.

Organic Pink Mini Festival is an organic community event in Indonesia with a total of 60 organic craftsmen/entrepreneurs and health products with various programs in it to support the breast cancer campaign. In this exhibition, researchers conducted interviews of 3 respondents.

### 3.2 The research process

The researchers conducted interviews and observations to get the information needed. The place chosen by the researcher is the MSME exhibitions located in Jakarta and Tangerang. Researchers used the location of the MSME exhibition to facilitate research covering MSMEs throughout the territory of Indonesia. The research period was from October to November 2018.

This study conducted descriptive qualitative research because researchers used interviewing techniques with taxpayer MSMEs that are in the exhibition MSMEs in Jakarta and Tangerang. The qualitative research method is a research method that is based on a post positivism philosophy, which is used to examine natural object conditions where the researcher is a key instrument, data source sampling is done purposively, data collection techniques are triangulated, data analysis is inductive/qualitative, and qualitative research results emphasise more meaning than generalisation (Sugiyono, 2012).

The following are the list of interview questions in this study (Irjayanti & Azis, 2012; Hendri, 2016):

1. Profile of respondents
2. What type of business is managed?
3. Do business people know about taxes for MSMEs?
4. Do businesses pay the MSME tax?

5. How do I/procedure to pay taxes?
6. According to respondents, did other business operators comply with tax payments for MSMEs?
7. What obstacles are faced when paying MSME taxes?
8. Solutions for Indonesia's MSMEs in tax collection and the role of the government in developing MSMEs on the international scene?

### 3.3 The data analysis

The data analysis method used in this study is triangulation. Triangulation is a combination of various methods used to study interrelated phenomena from different perspectives (Rahardjo, 2010). According to him, triangulation includes four things namely, triangulation of methods, triangulation between researchers (if research is conducted with groups), triangulation of data sources, and theory triangulation. This study used triangulation of data sources namely: interviews, observation and documentation.

## 4. Result and Discussion

### 4.2 The overview of respondents

In this study, primary data were obtained through interviews to examine various problems faced by MSMEs in Indonesia. The researchers first observed in the field, then conducted interviews with business actors, and took photos with MSME respondents for documentation. There are 8 interview questions. Researchers managed to gather respondents in 3 different locations with a total of 17 MSMEs.

The first respondent is Lombalio. Lombalio is a fashion business that sells a variety of women's bags from raw materials from Lombok, Bali, Kalimantan, Flores, Kupang and Nusa Tenggara Timur (NTT). The second respondent is Violet Kitchen. Violet Kitchen is a food and beverage business that sells Gra Nola beans and originates from the capital city of Jakarta. The third respondent is Gado-gado 75C. Gado-Gado 75C is a business engaged in the field of food and beverage that sells home-made gado-gado and Pecel spices. The fourth respondent is Maduji. Maduji is a business that operates in the field of medicine, because the honey it produces is very useful for health. Maduji a forest honey yan g directly produced by bees from North Sumatra and is currently being marketed in the city of Tangerang. The fifth respondent is Alisya Collection who are engaged in fashion.

The sixth respondent is Beauty Barn Indonesia. Beauty Barn Indonesia is a business engaged in the field of natural medicine for health that sells various types of essential oils originating from Jakarta. The seventh respondent is Fres Green Organic from Malang. Fres Green Organic is a MSME that engages in food and beverage business that sells Surabaya sambal, organic rice products, non-MSG healthy broth, non-gluten local flour, natural noodles,

natural beans, and many more. The eighth respondent is Nusa Madu. Nusa Madu is a business that operates in the field of medicine, because it sells forest honey from wild bees from NTT, and is very useful for health. The ninth respondent is Havel Tea. Havel Tea is a start-up business engaged in the field of food and beverage that sells various types of tea that have been distributed to restaurants and cafes in Jakarta. The tenth respondent is Osadha. Osadha is a MSME that is engaged in food and beverage, which sells a variety of traditional herbal drinks, snacks and organic food originating from Jakarta. Eleventh respondent is Aquilla. Aquilla is a business that operates in the field of cosmetic products originating from Indramayu. The twelfth respondent is Angeluna. Angeluna is a MSME that is engaged in the treatment of tubules originating from Jakarta. The thirteenth respondent is Ilone. Ilone is a business that is engaged in body care (facial oil, essential oil, cleansing balm and masks) from natural ingredients originating from Jakarta. The fourteenth respondent is Hibo Organic Coffee. Hibo Organic Coffee is a business engaged in coffee that sells coffee beans of indigenous Papuan origin, including cold brew.

The fifteenth respondent is Coco Soap Works. Coco Soap Works is a MSME that is engaged in body care that sells bar soap products from natural ingredients/minerals originating from Jakarta. The sixteenth respondent is Towang. Towang is a business engaged in the field of food and beverage that sells organic tofu and originates from Malang. The seventeenth respondent is D'Natural. D'Natural is a MSME that is engaged in food and beverage which sells healthy snacks such as cashew butter cookies, dry sus cakes, brownies, rollcake and coconut sweet sauce originating from Surabaya.

#### 4.3 The MSME obstacles

Based on the results of previous studies (Iriyanti & Azis, 2012) there are 10 obstacles experienced by entrepreneurs of SMEs (the fierce competition between SMEs, access to finance from formal institutions, rising energy prices, less sophisticated technology, inefficient production costs, economic factors, lack of skills/employee training, administrative processes, poor sales performance, and difficulty in obtaining raw materials around the business location. Of the 10 obstacles researchers use research journals (Iriyanti & Azis, 2012) as a guide or reference to inquire constraints experienced by businesses to the respondent. From the results of the data obtained, there are a lot of obstacles faced by each respondent, the researchers decided to take at least 7 constraints based on the most votes that have been sorted according to the highest to lowest ranks experienced by MSMEs today. The results of these data can be seen in Table 1.

**Table 1: Seven obstacles faced by MSMEs**

Rank	Obstacles
1	Difficulty in getting raw materials around the business location
2	Administrative processes (related to complex, difficult and expensive procedures)
3	Poor sales performance (turnover not reached) which causes a lack of income
4	Lack of market marketing/education
5	Access to finance from formal financial institutions (the difficulty of getting money from banks)
6	Inefficient production costs (due to technological obstacles, making it difficult to manage production costs)
7	Economic factors (government fiscal and monetary policy, inflation, interest rates and foreign exchange rates) and government policies

#### 4.4 Potential solutions for MSME

The first obstacle, obtaining raw materials around the business location, is a major constraint for SMEs respondents. There was a solution offered. According to the Coordinating Minister for the Economy, Darmin Nasution, the Government gave MSMEs a super-easy package to import raw materials (Ariyanti, 2017).

The second, difficulties in business licensing for MSMEs, also pose obstacles in a difficult, complex and expensive administrative process. The **MyUKM** application appreciates the Government's step in issuing licensing policies trying to be integrated electronically (Mudassir, 2018).

The third was lack of marketing or market education. The solution offered from this obstacle is that according to the Ministry of Cooperatives and MSMEs, they continue to strive to introduce and improve digital skills for SMEs in Indonesia. For example, for registration of cooperative legal entities, since 2017 it has been an online system. Then they have also made what is called the **UMKM go digital**, and provided assistance (Herman, 2018). Then the steps the Government can take is the maximum utilisation of broadband that has been installed in 400 districts and 114 regions (Harmawan, 2018). Further solutions offered to overcome the lack of marketing especially online and market education is the **Qappas** application. Qappas is a Software As A Service (SaaS) platform that provides convenience to MSMEs by simply accessing a web browser and mobile application (Jeko, 2018).

The Fourth, a lack of access to finance from formal financial institutions that make it difficult to obtain loans from the bank is also an obstacle for the respondent MSMEs. One of the solutions offered is to access financing through online loans that have been registered as an alternative financing. The presence of Fintech companies in the form of online loans will

facilitate access to finance for MSME entrepreneurs (Dinisari, 2018). Then Bank Indonesia has also developed a financial recording administration system. With this application, it is easier for MSME players to get access to capital financing by banks (Setyadi, 2017). Cash loans for MSME businessman **Kredivo** is also a fintech that provides loan services for Indonesians who have been struggling to get credit facilities (Kompas, 2018).

Then responding to the respondents' solutions on how to do bookkeeping for MSMEs and to simplify the tax reporting process, the Ministry of Cooperatives launched the **Lamikro** application (Micro Business Accounting Report) for micro businesses and those who are just starting businesses or start-up entrepreneurs. Lamikro is a simple accounting application for micro businesses that can be used via smartphones with the Android operating system (Julianto, 2017).

To overcome the problem of MSME tax transactions, a digital application has been launched which functions as an online cashier as well as a means for calculation, payment and reporting of income tax of MSME actors, namely **Klik46** (Spice, 2018). MSMEs also need the support of many parties in order to be globally competitive. One effort to improve the competitiveness of SMEs is the cooperation of all business with the authority and role of each. One example is to facilitate licensing and provide tax incentives, to facilitate business activities. Access to marketing, access to capital and networking also makes Indonesian MSMEs less competitive with neighboring countries. Therefore, increasing access to capital can be done among others by providing special MSME financing schemes that are integrated with capacity building activities, and group empowerment in social capital (Ministry of Finance, 2016) .

## 5. Conclusions

The results of this study indicates that most of MSMEs respondent in Indonesia do not yet have sufficient understanding of taxation especially income tax rates for MSMEs. Until now, the main focus of Indonesian MSMEs is still limited to the area of marketing or market education. The study concluded that there are at least seven obstacles faced by MSMEs such as: difficulty in obtaining raw materials in the vicinity of the business; administrative processes are difficult and complex; sales performance poor that causes lack of income; lack of marketing/education markets; access to finance from formal institutions finance; technological obstacles that make production costs inefficient; and economic factors and government policies. These constraints are a challenge for government programs in order to overcome various obstacles to MSMEs and competition in the international market. Based on observations and interviews, many MSME actors cannot mention solutions for MSME taxation in Indonesia and the solutions for MSMEs to compete in the global market, so the researchers looked for solutions from various news media and the Ministry of Finance's website to be able to overcome the obstacles.

## Acknowledgement

Researchers are grateful for all the assistance that has been given. The researcher confirms that this article has been in seminars 7th National Tax Symposium, Trunojoyo University, Madura, Indonesia, and has never been journalised before.

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