

INVESTMENT SCAM IN INDONESIA (CASE STUDY: ERNI FASHION)

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ABSTRACT

Investment is a financial decision currently made by many people. Obviously, people must face the failure of their investment. Based on the case of investment scam in Erni Fashion in Salatiga - Indonesia, the main cause of failure is that investors do not have enough understanding of investment and of the asset or product of investment. Therefore, investment education plays an important role in enabling people to invest well, from gathering information until making a decision.

Keyword: Investment, Risk, Return, Profit Sharing

Introduction

Most people in Indonesia think that investment is practiced by wealthy people and associated with investment products like stocks. Middle-low income and less educated people think investment is not relevant to them, so they never evenly distribute their spending to an investment product. It happens because they never get enough investment education from either government or financial institutions. They also face illegal investment from illegal financial institutions, which offer high return products, whereas people invest to increase their money. It shows that investment education plays an important role for Indonesian people.

Generally, there is no big difference between personal and business institutions' cash flow, which includes cash-out and cash-in. Cash-out includes daily expenditure, extraordinary (emergency) and investment. Cash-in comes from revenue (wage, net income), return of investment and debt. The effort to increase return of investment is how to choose the right investment, which has greater return than its risk.

Investment is an activity intended to increase personal assets. The asset itself has two meanings, non-financial and financial. First, non-financially, increasing asset is increasing an intangible thing, such as ability and relationship. Second, in its financial, increasing asset is increasing the economic source, such as money.

Formally, people invest financially by saving money at financial institutions or buying property. At financial institution people can choose deposit, bond, or stock. If people save their money in property it can be land, houses, or gold. Yet, some people make an informal investment by entrusting their money into relative's or friend's business. The informal investment institution uses this condition to offer bogus investment for its advantage, such as QSAR, Ibist and Erni Fashion (See on table 1.). This kind of deception happens not only in Indonesia. All that institutions still have the same mode but different packaging. The phenomenon indicates that most people still lay about investment.

Table 1. Bogus investment 1987 – 2007 in Indonesia

Year	Case	Mode	Fund Raising (in billion IDR)	Member / Participant (person)	Person in charge	Judgement
1987	Yayasan Keluarga Adil Makmur (YKAM)	Credit Union (an institution that give saving and financing service)	20.7	74.000	Jusuf Handojo Ongkowidjaja	15 years of prison
1992	PT. Multi Jaya Indovesco	Trading	1.5	150	-	-
	PT. Suti Kelola	Illegal bank promised interest of 3.5% monthly, and then bonus of 2.5% annually	35	4.000	-	-

1995	PT. Sapta Mitra Ekakarya (Arisan Danasonic)	Arisan berantai (Money Game)	110	500.000	Anneke Kolondam and Sindi Husain	-
1998	PT. Banyumas Mulya Abadi (BMA)	Illegal bank promised profit of 90% per 21 days	3.000	120.000	Abdul Muthalib/Muhammad Yusuf	-
1998	Koperasi Simpan Pinjam (Kospin) South Sulawesi	Illegal bank	745	200.000	Suparman Ishak	-
1999	PT. Era Catur Wicaksana	Multi level marketing	1.000	40.000	Abok/Toni	-
2000	Yayasan Misi Islam Ahli Sunnah Waljama'ah	Sharing of 9 Indonesia kingdom's heritage asset	-	9 areas, 2.500 branches, 3.600 units	KH. Abdul Rahman	Starting trial Dec 16 th , 2002 at Bandung
2002	PT. Qurnia Subur Alam Raya (QSAR)	Agribusiness	500	-	Ramil Araby	8 years of prison and a 10 billion IDR fine
2003	PT. Adess Sumber Hidup Dinamika (ADD Farm)	Agribusiness	150	5.000	Ade Suhudin	Wanted since Dec 9 th , 2003
	PT. Probest International Indonesia	-	20.000	20.000	Burhan Sofyan	Arrested at Dec 9 th , 2003
2005	CV. Investindo	Illegal bank promised interest of 25% monthly	62.5	3.000	Krisbianto	13 years of prison and a 35 billion IDR fine
2006	Interbanking Bisnis Terencana (Ibist)	Illegal bank promised interest of 4% monthly	224	5.042	Wandi Sopian	Arrested at March 15 th , 2007
2007	PT. Wahana Bersama Globalindo	Sales agent of Dressel Investment Ltd	3.500	10.000	Krisno Arbiyanto	-

Source: Kompas, April 30th 2007

PORTRAIT OF ERNI FASHION

Erni Fashion was an apparel merchandising company, established around the year 2003 by Erni Idaruswati in the village of Gunungsari, Salatiga. Erni Fashion had grown from a street merchant business that traded apparel to an industry that produced apparel for sale in its own three stores, and to its business partner.

During its development time, Erni Fashion needed more and more capital to expand its business and capacity. Information circulated amongst the community, portraying Erni Fashion's business partners as nationally dispersed large garment industries. This was proven wrong when the scam was uncovered in the year 2006. The scam involved Erni Idaruswati's husband, Joko Mintarto, amassing capital from their relatives and community. Together, they influenced their relatives and community to invest their capital in Erni Fashion during family and community gatherings. Furthermore, the scams were spread even more by word of mouth of the unsuspecting victims themselves.

False information circulated by Erni's husband to lure investors consisted of bogus financial reports and data, projected profits, and even photographs related to the company. Interestingly, not all of the victims received the first hand and complete information. Some of them received distorted information from middlemen, and some of them even only received information regarding the profit if they became investors. And yet, still many of them fell victim to Erni Fashion.

Types of Investment in Erni Fashion

There were two types of investment in Erni Fashion, direct and indirect investment. On direct investment, investors directly contacted to Erni Idaruswati or Joko Mintarto. If there was a middleman, Erni Fashion gave commission to them. The investors would receive sum of return from Erni Fashion. The letter of agreement, if available, would be signed by Erni, and the investor, as would the receipt for the money invested. Direct investment consists of model 1 and model 2 as seen in Figure 1.

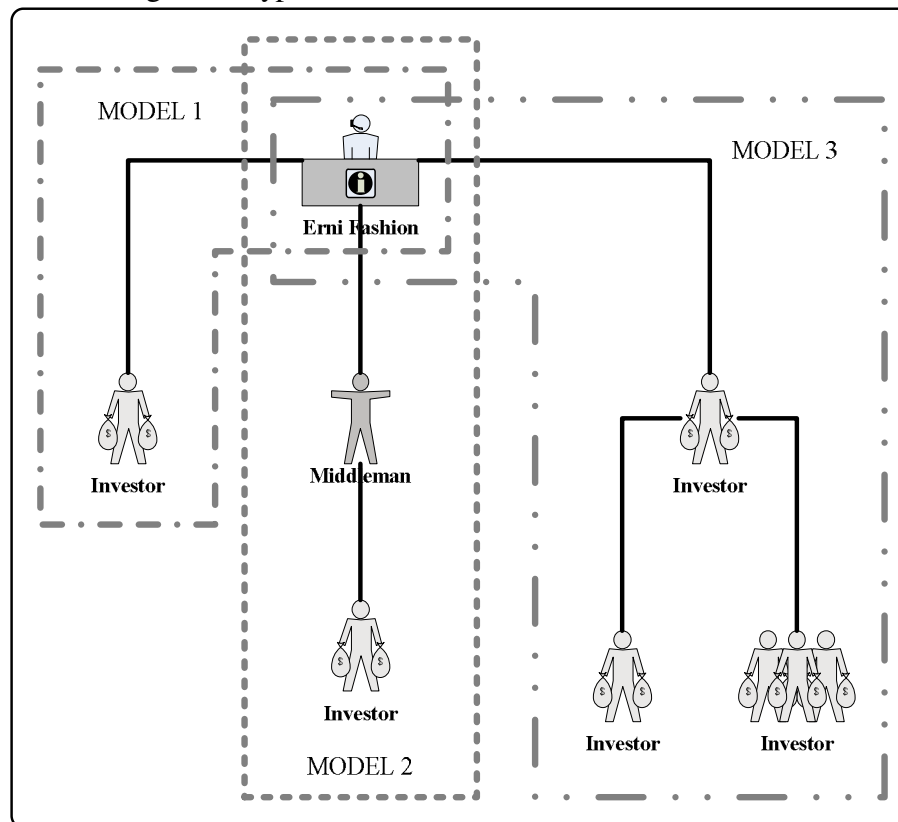
In the indirect investment, a middleman directly contacted to Erni Idaruswati or Joko Mintarto on behalf of several investors. The letter of agreement, if available, will be signed by Erni, and the middleman. And so did the receipt for the money invested. The investors had their agreement with the middleman, most without any legal documents at all. The middleman would take a profit based on their own calculation from the investor's return. The investors would receive sum of return from Erni Fashion minus the middleman is profit. Indirect investment is model 3 as seen in Figure 1.

Some of the investors had their agreement written in a sealed agreement letter, while some others didn't have any agreement letter at all. Some of the victims gave the money directly to Erni Idaruswati, while some other through a middleman. Some of them received sealed receipt, some of them received unsealed receipt, and some of them even received no receipt at all. Most of the victims that didn't receive any receipt were investing through their trusted middleman.

Erni Fashion promised their investors that after one month from investment date, the investor will receive around 4 percent to 12 percent monthly return from their investment (48 percent to 144 percent annually). The payout was promised every Friday or Saturday, weekly or twice weekly and then shrunk monthly. Most of the payout went out without any receipt. They were already prepared in envelopes, with the investor's or middleman's name and the sum written on it.

The investors could withdraw the amount invested at determined time for each investor. There was no document which canceled the letter of agreement previously. On the other hand, investor would forfeit their return if they withdrew the money invested. Withdrawal can only be done at agreed date written in the letter of agreement, and Erni Fashion must be notified one month prior.

Figure 1. Types of Investment in Erni Fashion



Source: Data processed, 2008

THE ERNI FASHION'S INVESTOR UNDERSTANDING OF INVESTMENT

Investment, Return and Risk

The investors of Erni Fashion have many terms for their investment activities. They are entrusting money, profit sharing, investment and depositing money. (*titip uang, bagi hasil, investasi, menabung*). The terms for the return – money investors accepted – are also named in many ways, interest, gains and *sisa hasil usaha* (SHU, profit sharing in cooperative institution). As written in the letter of agreement, the owner of Erni Fashion actually already named the investment activity. The heterogeneous terms appear because not all of the investors got a document as the evidence of their transaction. That is why the terms were different for each investor. The investors did not realize that they are investors. It indicates that they have relatively low understanding of investment.

Almost all of Erni Fashion investors have a simple notion of investment. They just think that by making an investment they will have 'gain'. But they just think about the gain, and have little understanding of the risk (inherent risk). This condition can be indicated from their reason for joining this investment. The big gain and very short payback period become a very interesting point when they decide to join the investment. There are some investors that already think about unlogical gain and the high possibility of exploitation, but still they decide to join the investment. This condition appear because they try to play with time, like in a money game. If they join the investment in the beginning they might to get the gain. Besides, they estimate that things which have higher risk will give higher return (the theory of risk and return).

This condition happens because there is asymmetric information between the investors and

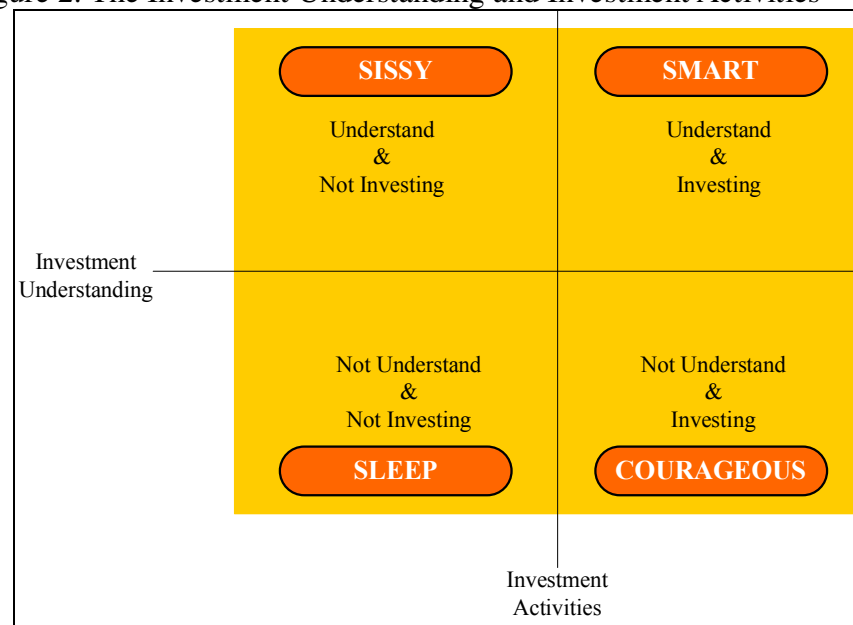
the owners of Erni Fashion. First, the owners just give the information about a high gain by a very interesting presentation (the Erni Fashion return is 4 -12 percent monthly, it is equal to 48 -144 percent annually, when the bank rate is + 12 percent annually). Second, the investors ignore the characteristic of the operation and just pay full attention to the rate of return. The owner of Erni Fashion did not give the clear information about the characteristic of its operation. Almost all of the investor which are the respondent, do not understand how the Erni Fashion operation can make a huge gain.

Beside their reason joining the investment above, the fund source can be an indicator of their understanding of investment knowledge. Some investors bravely take all of their savings and even pawn or sell their assets. The most interesting thing is investor take a debt to the bank or cooperative with land certificate or movable goods as the guarantee. They still have a gain which is the variance between return they get and the interest they have to pay. Actually, they are the real risk taker. If they have a good understanding of investment they will be a smart investor and able to choose well which investment is healthy and which one is unhealthy.

Doing Investment

The figure of the investment knowledge and investing below (Figure 2) shows that the investors fall into four categories :

Figure 2. The Investment Understanding and Investment Activities



- **Sleep**
People in this category mostly do not have enough investment knowledge and do not join the investment. Their reasons are they have limited funds; they have lack of information, knowledge and intentional/understanding; and they are also averse to risk.
- **Sissy**
People in this category mostly have enough investment understanding but they do not join the investment. They are called risk avoiders. The reason used by this category are they have a limited fund and they averse the risk.
- **Courageous**
People in this category do not have enough understanding of investment but they join the

investment. This people are called risk takers. This following reason cause this category are brave to take the risk and doing investment because the other investors.

- **Smart**
This category consists of people who have enough understanding of investment and they joint the investment. This category caused by brave to take the risk, regain conciousness of investing, and also understand the risk of investment

Erni Fashion's investors were spread in courageous and a little part in smart. This condition can be seen from their participation in Erni Fashion's investment. People in smart category are people who has take the benefit between return they get and interest they pay.

PRODUCT INVESTMENT ON BUSINESS BY PROFIT SHARING

As claimed in the documents which investors have, the letter of agreement and the money receipt, that the investment product is a profit sharing investment. Their kind of investment reminds us of the case of PT. QSAR (Qurnia Subur Alam Raya). The company offered agribusiness investment in which people could invest their money in land. The harvest of the land would be sold, and the money would be shared with investors by a profit sharing system. In August 2002 the investors went wild when the company could not pay the profit sharing. There were some huge investors; some of them even government officials.

Generally, there are two kinds of investment, investment in business (in a company) and investment in a financial product (in financial institution). Nowadays, a profit sharing system is most widely used on business investment. Certainly, profit sharing is not only used in business investment, such as investment by *shariah*. Dissemination of investment on business is mostly through personal word, such the successful investor who gets high return. Frankly it is usually talking about money.

Profit Sharing in Erni Fashion

In general, there are two kinds of profit sharing systems:

- **Absolute Profit Sharing**
Absolute profit sharing is a sharing system based on sum percentage of business profit. Sharing will be given when the company has the profit and no profit sharing when it has loss. For example, if there is profit IDR 100.000.000 (revenue – expenses) and the profit sharing is a 5 percent of profit, we will have IDR 5.000.000. On the contrary, when revenue minus expenses is equal to either zero or loss, we will have nothing.
- **Promised Profit Sharing**
Promised profit sharing is a sharing system based on a sum percentage of investment, apart from whether the company has either profit or loss. For example, if we invest money of IDR 20.000.000 and the agreement is a 2 percent of investment monthly for a year, we will have IDR 400.000 for twelve months, aside from whether the company has either profit or loss in each month.

The investors of Erni Fashion revealed that promised profit sharing was used in Erni Fashion. The method is used because it has not made difficulties for it has a schedule for distributing/sharing the money. Erni Fashion promised profit sharing of 4 - 12 percent of investment monthly and the percentage was different for different investors. The schedule of sharing was either Friday or Saturday at the end of month.

In principle, profit sharing is not a misleading thing. *Shariah* businesses or venture capital uses the profit sharing concept. The profit of investment is not only a return, but it also includes a risk. This is the information which was not explained by Erni Fashion. There are some logical thinking of investment and how to do investment. The logic is how to manage the inherent risks of the product investment. In the fashion business, it is true that people need cloth, but people will not consume cloth continually. It means the market will not absorb all fashion products. Frankly, there is an optimum point of both capital absorption and product marketed. This logic impact is not only technical aspect but also impacts the profit goal too. No matter how high the fashion demand, it is hard to reach profit of 48 -144 percent annually, as Erni Fashion offered.

How does the company guarantee the impossible return? There are some possibilities. First, the price of Erni Fashion's product is much higher than competitors. Second, Erni Fashion is extremely efficient, so the company spends nothing. Third, Erni Fashion runs a 'Business Matrix'. The first and the second are impossible because Erni Fashion is not a market leader and every company has operational expenses, even they are low. The third is that every business has its grace period. This is unbelievably condition of Erni Fashion. The strange thing is during investment period which is not yet profitable; Erni Fashion has to pay profit sharing to investors. Where does the money come from? The strong possibility is from other investors. In other words, money of current investors will be used to pay previous investors. Therefore the previous investors will get the profit longer than the current investors.

Business is a derivative of capitalist ideology. In this ideology, investors are averse to share the business profit. They are just eager to share the risk. Assuming that Erni Fashion really has profit of 48 -144 percent annually, the company would not seek to share. If they want to share the profit, it will be a much lower percentage which the company uses loan of bank. By 17 – 20 percent annually, Erni Fashion will have higher margin than using money of investors. But Erni Fashion did not use loan of bank which is accountable. Otherwise, if Erni Fashion is a good business, many banks will be interested to give financing. Evidently, no banks are interested. It means that Erni Fashion is clearly un-bankable.

By operational mechanism, Erni Fashion was an individually owned business which had no legalism. Actually, the company had to have a license as a fashion trading company. Moreover, Erni fashion began gathering money. When a real-sector company does money gathering from people, it should be done through financial instrument/product, such as stock. In fact, the company did not do that, even it has no legacy to gather money.

Choosing the Right Product Investment

Erni Fashion's investors did not understand that they were making an investment. They thought that they were making a deposit in Erni Fashion. Therefore, investors named their return as an interest income. It was a wrong understanding because deposit and investment are different things. Deposit is money set aside without expectation of the growth of the money. Depositing the money in the bank is a way of saving. Investment expects the growth of time value of money, so it will give return.

This wrong understanding is because Erni Fashion did not explain what kind of product investment was offered. The agreement of profit sharing did not reflect the kind of investment product. This confusion is used by Erni Fashion to deceive investors. Moreover, from the beginning of the offering, Erni Fashion has misled investors both by complicated computation and method about the high return. On the contrary Erni Fashion should explain how this investment product works.

In general, investment referred to stock is caused by poor education on financial products.

Actually, the role of investment institution is needed to enable learning by fund owners about the financial product offered so that the fund owner as an investor candidate can determine risk of product as well as its return.

CONCLUSION AND SUGGESTION

Conclusion

Erni Fashion offered its investment product between 2003 – 2006 and it multiplied by word of mouth (in Indonesian called “*getok tular*”). There are two types of investment, direct investment and indirect investment. The direct investment can be divided into two forms, investment with middle-man and investment without middle-man. In the indirect investment a middle-man is an investor too, like in multi level marketing system. The investor gets return as long as they invest the money in Erni Fashion. They get 4 – 12 percent monthly.

The investors had minimum information from Erni Fashion’s owners. They did not understand about the characteristic of the operation. There two facts show that the investors investment understanding was relatively low. They just paid full attention to the relative high return and did not pay attention to the risk.

The investors’ understanding of the investment product was also relatively low. This condition can be seen as their understanding about Promised Profit Sharing. The low understanding of investment made them unable to choose the investment product which fit to their category.

Suggestion

Based on the relatively low understanding of investment and investment products, it is necessary to develop an investment learning. it will be able to shift people’s understanding and people’s investment activities from sleep, sissy and courageous into smart ones. Developing an investment learning will be an interesting further research for that is actually what the people need.

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