Conference Paper

Building Sustainable Village-Owned Enterprises: The Institutional Change of Microfinance in Banyuwangi Regency

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Abstract.
The purpose of this study is to develop a model for the institutional transformation of a government-driven program, namely involving the transformation of DBM (Dana Bergulir Masyarakat) into Village-Owned Enterprises (BUMDesa). This research will hopefully help in developing the best transformation model to enhance policy effectiveness and empower BUMDesa as the primary pillar in the spirit of partnership, by taking into account BUMDesa policy after the publication of the village law and its derivative regulations in the face of complex policy challenges. The Nawacita agenda, recognition-subsidiarity principle, and granting local autonomy at the village scale were the core principles of the preceding BUMDesa policy shift. BUMDesa's current job is to change the government-centric agenda into practices that reflect the delegation of local power at the village scale, at both the village and rural area levels. Understanding the Berdesa tradition is essential for the broader policy agenda to promote village economic enterprises so that it is carried out in practice and still recognizes, respects, and elevates communities in Indonesia. Elinor Ostrom (1990) provides a thorough understanding of institutions in the management of common goods to achieve sustainability, and her work complements the conceptual framework developed by Douglass C. North and Bromley to understand the relationship between institutions and policies in the context of resource management. This study is guided by the theory of institutional change, and uses a qualitative approach with a case study design.

Keywords: institutiional transformation, village credit agency, microfinance institution

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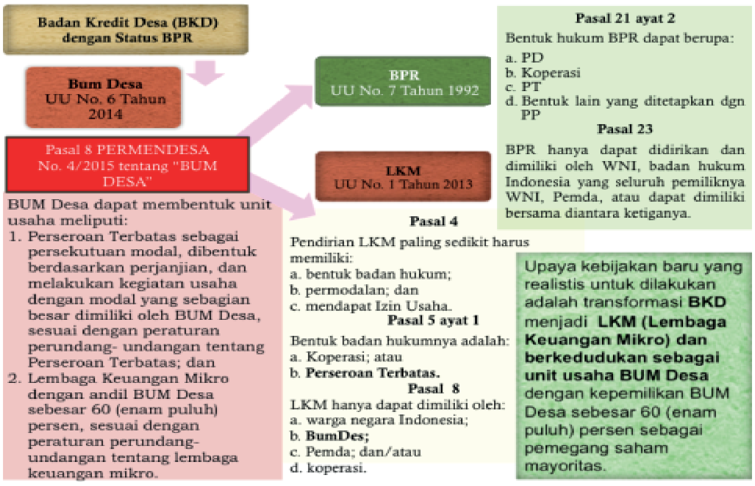
1. Introduction

Discussing poverty in Indonesia and many other developing countries cannot be separated from discussing the problem of poverty in rural areas because almost all poverty problems in developing countries are in the village Yustika, [1]. One of the most crucial issues regarding rural poverty is lack of capital Yustika and Baks, [2]. President Joko Widodo's Nawacita Vision raised the issue of building from the periphery Setiawan, [3]. Building from the periphery, in this case, is a commitment from President Jokowi to solve problems in rural areas. One of the main problems of development in rural areas is access to capital, and limited capital in rural areas is an important aspect that is a minor problem in almost all developing countries. Limited capital will not be able to circulate economic activities; without circulating economic activities, capital accumulation will not be possible.

Based on the above problems, policymakers recommended the establishment of microcredit as an instrument to address the institutional aspects of the financial sector in rural areas. Rural financial sector development emerged mainly in the 1990s Yustika [2]. The rural financial sector has been developed in many developing countries, such as Bangladesh, Indonesia, Thailand, Malaysia, Pakistan, Nigeria, and Zambia. Some countries are considered successful, such as Bangladesh, through Grameen Bank Yunus & Weber, [4]. Many people view microfinance as an important component of economic growth, particularly in rural regions, and support it as a tool for eradicating poverty. This finding is in accordance with Stiglitz's [5] assertion that the expansion of rural loan markets and economic growth are interdependent. To address market failures caused by asymmetric information, imbalanced market power, and the impact of negative externalities, government engagement in the creation of financial services legislation is justified from a public-policy standpoint Freixas and Rochet, [6]. Various regulations were issued by the Indonesian government and changed with each regime until Law No.1 Year 2013 was born, which regulated Microfinance Institutions (MFIs) and changed the diversity of the legal status of rural microfinance that had been regulated previously through ministerial regulations.

One of the rural microfinance organizations that has undergone institutional transformation is the Village Credit Agency (BKD). Established in 1929, the BKD survived the onslaught of changing regulations, as shown in Figure 1. This phenomenon has sparked critical thinking to further explore the regulatory dynamics and community responses to these regulatory changes.

Regulatory changes that mark the institutional changes of rural microfinance have been widely captured by previous researchers, who recognize that the activities of Microfinance Institutions (MFIs) are shaped by their broader institutional context Chliova et al., [7]; Siwale [8] and/or can be important actors in shaping institutional arrangements. and/or can be important actors in shaping new institutional arrangements Khavul et al., [9]. Similarly, neo-institutional theory has helped understand various organizational phenomena Bruton et al., [9], particularly notions of agency and the context of institutional change Maguire et al., [10]; Mair and Marti, [11]. The use of networks to implement



Source: Book 7 Village-Owned Enterprises Village Collective Business Spirit (Putra, 2015)

Figure 1: Transformation of Village Credit Bank into BUM Desa.

institutional change McKague & Oliver, [12]; McMullen, [13] or institutional change as a corruption-fighting mechanism Rajwani & Liedong, [14].

This study focuses on the transformation of rural credit institutions and the response of Village Credit Agency (BKD) managers to the demands of institutional transformation. More explicitly, this study aims to examine the transformation undertaken by BKDs spread across 66 villages and 20 sub-districts in the Banyuwangi Regency in response to the demands of institutional change governed by various national regulations.

1.1. Institutional Change

The grand theory of this study is the Theory of Institutional Change Yustika [2]. Institutional change leads to changes in conditions that then make the necessary new adjustments through external factors (permanent feedback process), and so on. Institutional change is considered a permanent transformation process; hence, it can be a major factor in structural change in a given social system, regardless of the speed or source of change. The following five propositions define the basic characteristics of institutional change North [15].

1. Continuous interaction between institutions and organizations is key to institutional change.
2. Competition allows organizations to invest in skills and knowledge to survive.
3. The institutional framework dictates the types of skills and knowledge considered to have maximum returns.

4. Perception comes from players/performers' mental constructs.

5. The economic scope, complexity, and network externality of the institutional matrix increase institutional change and path dependency.

The reasons for institutional change are mapped into two factors, namely *the demand of constituents* (labor in the company) and *the supply of* institutions that have specific *authority/supply from a specific authority,* such as changes in laws by the government. North also emphasizes that there are two main factors in understanding the dynamics of institutional change Hira and Hira, [16]. First, institutional change is a *symbiotic relationship* between an institution and organizations surrounding the incentive structure provided by the institution. Second, institutional change is a *feedback process* in which individuals perceive and react to changes in their opportunities. Based on these propositions, North argues that there are fundamental challenges to creating efficient institutions. North argues that there are fundamental challenges in creating efficient institutions, namely, aligning informal aspects with formal constraints and creating and maintaining a polity that will support adaptively efficient institutions.

According to Davis-North [17] and the following four factors, which include individuals or groups seeking to change institutional arrangements or the institutional environment, can be considered sources of change .

1. Changes in relative prices in the long run may lead to an increase in certain economic activities or create new economic activities.

2. New technological opportunities can create revenue.

3. Rent-seeking opportunities can trigger interest groups to make institutional changes to adjust rent and income redistribution to their liking.

4. Changes in collective attitudes, as Bromley [18] points out, can lead to institutional change.

There are two types of institutional changes. First, *institutional changes* are induced. Second, *institutional changes* were implemented. The transformation of microfinance institutions uses Bromley's conception approach, which divides policy into three levels: policy, organization, and operational Tachjan et al., [19]. Bromley's policy process model explains that at the political level, there are high state institutions or legislative bodies that have the authority to issue regulations (policies) on the broadest scale, for example, in the form of Laws or Government Regulations. Furthermore, to be able to implement laws or regulations at the organizational level, the government has agents in the form of departmental or non-departmental institutions as a further elaboration of higher policies. This means that the political and organizational levels are bound by an institutional arrangement that lays out the rules of the game of how these organizations work or operate. The next institutional arrangement occurs between the organizational and operational levels occupied by individuals, officers or officials of microfinance institutions, people's economic actors, banking circles, and so on.

The transformation process implies moving to a shareholder ownership structure and most often includes being subject to supervisory regulation by national banking authorities. The arguments for transformation are manifold and include the importance of becoming independent from donors, better access to commercial funding, better governance structures, and the possibility of providing clients with savings accounts. However, some argue that commercialization and transformation tend to push MFIs away from their mission to serve the poor Dichter and Harper, [20]. For example, studies such as show that transformed MFIs increase their loan size and tend to reduce services to women clients.

These facts suggest that institutional change does not happen quickly without obstacles, nor does it always lead to improvements in efficiency and service. As North [15] suggests, continuous interaction between institutions and organizations is the key to institutional change. On the other hand, the claim of regulation as an improvement in services is rejected by the results of empirical studies in many countries that found that regulatory power has no impact on the performance and assessment of financial services institutions; regulatory power is used only as a change in status. The results show that outreach is influenced by the level of deposits (savings), not by regulation, and the indirect effect of regulation is the only method for MFIs to attract deposits Barth et al., [21]. The dynamics and response to change also indicate a widespread debate on the shifting mission of MFIs away from market segmentation for the poor and towards new segments Mersland and Øystein Strøm, [22].

The scheme of the long history of BKD arrangements, referring to Scott's [23] statement that institutional change in a historical context, which identifies four phases of institutional change models, one of which is change due to the *evolution of common law,* can be triggered by formal authority (through regulation). Any analysis of institutional change is not in a position to determine which model of institutional change is more ideal. Most analysts can analyze the weaknesses and strengths of each type.

Based on the literature review above, institutional change is only seen based on changes that occur at the level of changes that occur in the organization alone, and in the context of institutional change, there is also no model that can bring together several organizations that then emerge as a consequence of institutional change. In this context, there are three major organizations that emerge in the dynamics of microfinance institutions in Indonesia: the State, the Community (village), and the Financial Services Authority. Another reality is that the transformation of BKD into a Business Unit in Bumdesa is also a turning point that becomes a crucial point in the governance of microfinance institutions, where there is a change in the status of financial institutions from private goods banks secondary to BRI) to BUMDesa, which is more reflective of a model of common ownership (commons resource property); at this time, the dialectic of thought leads to the potential emergence of social tragedy due to the use of common resource property in the community Hardin, [24]. One of the options that emerged was to give management rights to the state or private sector. This solution was then considered an unnecessary solution because the state was considered unnecessary to intervene because enough communities (villages) would be able to solve the tragedy of the commons problem (Ostrom, 1990). The debate between Hardin then split the two models of managing commons resources between the state and the community, so to end the debate between Hardin and Ostrom formulated a hybrid institutions model (German and Keller, 2010). In this case, BUMDesa, which received the assets of the former BKD and carried out two missions between sustainability and inclusiveness, which can also be categorized as a hybrid institutions model, requires an institutional model that is also mixed in style.

1.2. Institutionalisation in Public Administration

Public policy is a method of government (and public) intervention to find ways to solve problems in development, services, and empowerment and to support better development processes, services, and empowerment. Policies are efforts, methods, and approaches that promote harmony between policies and institutions that are difficult to separate, such as the two sides of a coin.

Experience shows that the failure of development, service delivery and empowerment often stems from the failure of government (and the public) to make and implement the right policies as well as neglecting institutional development that should be the foundation of the entire process of development, service delivery and empowerment The importance of institutions and policies in the administration of government by the government bureaucracy, shows that institutions are an equilibrium in making good public policy. Governance public policies are often set in the form of rules and regulations, which are key elements of an organization.

2. Methods

This study used descriptive qualitative research. This study uses qualitative descriptive research for two reasons. First, the experience of institutional change is used to find and understand what is hidden behind phenomena that are sometimes difficult to satisfactorily understand. Second, the study produces discoveries about changes in the functionalization of organizations, social activities, community life, producing descriptive data in the form of written words, and relevant books, or orally from people observed behavior and not numbers. This study examines the institutional dynamics of microfinance institutions in the Banyuwangi Regency. It presents the institutional changes of the Microcredit Agency (BKD) to Microfinance (MFI), which is incorporated as a Limited Liability Company (PT) formally supervised by the Financial Services Authority (OJK), and all assets are owned by the village government.

Third, data were collected through a series of in-depth interviews, participant and non-participant observations, and a document review. The collected data were tested for validity through a series of source triangulation, method triangulation, and time triangulation. The informants were selected using a number of criteria, including a) those who were actually involved in the transformation process and management of the management organization, b) those who did not have a tendency to exaggerate or underestimate information, c) those who were suggested by at least two previous informants, and d) those who expressed their willingness to be interviewed and were willing to take the time to do so. The tested data were then analyzed using the interactive analysis technique developed by Miles et al. [25].

3. Results and Discussion

3.1. Dynamics oFRural Microfinance Institutional Change: The Formal Context

The history of the establishment of the BKD was regulated in the Staatsblad of 1929. 357, Rijksblad of 1937 No. 9, and the 1938 No. The 3/H Ordinance dated September 14, 1929, concerning *village barns* as village credit institutions whose functions are increasingly shrinking and replaced by village banks as lending in the form of money but not optimal, so that it underwent reorganization into the Village Credit Agency (BKD) whose status as BPR with the enactment of Banking Law No. 7 of 1992, which was subsequently supervised under BRI in 1993. (Government of the Republic of Indonesia 1992). Badan Kredit Desa (BKD) is a village-owned company that operates in the village area. BKD is managed as a separate company and is separate from the other assets owned by the village concerned. In accordance with the Decree of the Board of Directors of Bank Indonesia Number:31/63/KEP/DIRR dated July 09, 1998, BRI appointed the Implementation of Guidance and Supervision of Village Credit Agencies (BKD) for the intended task. In connection with this, for the branch office level, the BRI Branch Manager automatically becomes the BKD supervisor, which is reaffirmed in Bank Indonesia Regulation Number6/27/PBI/2004 dated December 28, 2004 (Bank Indonesia, 2004) concerning the Implementation and Supervision of the Village Credit Agency (BKD) by PT Bank Rakyat Indonesia.

They made a joint decision in the field of empowering the people's economy through the supervision, guidance, and development of BKD, which needs to be intensified through the guidance and supervision of both institutional and operational finance and human resources. BKD empowerment is carried out in detail and followed by the Ministry of Home Affairs, BI, PT BRI Tbk, and Trade Unions. In accordance with the POJK No. 10/POJK.03/2016 (Financial Services Authority, 2016) regarding fulfillment of the provisions to transform BKD found in Article 10 Paragraph 1 BKD, which is based on its consideration when it cannot fulfill the provisions of BPR, it can choose to transform into business activities into PT LKM, can also become a Village-Owned Enterprise or BUM Desa business unit. In the event that OJK deems it necessary, OJK may request BKD to revise the action plan submitted by BKD, as contained in Paragraph 2, that it must submit the action plan to OJK no later than December 31, 2019. Previously, there was also a Joint Ministerial Decree of three Ministers and BI that had signaled to the BKD to clarify its legal entity as BUM Desa.

3.2. Microfinance Institutional Transformation: a Series of Challenges

BKD in the Banyuwangi Regency, as many as 63 villages can survive and transform, still survive with the various demands of institutional change, organisationally BKD works through operational guidelines issued by BRI as the parent, and as if it is a BRI unit. This is one of the reasons why BKD survived. Various forms of protection exist, such as additional capital, expansion of coverage, bad debts, conflicts with customers, and other facilities. The experience of being a BRI unit became an important factor in managing microfinance after the transfer of ownership by the village government. The BKD had to take a pivotal position in the success scenario of a transformation process that was extremely complicated and inefficient in improving services. In the context of this BKD, if observed, BUM Desa transforms *government-driven* programs into village-owned ones. Putra et al., [26]. The following is a flowchart of the Village Credit Agency (BKD) transformation process, which illustrates that there are many stages that are passed, and each stage requires coordination and communication that is not equal, meaning that BKD actors are central actors who have resources, knowledge, and management experience, while the village government does not know enough about the ins and outs of microfinance operations; thus, the government, which is positioned as the owner of the former BKD assets, takes various attitudes or decisions, triggered by the benefits that will be obtained from the transformation. Facing this conflict of interest, BKD continues to adhere to the *action plan* decision agreed upon by 66 BKD to transform into PT LKM and approved by OJK.

In response to the SKB 3 Ministerial Decree, the BRI's position as the parent bank that oversees, fosters, and supervises the BKD ignored and asks BKD to continue running the BRI scheme. Likewise, Commission 1, which was held by the village head, did not respond to the clarity of BUM Desa's legal entity, as in the second dictum that ordered BKD to transform into BUM Desa or BPR. This is similar to the demands of the OJK (Financial Services Authority) in the form of POJK No. 10 of 2016, which specifically and explicitly regulates the form of BKD's institutional transformation by choosing the form of BKD's legal entity to be BUM Desa, if it is unable to meet the requirements to become a BPR.

Almost none of the BKDs in the Banyuwangi Regency were eligible to become BPRs. Thus, the mantri swiftly saved the fund transfer assets by drafting an *action plan*, namely to become a service based on 66 village cooperation, uniformly designing an agreement with the JTU and Commission 1 to become a PT-incorporated MFI with district-level service coverage. However, when applying for a PT legal entity, it was rejected by the Ministry of Law and Human Rights because of unclear ownership. This means that the BKD cannot directly apply for a PT license. Local governments also did not respond to this demand, resulting in a deadlock. The MFI Law, POJK, and joint decree (SKB) 4 ministers do not technically mention how and who has the role of facilitating the transformation process and procedures; there is still one regulation that must be fulfilled for BUM Desa legal entity and asset ownership by the village, namely the Village Law, village ministerial regulation No. 4 of 2015, and permendesa no. 2 of 2015 on village consultation as the structure of BUM Desa institutions. **Figure** ?? **BKD transformation process flow**

3.3. Result of BKD Institotional Change to PT LKM BKD MANDIRI

The results of the institutional change of the Village Credit Agency (BKD) to PT LKM BKD Mandiri Banyuwangi, which received an official permit KEP-17/KO.043/2020 and revoked the old permit, are presented below.

Table 1: Institutional Change from BKD to LKM.

	Village Credit Agency (BKD)	PT LKM BKD Mandiri Transformation Results
Legality		Permit Number KEP.0403/2020
Form of Regulation Management	Guidance from BRI BRI Circular Letter	Village Regulation on asset transfer Joint Village Head Regulation on BKAD Joint Regulation on the Establishment of BUM Desa Village Head Decree on Village Delegation
Structure	Mantri, JTU, Commission	BUMDesma structure as owner: Supervisor: BKAD management as the village delegate Chairman, secretary, treasurer Fields Structure of PT LKM as a business unit Commissioners, Directors, Managers,
Surveillance	BRI	FSA
Ownership	Village-owned	Village-owned - Village in the form of Bumdesma business units inter-village work
Village Head Position	Commission 1	Commissioner

Source: Primary data, 2022.

3.4. Dynamics of Institutional Change and Transformation of Village Credit Agency (BKD)

In the case of BKD since its establishment in 1929, it was able to meet the demands of changing times, when it was still before the Independence of the Republic of Indonesia in 1945 until BK became a secondary bank of BRI, BKD still existed to serve the community. Since the emergence of the Financial Services Authority through POJK No. 10 of 2016, which specifically and explicitly regulates the form of BKD institutional transformation, by choosing the form of BKD legal entity to become BUM Desa, if it does not meet the requirements to become a BPR. Coupled with the emergence of the Governor's Letter No. 411.2/10419/112.3/2008. Subject: Support for the Transformation of Village Credit Agencies in East Java, which confirms that the ownership of BKD assets belongs to the village; the letter comes in response to a request from OJK. ... during the chaos and tug of war over the status of asset ownership between the village government and BKD. In the transformation stage, there was also the establishment of new institutions at the village level in the form of a village consultative decision on asset ownership and a delegation that takes care of inter-village cooperation, both inter-village consultative meetings in the form of BKAD (Inter-Village Cooperation Agency) organizations as the highest forum for determining joint business decisions, also carried out by BKD itself. In this case, it is evident that the experience and capacity of knowledge and skills at the operational level can maintain the sustainability of the microfinance business.

BKD transformation using the Bromley approach [18] which basically divides the level of a policy into three levels or three levels, namely the *policy level*, *organization level,* and *operational level* According to Bromley [18] each of these policy levels is bound by institutional arrangements, which describe the rules of the game regarding how the organization works and operates. Thus, the pattern of interaction between levels from top to bottom is always bound by institutional arrangements. Policy changes at the *policy level*, as the highest authority in policymaking, affect institutional arrangements at lower levels.

Through a complicated coordination hierarchy/bureaucratic hierarchy mechanism that does not support each other, between the OJK as the decision maker, the local government as the facilitator and regulator, the village government as the owner of the former BKD assets, and the BKD actors, the complicated internal rules of the village government, as shown in the scheme in Fig. 2. 2. As described by North, the process of institutional change cannot happen quickly, without obstacles and full twists and turns, and does not always lead to improved efficiency. The government's efforts to guide the change process are not free because any offer of institutional innovation requires substantial political resources. This was the case with deliberations held to support the BKD transformation process. To design new institutions and conflicts arising from interest groups. At this point, any institutional change requires organizing as an instrument to guide and calculate benefits and costs(Hayami & Ruttan, 1985).

The transformation of BKD into a Microfinance Institution and positioned as a BUM Desa business unit, there are several conditions in which there is no synchronization of legislation products from the *policy level* between the Village Law and the Limited Liability Company Law, so that when BKD wants to fulfill the demands of becoming a legal financial institution with a legal entity, BUM Desa is not a legal entity. During the registration process of the legal entity PT.LKM formed through the Law of the Republic of Indonesia.(Pemerintah Republik Indonesia, 2014) cannot continue the registration process. To get around this regulatory impasse, BKD chose to abide by the rules in Law No. 40 of 2007(Pemerintah Republik Indonesia, 2007) on Limited Liability Companies rather than Village Law. One of the driving factors is that the Law on Limited Liability

Companies has legal sanctions, whereas the Village Law does not. The anticipation of this regulation led to the birth of PT BUM Desa, which raised many questions regarding whether a village-owned enterprise could be transformed into a Limited Liability Company.

During the long period of implementing these demands for change, conflicts arose within the management organization in the form of *free rid*ers who took advantage of the existence of loyal customers to establish a Savings and Loan Cooperative (KSP) by the JTU and Commission 3 as marketers, who spearheaded the loans. These events are similar to those described that institutional change is the result of the struggle of various groups who hope to get a better share if it is not appropriate, then in the long run many conflicts arise. This is corroborated by Haggard and Kaufman, who found that the process of economic reform is fraught with political obstacles that are often unfriendly, one of which is whether economic reform policies that touch on public goods always cause problems for illegal riders. Therefore, there is an effort to build a collective attitude among BKD managers to save assets that will provide sustainable benefits. Similar to Bromley's conception [18], one of the sources of change is a collective attitude toward the protection of the work environment, including income distribution. The occurrence of conflict in institutional change is an unavoidable condition, as argued by Zikos [27], who states that institutional change is actually a process of conflict creation. According to Paavola, conflict emerges as a direct link to the hypothesis of a reciprocal mechanism because of circumstances in which different groups conflict over the use and protection of *natural resources*.

One of the crucial points of this institutional change is when the BKD decision turns into a Microfinance Institution and is a BUM Desa Business Unit, then the BKD changes its character into an item that is almost like a Commons *Resource (Quasy Commons Resource),* so the character of its management has also changed. *Commons Resources* itself refers to conditions where there are (1) difficulties in excluding other users from its utilization (*exclusion problems)* and (2) difficulties in equally sharing the resource or its benefits (*subtractability problems*). The existence of illicit riders by other parties and *the rivalry of extraction* leads to the over-utilization and degradation of resources Hardin, [24]. The dynamics of this change are very important, especially how to manage the *Commons Resource,* which was once the subject of a heated debate between Hardin and Ostrom. The debate on how the management of this common resource should be carried out when Hardin published his book *The Tragedy of the Commons* Hardin, [24],which puts forward the thesis that there will be a social tragedy when each individual acts selfishly in utilizing shared resources. Hardin [24] argued that social tragedy can be avoided if the government intervenes to resolve or hand over management to the private sector or the state as a manager. However, Ostrom [28] rejected this opinion and stated that the government does not need to step in to solve the problem if the management of the *Commons Pool Resource is* left to the community. Therefore, institutions need to manage and bridge private, group, or state ownership with a clear system of rules to avoid conflicts in managing *open access* common property resources Bromley, [18]. In line with Ostrom, Wade (1987) argues that local organizations can be a solution because they can accommodate the collective actions of the community rather than being regulated by the private sector or the state, which is often costly and ineffective.

What is the solution to managing the *Commons Pool Resource,* and trying to find the meeting point of the debate between Ostrom and Hardin, German and Keller then formulated a *hybrid institution.* Microfinance Institutions and BUM Desa Business Units should be managed using a *hybrid institution* mechanism. This condition is very important because after the Microfinance Institution is a BUM Desa Business Unit, the MFI can no longer be managed using a *private* management mechanism, so to avoid potential conflicts, *hybrid institutions are* needed. This is also conveyed by Meyer and Hudon, BKD, which was initially seen as *a private good,* then transformed into BUM Desa with the character of *Commons Resource* so that there was a mixture of characters between *private* and *commons,* making BKD itself a *hybrid institution*.

The end result of all the institutional dynamics and chaotic transformation of the Village Credit Agency (BKD) into the BUM Desa can be seen in the form of behavior and interaction patterns that emerge at the lowest level, namely, the operational level, because it will determine the final results or consequences that arise from the transformation of the existing rules of the game, whether it is getting better or worse. Therefore, *feedback* from the bottom is needed to evaluate the public policy choices made. In the context of the dynamics of microfinance institutional change in Indonesia, the end result of institutional change is faced with two aspects: the sustainability and inclusiveness of microfinance institutions in Indonesia.

One of the final results that can be seen from all the transformation processes of microfinance institutions is the adaptability of microfinance institutions, whether or not they can continue to exist by carrying out two missions between social missions, which refers to the existence of equal access for all communities to be served in terms of access to financial institutions. The other mission is the business mission, namely, *sustainability,* which refers to the ability of MFIs to generate profits over a long time horizon. This study finds that the institutional dynamics that occur in the transformation of microfinance institutions in Indonesia cannot be separated from the efforts to find a meeting point between the dilemma of the Sustainability or Inclusiveness mission of Microfinance Institutions. The choice to emphasize the sustainability mission will neglect the inclusiveness mission. Conversely, expanding the mission of inclusiveness will also neglect the sustainability side (*trade-off*). Therefore, placing Microfinance Institutions as *hybrid organizations is one* of the most viable solutions compared to other options, as done by Battilana and Dorado and Marconatto *et al*. In the Indonesian context, the *hybrid* model occurred when BKD was transformed into one of the BUM Desa business units. On the one hand, this change has positioned BKD as an *equilibrium institution* between its social and business missions. The *hybrid institution* model as an option for the transformation of BKD into a part of the BUM Desa from the perspective of institutional change analysis cannot be seen as the most ideal option. The maximum that can be reached is an analysis of the advantages and disadvantages of each option Yustika, [2].

After the transformation of BKD finally became one of the BUM Desa business unit MFIs, then there has been a change in character from *private goods* to *commons goods,* if seen by its character, then the BUM Desa business unit MFI has become a hybrid *organization*. Conceptually, as an institutional model that positions the BUM Desa business unit MFIs as *hybrid institutions, it* can be seen from the mission carried out between social and commercial missions and the character as *commons goods and the* potential for *tragedy of the commons,* departing from the debate between Hardin and Ostrom, the processing that can be done with the *hybrid institution* model. *The* use of this hybrid model is not without risk. The *hybrid institution* model contains several risks. According to Brandsen and Karré , some of the risks faced include *financial, cultural, and political risks.*

The use of a settlement using the *hybrid institutions model* must ultimately be seen as a *collective action* because the management of BKD involves several parties, including the village as the recipient of the 'treasure' of the former BKD, the Ministry of Villages PDTT, and the Financial Services Authority, according to Olson (2003). According to Olson (2003), the existence of *hybrid institutions* as *cooperative solutions* and the success of BKD management in BUM Desa are largely determined by several important determinants for the success of a joint action, namely *size, homogeneity,* and the *purpose* of the *group*. Hypothetically, the larger the group, the more difficult it will be for the organization to work effectively; conversely, the smaller it is, the more likely it is to work effectively. Next, is related to *homogeneity* (*homogeneity*), the diversity of interests of group members involved in BKD management, and the more complicated the formulation of a collective agreement because they will bring their own interests.

The third was the *purpose of the group*. The broader the goal to be addressed, the more blurred the goal to be achieved, and this condition leads to the fragmentation of the common goal to be addressed.

One of the characteristics of the hybrid institutional model is the presence of community and state representation. In the context of BUM Desa management, it is necessary to clarify who represents the state and community. This is because of the specific existence of the village as a community and the village as the lowest unit of government. Therefore, it is good to see an important definition of the village based on the Village Law below, Article 1 number 1 reads:

"Villages are villages and customary villages or referred to by other norms, hereinafter referred to as Villages, are legal community units that have territorial boundaries that are authorized to regulate and manage government affairs, the interests of the local community based on community initiatives, origin rights, and/or traditional rights that are recognised and respected in the system of government of the Unitary State of the Republic of Indonesia." (Pemerintah Republik Indonesia, 2014).

Based on the above definition, it is quite clear that the village is a representation of the community or legal society, not part of the local government, because it does not contain elements of the community, but a bureaucratic apparatus Putra et al., [24]. Therefore, in the context of the *hybrid* model of *the institution*, the village is positioned as a community, while the state institution in this case is represented by the Ministry of Villages PDTT Putra et al., [26]. In addition, the position of the village in Article 5 of Law No. 6/2014 on Villages states that the village is a community-based government organization (*self-governing community*) and (*local self-government*) whose position is within the Regency/city area, but not subordinate to the regency/city. The village is referred to as a community-based government (*self-governing community)* and (*local self-government*) whose existence is related to the daily life of the community Putra et al., [26].

From the *communitarian view,* community groups represent social capital that exists in society (Woolcock, 1998). Handing over the management of financial institutions, such as MFIs, is certainly very risky, and the three risks inherent in the *hybrid institutions* model include *financial, cultural, and political.* Learning from the success of BKD, which is able to exist by relying solely on guidance and guidance from BRI, in the management of BKD after the transformation into BUM Desa, a supervisory body is needed, in this case the Financial Services Authority (OJK) as an independent official specific institution in the financial services sector to be able to technically guide the implementation of post-transformation BKD management.

The management of MFIs cannot be equated with the management of natural resources such as ponds, pastures, and forests, such as *open access.* Microfinance Institutions (MFIs) in BUM Desa already have a management model and regulatory system inherited from BKD that will regulate the governance of MFIs so that not all parties can exploit MFIs. However, there is still a risk of conflict, or utilization of the Microfinance Institution (MFI) by certain groups in the village, which will hamper the inclusiveness of the Microfinance Institution (MFI). This potential institutional risk arises from the fact that the pattern of interaction between the village, village administration, and village head has not been clearly defined. This is crucial, as the pattern of interaction determines how MFIs are managed in practice. In some cases, the Village Head often shows that he/she is representative of the village itself, and the presence of the Financial Services Authority is needed to provide certainty about governance based on the correct financial system.

The existence of the Financial Services Authority, communities, and villages is expected to synergize by considering local cultural aspects so that hybridization can be realized. According to Ostrom [28], the community is an institutional mechanism that can reduce government intervention in local cultures. According to Ostrom [28], the community is an institutional mechanism that can reduce government intervention in the management of shared resources. The Financial Services Authority is not needed if it is only to standardize the technicalities of how MFIs operate. Moreover, economic institutional change, such as the transformation of BKD into BUM Desa, is usually very specific. This means that this kind of institutional transformation process is good and suitable for MFIs but may not be suitable for other business units. The recognition of *local wisdom in the* community is needed. Local mechanisms such as payments following the harvest cycle for farming communities in Java or bi-weekly payments for plantation communities can provide flexibility in managing services to the community based on *local* property. According to Hess and Ostrom [28], local communities have *local knowledge* that they use as communal guides to manage the common resources that they own for generations.

Institutional design based on the structure or hierarchy of society, both the structure of values and social structure, is one part of the implementation of the principle of recognition and the principle of subarity towards the village, where there is recognition of the authority of the village's right of origin (Putra et al., [26]. Therefore, the adaptation of values so that the absorption of the social system provides good performance, usually in preventing bad credit. The uniformity of the procedures offered by OJK will trap MFIs in the problem of bad debts Yustika, [2], and the existence of the Financial Services

Authority is still needed as a specific authority institution that has a psychological impact on the existence of Microfinance Institutions in BUM Desa, which is a form of village economic business that is collective between the village government and the village community. OJK also needs to recognize and respect the village, meaning that actions are needed to utilize, support, and strengthen village institutions, rather than emphasizing intervention and coercion toward MFIs.

4. Conclusion

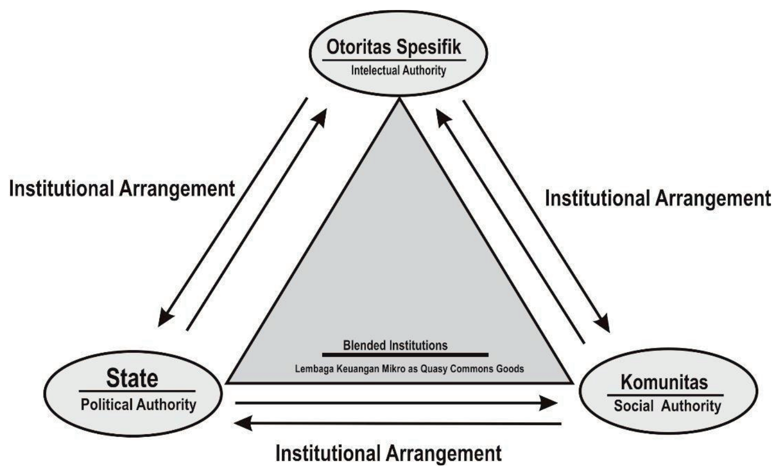
Institutional change from the Village Credit Agency (BKD) to PT LKM BKD is a form of public policy contained in regulations that reflect the clarity of asset ownership (capital) as well as regulations and official supervision by the financial services authority (OJK). The presence of new agreements at the local level is signaled by the issuance of local village regulations. The formation of a new organizational structure as a result of the transformation and coordination between parties also creates new arrangements. Not to mention the arrangements that arise from internal business units and actors. It is necessary to understand the dynamics of institutional change that produce new institutions. Every process of establishing new institutions creates incentives and is not always effective. The change of microfinance institutions from Badan Kredit Desa (BKD) to PT LKM Mandiri is seen as a government design in the form of legislation. This can be categorized as a public administration paradigm that leads to the formation of many uniform rules.

The transformation process is fraught with inhospitable political obstacles and is vulnerable to the threat of illicit riders, especially those dealing with public goods. If illicit riders control more profits, then the transformation has the potential to fail. Another classic problem is that the costs of transformation are usually borne by one group, and many benefits are enjoyed. Therefore, its success depends on the strength of the resistance of the groups that are most affected by transformation.

This study is limited to an analysis of the dynamics and responses to institutional change but does not provide a comprehensive picture of the impact on the performance of the managing organization. Owing to these limitations, this study suggests the need for further research by focusing on aspects of the impact on organizational performance in realizing inclusive finance.

POLICY RECOMMENDATIONS AND THEORETICAL CONTRIBUTIONS OF THE RESEARCH

Based on the results of this research, in addition to the Village Government as part of the state authority at the lowest level, there is also a specific authority that has professional management *expertise* so that researchers propose a management model called **Blended Institutions***, in terms of* characteristics: **Blended Institutions are** similar to *hybrid institutions,* but there is development with the addition of a specific authority, in this case the OJK, which needs to be added as an intellectual guardian of MFI management. If *hybrid institutions* only bring together the state, namely the Ministry of Villages and PDTT with the Village, then Blended *Institutions* include a specific authority, namely OJK. In the context of MFI management as *quasi-commons goods, the* presence of the Village as Community Representation, the presence of the government through the Ministry of Village, and PDTT requires an institution that has specific authority in financial services governance. **Blended Institutions** are middle-ground institutions that are believed to provide a compromise on the management of Microfinance Institutions in Indonesia because they provide space for village community empowerment (*pro-poor oriented*) by utilizing village productive assets (*profit-oriented*) within the institutional corridor. Why **Blended Institutions** instead of *Hybrid* **Institutions***?* Based on the theoretical construction used in this study, **Blended Institutions are** considered a *New Equilibrium* between interacting groups. Individual communities are one side that has their own interests, especially the poor in rural areas as the party that needs capital; the government, either as administrative officers or political officials at all levels of government, have a preference for public power so that they are considered in the design of formal institutions of interaction between the two in the management of shared resources such as MFIs.



Source: Developed by Researcher

Figure 2: *Blended Institution* Conceptual Model.

What exactly are CPRs? These resources have two main characteristics: (1) the difficulty of excluding other users from their utilization (*exclusion problems)*, and (2) the difficulty of equally sharing the resource or its benefits (subtractability problems). *Free-riding* on the efforts of others and *the rivalry of extraction* lead to over-utilization and resource degradation.

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