

# Now and Forward: Customer Deposit Insurance of Sharia Bank in Indonesia

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## Abstract

Sharia banking's characteristic, which underpins its activities on sharia principles, requires a customer protection mechanism in accordance with its characteristics, including customer deposit insurance. This study aims to determine the readiness of sharia banking regulations on customer deposit insurance in Indonesia to strengthen the protection mechanism for Sharia Banking Customers. This article is a normative juridical research that applies an analytical descriptive approach. The insurance for customer deposits of sharia bank in Indonesia is regulated explicitly in the Regulation of Deposit Insurance Corporation No. 1 of 2020 concerning the Implementation of Sharia Bank Deposit Insurance and Resolution. The regulation determines that deposit insurance must be carried out through a kafalah contract between the Deposit Insurance Corporation and the Customer. However, it does not yet provide a specific arrangement regarding the protection of deposits on social funds in sharia banking. In the future, it is necessary to have regulations related to deposit insurance for social funds in sharia banking in implementing the social functions of sharia banking, especially as Sharia Financial Institutions-Recipients of Money Waqf and arrangement of Money Waqf Nazhir.

## 1. INTRODUCTION

Sharia banking, as part of the sharia economic system, underpins its activities on Sharia principles which contain the values of justice, expediency, balance, and universality (*rahmatan lil'alam*). In Islamic economics, *rahmatan lil'alam* philosophically is defined as a carrier of mercy to the universe which is manifested by implementing social interests such as endowments.<sup>1</sup> The position of *rahmatan lil'alam* in Islamic economics is very fundamental in order to create a just life and reduce social inequalities in human life.<sup>2</sup> Provisions in the *Qur'an* also regulate

<sup>1</sup> Hisam Ahyani, Memet Slamet, and Tobroni, "Building the Values of Rahmatan Lil'Alamin for Indonesian Economic Development at 4.0 Era from the Perspective of Philosophy and Islamic Economic Law," *al-ikhram: Jurnal Hukum dan Pranata Sosial* 16, no. 1 (2021): 112.

<sup>2</sup> *Ibid.*

economic, financial, constitutional and commercial issues that fall within the scope of the highest goal of Islamic law (*maqashid*).<sup>3</sup>

These values are also applied in Indonesia through the establishment of Law No. 21 of 2008 concerning Sharia Banking (Sharia Banking Law), which has specifically regulated sharia banking since its promulgation, including after the its amendment in 2023 through Law No. 4 of 2023 concerning the Development and Reinforcement of the Financial Sector (Development and Reinforcement of the Financial Sector Law). This law is omnibus in the financial services sector which amends not only the Sharia Banking Law but also other laws in the financial sector that regulates the Financial Services Authority Bank Indonesia, Deposit Insurance Corporation, and capital market.

One of the essential changes in this law is related to the social function of sharia banking in managing money *waqf*. Initially, the position of sharia banking was only as a Sharia Financial Institution - Recipient of Money *Waqf* (LKS-PWU), which has the task of receiving money *waqf* deposits from the *Wakif*, which is then handed over and managed by *Nazhir*. After the amendment of the Sharia Banking Law, the position of Sharia banking is not only as an LKS-PWU but can also act as *Nazhir* who directly manages money *waqf* funds collected from the public. Referring to the provisions of *waqf* legislation in Indonesia, the money *waqf* must be submitted through LKS-PWU.<sup>4</sup> LKS-PWU only acts as money *waqf* recipient, issues a money *waqf* certificate, places the money *waqf* into savings based on a *wadi'ah* contract on behalf of *nazhir*, while managing the money *waqf* is *nazhir's* responsibility.<sup>5</sup>

The position of Sharia banking in carrying out its social functions has an impact on its deposit products which do not only come from general public funds but also come from social funds collected from the public. The public entrusts these funds to Sharia banking and must be protected. Applying Islamic economic values in Sharia banking operations can help maintain the bank's soundness level, which significantly impacts protecting customer funds. Moreover, good banking performance has a significant impact on increasing investment and capital stock,<sup>6</sup> so that the position of the bank as a wheel of the economy can be realized.

Historically, the concept of Islamic banking had spread widely in Indonesia since the beginning of the 1990s when Bank Muamalat Indonesia became the first commercial bank that adopted Islamic principles.<sup>7</sup>

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<sup>3</sup> Sami Al-Daghistani, *The Making of Islamic Economic Thought* (Cambridge: Cambridge University Press, 2021), 130-131.

<sup>4</sup> Nun Harrieti and Lastuti Abubakar, "The Urgent Need for the Establishment of Waqf Bank: The Case of Indonesia," *Hamdard Islamicus* 43 (2020): 868.

<sup>5</sup> *Ibid.*, 865 and 867.

<sup>6</sup> Mohammed Ayoub Ledhem and Mohammed Mekidiche, "Economic Growth and Financial Performance of Islamic Banks: a CAMELS approach," *Islamic Economic Studies* 28, no. 1 (2020): 49.

<sup>7</sup> See Shahyb Handyanto, Monita Astuti, and Kevin Ajiputra, "Indonesia Sharia Bank Merger Process Reviewed from Business Competition Laws," *Lex Scientia Law Review* 5, no. 1 (2021): 46, 51; and Nur Hidayah, Moch. Bukhori Muslim, and Abdul Azis, "Complying with Sharia while Exempting from Value-Added Tax: Murābahah in Indonesian Islamic Banks," *Ahkam* 22, no. 1 (2022): 65.

Currently, Indonesia applies two banking systems, i.e., conventional banking and sharia banking.<sup>8</sup> While Law No. 7 of 1992 concerning Banking and its amendments do not provide a definition related to conventional banks, the Development and Reinforcement of the Financial Sector Law states that commercial banks are banks that carry out business activities conventionally and/or based on sharia principles which within their activities provides services regarding payment traffic.<sup>9</sup> Sharia banking as part of the national banking system requires regulatory readiness support according to its characteristics. Previous research found that regulatory variables have a very significant positive impact on the performance of sharia banks in the Asian region.<sup>10</sup> Sharia banking has specificity compared to conventional banking, so that regulations separation between conventional banking and sharia banking is the appropriate and forward step to advance development and improve people's welfare. The particular main thing is the principle in carrying out its business activities. Conventional banking underpins its activities on conventional economic principles, while sharia banking underpins its activities on sharia economic principles or sharia principles.

The sharia principle in banking activities is based on a fatwa issued by an institution that has the authority to issue fatwas in the sharia sector, namely the National Sharia Council (*Dewan Nasional Syariah/DSN*) under the Indonesian Ulama Council (*Majelis Ulama Indonesia/MUI*). The OJK as a regulator in the banking sector (including sharia banking) has an obligation to ensure that the provisions contained in the DSN-MUI fatwa can be transformed into formulations of legislation that have a legal force and are generally binding.<sup>11</sup> The fatwas issued by the DSN-MUI serve as a reference for the OJK in issuing regulations in the sector of sharia economics including in the regulation of sharia banking.

As an act that regulates specifically sharia banking, this act regulates the issue of sharia compliance, whose authority lies with the MUI, which is represented through the Sharia Supervisory Board (*Dewan Pengawas Syariah/DPS*), which must be established at each Sharia Bank and Sharia Business Unit (*Unit Usaha Syariah/UUS*). The duties of the DPS are to provide advice and suggestions to the directors as well as supervise the bank's activities to comply with sharia principles. In other words, the DPS's primary obligation is to strictly supervise the application of sharia principle within all sharia banking activities.<sup>12</sup> Non-compliance by sharia banks in

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<sup>8</sup> Nunung Ghoniyah and Sri Hartono, "How Islamic and Conventional Bank in Indonesia Contributing Sustainable Development Goals Achievement," *Cogent Economics & Finance* 8, no. 1 (2020): 2.

<sup>9</sup> Law No. 4 of 2023 concerning the Development and Reinforcement of the Financial Sector, Art. 14.

<sup>10</sup> Nafis Alam, Sara Sophia Binti Zainuddin and Syed Aun R. Rizvi, "Ramifications of Varying Banking Regulations on Performance of Islamic Banks," *Borsa Istanbul Review* 19, no. 1 (2019): 49.

<sup>11</sup> Nun Harrieti, "The Use of Hybrid Contract in the Innovation of Islamic Banking Product," *Hasanuddin Law Review* 4, no. 1 (2018): 72.

<sup>12</sup> Niji Mansour Nomran and Razali Haron, "A Systematic Literature Review on Shari'ah Governance Mechanism and Firm Performance in Islamic Banking," *Islamic Economic Studies* 27, no. 2 (2020): 92.

implementing sharia principles can erode their reputation and affect their financial resilience.<sup>13</sup> Sharia compliance as a priority for sharia banking including ethical and social issues as a measure to attract depositors to place their money in sharia banking.<sup>14</sup>

The specificity of sharia banking is also reflected in the legal relationship between it and its customers. The legal relationship will have different juridical consequences depending on the type of contract agreed between sharia banking and its customers. Contracts used in sharia banking fundraising products in Indonesia are *wadi'ah* and *mudharabah*.<sup>15</sup> For example, in deposit products, the applicable principles in the form of savings are *mudharabah* and *wadi'ah* as specified in the DSN MUI Fatwa No. 02/DSN-MUI/IV/2000 concerning Savings.<sup>16</sup> In the codification of standard products and activities of sharia commercial banks and sharia business units issued by the OJK, it is determined that the contract used in savings products is a *wadi'ah* contract for savings.

The juridical consequences of the contract affect the rights and obligations of each party, both sharia banking customers and sharia banking itself, including the customer deposit insurance mechanism. Deposit insurance is a legally established and explicitly recognized system to protect certain deposit categories. The categories are placing funds in a bank within a specified maximum amount and the occurrence of a bank failure.<sup>17</sup> Islamic deposit insurance is defined as a system established with the Shariah-compliant design features to protect depositors against the loss of their insured Islamic deposits in the event that an Islamic bank is unable to meet its obligations to the depositors.<sup>18</sup>

The institution that insurances customer deposits in Indonesia is LPS which was formed under Law No. 24 of 2004 concerning Deposit Insurance Corporation (LPS Law).<sup>19</sup> As of April 2023, total deposits at commercial banks and sharia commercial banks in Indonesia have reached 511.66 million accounts. Most of which are savings which cover 97.9% of the total savings account and the largest nominal deposits were in the types of

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<sup>13</sup> Abderazak Bakhouché, Teheni El Ghak, and Mohammad Alsihab, "Does Islamicity Matter for the Stability of Islamic Banks in Dual Banking System," *Heliyon* 8, (2022): 4.

<sup>14</sup> Keria Kontot, Jamil Hamali, and Firdaus Abdullah, "Determining Factors of Customers' Preferences: A Case of Deposit Products in Islamic Banking," *Procedia Social and Behavioral Sciences* 224 (2016): 173.

<sup>15</sup> Regarding *mudharabah*, see Azharsyah Ibrahim and Abdul Jalil Salam, "A Comparative Analysis of DSN-MUI Fatwas regarding Murabahah Contract and the Real Context Application (A study at Islamic Banking in Aceh)," *Samarah: Jurnal Hukum Keluarga dan Hukum Islam* 5, no. 1 (2021): 379, 387.

<sup>16</sup> DSN-MUI Fatwa No. 02/DSN-MUI/IV/2000 concerning Savings, para. I.2.

<sup>17</sup> Djurdjica Ognjenovic, *Deposit Insurance Schemes* (Switzerland: Springer Nature, 2017), 2.

<sup>18</sup> Islamic Financial Services Board and International Association of Deposit Insurers, "Core Principles for Effective Islamic Deposit Insurance System," [https://www.iadi.org/en/assets/File/Core%20Principles/IADI-IFSB%20CPIDIS\\_IFSB%20Approved\\_05%20July%202021%20Clean.pdf](https://www.iadi.org/en/assets/File/Core%20Principles/IADI-IFSB%20CPIDIS_IFSB%20Approved_05%20July%202021%20Clean.pdf), 11.

<sup>19</sup> This Law was lastly amended by Law No. 4 of 2023 concerning Development and Reinforcement of the Financial Sector.

deposits which accounted for 36.7% of total deposits.<sup>20</sup> The LPS Law was formed several years before the enactment of the Sharia Banking Act, the only sharia-related Article in the LPS Law is related to the implementation of the LPS function in insure customer deposits and participate actively in maintaining the stability of the banking system according to their authority for sharia banks which is mandated to be further determined in government regulation.

In 2020, LPS stipulated a Regulation No. 1 of 2020 on the Implementation of Sharia Bank Deposit Insurance and Resolution (PLPS 1/2020).<sup>21</sup> The stipulation of the regulation was motivated by the regulation of the implementation of deposit insurance and bank resolutions regulated in the PLPS concerning the deposit insurance program, treatment of systemic banks experiencing solvency problems, solution of banks other than systemic banks experiencing solvency, and bank liquidation, still not fully accommodate the implementation of insurances and resolutions with sharia principles.<sup>22</sup> Given the specifics and characteristics of sharia banking, it is necessary to carry out research on the readiness of regulation on deposit insurance to strengthen the protection for sharia banking customers in Indonesia.

According to Sjafrudin (2020), countries' application of a deposit insurance system generally aims to achieve financial stability.<sup>23</sup> As revealed by Adema, Hainz, and Rhode (2019), the United States of America and Germany are the first countries to introduce deposit insurance system in 1933 and 1934 and subsequently continued by many countries to anticipate a banking crisis and to support the national financial stability and banking system.<sup>24</sup> Baehaqi, Fahmi, and Beik (2017) found that the application of the deposit insurance scheme has an impact by increasing the level of bank deposit.<sup>25</sup> It, therefore, has a significant influence against the implementation of the Islamic Banking intermediation function, which as a driving force for the economy. In addition, research conducted by Aysan et al (2017) found that the deposit insurance reform has increased the market discipline in the Turkish Islamic banking sector.<sup>26</sup> In the period when Islamic deposit insurance was introduced and compared with their conventional peers, the sensitivity of Islamic depositors to bank risk was

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<sup>20</sup> Indonesia Deposit Insurance Corporation, "Deposit Distribution of Commercial Banks April 2023," [https://www.lps.go.id/documents/10157/197446/Distribusi+Simpanan+Bank+Umum+April+2023\\_Rev.pdf/074bbc3e-ae81-430a-a539-80eab1a1f784](https://www.lps.go.id/documents/10157/197446/Distribusi+Simpanan+Bank+Umum+April+2023_Rev.pdf/074bbc3e-ae81-430a-a539-80eab1a1f784), 4.

<sup>21</sup> See considering part of Regulation of Deposit Insurance Corporation No. 1 of 2020 concerning the Implementation of Sharia Bank Deposit Insurance and Resolution

<sup>22</sup> *Ibid.*

<sup>23</sup> Sjafruddin, "Penerapan Coverage Limit Sistem Penjaminan Simpanan Pada Perbankan Syariah di Indonesia" (Master Thesis, Faculty of Economy and Business Universitas Islam Negeri Sunan Kalijaga Yogyakarta, 2020), 1.

<sup>24</sup> Joop Adema, Christa Hainz, and Carla Rhode, "Deposit Insurance: System Design and Implementation Across Countries," *Ifo DICE Reports* 17, no. 1 (2019): 43.

<sup>25</sup> Sofyan Baehaqi, Idqan Fahmi, and Irfan Syauqi Beik, "Determining Factors of Deposit Level of Islamic Bank in Indonesia," *Al-Iqtishad* 9, no. 2 (2017): 213.

<sup>26</sup> Ahmet Faruk Aysan et al, "Islamic Banks, Deposit Insurance Reform, and Market Discipline: Evidence from a Natural Framework," *Journal Finance Service Research* 51 no. 2 (2017): 258.

annihilated.<sup>27</sup> Further, Supriyatni and Nurjamil (2021) the urgency of handling non-performing financing in sharia banks in the development of Indonesian found that non-performing financing has an impact on the banking system, the health of the bank and national economy, at a certain level it causes losses and bankruptcy.<sup>28</sup>

Differs from the above studies, this research analyses the readiness of regulations on sharia banking deposit insurance in Indonesia to strengthen sharia banking customer protection. This article is a normative juridical research that applies an analytical descriptive approach. It focuses on research on secondary data consisting of primary, secondary, and tertiary legal substances that reflect a positivist character of legal studies and.<sup>29</sup> The analysis on legal theories represents a distinctive approach to conceptual issues.<sup>30</sup>

## 2. RESULT AND ANALYSIS

### 2.1. The Implementation of Sharia Banking Principles in Indonesia

Sharia banking concerns both sharia banks and UUS, including institutions, business activities, methods, and processes in carrying out their business activities. Sharia bank is a business entity that collects funds from the public in the form of savings and investments and distributes them back to the public through financing, which bases all of its business activities based on sharia principles to improve the standard of living of the people. Sharia banks must carry out both Intermediation and social functions to support the implementation of national development to increase justice, togetherness, and equity of people's welfare. The intermediation function of sharia banks, in particular, upholds the sharia principles and refers to the fatwa issued by the DSN-MUI.

Sharia banking applies social ethics that are inspired by sharia principles.<sup>31</sup> In carrying out business activities, sharia banking adheres to sharia principles as a whole (*kaffah*) and is consistent (*istiqomah*), which lead to a sharia compliance towards public accountability:<sup>32</sup>

1. *usury*, illegal addition of income (*batil*), i.e., exchange of similar goods that are not of the same quality, quantity, and time of delivery (*fadhil*) or in lending and borrowing transactions that require the facility recipient customer return the funds received more than the loan principal due to the passage of time (*nasi'ah*);

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<sup>27</sup> *Ibid.*, 279.

<sup>28</sup> Renny Supriyatni and Nurjamil, "The Urgency of Handling Non-Performing Financing in Sharia Banks in the Development of Indonesian Sharia Economics," *Padjadjaran Journal of Law* 8, no. 1 (2021): 29.

<sup>29</sup> See Theresia Anita Christiani, "Normative and Empirical Research Methods: Their Usefulness and Relevance in Study of Law as an Object," *Procedia Social and Behavioral Science* 219, (2015): 205; and Pradeep M.D., "Legal Research-Descriptive Analysis on Doctrinal Methodology," *International Journal of Management, Technology, and Social Sciences (IJMTS)* 4, no. 2 (2019): 97.

<sup>30</sup> See Matyas Bodig, *Legal Doctrinal Scholarship* (Cheltenham: Edward Elgar Publishing Limited, 2021), 13.

<sup>31</sup> Ishaq Ahmad et al, "Objectives of Islamic Banks: a Massive From Mission Statements and Stakeholders' Perceptions," *Journal of Islamic Accounting and Business Research* 8, no. 3 (2017): 289.

<sup>32</sup> Law No. 21 of 2008 concerning Sharia Banking (Sharia Banking Law), Art. 2.

2. *maisir*, transactions that are dependent on an uncertain situation and are chancy;
3. *gharar*, transactions with an unclear, not owned, and unknown object, or cannot be submitted at the time the transaction is made unless otherwise regulated in sharia;
4. *haram*, transaction in which the object is prohibited in sharia; or
5. *zalim*, transactions that cause injustice to the other party.

Sharia economic activity that contains the values of justice, togetherness, equity, and benefit are in line with the principles of economic democracy.<sup>33</sup> Meanwhile, the precautionary principle is a guideline for managing a bank that must be adhered to in order to create a healthy, strong and efficient banking system in accordance with statutory provisions.<sup>34</sup>

In practice, disputes still occurred within the sharia banking sector, mainly due to defaults from debtors. This can be seen from the decisions of the Situbondo Religious Court in 2017 and Tasikmalaya Religious Court in 2020, in which the sharia banks claimed compensation for defaults committed by customers. Therefore, banks should always adhere to banking principles to carry out their functions optimally and at the same time prevent the potency of disputes.

The Sharia Bank Intermediation function is carried out by collecting funds from the public through Savings and Investment products and then channeling these funds back to people through financing products. Through this intermediary function, Sharia banking can connect people who experience a surplus of funds with those who experience a lack of funds. People who experience a surplus of funds place their funds in savings and investment products in sharia banking. Sharia banking then channels these funds to people who need more funds through financing products. Through this intermediation function, sharia banking can turn the wheels of the economy, so it also acts as the economy's lifeblood. Implementing such a function requires public trust.<sup>35</sup>

Both conventional banking and Sharia banking are mandated to perform the intermediation function. However, applying sharia principles to sharia banking causes the intermediary function to have its own characteristics that are different from conventional banking. Table 1 below provides a comparison of the intermediation function in Sharia banking and conventional banking:

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<sup>33</sup> *Ibid.*, Explanation of Art. 2.

<sup>34</sup> *Ibid.*

<sup>35</sup> Samreen Ashraf, Yasmin Sekhon, and Julie Robson, "Consumer Trust and Confidence in the Compliance of Islamic Banks," *Journal of Financial Services Marketing* 20, no. 2 (2015): 2.

**Table 1. Intermediation Functions Comparison of Sharia Banking and Conventional Banking**

<b>Comparison Element</b>	<b>Sharia Banking</b>	<b>Conventional Banking</b>
Principle	Sharia principles, economic democracy, and the principle of prudence	Economic democracy and the precautionary principle
Customer	Deposit Customer, Investor Customer, Facility Recipient Customer	Debtor Customer, Creditor Customer
Fundraising	Through Savings and Investment Products that are free from elements of <i>usury, haram, gharar, maisir</i> , and injustice	Through savings products with an interest system
Fund distribution	Through Savings and Investment Products that are free from elements of <i>usury, haram, gharar, maisir</i> , and injustice	Through Credit with Interest system

Source: abstracted from various sources<sup>36</sup>

Table 1 describes that sharia principle becomes the differentiator between sharia banking and conventional banking. The principle limits the intermediation function of sharia banking free from elements of *usury, haram, gharar, maisir* and injustice, while conventional banking implements an interest system. Customers who place their funds in Sharia banking are divided into 2 (two), namely Depositing Customers and Investor Customers. It depends on the purpose of the placement of funds conducted by the customer. Depositing Customers are customers who place their funds in a Sharia bank and/or UUS in the form of Deposits based on an agreement between the Sharia Bank or UUS and the customer concerned. The contract used in savings products in Sharia banking is the *wadi'ah* contract, for example Current Accounts and Savings based on *wadi'ah* contracts. A *wadi'ah* contract is a contract used in sharia bank deposit products in the form of a deposit between the owner of the fund and the recipient of the deposit who is entrusted to maintain it.<sup>37</sup> Based on *mudharabah* contract, the customers in investment deposits act as *rabbul mal* who seek investment opportunities through a bank that acts as *mudharib* or fund manager.<sup>38</sup>

<sup>36</sup> See Sharia Banking Law, Arts. 1, 2, 3 and Law No. 7 of 1992 concerning Banking (Banking Law).

<sup>37</sup> See Sharia Banking Law, Art. 1 (20), (21), (22).

<sup>38</sup> Sri Rahayu Hijrah Hati, Sigit Sulistiyo Wibowo, and Anya Safira, "The Antecedents of Muslim Customers' Intention to Invest in an Islamic Bank's Term Deposits: Evidence From a Muslim Majority Country," *Journal of Islamic Marketing* 12, no. 7 (2021): 1363.

## 2.2. Readiness of Sharia Banking Customer Deposit Insurance Regulations in Indonesia

The Sharia Banking Law creates legal definitions regarding savings, current accounts, and time deposits. Savings are defined as deposits based on a *wadi'ah* contract or investment funds based on a *mudharabah* contract or other contracts that do not conflict with Sharia Principles. Its withdrawal can only be made according to specific agreed terms and conditions but cannot be withdrawn by cheque, transfer form (*bilyet giro*), and/or another equivalent instrument.<sup>39</sup> Current accounts are deposits based on *wadi'ah* contracts or other contracts that do not conflict with the Sharia Principles, which can be withdrawn at any time using cheques, transfer form, other means of payment orders, or by book-entry orders.<sup>40</sup> Time Deposit is an investment of funds based on a *mudharabah* contract or other contracts that do not conflict with the Sharia Principles, the withdrawal of which can only be made at a particular time based on an agreement between the depositing customer and the sharia bank and/or UUS.<sup>41</sup>

The difference in the agreement agreed between sharia banking, depositing customers, and investor customers generate a different juridical consequence for the parties, depending on the type of contract. Savings, current accounts, and time deposits that are based on interest calculation are not justified by sharia. They are only justified if based on the *mudharabah* and *wadi'ah* principle.<sup>42</sup> General Provisions for fatwa DSN-MUI Fatwa No. 01/DSN-MUI/IV/2000 and DSN-MUI No. 02/DSN-MUI/IV/2000 concerning Savings stipulates that savings and current accounts based on *wadi'ah* are entrusted which can be taken at any time (on call) based on an agreement with no compensation required, except in the form of *athaya*, a voluntary gift, from a sharia bank.<sup>43</sup> *Wadi'ah* is included in the *tabarru* contract<sup>44</sup> which is intended for the purpose of helping each other, while deposits are not allowed to based on *wadi'ah* contracts because deposits are included in the type of investment included in the *tijarah* contract which in this case is in the form of a *mudharabah* contract.

Based on *mudharabah*, savings, current accounts, and time deposits are a form of investment in which the investor customer acts as *shahibul mal*, the owner of the funds, and the sharia bank acts as *mudharib*, the fund manager.<sup>45</sup> Sharia banks in their capacity as *mudharib* can carry out

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<sup>39</sup> Sharia Banking Law, Art. 1 (21).

<sup>40</sup> *Ibid.*, Art. 1 (22).

<sup>41</sup> *Ibid.*, Art. 1 (23).

<sup>42</sup> See DSN-MUI Fatwa No. 02/DSN-MUI/IV/2000 concerning Savings, paras. I.1 and I.2; DSN-MUI Fatwa No. 01/DSN-MUI/IV/2000 concerning Giro, paras. I.1 and I.2; DSN-MUI Fatwa No. 03/DSN-MUI/IV/2000 concerning Deposit, paras. I.1 and I.2.

<sup>43</sup> DSN-MUI Fatwa No. 02/DSN-MUI/IV/2000 concerning Savings paras. III.1, III.2, and III.3.

<sup>44</sup> *Tabarru* contract means an agreement on non-profit transaction. See Jamal Abdul Aziz and Uus Uswatusolihah, "The Dichotomy Between Tabarru' and Mu'awadah Contracts: Perspective of Indonesia Law of Obligation," *Al-Manahij* 16, no. 1 (2022): 103.

<sup>45</sup> Hidayah, Muslim, and Azis, *loc.cit.*

various kinds of businesses that do not conflict with sharia principles and develop them as well, including *mudharabah* with other parties. Capital must be stated in the amount in cash and not accounts receivable, while profit sharing must be stated in the form of a ratio and the account opening contract. The bank covers the operational costs of the savings as a *mudharib* using the profit ratio to which it is entitled. Banks are not allowed to reduce a customer's profit ratio without the approval of the person concerned. The relationship between the investor and the bank is based on the principle of profit and loss sharing, which is considered the cornerstone of sharia banking intermediation.<sup>46</sup> The application of the profit and loss sharing mechanism starts with a deposit investment which is considered a form of equity investment with a limited duration.<sup>47</sup>

In principle, the general provisions for Savings, Current Accounts, and Time Deposits are based on *mudharabah* in the DSN-MUI Fatwa No. 01/DSN-MUI/IV/2000 concerning Giro,<sup>48</sup> DSN-MUI Fatwa No. 02/DSN-MUI/IV/2000 concerning Savings<sup>49</sup> and DSN-MUI Fatwa No. 03/DSN-MUI/IV/2000 concerning Time Deposits<sup>50</sup> is the same because the contract is also the same, the only difference is in terms of the characteristics of savings, current accounts, and time deposits themselves, where savings which can be withdrawn directly and at any time, demand deposits which are withdrawn using cheque, transfer form, other means of payment orders, or by book-entry, and time deposits which can only be withdrawn at a certain time agreed between the sharia bank and the customer.

Apart from the intermediation function, sharia banking also performs a social function. Article 4 of the Sharia Banking Law stipulates that Sharia Banks can carry out social functions in the form of *baitul maal* institutions, namely receiving funds from *zakat*, *infaq*, alms, grants or other social funds and channeling them to *zakat* management organizations.<sup>51</sup> Sharia Banks and UUS can collect social funds originating from cash *waqf* and distribute them to the *waqf* manager (*nazhir*) according to the will of the *waqf* provider (*wakif*). In this case, the sharia bank acts as a Sharia Financial Institution-Recipient of Cash Waqf (LKS-PWU), which receives cash *waqf* funds and places it into a savings account based on the *wadi'ah* principle on behalf of *nazhir*. After the enactment of the Development and Reinforcement of the Financial Sector Law, Sharia Banks act not only as LKS-PWU, but also as *Nazhir* who directly manage money *waqf* funds. The social function as one of the uniqueness of sharia banking should be seen as the selling point

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<sup>46</sup> Hichem Hamza, "Does Investment Deposit Return in Islamic Banks Reflect PLS Principle?," *Borsa Istanbul Review* 16, no. 1 (2016): 32.

<sup>47</sup> *Ibid.*

<sup>48</sup> DSN-MUI Fatwa No. 01/DSN-MUI/IV/2000 concerning Giro, para. II.

<sup>49</sup> DSN-MUI Fatwa No. 02/DSN-MUI/IV/2000 concerning Savings, para. II.

<sup>50</sup> DSN-MUI Fatwa No. 03/DSN-MUI/IV/2000 concerning Deposit, para. II.

<sup>51</sup> Regarding Baitul Mal, see Erisa Ardika Prasada, Joni Emirzon, and KN. Sofyan Hasan, "Philosophy to Strengthen Baitul Maal wat Tamwil Law in Indonesia," *Sriwijaya Law Review* 4, no. 2 (2020): 272 and Mahdi Syahbandir et al, "State Authority for Management of Zakat, Infaq, and Sadaqahas Locally-Generated Revenue: A Case Study at Baitul Malin Aceh," *al-Ihkam: Jurnal Hukum dan Pranata Sosial* 17, no. 2 (2022): 558, 562.

of Sharia banking itself.<sup>52</sup> Furthermore, social functions through the distribution of *zakat*, *infaq*, *alms*, and endowments can have a multiplier effect on the financial performance of Sharia banking.<sup>53</sup>

Economic activity is facilitated by a bank service as an intermediary institution to meet the investment and liquidity needs of economic actors in the financial system.<sup>54</sup> Deposits and investment funds of depositing customers and investor customers must be protected in accordance with the consequences of the contract agreed between the sharia bank and the customer. *Wadi'ah* and *mudharabah* contracts provide different rights and obligations for the parties involved (sharia banks and customers), which correlates with the deposit insurance mechanism of the sharia bank. Moreover, social funds placed in Sharia banking deposits are crucial to protection.

The National Sharia Council-Indonesian Ulama Council (DSN-MUI) has issued several fatwas related to insure deposits of sharia bank customers namely DSN-MUI Fatwa No. 118/DSN-MUI/II/2018 concerning Guidelines to insure Sharia Bank Customer Deposits (DSN-MUI Fatwa No. 118/DSN-MUI/II/2018) and DSN-MUI Fatwa No. 130/DSN-MUI/X/2019 concerning Guidelines for Deposit Insurance Corporation in Handling Implementation or Settlement of Sharia Banks Experiencing Solvability Problems (DSN-MUI Fatwa No. 130/DSN-MUI/X/2019). It is stated in the fatwa that *wadi'ah* is customer deposits in the form of deposits that may be used by Sharia banks and must be returned at any time once it is required. *Wadi'ah* is a pure deposit from one party to another which must be guarded and returned whenever the depositary wants it.<sup>55</sup> Likewise with sharia banks as recipients of deposits (*wadi*), they are obliged to maintain the integrity of these deposits. *Mudharabah* is a business cooperation contract between the capital owner (*shahibul mal*), who provides all the capital, and the manager (*mudharib*). The business profits are shared between them according to the ratio as agreed in the contract.

General provisions of the DSN-MUI fatwa No. 118/DSN-MUI/II/2018 stipulates that LPS is a legal entity established under law with a function to insure bank customer deposits and play an active role in maintaining the stability of the banking system in accordance with its authority.<sup>56</sup> This fatwa underlines that the insurance is carried out by LPS, which is determined in accordance with statutory regulations. The LPS Law determines that the Deposit Insurance Corporation carries out 2 (two) functions, namely to insure deposits of depositors and actively participate in maintaining the banking system's stability in accordance with their authority. LPS may issue

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<sup>52</sup> Sulhani, Abdul Mughni, "Menyingkap Fungsi Sosial Perbankan Syariah dan Pengaruhnya Terhadap Kinerja Keuangan," *Jurnal Perbankan Syariah* 3, no. 2 (2022): 87.

<sup>53</sup> *Ibid.*

<sup>54</sup> Saira Ghulam Hasan and Waeibrorheem Waemustafa, "The Funding Liquidity Risk and Bank Risk: A Review on the Islamic and Conventional Banks in Pakistan," *Hamdard Islamicus* 43, no. 1 (2020): 85.

<sup>55</sup> Murniati Ruslan, "Islamic Perspectives on the Implementation of Wadi'ah Products at Islamic Banks in Indonesia," *Journal of Economics, Management and Trade* 27, no. 9 (2021): 39.

<sup>56</sup> DSN-MUI Fatwa No. 118/DSN-MUI/II/2018 concerning Guidelines for Insurancing Sharia Bank Customer Deposits, para. I.1.

policies to actively participate in maintaining the banking system's stability; formulate, determine, and implement policies for settling bank resolution that does not have a systemic impact; and carry out the management of collapsed banks with systemic impacts.<sup>57</sup>

The LPS authorities are:<sup>58</sup>

1. determine and collect guarantor premiums;
2. determine and collect contributions when the bank becomes a participant for the first time;
3. manage the assets and liabilities of the LPS;
4. obtain customer deposit data, bank health data, bank financial statements, and bank inspection reports as long as they do not violate bank secrecy;
5. to reconcile, verify and/or confirm the data;
6. determine the terms, procedures, and conditions for claims payment;
7. appoint, authorize, and/or assign other parties to act for the interests of and/or on behalf of LPS to carry out certain tasks;
8. conduct counseling to the bank and the public regarding deposit insurance; and
9. impose administrative sanctions.

LPS, in insuring deposits of sharia bank customers, also continues to collect premiums and contributions from sharia Banks, as regulated in PLPS 1/2020. Every bank conducting business activities in the territory of Indonesia is required to become a Deposit Insurance participant by LPS. It was found that the introduction of sharia deposit insurance schemes has substantially dampened the sensitivity of depositors against the capitalization of sharia banks.<sup>59</sup> The presence of LPS on the deposit guarantee scheme at sharia banks is expected to impact public trust positively.

Deposits referred to in this context are funds entrusted by customers to sharia banks in accordance with applicable laws and regulations, whether in the form of demand deposits, savings, time deposits, certificates of deposit, or other forms. The meaning of savings is not similar in Sharia Banking Law and DSN-MUI Fatwa No. 118/DSN-MUI/II/2018. The Sharia Banking Law differentiates customer deposits through deposits and investments. Article 1 (20) of the Sharia Banking Law determines that deposits are funds entrusted by a customer to a sharia bank and/or UUS based on a *wadi'ah akad* or other *akad* that does not conflict with sharia principles in the form of savings, current accounts, or other equivalent. Further, Article 1 (24) of the Sharia Banking Law states that Investments are funds entrusted by customers to Sharia banks and/or UUS based on *mudharabah* contracts or other contracts that are not against sharia principles in the form of deposits, savings, or other equivalent forms. Therefore, savings referred to in this fatwa also covers the definitions of savings and investments referred to in the Sharia Banking Law.

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<sup>57</sup> LPS Law, Art 5 (2).

<sup>58</sup> LPS Law, Art 6 (1).

<sup>59</sup> Aysan et al, *op.cit.*, 280.

Differing from the definition stipulated in Sharia Banking Law, DSN-MUI Fatwa No. 118/DSN-MUI/II/2018 stipulates that the insurance carried out by LPS on deposits of sharia bank customers must comply with the fatwa provisions. The study of the sharia insurance blueprint makes this fatwa become the basis for implementing bank customer deposit insurance based on sharia principles, especially in the aspect of compliance. The provisions of this fatwa stipulate that the principle used by the LPS in underwriting sharia deposits is based on the *kafalah* principle, where the s as the guarantor (*kafil*). Sharia banks as recipients of customer deposits (*makful 'anhu*) are required to pay contributions/premiums to LPS, Customers depositing funds in sharia banks as *makful lahu* (insured parties), and customer deposits in sharia banks as *makful 'alaih/bihi* (collateral objects). Sharia banks are required to pay contributions and premiums in accordance with statutory provisions, and LPS are required to pay customer deposit claims in accordance with the object of sharia deposit insurance. LPS, for consideration of benefit, may not pay Sharia Deposit Insurance claims if customer deposits meet the criteria of being unfitted to pay, as follows:<sup>60</sup>

1. The customer's deposit data is not recorded at the bank;
2. The depositing customer is the party who benefits unreasonably, and/or;
3. Depositors are parties that cause the bank to become unsound.

Provisions related to the *kafalah* principle are stipulated in the DSN-MUI Fatwa No. 11/DSN-MUI/IV/2000 concerning *Kafalah*. *Kafalah* contract is insurance given by the guarantor (*kafil*) to a third party to fulfill the obligations of the second or borne party (*makfuul 'anhu, ashil*). The *kafalah* contract is a guaranteed contract that is widely used in sharia banking, *kafalah* is versatile in its modern usage and provides benefit to both banks and customers, depending on the way the concept is used. Statements of consent and *qabul* in a *kafalah* contract must be stated by the parties to show their will in entering into a contract and in the *kafalah* contract the guarantor (*kafil*) can receive a fee as long as it is not burdensome, the *kafalah* in return is binding and cannot be canceled unilaterally.

Sharia deposit insurance provisions in the DSN-MUI Fatwa No. 118/DSN-MUI/II/2018 stipulates that Sharia banks are required to pay premiums as *rasm al-isytirak* which are paid for a certain period according to laws and regulations. It is stated in the fatwa that the premium is the amount of money received by the LPS based on the law as *rasm al-idariyah* for the deposit insurance program, the provisions of this fatwa do not explain further regarding *rasm al-idariyah* nor in PLPS 1/2020 which also provides the exact definition of premium as the DSN-MUI Fatwa No. 118/DSN-MUI/II/2018. According to laws and regulations, the term *rasm al-isytirak* is compulsory premiums paid for a certain period.<sup>61</sup> IDIC invests these premiums and contributions by placing them in sharia financial

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<sup>60</sup> PLPS 1/2020, Art. 6 (1).

<sup>61</sup> DSN-MUI Fatwa No. 118/DSN-MUI/II/2018 concerning Guidelines for Deposit Insurance Sharia Bank Customers, para. IV.1.

instruments in accordance with the laws and regulations, where the recording and management must be separated from conventional banks considering that LPS provides insurance for conventional bank customer deposits and sharia banks.

Premiums are paid by sharia banks 2 (two) times in 1 (one) year, namely no later than January 31 for the period January 1 to June 30 and no later than July 31 for payments for the period July 1 to December 31.<sup>62</sup> Premiums from sharia banks are paid through the LPS account determined by the LPS Chief Executive.<sup>63</sup> Participation contributions, sharia bank premiums and conventional bank premiums calculated from UUS are managed by LPS based on sharia principles by placing them in sharia financial instruments in accordance with the provisions of laws and regulations.<sup>64</sup> Payment of insurance claims for customers of sharia banks or UUS customers from conventional banks whose business license has been revoked using funds originating from participation and premium contributions, including the results of their management.<sup>65</sup>

Sharia deposit insurance based on DSN-MUI fatwa No. 118/DSN-MUI/II/2018 may only be made on *mudharabah* capital (*ra's al-mal*) and profit sharing that has become the customer's right but not yet paid until the business license and *wadi'ah* principal are revoked (*mablagh al-wadi'ah*) and bonuses that have been determined by the bank to be the right of the customer but have not been paid until the business license is revoked.<sup>66</sup> This is in line with Article 5 PLPS 1/2020 which stipulates that the value of deposits insured by LPS includes the balance on the date of revocation of the bank's business license.

The balance is in the form of capital (*ra's al-mal*) *mudharabah madhmunah* and profit sharing that has become the customer's right but has not been paid until the bank's business license is revoked, and *wadi'ah* principal (*mablagh al-wadi'ah*) and bonuses that have been paid to customers until the bank's business license is revoked. Deposits based on Sharia Principles that are insured include:<sup>67</sup>

1. demand deposits based on *wadi'ah* contracts;
2. demand deposits based on *mudharabah* contracts;
3. savings based on *wadi'ah* contracts;
4. savings based on *mudharabah muthlaqah* contracts or *mudharabah muqayyadah* contracts whose risks are borne by the bank;
5. deposits based on a *mudharabah muthlaqah* contract or a *mudharabah muqayyadah* contract whose risks are borne by the bank; and/or

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<sup>62</sup> LPS Law, Art 12 (1).

<sup>63</sup> PLPS 1/2020, Art. 4 (1).

<sup>64</sup> PLPS 1/2020, Art. 7.

<sup>65</sup> PLPS 1/2020, Art. 8 (1).

<sup>66</sup> DSN-MUI Fatwa No. 118/DSN-MUI/II/2018 concerning Guidelines for Deposit Insurance Sharia Bank Customers, paras V.1 and V.2.

<sup>67</sup> PLPS 1/2020 Art. 3 (1).

6. deposits based on other Sharia principles determined by LPS after receiving OJK consideration including incoming transfers and outgoing transfers.

Since 13 October 2008, until now, the insurance balance for each customer at one bank is a maximum of IDR 2.000.000.000,- (two billion rupiahs) or equivalent to 133.333 USD (one hundred thirty-three thousand three hundred and thirty-three USD).<sup>68</sup> If the customer has a deposit amount above two billion rupiahs, it will be settled by the Liquidation Team based on the liquidation results of bank assets.<sup>69</sup>

This can be detrimental to customers, considering that sharia banking does not only carry out intermediary functions but also social functions, one of which acts as LKS-PWU and money *waqf nazhir*, where the collection of cash waqf funds is carried out through savings products at sharia Banks in the name of *nazhir* based on the *wadi'ah* principle. Considering that these funds are social funds entrusted by the public is through sharia banking, extra protection is needed so that there are no social funds that LPS does not insure because they exceed the maximum insurance deposit value. It then needs to be resolved based on the liquidation of bank assets which is time-consuming, and the results may not fully cover the entire value of existing deposits. Moreover, cash waqf funds are mandated to be preserved and eternal. Sharia banking does not only have a theological mission as the enforcement of sharia values in banking financial activities, but also has a social mission to achieve economic prosperity.<sup>70</sup> This mission is reflected within its intermediary and social function so that the deposit insurance must be able to cover both of these aspects.

### 3. CONCLUSION

The readiness regarding insurance for customer deposits of sharia bank in Indonesia is regulated explicitly in the Deposit Insurance Corporation Regulation No. 1 of 2020 concerning the Implementation of Insurance and Resolutions of Sharia Bank. The Deposit insurance mechanism is carried out through a *kafalah* contract between the deposit insurance corporation and the customer to fulfill the obligations of sharia banks over customer deposits in sharia banks as an object of insurance to customers with a maximum nominal insurance of two billion rupiahs. The above regulation does not yet provide a specific arrangement regarding the protection of deposits on social funds in sharia banking. In the future, it is necessary to have regulations related to deposit insurance for social funds in sharia banking in relation to the implementation of the social functions of sharia banking, especially as LKS-PWU and Money Waqf Nazhir, considering that the funds placed in sharia banking savings products are the community social funds that must be preserved.

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<sup>68</sup> Lembaga Penjamin Simpanan, "Simpanan yang dijamin," <https://www.lps.go.id/simpanan-yang-dijamin>

<sup>69</sup> *Ibid.*

<sup>70</sup> Wahyudin Darmalaksana, "The Need for Social Theology to Strengthen the Social Functions of Islamic Banking in Indonesia," *HTS Teologiese Studies* 78, no. 1 (2022): 2.

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