



## Normative Review of Economic Democracy in The Indonesian Sharia Banking Legal Framework

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**Abstract:** *This research is a normative review of economic democracy within the legal framework of Indonesian sharia banking. In this context, this article aims to explore how the principles of economic democracy are reflected in the legal regulation of Islamic banking in Indonesia. The research method used is a normative approach involving a literature review and legal analysis of sharia banking regulations in Indonesia. The research results show that bank regulations in Law no. 7 of 1992, Law no. 10 and 21 of 1998, as well as other regulations, consistently promote democratic principles in Indonesia's national financial system. The Indonesian sharia banking institutional system which began in December 1983 marked an important first step in integrating sharia principles into the national banking system. Apart from that, the importance of the prudential principle in regulating sharia banking in Indonesia is also emphasized in this research. The precautionary principle aims to ensure that banks operate legally and in accordance with the principles of sharia law, as well as to protect consumer interests. This research provides valuable insight into how economic democracy is reflected in Indonesia's Islamic banking legal framework. The implications of these findings can be used to increase understanding of the importance of economic democracy in building an inclusive and sustainable financial system in Indonesia.*

**Keywords :** *normative review, economic democracy, legal framework, Indonesian sharia banking*

## Introduction

The banking function includes the mediation of profits and shortages of money.<sup>1</sup> Invokes the automatic formation of a customer-bank connection, tensions can rise under this contractual arrangement, leading to a conflict between the bank and the client if they are not handled. A client of a bank is legally defined as a party who uses the bank's services by the Banking Law. Every banking institution protecting customers needs attention because if protection for customers is weak, complaints can make customers feel dissatisfied with the services offered by banks that are not by the advertisements. Not to mention the interests and rights of customers, which the bank feels are not paying enough attention to, causing disputes between the bank and the customer.<sup>2</sup>

Law of Indonesia, Number 10 of 1998, divides banks into two categories: those that conduct "traditional operations" and those that adhere to the principles of Sharia law. Article 1 Article 13 explains that Sharia principles are the deposit of funds and the disclosed commercial activity between banks and other parties following Islamic law. Specifically, *Mudharabah*, *Musyarakah*, *Murabahah*, *Ijarah*, and Bank Ownership of Goods Leased to Others are all Islamic Financing Methods (*ijarah wa iqtina*).

Engaging in commercial ties or partnerships with consumers who share these values is essential for the banking system to be just, healthy, and transparent. Banking principles are legal principles, and there are legal principles in banking.<sup>3</sup> These rules are born by themselves and are based on certain philosophical foundations. The principle of law is intended as the heart of the rule of law; This is one of the laws and regulations that combines legal regulations (positive law) with social ideals and social ethics (customers). Based on Article 2 Number 7 of the 1992 Banking Act concerning Banking states that Indonesian banks are based on preventive economic democracy in their business operations.

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<sup>1</sup> Richard A Werner, "A Lost Century in Economics: Three Theories of Banking and the Conclusive Evidence," *International Review of Financial Analysis* 46 (2016): 361–79, <https://doi.org/https://doi.org/10.1016/j.irfa.2015.08.014>.

<sup>2</sup> S Sefriani, "Hukum Internasional Suatu Pengantar Edisi Kedua," *Jakarta: Raja Grafindo Persada*, 2016.

<sup>3</sup> Ross Cranston et al., *Principles of Banking Law* (Oxford University Press, 2018).

The founding document, the 1945 Constitution, conveys the founders' vision of economic democracy. However, Moh's Article 33 of the 1945 Constitution codifies the concept of popular sovereignty in economic matters. Hatta guides the economic growth of the country. Economic democracy seeks the well-being of all citizens by guaranteeing them an equitable share of economic benefits, encouraging their participation in economic life, and allowing them to share in the fruits of their labor.<sup>4</sup>

The economic democracy in Indonesia is guided by ethical principles and puts the needs of the people first. According to paragraph 33 of the Constitution of 1945, a true economic democracy prioritizes the people's demands. Article 33 of the 1945 Constitution is a purportedly Western-first example of economic democracy. This ideology is representative of Indonesian society and economy. Indonesia's economic democracy, which Moh Hatta claims is ingrained in the country's religious system and socialist economy, is given fuel by Article 33 of Indonesia's 1945 Constitution.<sup>5</sup>

Constitutionally, economic democracy rests on Article 33 of the 1945 Constitution, and ideologically, it rests on Pancasila. There is no more specific explanation regarding economic democracy. However, the GBHN/TAP MPR IV 1978 notes the positive characteristics of economic democracy: First, the economic system is organized around communal pursuits based on kinship. Second, the government controls major industries that provide for most citizens. Third, the utilization of natural resources for the benefit of its citizens. Fourth, The National Assembly uses national assets and financial resources for advice, and the National Assembly is also responsible for overseeing its policies. Five, People have the option to work, have the legal right to do so, and earn a living wage. Six, Property rights are respected but cannot be used against the common good. Seven, As long as it is not against the public interest, citizens can use their full potential, independence, and creativity. Eight, Children who are destitute or neglected are under the state's care.

Previous research tends to only look at Islamic banking from the implementation side. Ramadani, for instance, writes that Indonesian Islamic banks

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<sup>4</sup> Yustian Dewi Widiastuti, "Implementasi Asas Demokrasi Ekonomi Pada Pembiayaan Murabahah (Studi Kasus Bank Rakyat Indonesia Syariah Dan Bank Syariah Mandiri)" (Universitas Islam Indonesia, 2011).

<sup>5</sup> Ali Murtadho, "Kontribusi Ekonomi Islam Dalam Undang-Undang Dasar 1945", Vol. 24, No. 1 (2016): 137–64.

operate with the idea of caution. A trihantana article also states that economic democracy can be seen in Sharia banking contracts, such as musyarakah and mudharabah. However, in a murabahah contract, the principle of democracy cannot be fully implemented. This article seeks to provide understanding and confirmation regarding the operational basis of Islamic banking, namely based on Economic Democracy, which comes from the pillars of the Indonesian nation. In groups or monopolies, economic democracy avoids the problems of the economic system of liberalism, nationalism, and concentration of economic power. When a liberal economic system appears that leads to exploitation and exploitation of fellow human beings, then a liberal economic system must be avoided. In addition, a state-controlled economic nationalist system is avoided because it can kill non-national companies such as cooperatives, SMEs, and citizens.

## **Literature Review**

### **1. Economic Democracy**

The economic viewpoint holds that a normative basis is required for the direction of plans, policies, and programs. Article 33 of Indonesia's Constitution from 1945 serves as the legal foundation for the country's dynamic economic structure. The Republic of Indonesia's economic system is founded on kinship partnerships, as stated in Article 33 (1) of the country's 1945 constitution. The articles produced by the founding fathers have a slightly socialist feel, not in a competitive spirit, but in a family spirit, group spirit, and a spirit of unity.<sup>6</sup> However, do not rule out the application of the principle of a market economy system. In the fourth paragraph, we see that our economic system is democratically organized and guided by the values of cooperation, efficiency, fairness, longevity, concern for the natural world, autonomy, and stability.

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<sup>6</sup> Yudi Latif, "The Religiosity, Nationality, and Sociality of Pancasila: Toward Pancasila through Soekarno's Way," *Studia Islamika* 25, no. 2 (2018): 207–45, <https://doi.org/DOI:10.15408/sdi.v25i2.7502>.

The form of the Indonesian economic system after the change is economic democracy. The principle contained in economic democracy is togetherness but implementing the realistic principle of justice.<sup>7</sup> Normatively, a sense of unity is vital because the meaning of social and economic life lives together. However, in economics, the principle of operation is efficiency, which means producing high-quality and cheap goods and services to meet human life's needs. This principle of efficiency allows us to develop a faster rate of economic development. With high economic growth, the opportunity to realize prosperity is far more excellent than with low economic growth. However, principles contain elements of competition with negative externalities to eliminate these harmful elements, namely ethics, norms, and principles of justice.

The economic model most suited to the Indonesian state was determined by its founders using the notion of economic democracy. Because building Indonesia's economic system is difficult, so this concept must be applied and continuously developed. According to Sritua Arief, Juoro believes economic democracy has moral implications but is more emphasized as integrating political, business, and cultural morals. Everyone has a good relationship because the moral, political, economic, and cultural systems function in a positive, balanced, and non-subordinate way.<sup>8</sup>

Countries in the world have different models of modern economic democracy. In other words, from the conservative democratic model to liberal democracy and social democracy. As Moh Hatta has noted, however, popular sovereignty is the defining feature of Indonesian democracy and our own. In such a circumstance, those in authority and the government must act by the people's will. The primary difference that Hatta later emphasized was that the basis of our democracy is not the spirit of individualism but the spirit of unity in a collective sense.<sup>9</sup>

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<sup>7</sup> Aan Jaelani, "Fiscal Policy in Indonesia: Analysis of State Budget 2017 in Islamic Economic Perspective," *International Journal of Economics and Financial Issues* 7, no. 5 (2017): 14–24, <https://doi.org/https://dx.doi.org/10.2139/ssrn.2881093>.

<sup>8</sup> Reka Dewantara, "Rekonseptualisasi Asas Demokrasi Ekonomi Dalam Konstitusi Indonesia," *Arena Hukum* 7, no. 2, SE- (August 2014): 195–209, <https://doi.org/10.21776/ub.arenahukum.2014.00702.3>.

<sup>9</sup> Dodi Faedlulloh, "Membangun Demokrasi Ekonomi: Studi Potensi Koperasi Multi-Stakeholders Dalam Tata Kelola Agraria Indonesia," *Masyarakat Indonesia* 42, no. 1 (2016): 65–76, <https://doi.org/https://doi.org/10.14203/jmi.v42i1.356>.

## **2. History of Banking In Indonesia**

In the broadest sense, Islamic banks are banks whose practices are consistent with Islamic law. There are other names to refer to Islamic banking entities other than Islamic banking entities, namely Interest-Free Banks, Lariba Banks, and Islamic Banks. The Indonesian legal system officially refers to such institutions as "Sharia Banks" or, more formally, "Banks Operating with Sharia Principles".<sup>10</sup> Islamic banks have main principles, which include prohibiting transactions; conducting business activities in an equal, fair, and open manner; establishing mutually beneficial partnerships; and the obligation to obtain a legal and commercial advantage. To further the improvement of society as a whole, Islamic banks are tasked with issuing and overseeing zakat donations.<sup>11</sup>

There have been Islamic banks in Indonesia since 1983, starting with the package (Pakdes 83) in December 1983. Includes several regulations in the banking sector, including A system that allows banks to borrow money at 0% interest (zero interest). As a result of these occurrences, Radius Prawiro, the Minister of the Treasury, introduced some banking sector policies as part of the October 1988 package (Pakto 88). Pakto 88 was under bank deregulation and could build new bank buildings, so banking companies at that time were overgrowing. In 1991, Bank Muamalat Indonesia (BMI) became Indonesia's first and only profit-sharing commercial bank. Banking Law 7 of 1992 and Decree 72 of 1992, founded on the Profit Sharing Principle, established a legal framework advantageous to banks. Therefore, since 1992, Indonesian banking has been treated professionally with the term "profit-sharing bank." On the other hand, Islamic banks are not only founded on profit sharing. However, they may also carry out other customary Islamic contracts in their interest-free banking activity.

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<sup>10</sup> Ni Nyoman Adi Astiti and Jefry Tarantang, "Kedudukan Sharia Compliance Perbankan Syariah Di Indonesia Perspektif Yuridis-Filosofis," *Jurnal Al-Qardh* 5, no. 2 (2020): 119–33, <https://doi.org/https://doi.org/10.23971/jaq.v5i2.2454>.

<sup>11</sup> Zulfikar Hasan, "The Mechanism of Managing Zakat Funds in Islamic Banking as Implementation of Corporate Social Responsibility (CSR)," in *Indonesian Conference of Zakat-Proceedings*, 2020, 385–96, <https://doi.org/https://doi.org/https://doi.org/10.37706/iconz.2020.203>.

Traditional Islamic contracts or principles commonly referred to as Sharia law are tools that take over the traditional system of interest, uncertainty, gambling, and vanity, which Islam prohibits. Based on this pattern and the empirical fact that many traditional banks cannot survive the financial and currency crises, the government has pushed the government to amend, Specifically, Act 7 of 1992 and Act 10 of 1998. There have always been Islamic banks in Indonesia, but now it is official. A two-tiered banking structure was established in Indonesia after the passage of Law No. 10 in 1998.<sup>12</sup> Following the rules above, conventional commercial banks can set up a Sharia Business Unit and offer Islamic window Sharia services (UUS). Therefore, many conventional banks comply with Shariah by offering their customers Shariah-compliant services.

Providing Sharia services has become more accessible due to applying the office channel concept to Bank Indonesia Regulations (PBI) in 2006.<sup>13</sup> The core concept behind the office channel is to supply Sharia services to conventional commercial banks that have already implemented UUS at the corporate headquarters level. When a sharia counter or branch is needed, it is added to an existing location rather than opening a separate branch. Eliminates the need for new infrastructure such as buildings, office equipment, employees, and information technology, ensuring bank savings. PT. Bank Susila Bhakti Persero "Tbk," one of the Islamic Commercial Banks (BUS) founded after adopting Law No. 10 of 1998. As well, PT. Bank Mega followed suit by launching Big Islamic Bank. While some banks have left the UUS framework, others, like PT. BRI, PT. BNI, Bank Permata, and others continue to offer Sharia-compliant services.

BUS can carry out a more comprehensive range of business activities than traditional bank UUS. Regarding exclusive business functions performed exclusively by BUS, these include, in no particular order: (1) issuing guarantee bonds; (2) making deposits with third parties; (3) acting as a trustee; (4) investing in stocks and

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<sup>12</sup> Muhamed Zulkhibri and Raditya Sukmana, "Financing Channels and Monetary Policy in a Dual Banking System: Evidence from Islamic Banks in Indonesia," *Economic Notes* 46, no. 1 (2017): 117–43, <https://doi.org/10.1111/ecno.12076>.

<sup>13</sup> M. Nur Rianto Al Arif and Yuke Rahmawati, "Office Channeling and Its Impact on the Profitability of Islamic Bank," *Jurnal Aplikasi Manajemen* 15, no. 2 (2017): 245–51, <https://doi.org/10.21776/ub.jam.2017.015.02.08>.

bonds; (5) handling and monitoring retirement accounts; (6) long-term securities that adhere to Sharia law and are issued, disseminated, and traded. When creating new products, Islamic banks must conform to the standards set out by the National Sharia Council. *Murabahah*, *Mudarabah* Financing, and *Musyarakah* Financing are only a few examples. PBI, in 2005, Contracts for the Collection and Distribution of Funds for Banks Operating following Sharia Principles, states that since then, instructional information issued by DSN MUI has become diverse PBI content materials. Collection and Allocation of Funds and Application of Sharia Principles in Islamic Banking Services PBI were canceled and authorized by PBI in 2007 and PBI in 2008.<sup>14</sup>

PBI number dated 19 September 2007 states that in the activities of raising funds, allocating funds, and providing services, the application of sharia principles is as follows: fundraising through contracts of *Wadi'ah and Mudharabah*; funding via contracts of *Ijarah Muntakiya Bittamlik, Murabahah, Mudharabah, Salam, Istishna', Ijarah, Musyarakah, and Qardh*; providing services via contracts of *Kafalah, Hawalah, and Sharf*.

According to Ali<sup>15</sup>, Before Law 10 of 1998 came into effect, Indonesia went through an "introduction period," characterized by the passage of Law Number 7 of 1992. The next step is hoped to be the "justification stage," which will be distinguished by introducing rules and regulations about Islamic banking. Thus, the Sharia Banking Law passed on 17 June 2008 and Law Number 21 concerning Islamic Banks, promulgated in the State Gazette on 16 July 2008, have revealed the "justification stage." Some new components and legal entities have been made public in this law, all of which are meant to aid in realizing national development goals for fostering justice, cooperation, and social equality.

Islamic banking mutual benefit societies (UUS) help people reach their objectives. For example, (1) Islamic banks and UUS must collect and distribute public monies. (2) Islamic banks and business units perform social tasks via finance by collecting and redistributing revenues from zakat, expenditure, zakat, grants, or other

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<sup>14</sup> Hamzah Ali and Abd. Shomad, "Implementation Of Restructuring Istisna Housing: Controlling The Financing Risk In Sharia Banking," *Pjatee* 17, no. 4 (2020): 2267–72.

<sup>15</sup> Ali and Shomad.



social facilities. (3) Commercial banks adhering to Sharia law and Sharia-compliant businesses can utilize cash Waqf to contribute to charitable causes and, at the Waqf Manager's (Nazir) discretion, distribute the funds as needed. Islamic banking demonstrates its dual role as a financial and social intermediary by carrying out the social responsibilities mandated by law and regulation. Legal examples include Law 38 of 1999 on the Administration of Zakat and Law 41 of 2004 on Waqf.<sup>16</sup>

The Islamic Banking Law introduces new institutional challenges with unbundling. UUS services are usually provided by conventional commercial banks to be converted into BUS—the process of legally dividing a bank into several companies. According to a Bank Indonesia study from November 2008, four Sharia commercial banks—Bank Mandiri Syariah, Mega Indonesia Sharia Bank, Bank Muamalat Indonesia, and BRISyariah banks—form a network of branches. About 189 Islamic financial institutions, including 14 BUS, 20 UUS, and 164 Islamic People's Financing Banks, were active in Indonesia in 2019.<sup>17</sup>

### 3. The Precautionary Principle

Banking activities use public funds based on trust, so each bank participant must maintain public trust. Public confidence in it will be maintained if the banking industry is organized and managed with prudence to maintain its health. Judging from the Big Indonesian Dictionary, prudence means being careful or on guard. Prudence is closely related to thoroughness, precision, and accuracy and has the same meaning.<sup>18</sup> In banking law, prudence relates to bank supervision and management benefits, which became widely known in the 1980s. The word "careful" literally means wise in Indonesian. In the banking industry, this term is used to denote the prudential banking principle. Therefore, in Indonesia, the term bank supervision or management is based on prudence.

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<sup>16</sup> Wahyu Akbar and Jefry Tarantang, *Manajemen Zakat (Hakaikat Dan Spirit Al-Qur'am Surah At-Taubah [9]: 103)* (Yogyakarta: K-Media, 2018).

<sup>17</sup> Rosyid Nur Anggara Putra, "Karakteristik Pembiayaan Dan Non Performing Finance Perbankan Syariah 2015–2018," *MALIA: Journal of Islamic Banking and Finance* 3, no. 1 (2019): 1–16.

<sup>18</sup> Ni Putu Achintya Wibawa Putri et al., "Effect of Independence, Professionalism, and Experience of Internal Auditors on Fraud Prevention With Organizational Culture As Moderating Variable," *Linguistics and Culture Review* 6 (2022): 565–80, <https://doi.org/10.21744/lingcure.v6ns1.2108>.

If banks are to responsibly administer the benefits and conduct the commercial operations that the public entrusts them with, they must adhere to the principle of sound banking. With the public's money on the line, banks need extreme caution, as outlined by the precautionary principle. The prudential principle aims to keep banks in good enough shape to reliably carry out their operations and conform to the various regulations and laws governing the financial sector.<sup>19</sup>

The banking industry's prudential principle is adhered to because notaries, as public officials, must adhere to the precautionary principle so that behavior that causes legal problems does not occur in the future.<sup>20</sup> The banking law does not explain the meaning of the prudential principle, both in its clauses and interpretation. The Banking Law only mentions the terms and scope outlined in Article 29 (2), (3), and (4). Without exception, all banks, including Islamic and traditional banks, must apply the precautionary principle, further elaborated in the form of bank health signs or prudential standards in conducting business activities. Administrative sanctions that Bank Indonesia can impose on banks and their management and owners, as well as criminal and civil sanctions against the management of Islamic banks, will be imposed for violations of these indicators.

The banking industry constantly evolves regarding collecting and distributing cash in a community. With this growth comes a greater complexity in the services it provides to the general public. These banking services include<sup>21</sup>: Bank cards, Money transfer services (Transfer); Money Collection Services (Inkaso); Clearing Services (Clearing); Sales of forex services; Letters of Credit; safe deposit box services; traveler's checks; Bank guarantees and bank references.

With the many services offered by banks, it is necessary to have a cautious attitude on the part of the banking sector regarding these services, lest the intention of the services provided to expedite the business world turns out to be a scourge to set back the banking world. The precautionary principle is an essential guideline for

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<sup>19</sup> Detisa Monica Podung, "Kredit Macet Dan Penerapan Prinsip Kehati-Hatian Dalam Perbankan," *Lex Crimen* 5, no. 3 (2016).

<sup>20</sup> Ida Bagus Paramaningrat Manuaba, I Wayan Parsa, and I Gusti Ketut Ariawan, "Prinsip Kehati-Hatian Notaris Dalam Membuat Akta Autentik," *Acta Comitatus* 03 (2018), <https://doi.org/10.24843/AC.2018.v03.i01.p05>.

<sup>21</sup> Dr Kasmir, "Dasar-Dasar Perbankan Edisi Revisi 2014," *Jakarta: Rajawali Pers*, 2015.

the banking world to support all forms of existing banking expansion, but ordinary people often misinterpret it. This principle is considered only a legal obligation for banks and immediately eliminates legal obligations for the bank's customers.<sup>22</sup> The

5C Principles consist of the following:

- a. Character; Character, meaning morals, characteristics, and habits of the debtor (borrower), dramatically influences the process of granting credit. Creditors can see if the prospective debtor is included in the list of disgraceful persons (DOT), allowing creditors to view biodata and information from the business environment. Information from the business environment is available from suppliers, customers, and debtors. Central bank information is also available but not to the general public. It is only available to bank staff in the lending department using passwords connected to the central bank and online computers.<sup>23</sup>
- b. Capacity; Capacity or ability to assess client capabilities, such as prospective borrowers, the bank-owned business, or management carried out by the bank for the company so that it can give confidence to clients to pay off loans on time. Of course, small businesses have poor creditworthiness and should not be credited if their performance deteriorates.<sup>24</sup>
- c. Capital; Assessment of capital or capital; If a bank needs to assess the capital of a credit applicant or prospective debtor, this assessment is not only based on the amount of debtor's capital but also on the distribution of issued capital that can effectively implement existing sources.<sup>25</sup>
- d. Collateral is a form of collateral assessment (down payment) if the procedure for granting a loan to a bank shows that the debtor requires a loan approval guarantee. It acts as a bank guarantee for actual or future bank risks. For example, for bad debts, collateral must be high quality for the loan amount

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<sup>22</sup> Kasmir.

<sup>23</sup> Rahmad Hardiyanto, "Sistem Pengendalian Pembiayaan Untuk Mempertahankan Tingkat Likuiditas (Studi Kasus BPRS Aman Syariah)" (IAIN Metro, 2019).

<sup>24</sup> Hardiyanto.

<sup>25</sup> I Made Adi Guntara and Ni Made Ari Yulianti Griadhi, "Penerapan Prinsip 5C Sebagai Upaya Perlindungan Terhadap Bank Dalam Menyalurkan Kredit," *Kertha Semaya: Journal Ilmu Hukum* Vol 7 No 8 (2019): 1–15.

borrowed by the collateral debtor. Collaterals provided by loan applicants must be examined legally and economically to see whether they are feasible and meet the requirements set by the bank.<sup>26</sup>

- e. Condition; The economic situation in which the bank evaluates the debtor customer's business prospects, the bank knows the economic environment, and the location of the loan applicant's business domain is of concern to the bank to minimize the risks arising from this economy.<sup>27</sup>

#### 4. Indonesian Banking Legal Principles

The legal principles of banking in Indonesia are divided into 5, namely:

- a. Principles of Economic Democracy. Article 2 of Law No. 7 of 1992 restated the notion of economic democracy as revised by the legislation of 1998 concerning Banking. Meanwhile, the financial system in Indonesia is guided by economic democracy and the value of caution.<sup>28</sup>
- b. Principle of Precautions. Specifically, the precautionary principle states that banks must take extra measures to safeguard the public funds entrusted to them wherever possible. Banks can remain solvent and compliant with industry standards and laws if this concept is strictly enforced.<sup>29</sup>
- c. The principle of trust. A trusting connection between a bank and its clients is essential to conducting business according to trust. Banking is financed by funds from the community based on trust, so all banks need to maintain and maintain public trust while maintaining the health of their banks.<sup>30</sup>
- d. Confidentiality principle. The policy of insisting on complete privacy for banking clients' personal and financial information. As is customary in the banking business, we must keep the bank's existence under wraps. According to Article

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<sup>26</sup> Hardiyanto, "Sistem Pengendalian Pembiayaan Untuk Mempertahankan Tingkat Likuiditas (Studi Kasus BPRS Aman Syariah)."

<sup>27</sup> Elizabeth Tiur Manurung and Elvy Maria Manurung, "A New Approach of Bank Credit Assessment for SMES," *Academy of Accounting and Financial Studies Journal* 23, no. 3 (2019).

<sup>28</sup> Mohamad Nur Yasin, "The Pluralism Of Islamic Economic Law: Dialectic Of Moslem And Non-Moslem In The Development Of Sharia Banking In Indonesia," *JOURNAL OF INDONESIAN ISLAM*; Vol 10, No 1 (2016), June 2016, <https://doi.org/http://dx.doi.org/10.15642/JIIS.2016.10.1.113-138>.

<sup>29</sup> Yasin.

<sup>30</sup> Rr Ani Wijayati, "Penanggulangan Tindak Pidana Pencucian Uang Di Dalam Kerahasiaan Bank," *To-Ra* 1, no. 1 (2015): 41–47, <https://doi.org/https://doi.org/10.33541/tora.v1i1.1093>.

40 of Banking Law No. 7 of 1992, financial institutions must protect the privacy of their customers' savings information.<sup>31</sup>

The Principle of Knowing the Customer. Financial institutions may verify the identities of their clients and keep tabs on their dealings, including reporting any questionable activity, by using customer data. The Bank of Indonesia issued regulations on this concept in No. 3 of 2001 and No. 5/23/PBI/Tahun 2003, dated 23 October 2003.<sup>32</sup>

## Method

The normative research methodology was utilized in writing this paper, which entailed a literature review (library research) of books manufactured and sourced from numerous studies dealing with the topic<sup>33</sup>. Legal experts are not required to provide evidence to support their conclusions in this type of study because it is normative<sup>34</sup>, examining economic democracy in the legal system of Indonesian Sharia banking.

## Result and Discussion

### 1. Pancasila And The Indonesian Constitution Of 1945 As The Founding Documents For Sharia Banking

Indonesian legislation in 1992 for Banking and 1998 about Amendments to Indonesian legislation 21 of 2008 for Islamic Commercial Banks provide the legal framework for implementing democratic values in national banking. High goals contained in the principles of economic democracy must be applied to the management, legal interaction with clients and affiliates, and regulation of the country's Islamic banking sector. According to the Sharia Banking Law, economic

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<sup>31</sup> Yasin, "The Pluralism Of Islamic Economic Law: Dialectic Of Moslem And Non-Moslem In The Development Of Sharia Banking In Indonesia."

<sup>32</sup> Nur Fitriyani, "Penerapan Prinsip Mengenal Nasabah Pada Bank Perkreditan Rakyat Berdasarkan Pbi Nomor 12/20/Pbi/2010," *Dialogia Iuridica* 12, no. 2 (2021): 36–49, <https://doi.org/https://doi.org/10.28932/di.v12i2.3148>.

<sup>33</sup> Jefry Tarantang, "Teori Dan Aplikasi Pemikiran Kontemporer Dalam Pembaharuan Hukum Keluarga Islam," *Transformatif* 2, no. 1 (2018): 315, <https://doi.org/10.23971/tf.v2i1.882>.

<sup>34</sup> Ibnu Elmi Achmat Slamet Pelu and Jefry Tarantang, "Fatwa Majelis Ulama Indonesia Sebagai Solusi Permasalahan Umat Islam Di Indonesia," *Al-Manahij: Jurnal Kajian Hukum Islam* 14, no. 2 (2020): 307–16, <https://doi.org/10.24090/mnh.v14i2.3927>.

democracy means the economic activities of the Sharia Law, including the values of justice, unity, balance, and benefit.<sup>35</sup>

The economic system was discussed in the Indonesian state constitution in 1945. It is the only law that the founders of the Indonesian state used the idea of economic democracy to construct the national economy. Muhammad Hatta coined economic democracy before Indonesia's independence.<sup>36</sup> Hatta believed that without economic democracy, economic power (economic autonomy) would be concentrated in a group of economic rulers in a small group of political power. The legal framework in the Republic of Indonesia regulates the economic transition from a colonial system to a democratic national system.

The Indonesian Constitution of 1945 establishes economic concepts of unity and kinship as the foundation for economic democracy. The notion of collectivism and Indonesia's economic, democratic society prioritizes the people's interests<sup>37</sup>. Through economic democracy, society collectively plays an active role in economic development activities. In a democracy, the economy is organized as community service based on kinship with government involvement.

Economic democracy reflects people's sovereignty in the economic field. The political and economic authority must be distinguished, but the two functions are inseparable. People's sovereignty (the supreme power in the people's hands) includes political and economic sovereignty. People play the role of the final decision-maker in both politics and economics. As quoted by Hatta, he criticized the West for the inconsistent implementation of democratic thinking.<sup>38</sup> This contradiction is

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<sup>35</sup> Andrew Shandy Utama, "Abstract: History and Development of Islamic Banking Regulations in the National," *Hukum*, 2018, 1–14, <https://doi.org/https://doi.org/10.24042/adalah.v15i1.2446>.

<sup>36</sup> Putra Nugraha Adi, Triyuwono Iwan, and Ludigdo Unti, "Deconstruction of Financial Report Purposes Based on Indonesian Economic System: Mohammad Hatta's Democratic Economic Perspective," *Russian Journal of Agricultural and Socio-Economic Sciences* 72, no. 12 (2017): 217–30, <https://doi.org/10.18551/rjoas.2017-12.30>.

<sup>37</sup> Elli Ruslina, Siti Rodiah, and Nia Kania Winayanti, "Cooperative Principles (Partnership-Based Togetherness) as the Legal Basis of Democracy Economic Thinking BT - Proceedings of the International Conference on Law Reform (INCLAR 2019)" (Atlantis Press, 2020), 59–63, <https://doi.org/https://doi.org/10.2991/aebmr.k.200226.012>.

<sup>38</sup> Aurora Jilena Meliala and Jonathan Andre Woods, "The Synthesis of Indonesian Socialism According to The Constitution," *Constitutionale* 3, no. 2 (2022): 97–116, <https://doi.org/https://doi.org/10.25041/constitutionale.v3i2.2694>.

reflected in implementing a liberal or capitalist economic system that still maintains the spirit of democracy.

The development of popular sovereignty in Europe only emphasizes popular sovereignty in the political field. Economic sovereignty is entrusted to free market mechanisms, which lead parties (capitalists) with solid capital and control the people's economy. Weak people are increasingly oppressed in the economic field. In contrast to economic democracy, which is based on shared and kinship power, western liberal democracy and capitalist economic systems adhere to the principle that everyone is responsible for themselves and is economically unsuccessful, leading to equality problems.<sup>39</sup>

## 2. Economic Democracy Vs Liberal Democracy

The Democratic Economic System is a national economic system in Indonesia grounded in Pancasila and the Constitution of 1945. It places a premium on the contribution of families and communities to the common good. The advantages of economic democracy are:<sup>40</sup>

- a. A community initiative that continues to grow generates creative ideas.
- b. The possibilities of ideas are constantly expanding.
- c. The creativity of all citizens develops.

The disadvantages of economic democracy are:<sup>41</sup>

- a. The power of the new order always prioritizes economic growth.
- b. A deeply corrupt ruler paralyzes the very foundations of the economy.
- c. The government's trust is decreasing, and the citizens do not trust it.
- d. Nationalism is a dominant state that can kill economic units' potential and creative power outside the national sector.
- e. A system of free-fight liberalism that continues to expand human exploitation rapidly.

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<sup>39</sup> Murtadho, "Kontribusi Ekonomi Islam Dalam Undang-Undang Dasar 1945."

<sup>40</sup> Timbul Hamonangan Simanjuntak, Imam Mukhlis, and Andik Pratama, "Demokrasi Ekonomi Pancasila, Ekonomi Berdikari Dalam Menghadapi Arus Globalisasi-Revolusi Industri 4.0," *Seminar Nasional Ekonomi Pembangunan* 1, no. 2 (2021): 91–108.

<sup>41</sup> Abi Asmana, "Pengertian Demokrasi Liberal, Kelebihan Dan Kekurangan Demokrasi Liberal, Serta Berlakunya Demokrasi Liberal Di Indonesia," 2019.

- f. Centralization of economic power groups into one group in a monopoly container to harm society.

Liberal democracy means liberal and free democracy in representation or delegation. Therefore, liberal democracy generally can be interpreted as a form of democracy by representatives (delegations). The advantages of liberal democracy are:<sup>42</sup>

- a. The right to individual freedom is constitutionally protected.
- b. Great personal freedom.
- c. Parliamentary elections are held in person.
- d. All citizens who reach the legal age and meet the requirements have the right to elect leaders.
- e. The existence of institutions that control and limit government power reduces the potential for abuse of government power.
- f. The income level of the population is relatively high.
- g. Focus on the country's short-term plans.

The disadvantages of liberal democracy are:<sup>43</sup>

- a. Limited conditions dominate social and political life.
- b. With the increasing degree of individuality, individual freedom becomes more vulnerable to unhealthy competition.
- c. Allows the bourgeoisie to monopolize various regions.
- d. Due to limited government intervention, it is challenging to reduce social inequality.
- e. The market economy dominates the country.
- f. Allows for an increase in ethnic and religious conflicts
- g. Do not focus on the country's long-term plans.
- h. Liberalism has replaced Orthodoxy.

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<sup>42</sup> Hamonangan Simanjuntak, Mukhlis, and Pratama, "Demokrasi Ekonomi Pancasila, Ekonomi Berdikari Dalam Menghadapi Arus Globalisasi-Revolusi Industri 4.0."

<sup>43</sup> Abi Asmana, "Pengertian Demokrasi Liberal, Kelebihan Dan Kekurangan Demokrasi Liberal, Serta Berlakunya Demokrasi Liberal Di Indonesia."



## Conclusion

The architects of the Indonesian state conceived of economic democracy as a means of achieving an economic structure that reflects Indonesian culture. This idea must be used and refined since constructing an Indonesian economic system is challenging. In 1983 and October 1988, Indonesia established the first legislation for Sharia banking. Prudence, the foundation it stands, dictates that financial institutions use caution while handling customer cash and distributing monies to the general public. Prudence is at the heart of Indonesia's Islamic banking regulatory system, which banks must follow. Economic democracy, caution, trust, secrecy, and the "knowing customer principle" are the five pillars upon which Indonesian banking legislation rests. The Laws of 1992 on Banking and 1998 and 2008 on Islamic Banking form the legal framework for enforcing democratic values in national banking. This system refers to the People's Economy, the national economic system, Pancasila, and the 1945 Constitution. Its implementation is carried out in kinship and cooperation with everyone, accompanied by government guidance and supervision. So when compared with Liberal Democracy, which means representation, liberal democracy, in general, can be interpreted as a form of democracy carried out by representatives.

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