

# THE EXISTENCE OF SHARIA SUPERVISORY BOARD IN MAINTAINING THE PURPOSE OF SHARIA PRINCIPLES IN SHARIA BANKING

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## ABSTRACT

*National banking Activities are operationally carried out implementing both conventional and sharia principles. One important distinction between banking using conventional principles and Islamic principles is the existence of Sharia Supervisory Board (hereinafter is called DPS/Dewan Pengawas Syariah) in the institutional structure of sharia banking. Organizationally, DPS supervises sharia banking services as an effort of maintaining sharia principles. On the other hand, in the organizational structure of sharia banking (Limited Liability Company) there is commissioner as an organ of Limited Liability Company in addition to the General Meeting of Shareholders (GMS) and board of directors who perform the function of oversight. Besides, sharia banking are externally also supervised by Bank Indonesia as the central bank and FSA as an institution of the financial services authority. This paper is intended to determine the existence of DPS in maintaining the purity of sharia principles in sharia banking and the accountability of DPS in sharia banking institutions. Based on normative study, the existence of Sharia Supervisory Board in the operations of sharia banking is crucial in determining the implementation or failure of Islamic principles that have been set through the fatwa of National Sharia Council, among others by conducting operational analysis of sharia banking and undertaking an assessment of the activities and products of the bank. Ultimately, Sharia Supervisory Board can provide internal controls to ensure that sharia banking operations have been compliant with the fatwa issued by the National Sharia Council. In addition, the organizational accountability of the Sharia Supervisory Board on the implementation of supervisory tasks of sharia banking is reporting the results of monitoring of the implementation of sharia compliance of sharia banking to Bank Indonesia and reporting the results of sharia supervision at least every 6 months to the National Sharia Council-Indonesian Ulama Council.*

**Keywords:** Sharia Supervisory Board, Sharia Banking

## INTRODUCTION

The presence of sharia banking gives a great hope in the midst of society and other commercial banks. One of the expectations is the enactment of Law Number 10 of 1998 on the Amendment of Law Number 7 of 1992 on Banking in which the government provides the widest opportunity to public to conduct business activities based on sharia principles, including the

provision of opportunities for commercial banks to open branch offices, which specifically perform activities based on sharia principles.

In connection with sharia principles in Law Number 10 of 1998 on the Amendment of Law Number 7 of 1992 on Banking, sharia principles (profit sharing) is the treaty rules based on Islamic law between the bank and other parties to deposit funds/or financing operations or other activities in accordance with sharia.

In sharia banking, it is known sharia compliance, that is a compliance system having special emphasis on aspects of sharia that are based on statutory provisions in positive law, as well as internal policies and regulations contained in any sharia banking institutions.

Based on the needs of internal control system of sharia banking in terms of the implementation of the principles of sharia, it is arranged a provision regulating the necessity for an enterprise (banks in particular and companies in general) that run the business based on sharia principles to form Sharia Supervisory Board. In Article 109 paragraph (1) of Law Number 40 of 2007 on Limited Liability Company, it is stated that,

*“The company that runs business Activities based on sharia principles in addition to having the Board of Commissioners shall have Sharia Supervisory Board”.*

In line with the idea, specifically the obligation to establish DPS in sharia banking is also regulated in the provisions of Article 32 paragraph (1) of Law Number 21 of 2008 concerning Islamic Banking stating that

*“Sharia Supervisory Board shall be established in Sharia Banks and Commercial Banks that have Sharia Trade Unit.”*

Therefore, all the Activities of sharia banking are under the supervision of Sharia Supervisory Board. On the other hand, the provision of Article 29 (1) of Law Number 10 of 1998 on the Amendment of Law Number 7 of 1992 on Banking determines that

*“The guidance and supervision of banks are conducted by Bank Indonesia.”*

Therefore, there are two institutions to supervise sharia banking which in this case are Bank Indonesia and Sharia Supervisory Board. Meanwhile, if it refers to the provision of Article of Law Number 40 of 2007 on Limited Liability Company and Law Number 21 of 2008 concerning Sharia Banking, it is only found 1 (one article) in each, which regulates Sharia Supervisory Board, which are Article 32 on Sharia Banking Law and Article 109 on Limited Liability Company. To that end, the study seeks to assess the limits of authority of each supervisory institution (Bank Indonesia, DPS and Commissioner) in supervising the Activities of sharia banking with two legal issues: (1) How is the existence of Sharia Supervisory Board in the organ of Limited Liability Company on sharia Banking? (2) How does Sharia Supervisory Board account for the supervision of sharia banking?

## **METHOD OF STUDY**

This study is a normative legal study, which is based on norms, values, legal principles, legal concepts, legal opinions and research results. Therefore, the methods used involve (Amirudin, 2012):

### **Approaches**

Considering that this is a normative legal study, the approaches used are normative approach which includes statute approach, conceptual approach and analytical approach.

### **Source of Legal Material**

Legal material is obtained through library research which consists of primary legal materials in the form of Laws, Government Regulations, Presidential Regulations, Regional Regulations, and others; secondary legal materials in the form of concepts, expert opinions, and research results; and tertiary legal materials in the form of language dictionaries and legal dictionaries (Soekanto, 1984).

### **Legal Material Collection Technique**

The collection of legal materials is conducted by reviewing and analysing the literature materials, that is examining the laws and regulations as well as books, and the results of prior research related to this legal issue.

### **Methods of Analysing Legal Material**

The method used is descriptive normative, that is the analysis of legal materials by making legal interpretations, either authentic interpretation, grammatical interpretation, or systematic interpretation.

## **DISCUSSION**

### **The Existence of Sharia Supervisory Board in the Organ of Limited Liability Company on Sharia Banking**

Sharia banking or Islamic banking is a banking system developed based on sharia principles. Banking is said as sharia banking because it refers to sharia principles governing agreement based on Islamic law.

The role of banks conducting business Activities based on Sharia Principles needs to be improved to accommodate the aspirations and needs of the community. Therefore, the Law provides the widest opportunity for the community to establish a bank that conducts business Activities based on Sharia Principles, including the provision of opportunities to Commercial Banks to open branch offices specifically conducting Activities based on Sharia Principles.

In sharia banking supervision, legislation mandates to form a Sharia Supervisory Board. Sharia Supervisory Board is one important part of the institution of Islamic Financial Institution (hereinafter is called LKS/Lembaga Keuangan Syariah) in Indonesia.

According to Article 29 of Law Number 10 of 1998 on the Amendment of Law Number 7 of 1992 on Banking, that to conduct training and supervision of banks is Bank Indonesia.

In the explanation of Law Number 10 of 1998 on Amendment of Law Number 7 of 1992 on Banking, what are meant by guidance in paragraph (1) are the efforts done by setting regulations concerning the institutional aspects, ownership, maintenance, operations, reporting, and other aspects related to bank operations? While the definition of supervision in paragraph (1) includes indirect supervision mainly in the form of early supervision through research, analysis, and evaluation of bank statements and direct supervision in the form of investigation followed by corrective measures.

With the enactment of Law Number 21 of 2011 on the Duty of Financial Services Authority, supervision by Bank Indonesia will be submitted to the supervisory institution of independent financial service sector (Financial Services Authority). However, Bank Indonesia still positions as the central bank.

Accordingly, Bank Indonesia is given full authority, responsibility, and obligation to conduct guidance and supervision of the bank by pursuing preventive and repressive efforts. On the other hand, banks are required to have and implement an internal control system in order to guarantee the implementation of the decision making process in the management of the bank in accordance with the precautionary principle.

### **Accountability of Sharia Supervisory Board to Sharia Banking**

One characteristic that distinguishes sharia banks and conventional banks is the necessity of Sharia Supervisory Board (DPS) on sharia banks. DPS is in charge of overseeing all bank Activities in order to always comply with the principles of sharia. In other words, DPS is responsible for products and services offered to the public to conform to sharia principles; investments or projects handled by the bank should also be in accordance with the principles of sharia, and of course the bank itself must be managed in accordance with the principles of sharia.

The empowerment and development of control system and auditing of sharia compliance is pioneered by Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI). According DPS standards issued by AAOIFI are determined as follows: (Wirnyaningih, 2006)

1. Each annual report of Islamic banks must include the opinion of bank DPS which describes the bank's business activities in accordance with the principles of sharia (Islamic opinion).
2. There is an active supervision and auditing process from DPS to all business activities of the bank.

The aim of forming DPS is to oversee the aspects of sharia in banking, although technically the supervision of sharia banking has become the authority of Bank Indonesia (BI). Supervision guidelines and procedures for the submission of monitoring reports have been set in Circular Number 8/19/DPBS dated 24 August 2006 regarding Sharia Supervisory Guidelines and

Procedures for Reporting of Monitoring Results for Sharia Supervisory Board. Sharia monitoring reports along with the working paper prepared by DPS, in accordance with this regulation, are submitted to the Board of Directors, Commissioners, National Sharia Council, and also Bank Indonesia. Sharia monitoring report should contain at least some of the following:

1. Monitoring report of compliance of bank operations to the fatwa issued by National Sharia Council-Indonesian Ulama Council.
2. Sharia opinion about operational guidelines and products issued by banks.
3. Review result of new products and services without fatwa that need to be requested fatwa to National Sharia Council-Indonesian Ulama Council.
4. Sharia opinion on the implementation of the bank's overall operations in the bank's publication report.

DPS is a board established and placed on banks that do business activities based on sharia principle to ensure that the operations of sharia banks do not deviate from the principles of sharia. Bank Indonesia further establishes that the membership of DPS must get a recommendation from National Sharia Council established by Indonesian Ulama Council.

Therefore, the role of DPS and National Sharia Council becomes very significant from the aspect of sharia supervision. DPS ensures the operational activities, products and services of sharia banks are always in accordance with sharia principles. On the other hand, National Sharia Council is an institution that recommends members of DPS who have adequate sharia competence as well as issuing fatwa of products and services of sharia banks that are national so that it can be used as a uniform guidance for DPS.

There are three activities of Sharia Supervisory Board in implementing sharia supervision, according to Briston and Ashker cited by Yaya, which are: ex-ante auditing, ex-post auditing and calculation and payment of zakat. Ex-ante auditing is sharia supervisory activity by examining various measures taken by conducting a review of management decisions and conduct a review of all types of contracts made by the management of sharia banks by all parties (Sutedi, 2011 & 2009).

The credibility of a sharia bank is largely determined by the level of credibility of the Sharia Supervisory Board on the issue of performance, independence and competence. So that the role and function of Sharia Supervisory Board should be optimized (improved) in the internal supervision of sharia to establish sharia compliance assurance to all stakeholders of Islamic banks in Indonesia. Steps to optimize the role and function of the Sharia Supervisory Board in internal control sharia are to improve the external and internal aspects of Shariah Supervisory Board.

From the description above, organizationally the responsibility of Sharia Supervisory Board to the implementation of sharia banking supervisory tasks is to report the results of supervision over the implementation of sharia compliance in Islamic Bank to Bank Indonesia and to report the results at least every 6 months to National Sharia Council-Indonesian Ulama Council to be accountable to the GMS if DPS is proven negligent in performing their duties related to the implementation of fatwa and the implementation of sharia compliance.

## CONCLUSION

The existence of the Sharia Supervisory Board in the operations of Islamic banking is crucially determining the successful or failed implementation of Islamic principles that have been set through the fatwa of National Sharia Council. The programs include conducting operational analysis on Islamic Bank and undertaking an assessment of the activities and products of the bank, and ultimately conducting internal controls of sharia banking to ensure that the operations of the sharia banking is based on the fatwa issued by the National Islamic Council. In addition, DPS also gives an opinion from sharia aspects of the implementation of the bank's operations and products issued overall in published reports of banks, reviews new products and services without fatwa to be requested a fatwa to the National Sharia council. The banks ultimately should deliver the sharia monitoring reports at least six months to board of commissioners, National Sharia Board and Bank Indonesia.

Organizationally, the accountability of Sharia Supervisory Board to the performance of duties in the Islamic banking supervision is by reporting the results of supervision over the implementation of sharia compliance of Islamic Bank to Bank Indonesia and reporting sharia supervisory result at least every 6 months to National Sharia Council-Indonesian Ulama Council.

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