

***LEGAL FRAMEWORK FOR THE ESTABLISHMENT OF  
A LOCAL-OWNED BANKING ENTERPRISE:  
STUDY IN BATU CITY***

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**Abstract**

*The establishment of a Local-Owned Enterprises (BUMD) operating in the banking sector has a strategic role for the people and the Government of Batu City in order to improve the economic status, public service, and competitiveness in the financial sector, and is an attempt to increase the regionally generated revenue as mandated by Law Number 23 of 2014 and Government Regulation Number 54 Year 2017. However, with the regulatory space and authority it has so far, Batu City Government has not established the BUMD as intended. Moreover, this paper will explain sociological aspect and the choice for politic of law for the Batu City Government in the framework of BUMD establishment in banking sector. Based on these circumstances, this paper uses a normative juridical research method to see regional community needs for banking financial institution owned by the Batu City Government. Based on the provisions of the legislation, the Batu City Government in preparing the process of establishing a BUMD begins with the formation of a BUMD formation team consisting of elements of the relevant Regional Apparatus, and prepare a research of regional needs and the feasibility of business fields in the banking sector to ensure the next step is to prepare and compile Regional Regulations governing the establishment of BUMD and ratification of legal entities by a notary through the Legal Entity Administration System of the Ministry of Law and Human Rights. According to theory and authoritative regulations, the formation of BUMD may be carried out in the form of a Legal Entity for a Regional Corporation, while the banking enterprise activities may be in the form of People's Credit Banks (BPR) or Sharia People's Financing Banks (BPRS).*

**Keywords:** *Legal Framework; Local-owned enterprises; Regional Governments; Batu City*

**INTRODUCTION**

Regional development has the sole objective for improving the quality of people in those regions, whether by economy, education, and healthcare, as well as through public service that is easily and quickly accessible to the people for whom it is necessary. The issue of decentralization is not only related to delegation of central authorities but also to the delegation of regional authorities to manage finances. By theory and *de jure*, all

regional authority in budget management is regulated in part by Law Number 33 of Year 2004 on Financial Balance between the Central Government and Regional Governments.

Regarding this matter, with the existence of regional budgets that then becomes one of the authorities of Regional Governments to execute governance in their areas, investment then becomes one of the answers for the existing authorities. Development of investment of regional governments becomes one of the efforts of the government in advancing the economy, including for regions that begin to provide opportunities for companies undergoing future development or current development, or have reached stability, for each of them to be able to compete together and expand employment<sup>1</sup>.

Preparation for the growth of investment in the future will certainly require several commitments to make investment as an opportunity for increasing the growth of and improve the economy at a large scale, whether domestic or international. Investment with this definition can be said to be an activity that is conducted to add, expand, increase, or create business areas that are economical in nature and scale for Regional Governments.

Thus, the goal of investment itself, for which it is able to meet the desired targets, is to be able to improve the welfare of the people through respect for the local culture and attention toward regional potential and diversity. This may be realized if the investment activities conducted by the people, regional governments, or private parties are able to encourage or even provide simultaneous efforts for possible sustainable development. As such, the factor of investment becomes the determining factor for the progression of the economic activities of the people, seen from the standpoint of aggregate supply or aggregate demand from the source and usage of popular revenue. Therefore, matters that encourage or distort the existence of investment must always be monitored by business actors and investors, as well as policy makers<sup>2</sup>.

The City of Batu, as one of the regions in East Java, is inescapable from the investment carried out by the Government of the City of Batu, whether in the real or non-real sectors. Based on data obtained from the Department of Economic Affairs of the Government of the City of Batu, it was recorded that from 2011 to 2018, the largest amount of investment provided by the Government of the City of Kota Batu was for the real sector, comprising hotels, lodging, and restaurants, reaching a total of Rp. 1,058,942,026,015.- in those five years. Meanwhile, the smallest amount of investment was for the sector of rice milling, which only reached Rp. 300,000,000.- expended for the years from 2011 to 2018. In total, the value of investment expended by the Government of the City of Batu from 2011 to 2018 reached Rp. 6,248,895,847,409.00<sup>3</sup>.

Yet, on the other hand, there are certain particular remarks regarding investment in the field of savings and loans financing, specifically in the sector of Co-Operatives. In the period from 2011 to 2018, it was recorded that the Government of the City of Batu only invested funds to an amount of Rp. 28,032,552,675.-. This amount, in comparison with the total value of investment, is certainly very small. Yet, in the years from 2015-2017,

<sup>1</sup> Pheni Chalid, 2005, *Keuangan Daerah Investasi dan Desentralisasi Tantang dan Hambatan*, Kemitraan Partnership, Jakarta, pg. 2.

<sup>2</sup> Sugeng Prato, 2007, *Beberapa Problematika Investasi di Era Otonomi Daerah*, Yogyakarta: Jurnal Yustisia, No 71 May-August 2007, <https://eprints.uns.ac.id/901/>, diakses pada 28 Maret 2020.

<sup>3</sup> Data obtained from the Department of Economic Affairs of the Government of the City of Batu, 2019.

development of enterprises in the field of finance in Indonesia was overall in a good and maintained condition. This was conveyed in the Board of Commissioners' Meeting of the Financial Services Authority, who judged that the stability of the financial services sector and the condition of liquidities in the Indonesian financial market was in a maintained condition. The growth of the global economy was estimated to continue to improve, driven by the increased growth of the Indonesian economy<sup>4</sup>.

In relation to the investment practices that have been conducted by the Government of the City of Batu, it is considered important that investment be developed through the creation of "Local-owned enterprises"<sup>5</sup>, known locally as BUMD. The stipulations of Article 1 Number 40 of Law Number 23 of Year 2014 on Regional Governments provide the legal definition that the understanding of Local-owned enterprises (hereinafter abbreviated as BUMD) are enterprises for which all or a major part of their capital is owned by regions. In connection with this matter, the Government of the City of Batu, in its capacity as part of the organizers of Regional Governments by the law, is given the freedom to create various kinds of enterprises owned by the region in order to realize regional economy and competitiveness that is strong and reliable.

David Osborne and Ted Gaebler in their book *Reinventing Government, How the Entrepreneurial Spirit Is Transforming the Public Sector* explained and revealed a governance concept by developing the concept of an "entrepreneurial government"<sup>6</sup>.

The basic and most strategic essence of the views of Osborne and Ted is highly related to government bureaucracy that is no longer oriented to the culture of centralization, structuring, formalization, and apathy, but instead on empowerment decentralization, partnership, functionalization, and democratization. For the function of a modern government, its strategy must be directed to the support and encouragement to increase the involvement of the people in the processes of policy creation, government organization, and development execution.

Based on the above paradigm, in line with the development of regulations for Regional Governments, the limits related to the objectives of establishing BUMD, as expressed in Article 331 Paragraph (1) of Law Number 23 of Year 2014 on Regional Governments, have the aims to:

- a. provide benefits for the development of the regional economy in general;
- b. organize public utility in the form of procurement of quality goods and/or services for fulfilling the livelihoods of the people according to the conditions, characteristics, and potentials of the region of concern based on good company management practices; and
- c. obtain income and/or profits.

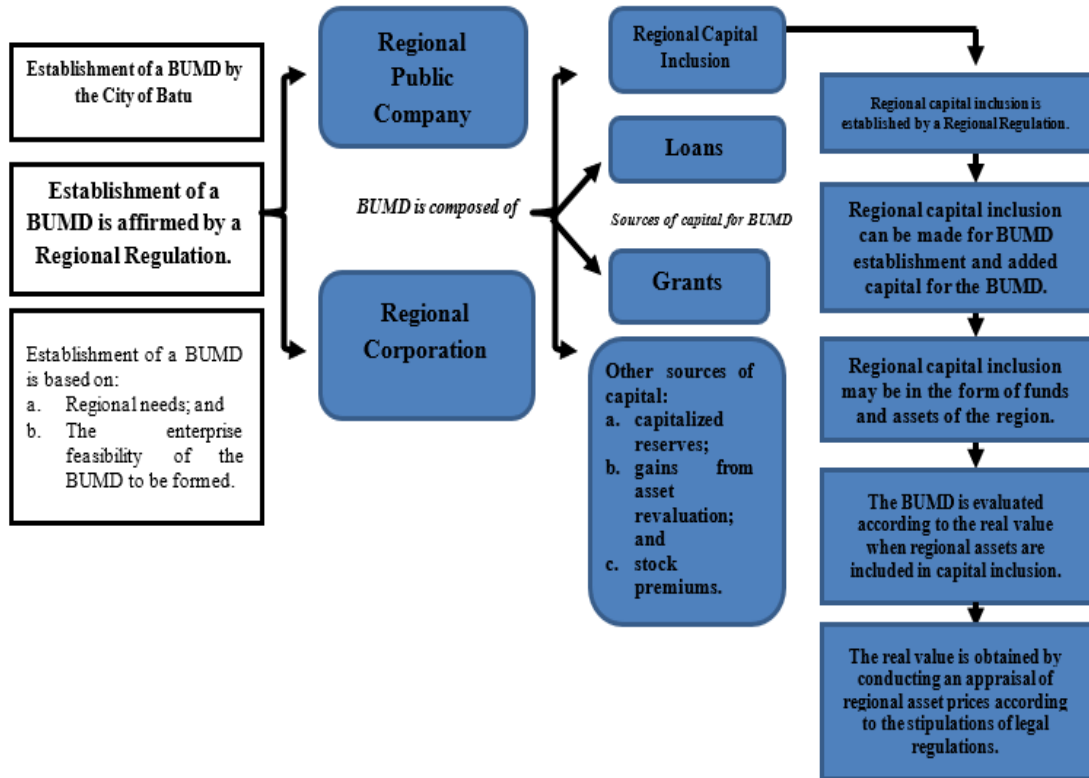
<sup>4</sup> Kunthi Fahmar Sandy, OJK Paparkan Stabilitas Sektor Jasa Keuangan Terjaga, Sindonews.com, Accessed on <https://ekbis.sindonews.com/read/1251833/178/ojk-paparkan-stabilitas-sektor-jasa-keuangan-terjaga-1508997981>, accessed on November 3, 2020, at 10:27 AM.

<sup>5</sup> Under KMK Nomor 914/KMK.01/2016, about Standar Terminologi/Istilah Dalam Bahasa Inggris Di Lingkungan Kementerian Keuangan BUMD is translated as Local-Owned Enterprises

<sup>6</sup> An entrepreneurial government focuses its energy not simply to utilize budgets, but also to create returns. They ask the people who are served to pay, demanding a return of investment. They utilize incentives such as enterprise funds and innovation funds to drive leaders of government agencies to think about how to obtain operational funds. This view rejects the assumption that the government should not seek profits from its activities. Conversely, the government must be encouraged to be able to expand its sources of revenue, including from activities of public service. Quoted from Osborne, D. and Gaebler, T. 1996. *Reinventing Government: How the Entrepreneurial Spirit Is Transforming the Public Sector*. Rosyid, A. (trans.). *Mewirusaha Birokrasi: Mentransformasi Semangat Wirausaha Ke Dalam Sektor Publik Jilid 2* (Translated), Seri Manajemen Strategi. Jakarta: PPM, p. 35.

Based on the above regulation, the formation of a BUMD can be systematized as in the following schema:

**Schema 1**  
**Stages of Formation of a BUMD by the Government of the City of Batu**



**Source: Examination of Regulations**

Based on the above schema, a BUMD is one of the enterprises that plays an important role in economic turnover in regions. A BUMD is established by Regional Governments with a variety of objectives by paying attention to the needs of the area and the feasibility of BUMD Business<sup>7</sup>. One of them is to be able to become a profit center for increasing regionally generated revenue through the earning of dividends. Regional governments as owners of BUMD certainly expect income from BUMD to increase regional revenue<sup>8</sup>. In relation to this, BUMD in its operational framework must be supported by the structuring of the legality of the legal entity.

Moving from the design of the formation and establishment of BUMD as detailed above, the establishment of a BUMD by the Government of the City of Batu that operates in the financial services sector needs to be responded positively in order to improve the economic status and competitiveness of regions. The banking sector, which possesses a strategic position as an intermediary agency and a support for payment systems with the

<sup>7</sup> Nasution, Darwin, and Sirait, Ningrum Natasya, Urgency of Local-Owned Enterprises (BUMD) Law as Good Corporate Governance Basis in Indonesia, ASSEHR, Vol 141, 2017, <https://www.atlantis-press.com/article/25889820.pdf>, diakses pada 4 April 2020.

<sup>8</sup> Budhisulistiyawati, Ambar, Muryanto, Yidho Taruno, and CN, Anjar Sari, Strategi Pengelolaan Badan Usaha Milik Daerah (BUMD) Persero untuk Mewujudkan Prinsip Tata Kelola Perusahaan yang Baik, Privat Law, Vol. III No 2, July-December 2015, <https://www.neliti.com/publications/164361/strategi-pengelolaan-badan-usaha-milik-daerah-bumd-persero-untuk-mewujudkan-prin>, diakses tanggal 1 Maret 2020.

principle of economic democracy and the primary function of collecting and distributing the funds of the people, plays a strategic role in supporting the execution of development in order to increase development equality and its results, and to grow the economy in the direction of elevating the livelihood status of many people.

Considering the role of banking institutions that are strategic in achieving the objectives of development, toward banking institutions there always needs to be effective guidance and supervision, with the basis of a strong operational foundation. This is required in order that banking institutions in Indonesia in general and in the City of Batu in particular can function in an efficient, healthy, and reasonable manner, and be able to face increased global competition, protect well the funds that are deposited by the people to them, and distribute popular funds to fields that are productive for the achievement of development objectives.

In the effort of supporting the continuity and increase in development execution, banking institutions have shown rapid developments, along with developmental advances in Indonesia and the development of the international economy and in line with the increased demands and needs of the people for banking services that are strong and healthy. With the increase of needs for banking services that have developed rapidly, the existing operational foundations for banking are considered to require adjustments at this time in order to be able to accommodate demands for development of banking services.

Based on the above explanation, the types of banking that may be facilitated in Local-owned enterprises (BUMD) are People's Credit Banks (BPR) and Sharia People's Financing Banks (BPRS). In relation, the Government of the City of Batu possesses two options for the plans of a formation of a BUMD that operates in the banking sector that is integrated with the various economic potentials present in the area of the City of Batu. Therefore, this research is to involve examination of the appropriate choices for politics of law for the Government of the City of Batu in making strategic policies in the formation of a BUMD operating in the banking sector.

Based on the above background, these problems are formulated:

1. What is the legal framework for the position of the Government of the City of Batu in the formation and/or establishment of a BUMD?
2. What is the sociological framework for the establishment of a BUMD by the Government of the City of Batu in the banking sector with the BPR and BPRS enterprise types?
3. What is the appropriate choice for politics of law for the Government of the City of Batu in the framework of the establishment of a BUMD operating in the banking sector?

Moreover, the type of this research is a normative legal research. Based on the view of Mukti Fadjar and Yulianto<sup>9</sup>, a normative legal research involves basic norms of legal principles, law codes or legal regulations, legal doctrines or teachings, contractual agreements, court verdicts, bureaucratic decisions, and all forms of legal documents that are formally created and possess legal power. The legal regulations are certainly related to the formation of a BUMD in order to be able to support the performance of

<sup>9</sup> Mukti Fadjar and Yulianto Achmad, 2010, *Dualisme Penelitian Hukum Normatif dan Empiris*, Pustaka Pelajar, Yogyakarta, pg. 36.

the Government of the City of Batu in providing banking and financial services through the schema of a BUMD. This research utilized the statute approach and the conceptual approach, and combines it with a survey method to see aregional aspects and community need for banking financial institutions owned by Batu city Government.

Difference from previous research that focus on general BUMD or regulation regarding BUMD, this research will focus on establishment BUMD in banking sector. This paper also will explain two type of banking sector for BUMD (BPRS and BPR) with the result that could help the reader to understand about banking sector under BUMD regime.

## DISCUSSIONS

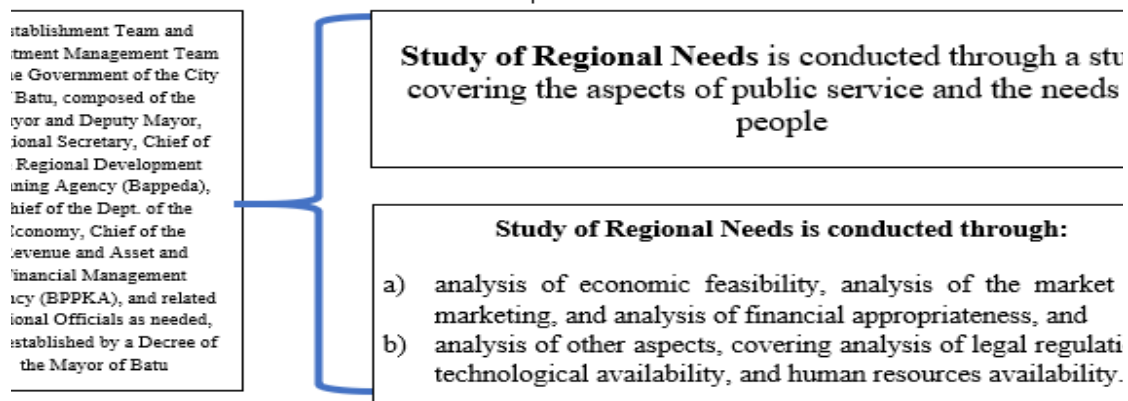
### Legal Framework for the Position of the Government of the City of Batu in the Formation and/or Establishment of a BUMD

The establishment and/or formation of a BUMD by the Government of the City of Batu is required to abide by the stipulations of applicable legal regulations. As stipulated in Article 1 Number 40 of Law Number 23 of Year 2014 on Regional Governments, there is the legal definition that Local-owned enterprises or BUMD are enterprises that have all or a major part of their capital owned by regions. As such, the Government of the City of Batu as one of the organizers of Regional Governments through the law is granted freedom to form various enterprises possessed by the region in order to realize strong and reliable regional economy and competitiveness.

Based on the above paradigm, it is possible to systematize the formation of a Regionally-Owned Enterprise (BUMD) in the following schema:

#### Schema 2

#### Preparation for the Establishment of a BUMD by the Government of the City of Batu



Source: Stipulations of Article 9 Paragraph (1) of Government Regulation No. 54 of Year 2017 on Local-owned enterprises

Based on the above schema, the position of a Regionally-Owned Enterprise (BUMD) is that of an enterprise that has all or most of its capital being owned by regions. The

enterprises should follow the regional regulation where the BUMD establish<sup>10</sup>. A BUMD is established with the objectives of providing benefits for regional economic development in general and organizing public benefits as the procurement of quality goods and/or services for fulfilling the livelihoods of people based on the conditions, characteristics, and potentials of the region in question based on good corporate governance.

### 1. Concept of a BUMD as a Regional Public Company (Perumda)

The conceptualization of a Regional Public Company (Perumda) has a constraint in that it is “*All companies that are established based on this law for which all or part of its capital comprises regional wealth that is separated, except if otherwise determined with or based on the law*”. The following is the Definition of a Regional Public Company according to Elita Dewi<sup>11</sup>:

- a. “*A regional company is a production unit that functions to provide services, organize public utility, and foster revenue.*”
- b. “*The objective of a regional company is to participate in conducting regional development in particular and to develop the needs of the people by prioritizing industrialization as well as work assurance and tranquility towards a fair and prosperous society.*”
- c. “*A Regional Public Company (Perumda) operates in the field that is appropriate to its domestic affairs according to the legal regulations that organize essential matters of regional governance.*”
- d. “*It involves branches of production that is important to the region and controls the livelihoods of many people in the region, for which the entirety of the capital comprises regional wealth that is separated.*”

Based on the above view, it can be concluded that a Regional Public Company is “*a production unit that functions to provide services, organize public utility, and foster revenue*”. A Regional Public Company is led by a Board of Directors for which the number of members and their organization is established in the founding regulations. The Board of Directors is placed under the supervision of the Regional Chief, shareholder or priority shareholder, or an assigned agency<sup>12</sup>.

Meanwhile, the Glossary of the Ministry of Domestic Affairs explains that it is “*a company for which its establishment is initiated by Regional Governments and its capital entirely or partially constitutes regional wealth that is separated*”<sup>13</sup>.

### 2. Concept of a BUMD as a Regional Corporation (Perseroda)

A (limited liability) corporation (*Perseroan Terbatas*, PT) is a business organization that possesses an official legal entity that is possessed by at least two people with responsibility that applies only for the enterprise without involvement of personal or individual wealth of anyone present within it. In a PT, the capital owners do not have to lead the corporation and can appoint people other than the capital owners as leaders.

The establishment of the corporation or PT requires a certain minimum amount of capital and fulfillment of other requirements. PT, also previously known as *Naamloze*

<sup>10</sup> Nuryana, Iwan, strategy Development and Implementation of Good Corporate Governance (GCG) on BUMN and BUMD in Indonesia, Jurnal AdBispreneur, Vol. 1, No. 2, August 2016, <http://jurnal.unpad.ac.id/adbispreneur/article/view/10237>, diakses pada tanggal 10 April 2020.

<sup>11</sup> Elita, Dewi. Identifikasi Sumber-sumber Pendapatan Asli Daerah dalam Rangka Pelaksanaan. Otonomi Daerah, Jurnal Universitas Sumatra Utara, 22, 2002, <http://repository.usu.ac.id/bitstream/handle/123456789/1261/manajemen-elita.pdf?sequence=2&isAllowed=y>, diakses pada 1 April 2020.

<sup>12</sup> Setiadi, Teguh, Urgendi Pengaturan Status Badan Hukum PDAM Tirta Pakuan Kota Bogor Menjadi Perusahaan Umum Daerah (PERUMDA), Pakuan Law Review, Vol. 5, No. 2, July- December 2019, <https://journal.unpak.ac.id/index.php/palar/article/download/1187/1017>, diakses pada tanggal 17 Maret 2020.

<sup>13</sup> [www.kemendagri.go.id](http://www.kemendagri.go.id), accessed on November 23, 2020.



*Vennootschaap (NV)*, is a partnership for running an enterprise that possesses capital in the form of shares or stocks, for which its owners possess a part as much as the number of possessed shares. Because its capital comprises stocks that may be bought and sold, changes in corporation ownership may be made without having to dissolve the corporation.

A corporation is an enterprise and the amount of capital of the corporation is denoted in the articles of association. The wealth of the corporation is separate from the personal wealth of the corporation owners and is thus all its own. Every person may possess more than one share, which becomes the proof of ownership of the corporation. The shareholders possess limited responsibility, as much as the amount of possessed stocks. If the corporation debt exceeds the corporation wealth, then the excess debt does not become the responsibility of the shareholders. If the corporation obtains profits, then the profits are distributed according to the established stipulations. The shareholders will obtain a portion of profits called a dividend, for which its size depends on the amount of profits obtained by the corporation<sup>14</sup>.

The establishment of a PT must be conducted with an official deed (a deed created by a notary) which contains the name of the corporation, capital, field of business, corporate address, and other information. This deed must be validated by the Minister of Law and Human Rights. After undergoing this process, the corporation becomes a valid legal entity and its own independent body, which would then be able to establish contracts and possess separated wealth from that of its owners. The base capital of the corporation is the amount of capital that denoted in the articles of incorporation up to the maximum amount if all the shares are issued.

The shares in BUMD could be owned by the local government 100%<sup>15</sup>. However, it is also “*possible if the society or non-regional government hold the share as long as the local government owned minimum 51 % from all of the shares*”.<sup>16</sup>

Based on the above explanation, several matters, among others, underlie the establishment of a BUMD. The first is the economic reason, which is as a way to optimize economic potential in the regions in the effort of uncovering and developing regional resources, providing public services, and seeking profits. The second is the strategic reason, which is to establish a business agency that serves the interests of the public, for which the people or other private parties are not (yet) able to do so because of major investments, great business risks, or extremely immense and broad externalities. The third is the budgetary reason, which is as an effort to seek other sources of revenue outside of taxes, retributions, and balancing funds from the central government to support the execution of governance functions in the regions.

In the end, the selection of the legal entity form Perseroda or Perumda is left back to the Batu City government, what type is needed in accordance with the goals and needs of the Batu city community. However, it would be better if the Batu City government choose Perumda for the first time establishment of BUMD because, the supervision function and company development can be monitored by local government. Consequently, if there is a problem the city government can act immediately. If in its development the Perumda growing rapidly, the legal entity form could be change into

<sup>14</sup> Budiarto, Agus, 2002, *Kedudukan Hukum dan Tanggung Jawab Pendiri Perseroan Terbatas*, Ghalia Indonesia, Jakarta, pg. 79.

<sup>15</sup> Article 7 (7), Act No. 40 year 2007, About Corporation

<sup>16</sup> Cahyaningrum, Dian, *Implikasi Bentuk Hukum BUMD terhadap Pengelolaan BUMD*, Negara Hukum, Vol. 9, No. 1, June 2018, <http://jurnal.dpr.go.id/index.php/hukum/article/download/997/pdf>, diakses pada tanggal 1 Maret 2020.



Perseroda in the hope of increasing access to capital and the companies can become public companies.

### **Sociological Framework for the Establishment of a BUMD in the Banking Sector with the BPR and BPRS Enterprise Types**

As explained in the previous section, in order to support the establishment of a BUMD, there needs to be a response by the people toward the level of needs of a region, in this case being the needs of the people of the City of Batu on the availability of a financial service agency. Related to this matter, based on the explanation of Article 331 Paragraph (5) of the Law on Regional Governments, the intent of Letter (a) “*is that regional needs are examined through studies that cover the aspects of public service and the needs of the people, including for drinking water, markets, transportation, and capital*”. This explanation can become a reference for the selection for the form of a Regional Public Company, in that the aspects of public service and popular needs include drinking water, markets, and transportation.

Adopting the concept of Public Companies in Law Number 19 of Year 2003 on State-Owned Enterprises, particularly the Explanation of Article 35 Paragraph (1), the establishment of a Public Company must fulfill the following criteria, among others:<sup>17</sup>

*“(1) the field of business or activities is related to the interests of many people, (2) it is established not merely to seek profits (cost effectiveness or cost recovery), and (3) it is based on analysis fulfilling the necessary economic requirements for the establishment of an (independent) enterprise.”*

The Explanation of Article 36 Paragraph (1) of Law Number 19 of Year 2003 on State-Owned Enterprises can also become a reference for the concept of a Public Company, in that the Explanation of the Article states that Public Companies are differentiated from Corporations because of the nature of their businesses. The enterprise of Public Companies is more emphasized on service for public utility, whether general services or the procurement of goods and services. However, as an enterprise, it should be able to remain independent, and for that, Public Companies need to obtain profits in order to be able to survive.

In tracing the concept of Public Companies upstream all the way to the 1945 Constitution, Article 33 Paragraph (2) can become a basis in that it states “*Branches of production that are important to the State and controls the livelihood of many people are controlled by the State*”. This is in line with the objective of Regional Public Companies, for which all their capital is controlled by the regions, and thus the regions through the regional chiefs as the representative owners of the BUMD possess absolute decisions on the management or policies of Regional Public Companies. This is unlike the form of a Corporation that is divided into shares, which allows for the possibility of intervention from other shareholders in running the BUMD. A vital understanding is that banking is not included because it cannot be categorized as concerning the livelihoods of many people, and even private parties can establish banking enterprises.

In relation to this, the Government of the City of Batu within the capacity as one of the Regional Government organizers by Law Number 23 of Year 2014 as amended by Law Number 5 of Year 2015 is granted freedom to form a BUMD. The formation of the BUMD constitutes one of the forms of regional investment, which is indeed a part

<sup>17</sup> See also, Kusumo, Dhimas tetuko, *Kajian Yuridis Bentuk Hukum Badan Usaha Milik Daerah (BUMD) di Bidang Perbankan Pasca Berlakunya Undang-Undang Nomor 23 Tahun 2014 tentang Pemerintah Daerah, Privat Law*, Vol. IV, No. 1, January – June 2016, <https://www.neliti.com/publications/164480/kajian-yuridis-bentuk-hukum-badan-usaha-milik-daerah-bumd-di-bidang-perbankan-pa>, diakses pada 5 April 2020.

of the vision for the City of Batu, according to the Middle-Term Development Plan for the City of Batu Region. In mission number 5, it is stated that optimization of regional investment is directed for increasing the prosperity of the people<sup>18</sup>.

The target for optimizing regional investment is in order to drive the economy of the people, which will bring about a multiplier effect on various areas of life of the people. Therefore, the establishment of a BUMD, in this case a BUMD that operates in the field of banking, is a form of regional investment optimization that is expected to be a driving force for the economy of the people. The importance of a BUMD that operates in the banking sector is that, in addition to improving economy of the people of the City of Batu and particularly SMEs, it is also expected to be a source of regionally generated revenue, as this becomes one of the objectives of conducting investment by Regional Governments. On the other hand, with the number of SMEs reaching 15,000, the need for access to capital certainly becomes a major segment for the BUMD.

In connection to the above explanation, for this research, a field study was conducted by conducting interviews with several related stakeholders, which in this case are the general public and SME entrepreneurs. In the field study, 165 respondents consisted of SME entrepreneurs and the general public in the City of Batu were sampled in order to examine the condition of knowledge and needs of the people for a banking institution. The following is a summary of the sociological study that is depicted through charts:

**Figure 1**

**Profile of Sub-Districts and Occupations of Respondents**

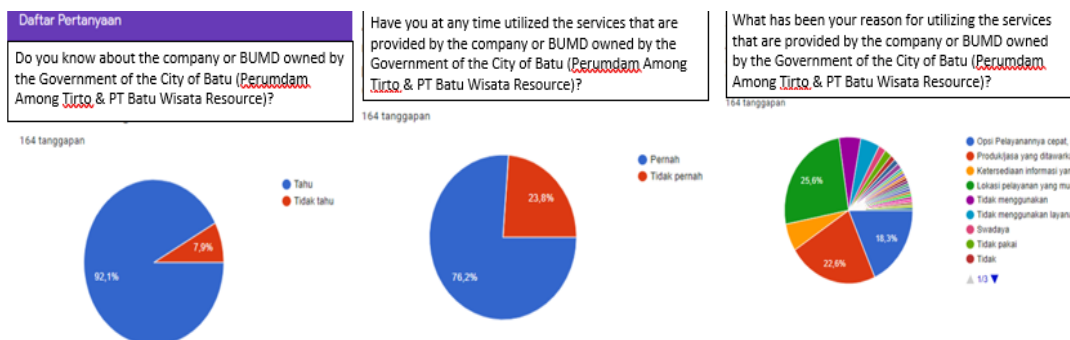


**Source: processed data from survey**

Based on the above charts, the sociological condition indicates that the respondents are spread out among three sub-districts in the region of the City of Batu, covering Bumi Aji Sub-District, Batu Sub-District, and Junrejo Sub-District. The results of the survey indicated that most respondents possess the occupations of civil servants or public officials, police or military officers, entrepreneurs, private employees, and laborers. The resulting subject portfolio fulfills the validity of subjects that later on will become the service targets with the financial and banking institution that will be formed by the Government of the City of Batu.

<sup>18</sup> Government of the City of Batu, Middle-Term Development Plan for the City of Batu Region, 2018-2023

**Figur 2**  
**Response of the People on BUMD Services of the City of Batu**

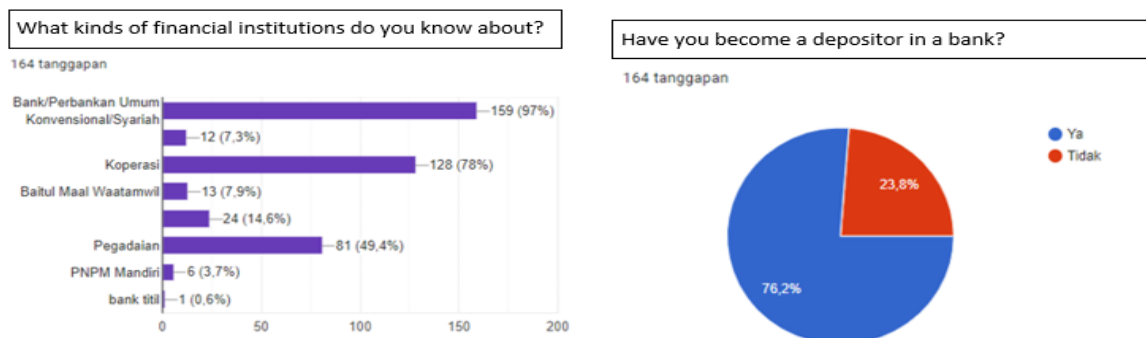


Source: processed data from survey

Based on the chart above, in principle the people of the City of Batu know about the Local-owned enterprises created by the Government of the City of Batu, which are Perumdam Among Tirta that operates in the sector of clean water or drinking water supply, and PT. Batu Wisata Resource that operates in the sector of fulfilling the livelihoods of the people of the City of Batu. The reasons of the people utilizing the BUMD services were easily accessible service locations (25.6 %, 42 respondents), good quality of offered products or services (22.6 %, 37 respondents), quick, friendly, and excellent services (18.3 %, 30 respondents), and easy access to available information (6.1 %, 10 respondents).

In this context, it is shown that the performance of the Government of the City of Batu in providing services to the people through the BUMD is judged to be successful. Even so, based on the survey results, respondents also provided input for the BUMD to be able to improve services by addressing services related to comfort, facilities, technology, and others (29.3 %, 48 respondents), uneven coverage of insurance and services (23.2 %, 38 respondents), business fields in operation that have not covered all the needs of the people (16.5 %, 27 respondents), and the lack of service locations, information availability, and other forms of guidance and instructions (12.2 %, 20 respondents).

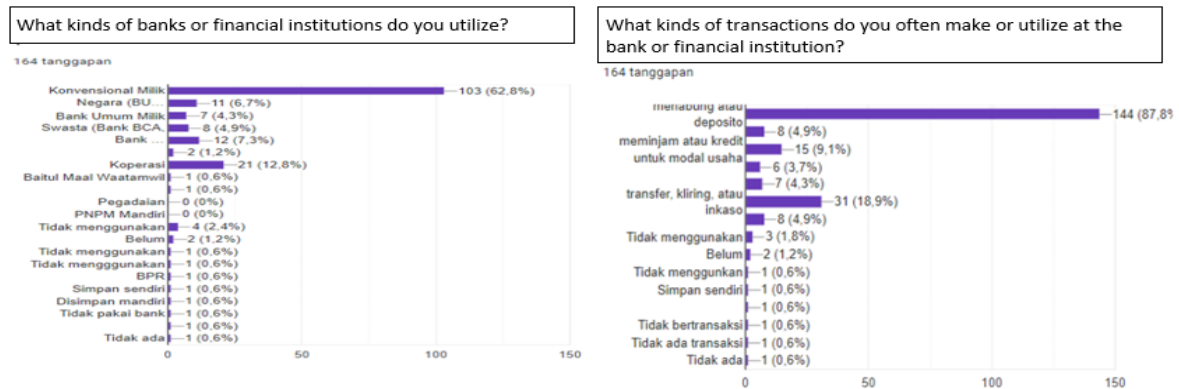
**Figure 3**  
**Response of the People toward Financial and Banking Institutions**



Source: processed data from survey

Based on the charts above, the knowledge and needs of the people of the City of Batu regarding financial and banking institutions are relatively high, with 76.2 % of respondents having become depositors in a bank. Most of the respondents in choosing to become depositors at financial institutions do so at conventional and Sharia banks, co-operatives, BMT (Sharia micro-financing), and Pegadaian (the national pawnshop).

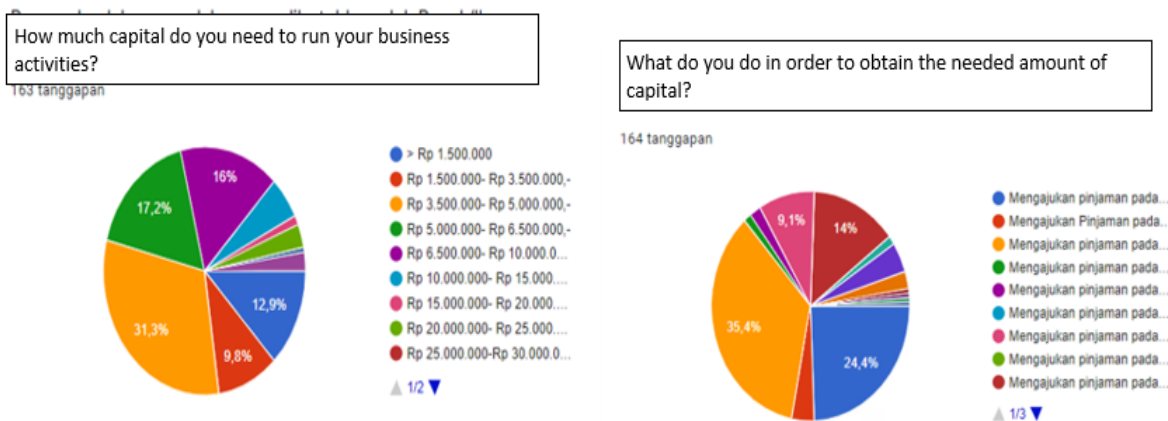
**Figure 4**  
**Response of the People toward Usage of Different Banking Services**



Source: processed data from survey

Based on the charts above, most of the people choose to utilize conventional banking owned by the state, co-operatives, BMT, and Pegadaian. Meanwhile, the usage needs of banking institutions cover savings, time deposits, loans, transfers, and payment of everyday consumptive needs (such as telephone, water, electricity, insurance, healthcare insurance, work insurance, tuition, and others).

**Figure 5**  
**Response of the People on the Need for Capital in Executing Business Activities**



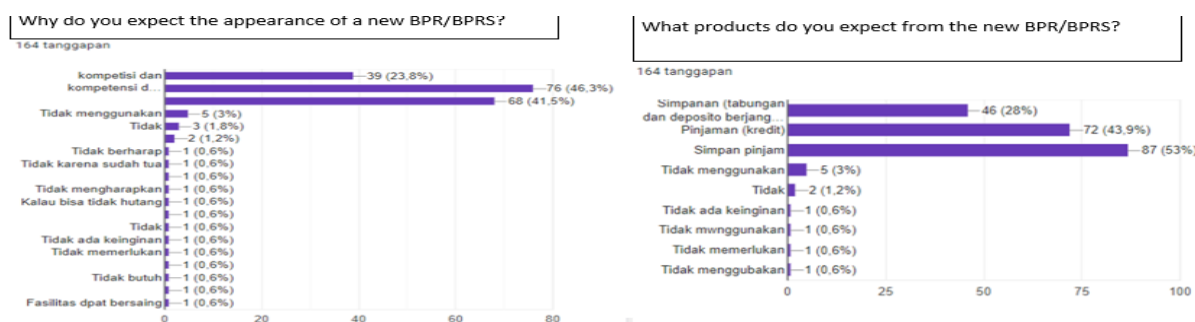
Source: processed data from survey

Based on the charts above, according to the respondents as people in the City of Batu, to possess capital to run their business activities, 35.4 % applied for a loan at a conventional state-owned bank, 24.4 % borrowed from relatives, 14 % applied for a loan at a co-operative, 9.1 % applied for a loan at a BPR/BPRS, 3.7 % applied for a loan from an individual lender, and 1.2 % applied for a loan at Pegadaian. From these results, it

can be analyzed that the availability of a financial and banking institution belonging to the regional government is considered important to intervene in the stimulus of loans among the people in order to cut out lenders and to display the portfolio of the role of the regional government in supporting the realization of prosperity for the people of the City of Batu, which becomes possible with a schema for a regionally-owned banking institution.

Figure 6

**Response of the People on the Presence of Financial and Banking Institutions (BPR/BPRS)**



**Source: processed data from survey**

Based on the above charts, the empirical response of the people is that the support the existence of a financial and banking institution through a BUMD created by the Government of the City of Batu. The need for investment credit, enterprise credit, and consumption credit among the people becomes a part of the business effort to increase the purchasing power and competitiveness of the people. Furthermore, the creation of a BPR/BPRS that have similar functions to a state-owned bank makes it very much possible to stimulate economic activities of the people through savings and deposits through various model programs that are easily accessible by the people.

Based on the sociological aspect, which includes services from existing BUMDs in Batu City, society knowledge about financial institutions, use of banking financial services, capital needs, expectations and future BPR/BPRS products, it turns out that the people of Batu City need a banking financial institution owned by the local government. In the end, the Batu City government should immediately respond to the needs of the community regarding banking financial institutions by establishing BUMD in banking financial sector.

**Appropriate Choice for Politics of Law for the Government of the City of Batu in the Framework of the Establishment of a BUMD Operating in the Banking Sector**

From the discussion in the previous section, the obtained information is that the response of the people of the City of Batu for the need of a financial and banking institution is greater. As such, institutional, regulatory, and financial support are considered important to stimulate the economy of the City of Batu through the formation of BPR/BPRS with the status of a regionally-owned enterprise BUMD.

There are two choices of banking business activities types that the Batu City government can choose, namely BPR or BPRS. Further explanation regarding these options will be described as follows:

**1. Characteristics and Criteria of a BPR and the Mechanism of Establishing a BPR**



**by a Regional Government**

People’s Credit Banks (BPR) are a kind of bank that is known to serve micro-, small-, and medium-scale entrepreneurs. It is in general located close to the place of the people who need its services. A BPR is an official banking institution that is regulated based on Law Number 7 of Year 1992 on Banking as has been amended by Law Number 10 of Year 1998. A BPR functions not only “to distribute credit to micro-, small-, and medium-scale entrepreneurs, but also to accept deposits from the people”. Its process of credit distribution to the people utilizes the principles of timeliness, accuracy, and directedness because of its relatively rapid credit process, simpler requirements, justifiability, and understanding of the needs of depositors.

The activities of a BPR cover the collection and distribution of funds with the objective of obtaining profits. BPR gains its profits from the spread effect and interest returns. These are the activities of a BPR:<sup>19</sup>

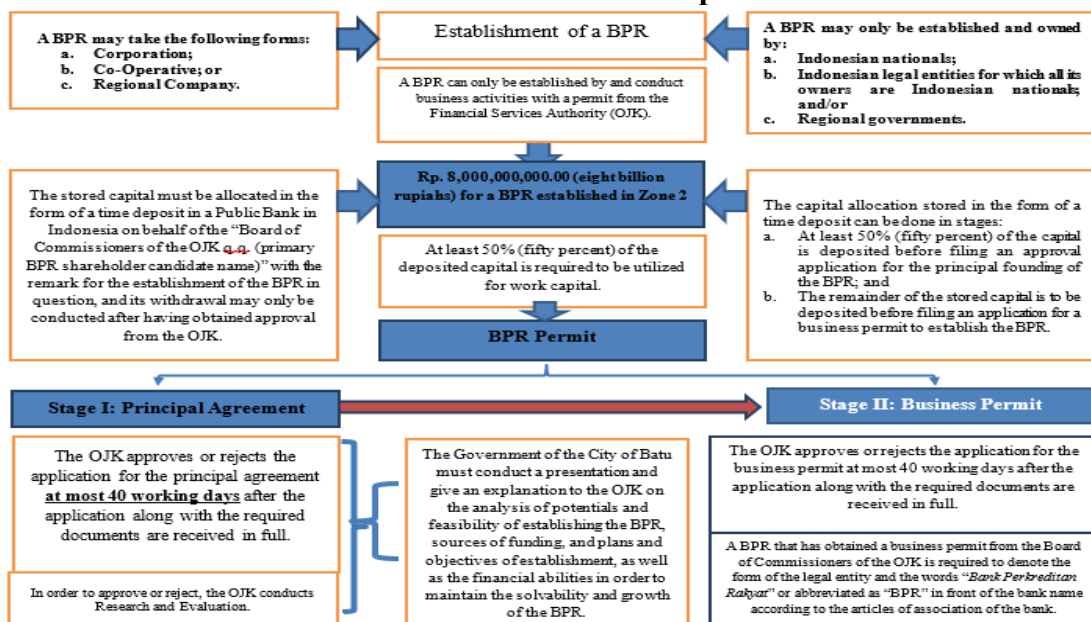
- a. To collect funds from the people in the form of savings as time deposits, direct deposits, and/or other equivalent forms.
- b. To provide credit.
- c. To provide funding for depositors based on the principle of profit sharing according to the stipulations established in Government Regulations.
- d. To allocate its funds in the forms of a Bank Indonesia Certificate (SBI), time deposits, deposit certificates, and/or savings in another bank. An SBI is a certificate that is offered by Bank Indonesia to a BPR if the BPR experiences over-liquidity.”

The establishment of BPR could be chosen because the establishment process is easier and more neutral for all community groups in Batu City. The capital allocation for BPR around eight billion rupiahs and at least 50% (fifty percent) of the capital is deposited before filing an approval application for the principal founding of the BPR.

The following are the mechanisms and stages to establish a BPR:

**Schema 3**

**Flowchart for the Establishment of a BPR Based on Financial Services Authority Regulation Number 20/POJK.03/2014 on People’s Credit Banks**



<sup>19</sup> Widjanarko. 1992, Hukum dan Ketentuan Perbankan di Indonesia, Grafiti, Jakarta, pg. 42.

## 2. Characteristics and Criteria of a Sharia BPR (BPRS) and the Mechanism of Establishing a BPRS by a Regional Government

A Sharia People's Financing Bank, also known as a Sharia BPR or BPRS, is one of the Sharia financial and banking institutions for which its operational patterns follow Sharia or Islamic (muamalah) principles. A BPRS is a bank that conducts business activities based on Sharia, which in its activities does not provide services in financial traffic. "Sharia banking, as Islamic legal principles in activities of banking", are based on a fatwa issued by the National Sharia Council of the Indonesian Council of Ulemas (MUI). In this case, a BPRS can technically be understood as a financial institution similar to a conventional BPR that utilizes Sharia principles in its operations, especially profit sharing.<sup>20</sup> There are several intended objectives of establishing a Sharia People's Financing Bank or BPRS. According to Sudarsono, the following are several objectives of establishing a BPRS.<sup>21</sup>

- a. *"To improve the economic welfare of Muslims, economically weak groups of people, who are generally in rural areas. The primary target of a BPRS is Muslims present in rural areas and at the sub-district level. People who reside in those areas are in general part of economically weak groups in society. The presence of a BPRS can become a source of capital for the development of enterprises of people in economically weak societal groups, which in turn will increase their income and welfare;*
- b. *To expand employment, particularly at the sub-district level, in order to be able to reduce the rate of urbanization. The presence of BPRS in the sub-districts helps to provide work opportunities for people who possess banking potential, in terms of both capital and expert staff. Thus, as more BPRS are present in the sub-districts, more labor will also be employed in the banking sector. In addition, the financing that is distributed by a BPRS for the people opens up ever-broader opportunities for business and work, and in turn, the presence of a BPRS will become a deterrent for urbanization;*
- c. *To guide fellow Muslims in economic activities in order to increase per capita income towards a decent quality of life. This has the meaning that in a BPRS, the value of ta'awun (mutual assistance) is developed between capital owners and job possessors. This value of ta'awun will foster togetherness between the bank and depositors, which becomes the most important factor in realizing an Ukhuwah Islamiyah ("Islamic brotherhood"). Through this togetherness, the business activities conducted by the people with the capital provided by a BPRS can increase the income of the people, and then at a higher level, this will also increase the per capita income at both the local and the national levels."*

Based on the explanation above, one of the forms of uncovering the potentials and forms of popular contribution to the national economy is the development of an economic system based on Islamic (Sharia) values by the inclusion of its principles into the national legal system. Sharia principles are founded on the values of justice, utility, balance, and universality (*rahmatan lil 'alamin*, blessings for all). The principles of Sharia banking are a part of Islamic teachings that are related to the economy.

If the Batu City government chooses a BPRS, the principles of sharia banking must also be considered in running the BPRS. In addition, there is also a need for a sharia board for the process of establishing a BPRS.

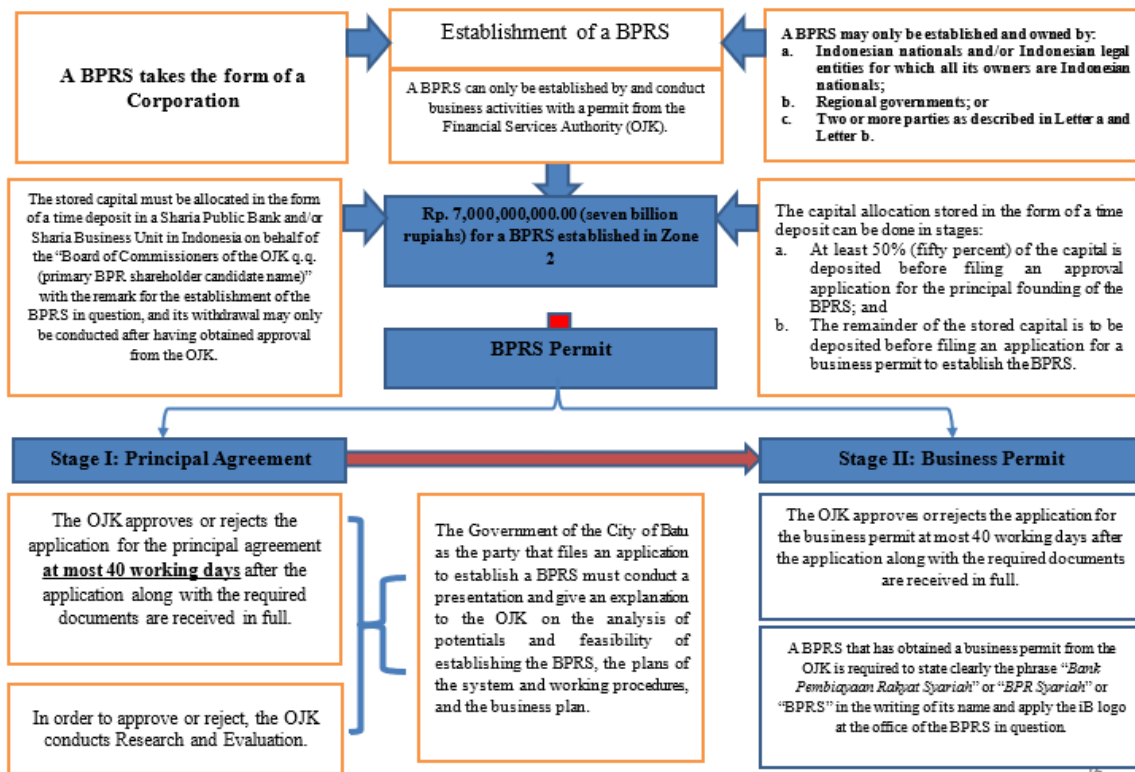
<sup>20</sup> Warkum, Sumitro, 1997, *Asas-Asas Perbankan Islam Dan Lembaga-Lembaga Terkait (BAMUI dan TAKAFUL)* Di Indonesia, Raja Grafindo Persada, Jakarta, pg. 111.

<sup>21</sup> Sudarsono, 2004, *Bank dan Lembaga Keuangan Syariah Deskripsi dan Ilustrasi*, Ekonisia, Yogyakarta, pg. 85.



Therefore, regarding this matter, the following is an explanation of the stages of formation and/or establishment of a BPRS based on Financial Services Authority Regulation Number 3/POJK.03/2016 on Sharia People’s Financing Banks:

**Schema 4**  
**Flowchart for the Establishment of a BPRS Based on Financial Services Authority Regulation Number 3/POJK.03/2016 on Sharia People’s Financing Banks**



Based on the description above, the researcher considers that the two types of activity models can be carried out by the Batu City government. However, if the choice is a BPR business activity, the legal entity can be in the form of a Perumda or Perseroda. Meanwhile, if the chosen one is a BPRS, the legal entity form must be Perseroda.

Consequently, it would be easier to the local government to choose BPR because they could also change the legal entity form Perumda and when the business growing well they could change to Perseroda. However, if they want choose BPRS the only legal entity form is Perseroda.

**CONCLUSION**

Based on the discussions in previous sections, for this research, it can be concluded that: First, The Government of the City of Batu as an organizer of governance in a region can execute regional policy in the forming and/or establishment of a BUMD based on the stipulations of Article 331 Paragraph (1) of Law Number 23 of Year 2014 on Regional Governments, by which the objectives of establishing a BUMD are to: provide benefits for the economic development of the region in general; organize public utility as the procurement of goods and/or services of a good quality to fulfill the livelihoods of people based on the conditions, characteristics, and potentials of the region in question based on good corporate governance; and obtain returns and/or profits. *Second*, based

on the based on the results of the sociological aspect, the Batu City government must immediately respond to the needs of its people in the field of establishing regional banking financial institutions. With this response, it will have a direct and positive impact on the service needs of access to capital in Batu City, and the expansion of the provision of banking financial institutions in the region. Thus, it is hoped that a prosperous society will be created in Batu City. *Third*, the appropriate choice for the politics of law for the Government of the City of Batu in the framework of establishing a BUMD operating in the banking sector is to form a conventional Perumda BPR or Perseroda BPR or a Perseroda BPRS that follows Islamic principles. This choice must really be considered by paying attention at the needs of the community and the development of banking companies owned by Batu City local government in the future.

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