

# habib ahmed

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## Habib Ahmed's *maqāṣid sharī'ah* concept on cooperative regulations in Indonesia

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This article discussed Habib Ahmed's *maqāṣid sharī'ah* concept on Islamic Financial Institutions (IFIs) contracts, regarding the dualism of cooperative regulations in Indonesia between sharia and non-sharia-based cooperatives. In initiating the New Institutional Economics (NIE) approach for IFIs, Habib Ahmed emphasized the vital role of embeddedness as a culture rooted in the knowledge system. This embeddedness is the starting point of IFIs adaptation. These informal institutions then influence the formation of formal institutions and are followed by institutional forms of organization. Finally, the transaction products are in line with the organizational form. In other words, according to Habib Ahmed, if the adaptation and transaction of the IFIs start from this stage, then the product will be entirely in line with the proper Islamic ontology and epistemology. This qualitative library research focused on the reality of cooperatives in Indonesia, assessed from Habib Ahmed's perspective. This study concluded that Indonesia's economy still does not represent the goal of its constitutional economy with a feeling of kinship and mutualistic organization, such as cooperatives. In addition, its significant economic growth, which places it in the top twenty countries (G-20) in Gross Domestic Product (GDP), is not inclusive.

Artikel ini mengkaji bagaimana pemikiran *maqāṣid sharī'ah* Habib Ahmed terhadap Akad Lembaga Keuangan Syariah (LKS). Berangkat dari dilema regulasi perkoperasian di Indonesia yang memiliki dualism antara koperasi berbasis syariah dan non-syariah. Habib Ahmed dalam menggagas pendekatan NIE (*New Institutional Economics*) bagi LKS, menekankan peran penting embeddedness ini yang disebut sebagai budaya dan mengakar pada system ilmu pengetahuan. Embeddedness inilah di mana adaptasi LKS secara intrinsic dimulai. Dari akar institusi informal ini kemudian mempengaruhi terbentuknya institusi secara formal yang menjadi dasar bagi didirikannya bentuk organisasi lembaga dan akhirnya produk-produk transaksi yang dihasilkan benar-benar sejawa dengan bentuk organisasi tadi. Dengan kata lain menurut Habib Ahmed, jika suatu adaptasi LKS dan transaksinya dimulai dari tahap ini, maka produk yang dihasilkan akan dapat benar-benar sejalan dengan otologi dan epistemology Islam

yang sebenarnya. Pembahasan dalam artikel ini<sup>27</sup> fokus pada realita perkoperasian di Indonesia bila dinilai dalam kacamata Habib Ahmed. Artikel ini tergolong dalam penelitian kualitatif dan merupakan penelitian pustaka. Hasil penelitian menyimpulkan bahwa Perekonomian Indonesia masih belum merepresentasikan apa yang menjadi tujuan Ekonomi konstitusi yang berasaskan kekeluargaan dan organisasi ekonominya yang bersifat mutualisme seperti koperasi. Dengan pertumbuhan ekonomi yang signifikan di kawasan sehingga masuk dalam jajaran negara-negara dua puluh besar PDB tertinggi dunia (G-20), namun pertumbuhan tersebut tidaklah inklusif.

**Keywords:** *cooperative, Habib Ahmed, maqāsid shari`ah*

### Introduction

Sharia finance, as has been the consensus of early Islamic economic thinkers, promotes equality and fairness in business transactions through the concept of *mudaraba* or profit and loss sharing (Musyafa, Pebruary, & Anam, 2018), even referred to as a financing model that is identical to Islamic finance (Kasri & Ahmed, 2015). Concerning the dominance of the neo-classical economic-financial system, one of which is financial intermediary, Islamic finance is indicated by its vision to shift from a debt-based intermediation financial system to a profit-sharing based financing model and bear the risk (Zeldi *et al.*, 2019).

Therefore, the principle of bearing profit and loss among business partners is important in the concept of Islamic economics. Choudhury (1982) makes profit and loss sharing (PLS) as one of the main instruments for Islamic finance application in addition to 3 other main instrument elements, namely: eliminating usury, eliminating *israf* (excessiveness), and zakat instruments. Therefore, Islamic economists from the beginning have proposed that PLS should ideally be applied to IFI, both on the funding and financing sides known as the two-tier *mudaraba* mechanism (Jobarteh, 2017). Modern Islamic economists initiated it in the early 70s to liberate the Islamic world from Western colonialism.

In banking practice, the two sides of the PLS principle can be applied to the funding side, where the investor/savers are as *rabbul mal* (beneficial owner) and the bank functions as *mudarib* (managing trustee). Meanwhile, banks act as *rabbul mal* on the financing side, and customers function as *mudarib* (Fajrianty, 2019 p. 16). Cooperatives as a financial institution have social and economic values at the same time as the principles and axioms of sharia economics, including the principle of profit and loss sharing.

Several studies have measured the performance of IFI, especially Islamic banking with *maqāṣid*. For example, an investigation of 13 banks from 6 countries over five years found indications that *maqāṣid* performance was not achieved as a whole (Asutay & Turkistani, 2016). Furthermore, Mergaliyev, Asutay, Avdukic, and Karbhari (2021) found that indicators of the Muslim population, the quality of the CEO (chief executive officer), sharia governance, and sharia banking lever variables have a positive impact on *maqāṣid*. However, the influence of GDP (Gross Domestic Product), financial development of a country's human development index, and its human rights and political ownership of institutions that are larger than its independent directors negatively impact the *maqāṣid* performance. However, the analysis of cooperative performance from the *maqāṣid* point of view is still limited.

Several studies discussing the relationship among cooperatives, regulation and *maqāṣid* reviews in Indonesia have only looked at cooperative activities in terms of the *maqāṣid* index. Kasri and Ahmed (2015) found that there was sharia compliance by sharia cooperatives against the *maqāṣid* index developed by Mustafa Omar Mohammed and Dzuljastri Abdul Razak from the International Islamic University Malaysia (IIUM) and the Regulation of the Supervision Deputy of the Ministry of Cooperatives and SMEs No. 07/Per/Dep.6/IV/2016 concerning Guidelines for Health Assessment of KSPPS and USPPS. Meanwhile, other authors saw that the absence of cooperative regulations specifically regulating sharia cooperatives is still a problem (Sofiana, 2014, p. 137).

In the national scope, it is necessary to examine how cooperative regulations in Indonesia can be in line with *maqāṣid sharī'ah* thinking in the economy. Therefore, this study analyzed the suitability of cooperative regulations in Indonesia with *maqāṣid sharī'ah* in forming a contract and its application by cooperative management. Therefore, the *maqāṣid sharī'ah* used as reference here is based on Habib Ahmed's thought. This study saw to what extent Habib Ahmed's concept of economic institutionalization affected a contract in cooperatives. Then, to get an overview of cooperative regulation problem, this paper explored how legal and economic politics affected cooperative regulatory policies in Indonesia.

## Method

This qualitative study used normative legal (Sonata, 2015) and institutional economics

approaches that integrated statutory, concept, and literary analysis to draw conclusions and reasoning. Extensive literature related to Islamic economics, cooperatives, and *maqāṣid shari'ah* were reviewed, analyzed, and used as a reference to find and identify to answer the research problems.

### **The concept of *maqāṣid shari'ah* in the Islamic financial system**

Concerning the universal *maqāṣid* dimension in Islamic economic, Chapra (1399, p. 6) formulated four goals to achieve by Islamic Economics: first, achieving economic prosperity within the framework of Islamic moral norms. Second, upholding brotherhood and universal justice. Third, achieving income equality, and fourth, achieving individual freedom from social welfare in an economic context that has emerged since the prophet era.

In other words, economic development in Islam aims to promote human welfare through the emancipation and empowerment of individuals and society towards improving living conditions, equitable distribution of wealth and income, and upholding justice and equity in every level of society as well as people in the development process of embeddedness in society (Asutay & Turkistani, 2016). Therefore, Ibn Asyur formulated that the benefits of individual property return to the general, as society's wealth. So, individuals' assets should benefit the individuals concerned and the society following Shari'a.

Ibn Asyur continued that the transfer of property ownership in Islam is carried out based on fair sharia contracts with rewards or *tabarru'* (rewards from Allah). Therefore, the goal of a Muslim in his economic activity is to achieve *falab* (glory) in the world and hereafter, because Islamic finance will focus on this glory maximization where humans are called homo-Islamicus, which is different from capitalism finance which concentrates on profit maximization where humans are called *homo-economicus* (Ibrahim & Ismail, 2020, p. 138).

In general, as described by Al-Ghazali *maqāṣid* can be divided into 3 categories, namely: *dharuriyah*, *hajiyah* dan *tahsiniyah* (Tahir, 2020). In the scope of *dharuriyah*, it requires the purpose of the Law to maintain some of the essential elements of the Law, which consists of 5 goals, namely: religion, life, property, reason and lineage. Some of them add to maintaining honor other than the 5 previously mentioned (Tutik, 2016).

In explaining their *maqāṣid* theory, some scholars ultimately make benefit (*maslaha*) an inseparable meaning from *maqāṣid*, even considered as synonym (Musyafa, Pebruary & Anam, 2018) so that in order to eliminate these 5 objectives of the Sharia, it can be categorized as *mafsada* and maintaining it is a *maslaha*. *Maslaha* is contained in the word *rahmah* as contained in al-Qur'an 21:107: "Indeed, we have sent you as a *rahmah* (mercy) to the worlds."

Because of that, the scholars set a rule that *maqāṣid* is not valid if it does not reach *maslaha* and hinders *mafsada*. Thus, its existence is intended for the benefit of humanity (Ahmed *et al.*, 2015) with the provision that it must be following sharia. This context further explains that any *maslaha* that is not intended to protect the objectives of Islamic Law according to al-Qur'an, as-Sunnah, and Ijma' are unacceptable and ruled out.

Thus the desired *maslaha* in Islam is not open to all thoughts. Sometimes something is seen as a benefit in thought, but if it contradicts the sharia, then it is not justified in Islam.

### Habib Ahmed's thoughts on the application of *maqāṣid shari'ah* in Islamic finance

#### Habib Ahmed's Profile

Habib Ahmed has been a professor of the Sharjah Chair in Islamic Law and Finance at Durham University Business School, the United Kingdom, since 2008. He obtained 2 (two) master's degrees in economics, the first from one of the universities in his home country, the University of Chittagong, Bangladesh and the second from the University of Oslo, Norway. Subsequently, he obtained a Ph.D. in Economics from the University of Connecticut the USA in 2004 and became a lecturer there.

He has also taught at the National University of Singapore, University of Bahrain, and Hamad Bin Khalifa University, Qatar. In addition, he has also had experience as a researcher with The Islamic Research and Training Institute (IRTI). He also has considerable professional experience, including a Consultant at IFSB, an economist at IsDB, and an R&D manager at National Commercial Bank, Saudi Arabia (Ahmed, 2014, p. 37). Habib Ahmed's idea related to the theme of this writing is the approach used in IFIs contracts through the NIE (New Institutional Economics) approach.

His work related to this idea is described in his article entitled *The Islamization of Economics and Knowledge: A New Institutional Economics Perspective*, published by the American Journal of

Islamic Social Sciences in 2012. In addition, he is also known for the idea of applying *maqāṣid sharī'ah* as a framework for testing in the development of Islamic financial products through his writings entitled *Maqāṣid al-Sharī'ah and Islamic financial products: a framework for assessment*, published by the ISRA International journal of Islamic finance in 2011. In addition, his writings also cover other topics related to sharia law and economics, from capital markets to sharia microfinance, with more than 70 works in various international publications.

### ***Maqāṣid sharī'ah* and product development: testing framework**

Based on the *maqāṣid* conception, Habib Ahmed formulated the idea of *maqāṣid* in applying Islamic finance. Special/micro-*maqāṣid* is specific at the micro-level, which aims to protect and enhance stakeholders' five essences (faith, soul, reason, lineage, and wealth) and fulfill the objectives set out in the contract. At the same time, general/macro-*maqāṣid* is to fulfill the conditions for realizing human welfare by increasing welfare (*maslaha*) and preventing damage (*mafsada*) as well as producing an economy that protects the public interest, balance between growth and equity (Ahmed, 1994, p. 92).

In other words, he sees *maqāṣid* at a broader level than the scope of individual obligation. Looking at *maqāṣid* on a broader macro scale will be able to see whether a contract or Islamic financial institution can fulfill the objectives desired by Islamic Economics or not. Although Islamic trade law is adaptable and dynamic, it is not as free as the Western business law system, with no boundaries (Ahmed and International Institute of Islamic Thought, 2002).

A capitalist economy with a profit maximization motif can use a liberal approach, while a sharia economy with *falah* maximization objective has guidelines that have been set by sharia to ensure that growth can be in line with equity. In this context, Ahmed (2006) emphasizes the need to expand the scope of *maqāṣid* from just the fiqh level to more general *maqāṣid* and sharia principles.

Ahmed (2011, p. 150) considered that in achieving the macro level of *maqāṣid*, Islamic economics requires legal and social requirements, including at the level of financial products/contracts. The legal requirements aim to produce a contract that simultaneously fulfills both form and substance. Meanwhile, social requirements will complement aspects of the form

and substance of the contract with macro aspects of *maqāṣid* as discussed above.

For example, the trend of Islamic banking management policies that are more dominant put forward financing with *murabaha* contracts or other fee-based contracts in their financing schemes. When viewed at the legal level, *murabaha* has met two legal requirements of *maqāṣid shari'ah*. However, at the macro level, the dominant tendency of Islamic banking financing to prioritize *murabaha* than PLS contracts is seen as not fulfilling the social aspects of Islamic *maqāṣid*. The social impact that appears in society in the form of a consumerism culture will grow even more than a productive culture through PLS financing. In addition, *murabaha* contracts often impact the loss of the customer's assets at the time of default due to certain conditions in which he cannot fulfill his installment payment obligations, such as being laid off, an unwanted disaster, or an accident. In contrast, the PLS contract promotes the rational sharing of profits and losses.

According to Ahmed (2011, p. 150), on the legal requirements, the sharia financial product must meet all aspects of *qawaid al-fiqhiyyah* to meet the form and substance. The conclusion of Ahmed (2011) regarding the substance of a contract can be understood as substance at the legal framework level, while in a more general framework, the substance of a contract is reached when it fulfills *maqāṣid shari'ah*. For example, a *murabaha* contract, where formal validity is legal from the authority and in substance, also fulfills all aspects of *qawaid al-fiqhiyyah*. This distinguishes it from the *Tawarruq* contract, which formally does have legality from the authorities in several Gulf countries but substantially does not fulfill the *qawaid al-fiqhiyyah* aspects.

If *qawaid al-fiqhiyyah* is not fulfilled, the contract only fulfills the form aspect but loses its substance. With the current approach to adopting conventional financial transactions to Islamize finance, many hybrid contracts consist of legal contracts, according to sharia. However, substantially, the outcome of these contracts will resemble conventional contracts.

The Islamic banking system adopts conventional banking, meaning that it is not neutral but born of capitalism. The purpose of banking is to maximize shareholder profits. The principle of muamalah is basically 'permissible' as long as there is no evidence that prohibits it. The capitalist economy is different from the Islamic economy. When adoption occurs, there will be friction, even though it is Islamized, but the character of the banking business related to shareholder profits does not disappear from Islamic banking. So then,



the popular contracts chosen follow the objectives of the characteristics of the previous commercial banking model.

*Murabaha* (cost-plus financing) in terms of fiqh is not a problem, but in the context of social *maqāṣid* some conditions become a problem in itself, like in a pandemic or in other conditions. The rise of the phenomenon of layoffs in companies, for example, makes them lose assets (collateral) by the bank.

These contracts focus more on form but ignore the substance desired by *qawaid al-fiqhiyyah* (Alziyadat & Ahmed, 2019, p. 4) (as in the previous example) driven by ambition to achieve functions and objectives similar to conventional financial contract structures. Efforts like this can be seen as *bilab*. It can produce outcomes that substantially contradict sharia principles or distort legal principles which will ultimately conflict with *maqāṣid* (Laldin & Furqani, 2016).

*Hilab* (legal trick) is disputed among scholars, but there is no problem as long as it does not conflict with *maqāṣid al-shari'a*. However, in practice, related to concept offered to Habib Ahmed, it cause a contract not to achieve the goals of *maqāṣid* coherently. As he said, a contract sometimes only fulfills *maqāṣid* legally but fails to achieve it socially. If a *bilab* contained in a contract, can fulfill the objectives of *maqāṣid* progressively, both legally and socially, then it is not viewed negatively.

Based on the idea of *maqāṣid shari'ah* he developed for IFIs, the contract products in IFI are classified into three groups. First, when a contract has lost its substance due to the above approach, it is a pseudo-sharia contract (Toriquddin, 2013). Its permissibility is legitimized, but it does not achieve the Sharia's desired substance. Second, if the contract meets the form and substance, it is categorized as a sharia-compliant contract. At this level, a contract still does not meet *maqāṣid* at a macro level because aspects of social requirements consisting of the target market and the level of need have not been achieved. Third, if the social aspects are met, in addition to the form and substance, then the contract can be called sharia-based (Moqbel & Ahmed, 2020).

### **The application of *maqāṣid* for ethical decision-making in Islamic financial transactions**

In another article with his colleague Alziyadat, Ahmed formulated the *maqāṣid* application in IFI. They based their concept Ash-Syatiby *maqāṣid* theory, which facilitates an understanding of the

relationship between *al-ahkam al-taklifiyya* (sharia law), *maslaha* (sharia benefits) and *maqāṣid* (sharia goals) to explain how ethical decisions are based on *maqāṣid* made. The conceptual framework was developed by Alziyadat and Ahmed (2019) for ethical decision-making by integrating the contemporary management concept of the PDCA (Plan, Do, Check and Action) cycles and sharia principles of legal methods related to ethics (Alziyadat & Ahmed, 2019, p. 9).

Furthermore, the process used in this method consists of 3 phases. The first is the planning phase inductively using the normative sharia rules framework. The second phase is implementation and evaluation (check) using a deductive approach. Finally, the implementation phase departs from the results of the second phase. The implementation of a legal decision needs to be projected in terms of the final result (*Ma'alat*) to reflect the implications of *maqāṣid al-sharia* by including economic, social and environmental issues.

**Table 1** The intensity of *maqāṣid* results and ethical decisions

Outcome	Type	Project 1	Project 2	Project 3	Project 4
1. Higher production/ contribution to the development	MS	High	Medium	High	Low
2. Profitability for shareholders	MS	High	Medium	High	High
3. Adverse impact of environmental degradation on community health	MF	Low	Medium	High	high
4. Impact on environmental degradation on future generations	MF	Low	Medium	High	high
Ethical Judgement		Mandub (recommended)	Mubah (neutral)	Makruh (disapproved)	Strongly Makruh (disapproved)

Source: (Alziyadat and Ahmed, 2019, p.26-27)

MS = *Maslaha*

MF = *Mafsada*

The first example shows that the contribution to economic growth and profits for shareholders are high, while the adverse impact on public health and future generations is low, the law of *mubab* changes to *mandub*. In the second example, all indicators show the same result, namely medium, so the original law of *mubab* does not change. The third example shows that all indicators of *maslaha* and *mafsada* are high, so that the original law of *mubab* becomes *makrub*. In the last example, from the two *maslaha*, one indicates low while another is high, but all indicators of *mafsada* are high, so the law of *mubab* changes to strongly *makrub*.

Furthermore, Alziyadat and Ahmed (2019) conceptualized the basic principles of Asy-Syatiby's permissibility in muamalah as long as no arguments (*dalail*) prohibit it as the basis for this phase of the PDCA cycle. A basic law of permissibility of a contract, such as *murabaha*, may change when its implementation has destructive excesses. For example, a *Murabaha* contract is awarded to an oil refining company. In practice, the *murabaha* contract may contribute to environmental damage so that the fundamental law of permissibility can change. Likewise, with other contracts such as *mudaraba*, if there are indications of damaging the environment, the contract will lose its legal basis of permissibility. Therefore, the 3 phases in the PDCA cycle above need to be applied by projecting sharia economic elements and others. From this, an ethical conclusion can be drawn on the transaction.

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#### Sharia cooperatives in the legal framework of cooperatives in Indonesia

In contrast to Islamic banking, no law explicitly regulates sharia cooperatives. Historically, the existence of sharia cooperatives first appeared in the Decree of the Minister of Cooperatives and SMEs No. 91/Kep/M.KUKM/IX/2004 of September 10, 2004, concerning Guidelines for implementing Sharia Financial Services Cooperative Business Activities (Ruslina, 1945). At the same time, Islamic banking has been regulated by Law since 1992 through Law number 7 of 1992, which became the basis for Bank Muamalat Indonesia, although the term Islamic bank has not been found in this Law because it only recognizes the concept, namely profit sharing (Nugraha, 2017, p. 278).

The acceptance profit-sharing concept in banking and the indecisiveness of the mention of sharia banking in this Law can be seen as a transitional phase of Islamophobia in Indonesian politics where Islamic Law is still in the shadow of the early political struggles of independence, starting from the debates on the Jakarta charter and other

political struggles at the time has reached the phase of Islamic revival since the 1980s (Fajrianty, 2019).

This Law was later amended by Law No. 10 of 1988, which explicitly confirmed the existence of Islamic banking. Furthermore, Islamic banking is regulated explicitly in Law no. 21 of 2008 concerning Islamic Banking (Tutik, 2016, p. 6). Comparing the legal developments of these two Islamic financial institutions, the focus of Indonesian legal politics on sharia cooperatives is still less than on sharia banking.

Currently, sharia cooperatives have been regulated in general in Law but do not specifically regulate sharia cooperatives, namely Law no. 11 of 2020 concerning Job Creation. This Law amends Law Number 25 of 1992 concerning cooperatives by inserting Article 44A (1): Cooperatives can carry out business activities based on sharia principles. Furthermore, paragraph 2 of the article states: Further provisions regarding Cooperatives that carry out business activities based on sharia principles are regulated in a Government Regulation. For this reason, the government issued Regulation no. 7 of 2021, which regulates the Ease, Protection, and Empowerment of Cooperatives and SMEs.

In simplifying the operation, the Government Regulation changes the number of sharia supervisors in cooperatives from two people to one person. The rules for implementing sharia cooperatives are regulated in more detail by the Regulation of Ministry of Cooperatives and SMEs no 11 of 2017 concerning the Implementation of Sharia Savings and Loans and Financing Business Activities by Cooperatives (Fajrianty, 2019). The derivative regulation of sharia cooperatives refers to Law No. 25/1992, where the existence of the Sharia Business Unit as part of the business of a cooperative is still recognized. This is different from Law 17/2012, which no longer allows a Savings and Loans Unit to emphasize the segregation of financial institutions and real economic activities that the Constitutional Court has since canceled.

That Ministerial Regulation defines Sharia Savings and Loans and Financing Cooperatives abbreviated as KSPPS, as cooperatives whose business activities are saving, loaning and financing according to sharia principles, including managing zakat, *infaq*, alms, and *waqf*. Interestingly, this definition is the integration of the function of *baitul mal*, which is not found in the definition of Islamic banks in Law no. 21/2008, where its function is only

supplementary.

The definition of a sharia financing cooperative that integrates the function of *baitul mal* is inseparable from historical factors. As previously mentioned in the early 1990s, Indonesia's legal politics and economy are still plagued by intense Islamophobia. Because it is different from most other Muslim-majority countries where Islamic economics and financial institutions have found a place in their legal and economic politics, in Indonesia the spirit of Islamic economic revival in this era has only taken root in civil society.

This is where the beginning of BMT (*bayt maal wa-at tammil*) was born in 1990, in subsequent developments, the majority of sharia cooperatives are BMTs (Sofiana, 2014), or identical (Dewi and Nourma, 2017). Thus, it can be said that sharia cooperatives have been recognized in the Law, but the new detailed regulation is at the ministerial regulation level.

### **The dilemma of BMT as a sharia savings and loans cooperative**

In terms of organizational structure, BMT may be different from cooperatives. If the cooperative is purely a business institution to prosper the community, then BMT has a business function (*tammil*) and a philanthropic function (*baitul mal*). The absence of appropriate regulations for this unique new institution is a problem for BMT, as scholars think cooperatives are similar to *syirkah* in Islam, and both have the goal of prospering the community in which some features are built following the sharia concept (Dewi & Nourma, 2017).

So the majority of BMTs adopted cooperative legal entities and their formal operations. In addition to choosing cooperative legal entities, some BMTs adopted foundations, informal institutions such as self-sustaining community or did not even have a legal entity in the early days. (Mursid, 2018). With its unique innovation, BMT is faced with several choices of existing institutional models. Therefore, BMT does not have the standard institutional model. However, most BMTs find that the cooperative model is ideal due to the reasons mentioned above.

This problem was further complicated when <sup>1</sup> Law Number 1 of 2013 concerning Microfinance Institutions was passed (Fajrianty, 2019). According to Article 39 Paragraphs (1) and (2) of the Law, BMT is allowed to choose <sup>31</sup> cooperative legal entity or a Limited

Company (Ltd, in Indonesia is called PT), and for those who choose a cooperative, BMT is also understood as one of the Microfinance Institutions (MFI).

In practice, the majority prefer cooperative legal entities because of the similarity of characters above, BMTs who choose Ltd/PT require that the local government own 60% of the shares. In other words, BMT as PT must be controlled by the local government. This is something new for BMT because BMT was born from the grassroots and driven by civil society but with this regulation, BMT began to enter bureaucracy in share ownership.

As for the problem for BMT, which chooses a cooperative legal entity, when the service function of the MFI includes non-members of cooperatives, the supervision is no longer under the cooperatives minister but under the Financial Services Authority (OJK) according to Law no. 1 of 2013 concerning Microfinance Institutions. This is also another new thing for BMTs, used to the supervision of the Minister of Cooperatives and SMEs. Now they will also face OJK supervision, where the supervision is known to be more highly regulated. For BMTs who still choose cooperative legal entities and the majority of them exist, Regulation No. 11 of 2017 and Law No. 1 of 2013 are seen as causing ambiguity in their application in the field (Fajrianty, 2019, p. 15).

Furthermore, in Article 27 of the Law, BMT cooperatives with the above MFI functions operating in more than one district/city area are required to transform into banks. According to Law number 7 of 1992 concerning Banking, as amended by Law number 10 of 1998, cooperatives can still maintain their legal entity of cooperatives. This is an opportunity for cooperatives to develop themselves by becoming a bank.

For example, compared to Europe, cooperative banks are allowed to develop to a global level. For example, the bank with the third most significant asset and the second largest customer in the Netherlands, Rabobank, its vast profits are not only enjoyed by a handful of shareholders but are shared by 20 million members. With achievements supported by national regulations, Even Rabobank can have subsidiary companies, which vary across continents, including one of the largest developer companies in Europe, Rabo Vastgoed Groep (Bager & Michelsen, 1994).

Likewise, with the cooperative banking model in Germany, a pool of cooperative banks can form several regional central banks and one federal central bank and account for more

than 50% of the total number of banks nationally (Jobarteh, 2017). Cooperative banks in Japan provide another exciting lesson. The Norinchukin Bank, one of Japan's largest banks with cross-border branches, is a cooperative central bank directly established by the government (Kheng, 1979). Due to its unique characteristics compared to commercial banks in general, cooperative banks in Japan are regulated by a particular law, namely Deed no. 93 of 2001 concerning Norinchukin Bank. This cooperative bank dramatically contributes to Japan's agriculture, fisheries, and forestry sectors. In addition, cooperative banks in Japan can protect the interests of farmers against the food import lobby (Kheng, 1979, p. 78).

Should refer to article 33 (1) of the 1945 Constitution, cooperatives in Indonesia must be given the most significant opportunity to develop by strengthening regulations that support the progress of cooperatives. Because the current regulation is still considered weak for the advancement of cooperative banking, two cooperative banks that once existed in Indonesia, namely Bukopin Bank and Bank Kesejahteraan Ekonomi (BKE), have turned into Limited companies. Ironically, the most significant shares are controlled by foreigners (Ruslina, 1945).

#### **Cooperative regulations in the review of institutionalization and Habib Ahmed's *maqāṣid sharī'ah* thought against IFI**

Cooperatives as a system of economic institutions have a firm basis in the 1945 Constitution. For Mohammad Hatta, as the proclaimer and first vice president of Indonesia, cooperatives are a national economic institution for Indonesia (Higgins, 1958, p. 8). Therefore, Article 33 of the 1945 Constitution directly absorbs a word born from the nation's traditional values to describe the basis of the economic **life of the Indonesian nation, namely the principle of kinship**. This principle, a traditional cultural value, is a unique cultural value embedded in the Indonesian nation's body and has been rooted in the structure of its society for centuries.

In initiating the NIE approach for IFI, Habib Ahmed emphasized the vital role of this **embeddedness**, which is called **culture** and is **rooted in the system** of knowledge. **This embeddedness is where the intrinsic IFI adaptation begins** (Ahmed, 2012). The roots of these informal institutions influence the formation of formal institutions that are the basis

for establishing the institutional form of organization. Finally, the transaction products are genuinely at the heart of the organizational form. In other words, according to Habib Ahmed, if the adaptation and transaction of the IFI start from this stage, then the product will be entirely in line with the proper Islamic ontology and epistemology.

The institutional approach to regulation fills the gaps in the neo-classical approach (capitalism), which sees the motivation of regulation only from the demand side. According to the neo-classical approach, regulation was born to fulfill group interests and ignore the supply side of a regulation which is the interaction of existing institutions (Çeti̇N & Basim, 2011). Meanwhile, cooperatives as financial institutions which historically were originally institutions built with an institutional framework made embeddedness in society as an operational reference in order to achieve goals that meet the interests of all stakeholders in the community (Kherallah, 2002).

Based on the Hegemonic Stability theory, an open and liberal world economy requires the existence of hegemonic or dominant power. The power of this hegemony aims to maintain the norms and rules of the liberal economic order, where without this hegemony, the liberal economic order will be significantly weakened (Gilpin & Gilpin, 2001). Because of this, the neo-classical liberal economic concept as a mainstream economic system influences all existing financial institutions, even though it does not come from the same conceptual framework, including cooperatives.

If the neoclassical approach is used to formulate a regulation, its impact meets the industry's interests and the regulator is trapped in that interest group (Stigler, 1971). So it becomes a problem when efficiency is more emphasized while equity is ruled out in making regulations even though the regulations were first drafted to overcome market problems related to efficiency and equity (Reynolds, 1981). In addition to formal institutions, informal institutions such as culture, norms, and religion also shape the economic character.

At the beginning of their emergence, cooperatives, closely related to agriculture, were governance institutions (Kherallah, 2002). In response to several contemporary issues related to cooperatives, the NIE (New Institutional Economics) approach is able to provide transaction design solutions that can increase economic efficiency that cannot be replicated by corporate institutions (Sykuta & Cook, 2001). This shows that the approach to dealing



with problems related to cooperatives is not solely a neo-classical approach, likewise, with the formulation of cooperative regulations. The neo-classical approach will only limit the development of the cooperative itself because neo-classical focuses on safeguarding the interests of shareholders and growth while cooperatives aim to achieve mutual prosperity.

The divergence of cooperatives' roles in Indonesia from the marginalized constitutional economy due to global and national factors in the discussion in the previous section is explained by institutional economics as a process of isomorphism (Bager, 1994) *decooperativization* and *demutualism* or also called *co-optalismo*. The last two terms better explain the process of shifting the value of cooperatives substantively through *decooperativization* and the strong influence of capitalism. This shift in the value of cooperatives can be observed for global and national causes in the Indonesian context, as in the previous section. Meanwhile, Bager (1994) reveals that isomorphism explains why organizations tend to imitate each other to achieve homogeneity among fellow organizations that influence each other based on formal and informal factors. Formal factors can be in countries, competitors, or group pressures, while informal factors are related to social life, learning processes, and daily activities. In terms of formal factors, isomorphism in the role of government can be seen in the development of cooperative regulations in Indonesia, which are more responsive to the interests of the market economy than the interests of community mutualism. This condition is observed vulgarly in Law no. 17/2012, later annulled by the Constitutional Court.

By no longer allowing a non-savings and loan cooperative unit to have a savings and loan unit, the Law prioritizes financial capital schemes over social and mutual cooperation capital schemes, which are the fundamental characteristics of cooperatives. This provision makes the practice of cooperatives in line with the tendency of financialization even though it is a typical form of behavior in capitalism that has been used as the reason for several world financial crises (Lapavitsas, 2013). In terms of *maqāṣid shari'ah*, a savings unit of cooperative answers the *bilab* problem that may arise in Islamic banking finance contracts.

As discussed earlier, *bilab* in Islamic banking financial contracts occurs because of strict restrictions on banking that prevent banks from being directly involved in actual business activities because of the intermediary financial function adopted by the commercial banking model adopted by Islamic banking. While on the other hand, Islamic banking is required

to transact in actual business activities (Siringoringo, 2017, p. 54), including PLS contract, sale-purchase, and lease. This situation made several Islamic banking financial contracts produced as a *bilab* mechanism so that the transactions failed to meet the overall *maqāṣid* requirements.

In contrast to cooperatives that are closely related where direct involvement in the productive real economy is one of the foundations, a savings and loan unit in a cooperative can mitigate the problem of the grant mechanism in the contract. A customer can directly carry out genuine and non-hybrid *murabaha* transactions with a business entity, namely a cooperative. Thus it can be concluded that prohibiting a Cooperative entity to have a savings and loan unit as stipulated in Law no. 17/2012 can prevent the achievement of *maqāṣid shari'ah* in cooperative transactions.

The saving and loan unit (USP) deals with loss mitigation because, unlike banking, it is not prohibited from owning inventory. As a result, USP transactions are more accurate because they are directly included in real buying and selling transactions. This is different from the sale and purchase transaction condition, which limits the seller's direct control of the object of the transaction because its character is purely financial intermediary, so a hybrid contract is required. Cooperatives that have a USP as one of their business units function as a financial intermediary and as an actual economic business model to meet the needs and benefits of their community members.

Furthermore, it is a cooperatives' shifting value through the isomorphism process due to the global hegemony of capitalism and the lack of a consistent constitutional economy in Indonesia. Isomorphism is a process of mutual influence between one organization and another, both externally and internally, through influence based on power and within the organization itself. In addition to this term, several other meaningful terms are also used by several other authors to describe the process of changing cooperative values, namely *decooperativization* and *demutualism* or *co-optalismo* (Lapavitsas, 2013, p. 797).

The last two terms better explain the process of shifting the value of cooperatives substantively through *decooperativization* or with the strong influence of capitalism. The character of the cooperative business model rooted in embeddedness needs to be preserved because it will differentiate cooperatives from intermediary financial institutions whose

operations and regulations are limited. So that the function of cooperatives as a unique business model is not then limited by the influence of capitalism to become only a financial intermediary as happened in Law no. 17/2012 (Siringoringo, 2017, p. 139).

Also, looking from an isomorphic perspective, in IFI adopted from a neo-classical framework such as banking, the institutional theory approach influences designing a good sharia governance framework for Islamic banking (Mukminin, 2019). Likewise, in terms of transactions, although the intermediation function generally significantly curbs the formation of financial products directly involved in real business, Islamic banking contracts contribute directly to the real economy because, in Islamic economics principle, the object of commodity transactions is not money.

Even in some instances, Islamic banking has succeeded in producing innovations closer to Islamic finance's true character. Departing from the *maqāṣid* desired by Islamic economics, early modern sharia economists revealed that the ideal character of Islamic finance is based on sharing profits and losses fairly (Chapra, 1399). By zoning, in Indonesia, BNI Syariah has applied for a permit to have inventory in the property sector developed on *waqf* assets for *murabaha* financing, approved by OJK as a pilot project (Tutik, 2016, p.5). With this innovation, it is possible for BNIS, which has now merged with two other public sharia banks, to become Sharia Bank of Indonesia (BSI), to control or own the object of the sale and purchase transaction as a legal condition for buying and selling in Islam, before the transaction is carried out so that the contract is called real *murabaha* (BSI).

Whereas Articles 6 & 7 of Law No. 10/1998 do not include activities that directly involve banks in real economic activities because there can be risks for banks in their function as financial intermediaries. However, this kind of Islamic banking innovation is assessed by the OJK as a consequence of the unique character values that animate Islamic banking which is different from conventional banking (Sofiana, 2014). According to Arif and Yati (2021), consistency in allocating funds for the real sector is one of the essential indicators of achieving *maqāṣid shari'ah*

With the integration of business and financing models in financial institutions, the obstacles to adjusting between contracts and business needs found in Islamic banking financing products can be mitigated. Overcoming this obstacle is usually done by combining

more than one contract into a hybrid contract. If this hybrid contract aims solely to replicate the conventional banking financing model, *bilab* emerges. *Hilab* is an Islamic legal term that applies tricks and cunning to avoid difficulties in one's commitment to Islamic Law (Musyafa, Pebruary, & Anam, 2018). The hybrid contract is a mixture where one contract consists of several contracts, such as *Musbaraqab mutanaqishab* and *Tawarruq* contracts.

Because basically, the contract in conventional banking only aims to fulfill the intermediary financial function, not for a real economic business scheme, which is an important character of Islamic finance. Thus the profit from the financing scheme refers to the time value of money, which then contradicts the principles of Islamic finance. So, if the purpose of the hybrid contract is to replicate the conventional banking financing model, it becomes a *bilab* trap. In figure 1, it can be seen why a hybrid contract is needed to mitigate obstacles in the intermediation model of Islamic finance.

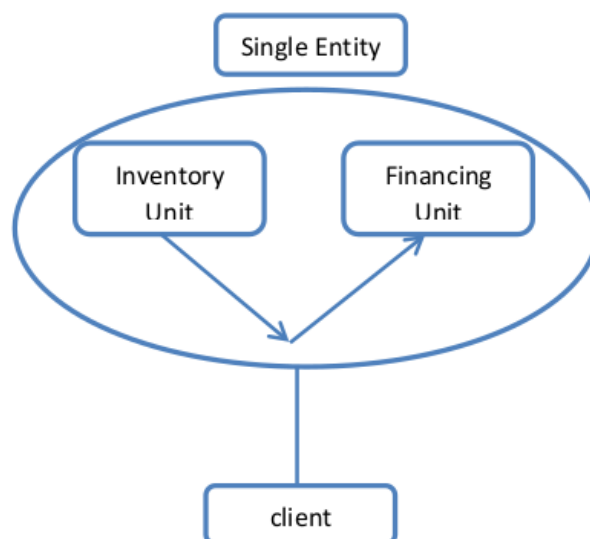
**Figure 1.**  
Murabaha financing scheme on the institutional model with purely financial intermediation



From figure 1, the demand for financing by a customer is faced by two different entities. The first is a financing entity for an intermediary institution, and the second is a business entity that is a customer need. However, because the financing entity adopts the intermediation model, one contract cannot solve the customer's needs. Then another entity is needed, which is an entity that meets the customer's business needs. Thus, at least a hybrid contract is needed to overcome this problem.

While in the Islamic financing model, financial institutions integrate financing and business schemes into one entity, such as cooperatives as regulated in Law no. 25/1992 or BSI with its Griya Swakarya product. Sharia economic contract can meet the customer's business needs to avoid combining several contracts, and *bilab* goals can be prevented. This can be depicted in figure 2 below.

**Figure 2.**  
Murabaha financing scheme on the institutional model with the integration of financial and business intermediation



If a customer wants to fulfill the needs of his business transactions, he just needs to go to one entity because the financing and inventory of the desired business assets are integrated in one entity. So that a sharia economic contract with the institutional entity can complete the desired transaction needs. So the contract is considered more resonant with all the requirements desired by the *maqāsid* as initiated by Habib Ahmed.

Another isomorphism can be observed in the provision of unlimited loan capital participation from third parties as regulated in Article 41 of Law No. 25/1992 or Article 66 of Law No. 17/2012, which the Constitutional Court has annulled. The provisions have the potential to create moral hazards by capitalist agents. Looking at several cases involving fraudulent investment modes using cooperative legal entities, with the limited supervision of the authorities, unlimited loan capital is promised irrational profits so that under certain conditions, it will result in default because the loan is recorded as an obligation that must be settled first before the distribution of the residual income (SHU).

Eventually, the cooperative will collapse. In other situations, this will also give birth to the moral hazard of other large capital owners to make cooperatives an attractive land for

loan sharks to maximize their profits, as has happened in several cases of online loans. Conditions such as making *maqāṣid* applications through the PDCA management model initiated by Habib Ahmed and Al-Ziyadat will be challenging to implement because, from the outset, the regulation has opened up space for agents with large capital owners, who have an interest in maximizing profits for their benefit, to take advantage of cooperative institutions. The application of PDCA management aims to achieve mutual benefits economically, socially, and environmentally, then the personal interests of these agents will conflict with the objectives of the *maqāṣid* application model.

In addition, the cooperative capital structure that undergoes a *co-optalism* process like this can also hinder the implementation of PLS (*mudaraba-musharaka*) contracts in cooperative financing. The orientation of large investors will undoubtedly be different from the purpose of the principle of mutualism in cooperatives. Large investors will feel more comfortable with debt-based financing contracts such as Islamic commercial banking practices.

### Conclusion

Seeing how sharia contracts can fulfill *maqāṣid shari'ah* in terms of an institutional economic approach as proposed by Habib Ahmed, this paper found that the liberal economic system still influences the dynamics of the development of cooperative regulations in Indonesia. This influence can be seen as global hegemony and interrelated national historical factors. The influence of financialization as one of the essential characteristics of capitalism was observed in Law No. 17/2012, which was later annulled by the Constitutional Court. The financialization of cooperatives resulted in contract products in cooperatives being alienated directly from the real economy so that the sharia contract structure will eventually follow the conventional banking contract structure pattern that adopts a hybrid pattern.

The hybridity of Islamic finance contracts, which is intended to replicate and achieve the same goals in conventional banking, can cause a contract to be trapped in a *bilab* so that the legal and social requirements in a contract initiated by Habib Ahmed will be difficult to achieve. On the other hand, the application of *maqāṣid* in the economic, social, and environmental sectors through PDCA management will also be challenging to apply to Indonesian cooperative regulations, which still open up space for large investors' capital

intervention as a moral hazard agent to achieve the goal of maximizing profit for personal interests. In addition, this capital structure can also hinder the application of PLS financing contracts as previously discussed. Agent moral hazard is when large investors take advantage of gap in the regulation to seek profit by utilizing cooperatives with a mass community base to make personal gains through their capital investments.

The problem of capital for cooperatives can be addressed with an institutional approach, for example, by forming a cooperative structure through the integration of cooperative communities with inter cooperative as contained in the Spanish cooperative regulations (Guadano, 2006). The principle of inter-cooperatives in cooperatives in Indonesia is still not good compared to European and East Asian countries. This approach is one of the effective ways to overcome capital by not neglecting the basics of mutualism.

Cooperatives need to be seen as a business model of institutionalism. Therefore, lawmakers need to think outside the box of the mainstream liberal economic framework and refer to an institutionalist approach to produce more constructive cooperative regulations for cooperatives in achieving the constitutional economic goals aspired by Indonesia's founding fathers.

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