

# **RISK MANAGEMENT IN THE PROVISION OF PEOPLE'S BUSINESS CREDIT AS IMPLEMENTATION OF PRUDENTIAL PRINCIPLES**

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## **Abstract**

*The bank is a financial institution that has an intermediary function that bridges the interests of parties who are excess funds (creditors) and those who need funds (debtors). Banks in channeling funds, among others, through the provision of credit to the public. However, loans issued by banks contain a lot of risk, one of them is People's Business Credit (KUR). Issues regarding the risks of granting credit above will be discussed in this study, which this study uses a normative juridical method using the statutory approach. This study shows the arrangements regarding risk management are regulated in PBI Number 11/25/PBI/2009 concerning the Application of Risk Management in Commercial Banks and in Regulation of the Financial Services Authority Number 18 / POJK.03 / 2016 Regarding the Implementation of Risk Management for Commercial Banks. The implementation of the prudential principle internally for a bank's Human Resources (HR) is to apply the Banking Risk Management Principles. Banking practices usually assess five aspects of debtors (the five C's analysis), namely: character, capital, capacity, economic conditions and collateral.*

**Keywords:** Risk Management; People's Business Credit (KUR); Prudential Principles

## **1. Introduction**

The bank is part of a financial institution that has an intermediary function that bridges the interests of the party with excess funds (creditors) and those who need funds (debtors). Based on this function, banks are referred to as intermediary institutions or intermediary institutions.<sup>1</sup> Besides having a general function it also has a special function that is directed as an agent of development, namely as an institution that aims to support the implementation of development and its results, economic growth and national stability towards improving the lives of many people.<sup>2</sup> The bank is part of a financial institution that has an intermediary function that bridges the interests of the party with excess funds (creditors) and those who need funds (debtors). Based on this function, banks are referred to as intermediary institutions or intermediary institutions.<sup>3</sup>

Banks in providing funds, among others, through the provision of credit is one of the sources of funds for development, because the wheels of the business world are highly dependent

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<sup>1</sup> Rahmani Timorita Yulianti, "Manajemen Risiko Perbankan Syari'ah", *Jurnal Fakultas Hukum UII* 3, No. 2 (2009): 151-165, p. 152

<sup>2</sup> Rahmani Timorita Yulianti, *Ibid.*, p. 153

<sup>3</sup> Lukmanul Hakim and Travilta Oktaria, "Prinsip Kehati-Hatian pada Lembaga Perbankan dalam Pemberian Kredit", *Keadilan Progresif* 9, No. 2 (2018): 164-176, p. 168

on loans issued by banks that will be used as capital for business, this is evident when in recent years the banking world was hit deterioration resulting in the impact of many entrepreneurs experiencing economic difficulties.<sup>4</sup>

Credit issued by banks carries risks so in its implementation banks must pay attention to sound credit principles, including:<sup>5</sup> a). Banks are not permitted to provide credit without written agreement; b). Banks are not permitted to give credit to businesses that from the beginning have been calculated to be unfair and will incur losses; c). Banks are not permitted to provide credit for the purchase of shares and working capital in buying and selling shares; ord). Providing credit exceeds the maximum lending limit.

Every credit especially the people's business credit must pay attention to the principles of prudence and sound banking principles, both internally and externally.<sup>6</sup> Externally, before a credit agreement is made, the bank always evaluates various aspects, by applying the provisions and its explanation in Act Number 10 of 1998 concerning Banking, banks are required to have confidence in the debtor's ability to repay loans on time, as agreed, the provisions regarding this guarantee materially refer more to the guarantee economically. Banking practices usually assess five aspects of debtors (the five C's analysis), namely: 1). Character; 2). Capital; 3). Capacity; 4). Economic conditions; and 5). Collateral.

The implementation of the prudential principle internally for a bank's Human Resources (HR) is to apply the Banking Risk Management Principles. Indonesian banking continues to experience significant changes in form and character.<sup>7</sup> The policies of the banking authority, the pressure of competition in the banking and financial markets as well as the demands for business performance and efficiency from stakeholders are increasingly dynamic causing banks to be proactively managed against business conditions and potential.<sup>8</sup>

The essence of the application of risk management is the adequacy of risk management procedures and methodologies so that the bank's business activities can be controlled within acceptable limits and benefit the bank. However, given the differences in market conditions and

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<sup>4</sup> Sulistya Adi Putra, "Evaluasi Sistem Dan Prosedur Pemberian Kredit Modal Kerja Dalam Upaya Meningkatkan Efektivitas Pengendalian Intern (Studi Pada PT. Bank Rakyat Indonesia Cabang Jombang Unit Plandaan)", *Jurnal Administrasi Bisnis* 27, No. 2 (2015): 1-10, p. 3

<sup>5</sup> Ikatan Bankir Indonesia, *Mengelola Bank Komersial*, (Jakarta Pusat: Gramedia Pustaka Utama, 2017), 183.

<sup>6</sup> Stefan Brehm, "Risk Management in China's State Banks-International Best Practice and the Political Economy of Regulation", *Business and politics* 10, No. 1 (2008): 1-29, p. 18

<sup>7</sup> Djoko Suhardjanto and Aryane Dewi, "Pengungkapan Risiko Finansial Dan Tata Kelola Perusahaan: Studi Empiris Perbankan Indonesia", *Jurnal Keuangan dan Perbankan* 15, No. 1 (2011): 105-118, p. 111

<sup>8</sup> Mario Tonveronachi, "Empowering Supervisors With More Principles And Discretion To Implement Them Will Not Reduce The Dangers Of The Prudential Approach To Financial Regulation." *PSL Quarterly Review* 63, No. 255 (2010): 361-376, p. 364

structure, size and complexity of the bank's business, there is no one universal risk management system for all banks, so each bank must build a risk management system in accordance with the functions and organization of risk management at banks.<sup>9</sup>

The existence of Risk Management is very important in the banking world. There are failures that occur in the banking world in Indonesia due to failures in implementing risk management, such as the risks that occurred in the 1997 monetary crisis when several business failures were eventually liquidated.<sup>10</sup> The inability of banks to pay their obligations can destroy not only the bank's shareholders, but also destroy third parties who place funds in the bank, this is an insolvency risk that comes from a drastic decline in the value of bank assets that cause bank capital decline. Therefore, seriousness and consistency are needed in conducting risk management for banks in Indonesia, especially in the provision of People's Business Credit (KUR).

Previous research relating to current research is research conducted by, Dewi Anggraini and Syahrir Hakim Nasution in 2013, this research focuses on the role of People's Business Credit (KUR) for the Development of MSMEs in Medan City.<sup>11</sup> Ashofatul Lailiyah in 2014, the research conducted focused on the 5C analysis of bank lending in minimizing risk.<sup>12</sup> As well as Lastuti Abubakar and Tri Handayani in 2017, the research conducted focused on the implementation of the banking prudential principle in Indonesia.<sup>13</sup> Based on previous research, although the theme is the same as the principle of prudence in lending, but the state of the art in this study is on risk management of the provision of People's Business Credit by banks as an effort to apply the prudential principle.

## **2. Methods**

The research is analytical descriptive, that is, this study examines and explains the problems of legal aspects related to the implementation of the bank's prudential principles. The method of approach used is the normative juridical approach, with emphasis on the study of

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<sup>9</sup> Lastuti Abubakar, "Implementasi Prinsip Kehati-hatian Melalui Kewajiban Penyusunan dan Pelaksanaan Kebijakan Perkreditan atau Pembiayaan Bank", *Jurnal Rechstidee* 13, No. 1 (2018): 62-81, p. 64

<sup>10</sup> Kasmir, *Bank Dan Lembaga Keuangan Lainnya*, (Depok: RajaGrafindo Persada, 2018), 221

<sup>11</sup> Dewi Anggraini and Syahrir Hakim Nasution, "Peranan Kredit Usaha Rakyat (KUR) Bagi Pengembangan UMKM Di Kota Medan (Studi Kasus Bank BRI)", *Jurnal Ekonomi dan Keuangan* 1, No. 3 (2013): 105-116, p. 105

<sup>12</sup> Ashofatul Lailiyah, "Urgensi Analisa 5c Pada Pemberian Kredit Perbankan Untuk Meminimalisir Resiko", *Jurnal Yuridika* 29, No.2 (2014): 217-232, p. 217

<sup>13</sup> Lastuti Abubakar and Tri Handayani, "Telaah Yuridis Terhadap Implementasi Prinsip Kehati-hatian Bank Dalam Aktivitas Perbankan Indonesia", *Jurnal De Lega Lata* 2, No. 1 (2017): 68-91, p. 68

secondary data, in the form of primary legal materials, namely legislation, secondary legal materials, both journals and the results of previous research and tertiary legal materials. Furthermore, the data obtained, both in the form of secondary data were analyzed in a qualitative juridical manner.

### **3. Result and Discussion**

#### **3.1 Prudential Principle in Credit Distribution**

Indonesian banking has an important function in economic development. In addition to its main function as an intermediary, which brings together the owners of funds (surplus of funds) with the users of funds (lack of funds), banks have a strategic role in driving the Indonesian economy, namely as agents of development, agents of services and agents of trust.<sup>14</sup> These three roles will work well if the intermediary function is working optimally. Banks become alternative financing for the business world and play a role in moving the economy by using funds entrusted by the public to banks. That is why banking is often referred to as the economic pulse, which drives the household sector, the business world, including micro-small businesses. The greater the distribution of funding to the business sector, economic development will increase, including income distribution through employment. This cycle puts banks as agents of development.<sup>15</sup>

Aside from being alternative financing, banks, especially Islamic banking, offer investment alternatives that can maximize the profits from funds entrusted to banks. Therefore, banks must be able to become agents of trust, trusted by both the owner of the fund and the user of the fund. Considering that the funds channeled by banks are third party funds, banks must be careful in their management.<sup>16</sup> That is why banks must pay attention to and implement the bank's prudential principles, as a form of bank accounts to third parties. In practice, this principle is dominantly used in the provision of credit or financing based on sharia principles.<sup>17</sup> This can be seen from the Bank's obligation to analyze credit or financing based on sharia principles is distributed.

The implementation of the principle of prudence in granting loans or financing aims to avoid the occurrence of bad credit or financing so that this principle is more interpreted as a way

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<sup>14</sup> Renny Supriyatni, "Tanggung Jawab Bank Syariah dalam Penerapan Prinsip Kehati-hatian dan Good Corporate Governance", *AHKAM: Jurnal Ilmu Syariah* 12, No. 1 (2012): 109-118, p. 110

<sup>15</sup> Ashofatul Lailiyah, *Op.Cit.*, p. 220

<sup>16</sup> Paripurna P. Sugarda, "Kontrak Standar: Antara Prinsip Kehati-Hatian Bank Dan Perlindungan Nasabah Debitur", *Mimbar Hukum-Fakultas Hukum Universitas Gadjah Mada* 20, No. 2 (2008): 193-208, p. 197

<sup>17</sup> Lastuti Abubakar, *Op.Cit.* p. 69

for banks to avoid bad credit/financing or bad credit. Non-performing loans / non-performing loans/financing are things that must be avoided by the Bank, bearing in mind that one measure in determining the Bank's soundness is the level of bank non-performing loans (NPLs).<sup>18</sup> Based on Article 2 of Bank Indonesia Regulation (PBI) No.13 / 1 / PBI / 2011 concerning Rating of Soundness of Commercial Banks, it is regulated that Banks are required to maintain and / or improve the Soundness of Banks by applying the principle of prudence and risk management in carrying out business activities.

In granting credit, based on Article 8 and explanation of Article 8 of the Banking Law, the implementation of the principle of prudence is translated as bank confidence based on in-depth analysis of good faith and ability, as well as the ability of debtor customers to repay their debts or repay their financing in accordance with the credit agreement. The same obligation is regulated in Article 23 of the Sharia Banking Law. To ensure that the precautionary principle is implemented properly, commercial banks must have and apply credit and financing guidelines based on sharia principles, by the provisions stipulated by Bank Indonesia.

As explained in the introduction, that confidence in the ability and ability of customers is an important factor that must be considered by banks.<sup>19</sup> Furthermore, to gain confidence, before giving credit or financing, banks must make a careful assessment of the character; capacity; capital; collateral; and business prospects (condition of economic), commonly known as the 5 C's analysis of credit.<sup>20</sup> In the explanation of Article 8, it is emphasized that collateral is one element in granting credit, so if based on other elements a confidence can be obtained on the ability of debtor customers to repay their debt, then collateral is only in the form of goods, projects, or collection rights financed with credit concerned.<sup>21</sup> This means compulsory collateral is the principal guarantee. In practice, to minimize the risk of bad credit, the Bank emphasizes the availability of collateral, both collateral, and additional collateral.<sup>22</sup>

The prudent banking principle is a principle or principle which states that banks in carrying out their business functions and activities must be prudent to protect public funds entrusted to them including in the distribution of funds originating from funds collected. Indonesian banks in conducting their business are based on economic democracy by using the principle of prudence.

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<sup>18</sup> Ashofatul Lailiyah, *Op.Cit.*, p. 220

<sup>19</sup> Roi Andang Sanjaya, Paramita Prananingtyas, and Siti Mahmudah, "Prinsip Kehati-hatian pada Pemberian Kredit oleh Pejabat Bank (Studi Kasus Pemberian Kredit oleh PT. Bni Tbk Kepada PT. Guna Inti Permata)", *Diponegoro Law Journal* 5, No. 4 (2016): 1-22, p. 17

<sup>20</sup> Renny Supriyatni, *Op.Cit.*, p. 111

<sup>21</sup> Lastuti Abubakar, *Op.Cit.* p. 72

<sup>22</sup> Ashofatul Lailiyah, *Op.Cit.*, p. 227

The principle of prudence referred to is a principle that confirms that financial institutions in carrying out business activities both in raising funds and especially lending to the public must be very careful.<sup>23</sup> The purpose of this precautionary principle is so that banks are always in a healthy condition to run their business properly and comply with the provisions and legal norms that apply in the banking world.<sup>24</sup> The precautionary principle stated in Article 2 and Article 29 paragraph (2) of the Banking Law, and as mentioned above, one of the indicators of bank health is the low value of the financial institution's NPL.

Explanation of the Banking Law which explicitly contains the substance of the precautionary principle can be observed, namely Article 29 paragraphs 2, 3 and 4 of the Banking Law. Article 29 explains as follows: 1). Banks are required to maintain the level of bank health by the provisions of capital adequacy, asset quality, management quality, liquidity, profitability, solvency and other aspects related to bank business and are required to conduct business activities by the principle of prudence; 2). In providing credit or financing based on Sharia principles and conducting other business activities, banks are required to use methods that do not harm the bank and the interests of customers who entrust their funds to the bank; 3). For the benefit of customers, banks are required to provide information about possible risks of loss in connection with customer transactions conducted through banks.

Letter of Approval from the Board of Directors of Bank Indonesia No. 27/162 / KEP / DIR dated 31 March 1995 concerning the obligations of commercial banks to make credit guidelines in writing. Based on this decree, each bank is required to make a written credit policy that can be used as a guide in daily lending. Guidelines in granting credit include, among others, demanding the application of the principle of prudence in the credit granting process.<sup>25</sup>

To support or guarantee the implementation of the decision-making process in bank management by the prudential principle, banks are required to have and implement an internal supervision system in the form of self-regulations.<sup>26</sup>

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<sup>23</sup> Roi Andang Sanjaya, Paramita Prananingtyas, and Siti Mahmudah, *Op.Cit.*, p. 18

<sup>24</sup> Liza Bayduri Nasution, et al, "Prinsip Kehati-hatian dalam Bisnis Kartu Kredit pada PT. Bank Negara Indonesia Sentra Bisnis Kartu Medan", *USU Law Journal* 3, No. 3 (2015): 72-83, p. 19

<sup>25</sup> Lailiyah.

<sup>26</sup> Maristella Pratiwi Damanik, and Moch Budiharto, "Pelanggaran Prinsip Kehati-hatian Dalam Penyaluran Kredit Komersil Oleh Pimpinan Bank (Kasus Pada PT. Bank Aceh Cabang Lhokseumawe)", *Diponegoro Law Journal* 6, No. 2 (2017): 1-14, p. 9

### **3.2 Arrangement for Application of Risk Management for Banks**

Risk management is a process of anticipating risks so that losses do not occur, Bank Indonesia (BI) as an independent Central Bank in Indonesia has confirmed its commitment to issue regulations that are driven by the application of banking risk management in accordance with international best practice by referring to the recommendations of the Bank for International Settlements through the Basle Committee on Banking Supervision.<sup>27</sup> BI establishes an obligation for banks to have risk management guidelines, clearer instructions regarding the intended risk management framework will be submitted several years later through PBI Number 5/8/PBI/2003 as amended by PBI Number 11/25/PBI/2009 concerning Application of Risk Management in Commercial Banks (hereinafter referred to as PBI on Risk Management). During this period, banks in Indonesia developed the principles and systems of risk management based on international best practices that are tailored to the needs of each bank. These principles are basically the standard for the banking world to be able to operate more cautiously within the scope of the rapid development of business activities and banking operations today.

After the regulation and supervision of the bank turned to the Financial Services Authority since December 31, 2013, in accordance with the mandate of Act Number 21 of 2011 concerning the Financial Services Authority (OJK). Banking regulation and supervision is currently carried out by OJK, thus BI will focus on controlling inflation and monetary stability. In enhancing the supervisory function of the OJK banks, they plan to strengthen risk management, which then published Regulation of the Financial Services Authority Number 18/POJK.03/2016 Regarding the Implementation of Risk Management for Commercial Banks. With the enactment of this POJK, the PBI concerning Risk Management is no longer valid. Whereas what is meant by Risk Management Article 1 number 3 POJK concerning Risk Management is a series of procedures and methodologies used to identify, measure, monitor and control risks arising from bank business activities.

In the world of business risk is always there, there is no business that is no risk, so at all times must be able to bear the risk, by minimizing the risk.<sup>28</sup> Risk is not enough to be avoided but must be dealt with in ways that can minimize the possibility of a loss. Banks that have high business size and complexity are required to implement Risk Management for all 8 risk

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<sup>27</sup> Andri Soemitra, *Bank Dan Lembaga Keuangan Syariah*, (Jakarta: Prenamedia Group, 2018), 59.

<sup>28</sup> Dewi Anggraini and Syahrir Hakim Nasution, *Op.Cit.*, p. 111

categories, namely Credit Risk, Market Risk, Liquidity Risk, Operational Risk, Compliance Risk, Legal Risk, Reputation Risk, and Strategic Risk.<sup>29</sup>

Basically, the types of risks faced by banks can be divided into 2 (two) large groups, namely: 1). Financial Risk Financial risk is related to direct losses in the form of loss of a sum of money due to the risks incurred, such risks include operational risk, legal risk, credit risk, liquidity risk, reputation risk and market risk; 2). Non-Financial Risk Non-financial risk related to losses that cannot be calculated clearly the amount of money lost. The financial impact of non-financial risks can not be felt directly and indirectly can make the bank a loss, but in turn non-financial risk has the potential to cause financial losses, such risks include reputation risk, compliance risk and strategic risk.

### **3.3 Implementation of Risk Management in the Provision of People's Business Credit (KUR) by Banks as a Prudential Principle of Banks**

The Bank's business activities are always faced with risks that are closely related to its function as a financial intermediary institution, especially risks in lending that have a significant impact on the survival of the bank's business. The rapid development of the external and internal environment of the banking system also causes increasingly complex risks in banking business activities.<sup>30</sup> Therefore, in order to be able to adapt in the banking business environment, Banks are required to apply Risk Management in providing credit, especially People's Business Credit (KUR).

Through the application of Risk Management, the Bank is expected to be able to measure and control the Risks faced in carrying out its business activities better. Furthermore, the application of Risk Management by banks will support the effectiveness of the Risk-based Bank supervision framework conducted by the Financial Services Authority.<sup>31</sup> Efforts to apply Risk Management referred not only to the interests of the Bank but also to the interests of customers. One important aspect in protecting the interests of customers and in the context of controlling Risk is the transparency of information related to the Bank's products or activities.

The application of risk management can vary from one bank to another according to the objectives, business policies, size and complexity of the business, financial capabilities,

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<sup>29</sup> Ikatan Bankir Indonesia., *Op.Cit.*, 167

<sup>30</sup> Etty Mulyati and Fajrina Aprilianti Dwiputri "Prinsip Kehati-Hatian Dalam Menganalisis Jaminan Kebendaan Sebagai Pengaman Perjanjian Kredit Perbankan", *Jurnal Acta Diurnal* 1, No. 2 (2018): 134-148, p. 138-139

<sup>31</sup> Lastuti Abubakar and Tri Handayani.*Op.Cit.*, 60



supporting infrastructure and human resource capabilities. The Financial Services Authority establishes this provision as a minimum standard that must be met by Indonesian banks in implementing Risk Management. With this provision, the Bank is expected to be able to carry out all its activities in an integrated manner in a risk management system that is accurate and comprehensive, particularly in the business activities of banks in providing funds through credit.<sup>32</sup>

Lending by the bank to customers due to trust after a thorough and thorough analysis of good faith and the ability and ability of prospective borrowers to repay their debts in accordance with what was promised. Providing credit means giving trust to the debtor by the bank even though the trust carries a high risk. Every bank credit must pay attention to the principles of prudence and sound banking principles, both internally and externally. Externally, before a credit agreement is made the bank always evaluates various aspects, by applying the provisions of Article 8 and its explanation in the Banking Law, banks are required to have confidence in the debtor's ability to repay loans on time, as agreed.

Banking practices before providing People's Business Credit (KUR) are required to conduct an assessment of five aspects to debtors or who are familiar with The Five C's of Credit Analysis (5C analysis), namely:<sup>33</sup> 1). *Character* or personality of the debtor is an important element in granting credit, which is meant by character is a good personal character, honest of the prospective debtor, namely those who always keep their promises and try to prevent despicable acts, and have a sense of responsibility. In this case, careful and thorough analysis of credit is needed to examine the curriculum vitae of the prospective debtor, how the reputation of the business environment; 2). *Capacity*, the target point for debtor assessment is the ability to control the business when the economy experiences sluggishness. Future business prospects, production and marketing, as well as raw materials, work equipment, financial administration, and even the ability to seize the market are at the bank's value; 3). *Capital*, in order to obtain credit from prospective borrowers, they must first have capital, the amount and capital structure of the prospective debtor must be investigated and their ratio and solvency levels are known. Banks cannot provide credit to entrepreneurs without any capital at all; 4). *Collateral*, collateral is usually defined as the property of the debtor which is used as collateral for the receivables. Considering that credit is always overshadowed by risk, to anticipate the emergence of this risk a guarantee is needed as a means of safeguarding the risks that may arise from the customer's

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<sup>32</sup> Etty Mulyati and Fajrina Aprilianti Dwiputri, *Op.Cit.*, p. 140

<sup>33</sup> Ashofatul Lailiyah. *Op.Cit.*, p. 228-229

promise being injured in the future; and 5). *Conditions of economic*, conditions or situations that have a positive impact on the business of prospective borrowers or as mentioned in the explanation of Article 8 of the Banking Act, namely the relationship of macroeconomic factors to the risk of its products. General economic conditions and conditions in the business sector of the loan applicant need attention from the bank to minimize risks that may arise due to economic conditions. This condition can be affected by social, political and economic conditions of a certain period and forecasts that will occur in the future.

Internally, the prudential principle for banks is that the bank's Human Resources (HR) is to apply the Banking Risk Management Principles. Indonesian banking continues to experience significant changes in form and character.<sup>34</sup> The policies of the banking authority, the pressure of competition in the banking and financial markets as well as the demands for business performance and efficiency from increasingly dynamic stakeholders cause banks to be proactively managed in terms of business conditions and potential.<sup>35</sup>

Banks are required to apply Risk Management effectively, both for Banks individually and for Banks on a consolidated basis with subsidiaries. Conventional Commercial Banks implement Risk Management which includes 8 risks, namely credit risk, market risk, liquidity risk, operational risk, legal risk, reputation risk, strategic risk, and compliance risk. Meanwhile, sharia banking business activities are inseparable from risks that can interfere with bank sustainability, and to manage these risks must implement risk management individually and on a consolidated basis in accordance with sharia banking business activities.<sup>36</sup> The application of Risk Management in Sharia banking is adjusted to the objectives, business policies, size, and complexity of the business and the ability of the Bank. Based on the Financial Services Authority Regulation Number 65/POJK.03/2016 Regarding the Implementation of Risk Management for Sharia Commercial Banks and Sharia Business Units, including Credit Risk, Market Risk, Liquidity Risk, Operational Risk, Legal Risk, Reputation Risk, Strategic Risk, Compliance Risk, Compliance Risk, Rate of Return Risk and Equity Investment Risk.

The scope of the application of Risk Management at least includes, among others, active supervision of the Board of Directors and the Board of Commissioners, which is the main line of defense to ensure that the bank he leads is running in a healthy manner and in compliance with

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<sup>34</sup> Putri, Elsa Yunita, "Pelaksanaan Pemberian Kredit Dengan Jaminan Resi Gudang (Bank Rakyat Indonesia Cabang Pekalongan)", *Unnes Law Journal* 2, No. 2 (2013): 87-96, p. 90

<sup>35</sup> Lastuti Abubakar. *Op.Cit.*, p. 79

<sup>36</sup> Ikatan Bankir Indonesia., *Op.Cit.*, 167

all applicable laws and regulations.<sup>37</sup> In order to carry out the authority and responsibilities of the Board of Directors must have an adequate understanding of the risks inherent in all functional activities of the Bank and be able to take the necessary actions in accordance with the Bank's risk profile.

Furthermore, the adequacy of policies and procedures for Risk Management and determination of Risk limits, at least includes, determination of Risks associated with banking products and transactions, determination of the use of measurement methods and Risk Management information systems, determination of limits and determination of Risk tolerance, determination of Risk rating assessments, preparation of plans emergency (contingency plan) in the worst conditions (worst case scenario); and establishment of an internal control system in implementing Risk Management. Whereas Risk Management procedures and determination of Risk limits must be adjusted to the level of Risk to be taken (risk appetite) for Bank Risk.

In meeting the adequacy of the identification process, banks need to collect and accumulate data about events, including losses that have occurred in the past, in other words, based on the experience of bank losses that have occurred. Measurement and monitoring of bank risk needs to determine risk oblique which is seen from the level of likelihood of occurrence and the impact of assessed risk.<sup>38</sup> Monitoring risk limits are not only aimed at transactions that exceed limits or activities that deviate from established policy lines. The Risk Management information system and internal risk control are effective in the implementation of business and operational activities at all levels of the Bank's organization, and are able to timely detect weaknesses and deviations that occur.

The risk categories associated with providing funds through credit include credit risk. Potential borrowers or debtor customers will fail due to their ability to fulfill their obligations in accordance with the agreement in the credit agreement.<sup>39</sup> This risk is caused by the debtor failing to carry out the content of the credit agreement, failing to choose a prospective debtor in the process of giving a bank's HR credit fooled by the appearance of the prospective debtor, in this case the importance of applying principle 5 C. For most banks, lending is the greatest source of credit risk. The high and low credit risk is influenced by several factors including credit

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<sup>37</sup> Maulina Yuliati and Moch Najib Imanullah, "Penerapan Prinsip Kehati-Hatian Bank Dalam Pemberian Kredit Dengan Jaminan Resi Gudang Di Bank Jateng Kantor Cabang Jepara", *Jurnal Privat Law* 6, No. 1 (2018): 133-142, p. 139

<sup>38</sup> Achmad Chosyali and Tulus Sartono, "Optimalisasi Peningkatan Kualitas Kredit Dalam Rangka Mengatasi Kredit Bermasalah", *Jurnal Law Reform* 15, No. 1 (2019): 98-112, p. 101

<sup>39</sup> Maulina Yuliati and Moch Najib Imanullah, *Op.Cit.*, p. 141

concentration, counterparty credit risk, and settlement risk. Credit concentration risk is the risk arising from concentrated provision of funds to 1 (one) party or group of parties, industries, sectors, and/or certain geographical areas that has the potential to cause substantial losses that could threaten the Bank's business continuity. Counterparty credit risk is the risk arising from the failure of the counterparty to meet its obligations and arises from types of transactions that have certain characteristics, for example transactions that are influenced by movements in fair value or market value. Settlement risk is the risk arising from the failure to deliver cash and/or financial instruments on an agreed settlement date from the sale and/or purchase of financial instruments.<sup>40</sup>

Another factor is the quality of credit analysts and the process of termination there is usually a connection with insiders, monitoring of the use of credit by the debtor, the quality of binding guarantees and overall economic conditions.<sup>41</sup> This risk must be understood, measured and identified before a facility is provided to the debtor customer. For this reason it is necessary to assess prospective borrowers on the following matters: debtor character and reputation in the market, good ownership and management, the collateral provided by the debtor meets the conditions of guarantee binding and the economic conditions that occur when facilities are provided such as competition, the type of product managed by the debtor customer.

Other risks associated with providing funds through credit are legal risks, exposures arising from weaknesses in juridical aspects, among others due to lawsuits, the absence of supporting legislation, changes in laws and external regulations that have a negative impact on operational capabilities.<sup>42</sup> Weaknesses of the agreement such as not fulfilling the legal requirements of an agreement or binding imperfect collateral.

The next risk is related to the distribution of funds through credit Operational Risk, namely Risks arising from inadequate or malfunctioning internal processes, human error or fraud, system failure in recording, recording and reporting transactions in a complete, correct and timely manner. Failure to comply with internal regulations or regulations, external problems such as changes in regulations or external events that affect the Bank's operations. Furthermore, Reputation Risk arises, among other things, due to the presence of media reports or publications and rumors regarding negative business activities of the Bank, as well as the existence of

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<sup>40</sup> Rahmani Timorita Yulianti. *Op.Cit.*, p. 163

<sup>41</sup> Desi Sistianti Permatasari and Moch Dzulkirom AR, "Analisis Sistem Akuntansi Pemberian Kredit Modal Kerja Dalam Upaya Meningkatkan Pengendalian Manajemen Kredit (Studi Pada Pt. bank Pembangunan Daerah Jawa Timur, tbk Cabang Nganjuk)", *Jurnal Administrasi Bisnis* 33, No. 2 (2016): 104-113, p. 111

<sup>42</sup> Andri Soemitra, *Op.Cit.*, p. 264

ineffective bank communication strategies. Negative public opinion of the bank's operations, resulting in a decrease in the number of bank customers or incurring large costs due to a court suit or a decline in bank income.

#### **4. Conclusion**

The regulation of banking risk management principles in Indonesia, through Bank Indonesia as the Indonesian banking regulator, has provided directives regarding commitments for risk management through Bank Indonesia Regulation (PBI) Number 11/25 / PBI / 2009 concerning Application of Risk Management in Commercial Banks (hereinafter referred to as PBI concerning Risk Management), which among others stipulates the obligation for banks to have risk management guidelines and instructions regarding the risk management framework. Then the Financial Services Authority Regulation Number 18/POJK.03/2016 concerning the Implementation of Risk Management for Commercial Banks, which regulates the improvement of identification, measurement, monitoring and risk control functions is intended so that business activities carried out by banks do not cause losses that exceed the ability of banks or that can interfere with the continuity of the bank's business.

The application of risk management to the provision of bank credit as a precautionary principle for banks is to include active supervision of the Directors and Board of Commissioners; the adequacy of Risk Management policies and procedures and the establishment of Risk limits; the adequacy of the process of identifying, measuring, monitoring and controlling Risk, as well as the Risk Management information system; and a comprehensive internal control system. Credit distribution is the biggest source of credit risk, high and low credit risk is influenced by several factors including credit concentration, counterparty credit risk, and settlement risk. Risks associated with lending are credit risk, operational risk, legal risk, and reputation risk.

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