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Strengthening the Deposit Insurance Corporation (LPS) with Authority as the Executor of the Restructuring Program (PRP)

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Abstract. *Public trust in banking is an important foundation for maintaining financial system stability. The formation of the Deposit Insurance Corporation (LPS) in Indonesia aims to protect customer funds and ensure the banking system's stability. This research aims to evaluate the effectiveness of LPS authority in implementing the Banking Restructuring Program (PRP) as mandated by Law No. 9 of 2016. The method used is descriptive analysis with a qualitative approach based on literature review and secondary data, including related regulations, the role of LPS in Indonesia, and comparisons with similar institutions in other countries. The research results show that LPS's authority, such as taking over problematic bank assets, providing liquidity, and implementing restructuring, has increased financial stability. However, challenges in the form of moral hazard are still the main issue. In addition, the success of LPS is highly dependent on the support of a strong legal framework and cooperation between financial institutions. In conclusion, strengthening LPS in implementing PRP can be an effective financial stabilization model, but it requires strict supervision to minimize negative impacts. The implications of this research highlight the importance of integrated policies between the government and the banking sector in facing potential crises in the future.*
Keywords: *Corporation; Deposit; Insurance; Stability.*

1. INTRODUCTION

Regulation and management of economic resources that are available, integrated, and fully utilized for the welfare of society is necessary for a country. As time passes, financial institutions, in general, and banking institutions, in particular, play increasingly strategic and important roles in driving the country's economy. As stated in Law No. 7 of 1992 concerning Banking, amended by Law No. 10 of 1998, banking institutions can actualize banking objectives, namely supporting national development to increase economic growth and national stability to improve people's welfare.

The Indonesian financial system consists of two categories: the monetary system and other financial institutions. The economic system includes the monetary authority and the public banking system, also known as commercial banks. According to Law No. 23 of 1999 concerning Bank Indonesia (Jo Law No. 3 of 2004 concerning Amendments to Law of the Republic of Indonesia No. 23 of 1999 concerning Bank Indonesia), Bank

Indonesia is responsible for monetary policy authority, usually referred to as the financial authority. [1]

Indonesian monetary policy entered a new era after ratifying Law No. 23 of 1999. Apart from being an independent institution, Bank Indonesia has one goal: achieving and maintaining stability in the value of the rupiah. Due to the floating money exchange rate system, Indonesia's monetary policy implicitly aims to maintain price stability. In other words, Bank Indonesia (BI) has one target: inflation. In early 2000, this new law went into effect. Since Bank Indonesia started setting the inflation target as the final target in its monetary policy, it has been an important part of the government's economic policy ever since, especially because the target is openly communicated to the public. Therefore, every economic policy in Indonesia must set an inflation target. [2]

Banks are one of the most important and influential financial institutions in people's lives, functioning as financial institutions offering credit and other financial services. Credit can be provided with your capital or funds from third parties or by circulating payment instruments in the form of demand deposits. Thus, banks do business with funds. Therefore, banks are very involved in the circulation of money as part of all financial-related activities carried out by the community. [3]

Mohammad Hatta, one of the founders of the Indonesian nation, said that banks are the pillars of society's progress, and if there were no banks around, progress would not occur as it does now. Underdeveloped countries have few good and correct banks. If they want to progress, companies must currently utilize banking services. [4]

The national banking system developed in five stages. These stages include rehabilitation and improvement from high inflation in 1967-1973, implementation of a net asset ceiling in 1974-1983, growth and deregulation in 1983-1988, acceleration in 1988-1991, and consolidation in 1991-1997 where at this stage, the principle of prudence -cautions are starting to be implemented, including capital adequacy and bank ratings. However, the crisis had already spread while the consolidation process was underway, and the bank's underlying conditions remained weak, including unresolved capital adequacy issue. Click or tap here to enter text.

Rehabilitation and improvement in inflation from 1967-1973 was the initial stage of the New Order government. These two policy characteristics then become the basis for assessing every policy made afterward. The emergence of Law Number 1 of 1967 concerning Foreign Investment (PMA) paved the way for the government's efforts to encourage the entry of foreign investment into Indonesia. From 1974 to 1984, Indonesia implemented an inward-looking policy (policies emphasizing economic development or domestic needs). In response to the large amount of foreign investment, especially from Japan, students staged a large demonstration in Jakarta on

[1] S H Hermansyah, (2014). *Hukum Perbankan Nasional: Edisi Kedua [Ed. Revisi]*. Kencana,

[2] Aulia Pohan, (2008). '*Kerangka Kebijakan Moneter & Implikasinya Di Indonesia'.* Jakarta: PT Raja Grafindo Persada,

[3] Muhammad Djumhana, (1993). '*Hukum Perbankan Di Indonesia', (No Title)*,

[4] Malayu S P Hasibuan, (2006). '*Dasar-Dasar Perbankan .* Bumi Aksara',

January 15, 1974. It was considered similar to an economic agreement. The Malari incident resulted in quite large losses due to the physical damage it caused. [5]

To counter the export industrialization strategy, Indonesia began implementing an import substitution industrialization strategy (also known as "inward-looking") in the 1970s. This strategy aims to prevent imports of certain products, especially high-tech products, because these products are already made domestically. The government deregulated the financial sector between 1982 and 1990, but only for state banking and not overall financial market liberalization. Indonesia's development paradigm, which is becoming more liberal, must also be considered in the current international structure. The development paradigm that is widely adopted is the paradigm that refers to the *Washington Consensus* (Washington deal), in addition to being driven by *bill depression*. Based on the *Washington Consensus,* The market is considered a universally effective method for allocating scarce resources and encouraging economic growth, which is influenced by the role of international financial institutions such as the World Bank and IMF, which motivate a country's government to avoid intervention in market mechanisms. [6]

Indonesia's economic crisis began in the second semester of 1997, preceded by a decline in the exchange rate. Indonesia's financial performance declined drastically due to this protracted crisis in various sectors. Because the Indonesian economy is very open and dependent on the foreign sector, the situation is worsening due to various fundamental weaknesses, especially at the micro level. [7]

In banking, the problems that caused the crisis came from various sources, one of which was a weak and inadequate regulatory system. This regulation causes financial institutions to be unable to be careful (*prudent*) *in* dealing with rising credit risks and rapid domestic price increases. When a bank is liquidated, customer deposits must be protected. Efforts to revitalize the banking industry require around IDR 650 trillion as capital injections when a bank is liquidated, so protection is needed for depositing customers. If we compare this with the United States, which already has the *Federal Deposit Insurance Corporation* (FDIC) as an institution responsible for protecting customer funds held in liquidated banks.[8]

The formation of the Deposit Insurance Corporation (LPS) was carried out by the Indonesian government on 22 September 2004 based on Law no. 4 of 2004 concerning the Deposit Insurance Corporation (LPS), which explains that public trust in the national banking industry is very important to maintain the stability of the banking industry so that a crisis does not occur again. Public confidence can be built through legal certainty in regulating and supervising banks and guaranteeing customer deposits, improving the continuity of healthy bank businesses, thereby increasing banks' role as funds providers for development and banking services.

Law no. 10 of 1998 concerning Amendments to Law no. 7 of 1992 concerning Banking mandates the establishment of a deposit insurance institution. Apart from that, the

[5] Syamsul Hadi, (2004). '*Strategi Pembangunan Indonesia Pasca* IMF', *(No Title),*

[6] Hadi.

[7] Zulkarnain Sitompul, (2007). *Lembaga Penjamin Simpanan: Substansi Dan Permasalahan* Books Terrace & Library,

[8] *Ibid*, p. 6-7.

Law contains other changes, one of which is that Conventional Commercial Banks can also conduct business based on Sharia principles. However, commercial banks based on Sharia principles cannot run business conventionally. Bank Indonesia grants business permits to carry out business activities. Bank secrecy is only limited to information about customers' status as depositors and the establishment of special institutions to make national banking healthy. [9]

In 1968, the idea of establishing a deposit insurance agency became a reality, as indicated in Article 30 of Law No. 13 of 1968 concerning the Central Bank, which states that "in the context of banking development, if the situation allows for greater guarantee of third-party money in question to banks, deposit insurance can be provided to foster public confidence in banking." [10]

Government Regulation (PP) no. 34 of 1973 concerning Guarantees for Money Deposits in Banks was created to implement the Central Bank Law. This regulation requires all banks, except foreign banks, to guarantee deposits in the form of current accounts, deposits, and savings. Bank Indonesia functions as an implementing guarantor, with a maximum guarantee of Rp. 1 million and a guaranteed premium of 0.5% (five thousandths) of total deposits in the bank. The banking industry rejected the PP because it caused additional costs, so it was not implemented and implemented at that time. Meanwhile, the banking sector is still in the process of consolidation. [11]

Law no. 9 of 2016 concerning Prevention and Handling of Financial System Crisis (UU P2SK) was enacted on May 15, 2016, almost twelve years after LPS was founded. Article 38 of the P2SK Law states that if a financial system crisis occurs and banking sector problems endanger the national economy, the Financial System Stability Committee (KSSK) provides recommendations to the president to determine the implementation of a restructuring program. This recommendation is included in the recommendations provided by the Financial System Stability Committee (KSSK). LPS implements the Banking Restructuring Program (PRP).

2. RESEARCH METHODS

This research uses a descriptive method with a qualitative approach to analyze the role and authority of the Deposit Insurance Corporation (LPS) in implementing the Banking Restructuring Program (PRP). The data used in this research consists of secondary data collected through a literature study. This data includes related regulations, official LPS reports, government policy documents, scientific articles, and relevant literature. Data analysis was carried out by identifying, comparing, and synthesizing various information regarding the legal framework, implementation of restructuring programs, and comparative studies with similar institutions in other countries. This research also pays attention to the historical context and dynamics of the Indonesian financial system to gain an in-depth understanding of the effectiveness of LPS's implementation of PRP. Data validation is carried out through source triangulation to ensure the accuracy and consistency of information. The analysis results are linked to key issues

[9] Djumhana.
[10] Hari Prasetya, (2016).*Mengupas Peran (Penting) LPS Dalam Sistem Perbankan* (Indie Publishing,
[11] Prasetya.

such as financial system stability, moral hazard, and efficiency in handling problematic banks, which provide a comprehensive picture of the implications of LPS authority in maintaining banking stability in Indonesia.

3. RESULTS AND DISCUSSION

3.1. Guaranteeing Customer Deposits in Banking in Various Countries

In large countries, namely the United States, Congress in the United States established pure deposit insurance. Members of Congress have attempted to adopt the Act for nearly fifty years. The United States National Deposit Insurance Act in 1933 was able to be adopted because of the progress of the times, the persistence of the Chairman of the Banking and Currency Committee in the House of Representatives, and the fact that there was great support from two groups that previously had different goals and interests (*divergent*), namely groups that seek to end the banking system, and groups that seek to continue the banking system. Looking back at the history of New York, it is known that there was a new governor and threats related to banking problems in 1829. With Martin Van Buren as the new governor, during his leadership, many problems arose because many bank programs or articles of association would expire in the next few years. There will be great public dissatisfaction with the current banking system in the future. Several ideas emerged at that time, such as eliminating all banks or creating a state-branch banking system owned and operated by the states. [12]

A businessman from Serakusa named Joshua Forman drafted a plan that became a reference for the governor, which was then submitted to the legislative body three weeks later. This law regulates insurance funds that all banks must deposit as a condition for renewing their charter (articles of association), indicates that the board of commissioners has full authority over regular bank inspections, and invests in state bonds or mortgages that are properly maintained. The basis of the guarantee plan itself is a fund called a "security fund." These funds are collected with the condition that each participating bank must pay an assessment fee to the State Treasurer of half or one percent of the paid-up share capital so that the total cost paid is three percent of the share capital.

Not long afterward, two other states, Vermont and Michigan, adopted the New York Bank Act. The guarantee (insurance) system will immediately be rigorously tested. After the Panic of 1837, there was one of the longest and deepest depressions in the country's history. The guarantee system collapsed when many bank failures in Michigan led to an inability to meet the obligations of the guarantee fund (insurance). Almost all insured (guaranteed) banks were frozen in 1841, and the guarantee system also ended the following year. The system made no payments to creditors of failed banks during its six years of operation. [13]

Before the economic depression in 1930, 1,493 banks in the United States failed in 1928/1929. Many other banks also closed until 1933. By providing guarantees to customers who held deposits through the *Federal Deposit Insurance Corporation (FDIC)*, emergency *bank panic* (bank panic) could have been prevented, and the domino effect that hit US banking at that time could have been stopped. Most causes

[12] Carter H Golembe, (1960), 'The Deposit Insurance Legislation of 1933: An Examination of Its Antecedents and Its Purposes', *Political Science Quarterly*, 75.2 181–200.
[13] Golembe.

of bank closures are problems at the micro level, such as speculative financing in stocks and real estate, loans to groups of individuals, management incompetence, careless lending, poor management, and greed. [14]

The FDIC was established under the Banking Act of 1933 in response to three years of bank failures in the United States that made people worry about their money in banks and withdraw their deposits to be kept in the form of *hoarding*. The FDIC initiated its ability to prevent bank panic, or "bank panic," by giving deposit holders confidence that their deposits would return. Later, the FDIC developed into an institution whose role was to guarantee deposits and regulate and examine banks in its jurisdiction. The FDIC is led by a board of three people, with the *comptroller of the currency* as one of its members.[15]

The Malaysian government formed the *Malaysian Deposit Insurance Corporation (PIDM)* in 2005 to provide benefits *takaful* and insurance, which protects bank deposits when the bank fails to pay. PIDM is a government institution established through the Law on *Deposit Insurance Corporation of Malaysia (PDIM Act)*.

PDIM was founded based on the *Laws of Malaysia Act 642* and the *Malaysia Insurance Corporation Act 2005.* This institution handles two financial consumer protection systems: the Bank Deposit Protection System (DIC), which protects bank depositors, and *takaful & Insurance Benefits Protection* or Insurance Benefits Protection (TIPS) for certificate holders *Takaful* and insurance policies. Initial regulations relating to PDIM, namely *Laws of Malaysia Act 642* Malaysia Insurance Corporation (Act 2005), include an article explaining the scope of protection entitled "*Scope of Coverage*." In the 2005 Law, no article regulates benefits for insurance policyholders, whether based on conventional or Sharia insurance. However, the article states that deposits guaranteed by PIDM can include traditional and Islamic (sharia) deposits, with a maximum return limit of 60,000 ringgit. [16]

Research conducted by Vasso Loamide and Jan de Dreu in Bolivia between 1998 and 2003 found that when banks offered high interest rates, deposit insurers would discourage savers from monitoring the banks. This will impact the bank's level of discipline in managing its business. Most researchers agree that banking is still a research subject because it raises pros and cons regarding possible disruptions in market discipline due to *moral hazard* (moral hazard). Decreased market discipline and moral hazard will indirectly cause instability in the banking industry. [17]

Additionally, many parties directly affected by deposit protection contracts may experience moral hazard (*moral hazard*). For example, the easing of fear of large withdrawals allows those who are not legally involved in the contract to change their behavior, and sometimes, in a sad way, borrowers choose to borrow from troubled

[14] Hendy Herijanto, (2021). *Selamatkan Perbankan! Demi Perekonomian Indonesia*. Expose,
[15] Elyana Novira, (2022). 'Restrukturisasi Bank Gagal Oleh Lembaga Penjamin Simpanan Dalam Sistem Perbankan Nasional' (Universitas Bung Hatta,
[16] Putri Nurul Hidayati, (2022), 'BENTUK KELEMBAGAAN PROGRAM PENJAMINAN POLIS DI INDONESIA (STUDI PERBANDINGAN ANTARA INDONESIA DENGAN MALAYSIA DAN KOREA SELATAN)', *" Dharmasisya" Jurnal Program Magister Hukum FHUI*, 2.1 36.
[17] Diana Ria Winanti Napitupulu, (2010). 'Lembaga Penjamin Simpanan Di Indonesia (LPS)', *Bumi Intitama Sejahtera*,

institutions rather than borrow from banks, which is healthy and avoids the risk of having credit decided by the acquirer or liquidator of a bank that has failed to pay.[18]

The results of experiments on the credit (loan) market show that guarantee schemes with high guarantee limits cause behavior *moral hazard*, especially in small banks when high guarantee limits are indicated by offering relatively high loan interest rates. High loan interest rates result from small banks' decisions to invest in high-risk projects. The research also found that individuals' mental maps regarding the LPS guarantee scheme include output, calm, happiness, and comfort. Customers and bankers also consider LPS to function to regulate regulations, overcome problems, and save from financial crises. [19]

In Japan, Deposit Insurance is managed by the *Deposit Insurance Corporation of Japan (DICJ).* DICJ is led by *the Policy Board* (policy council), which consists of eight members, including the governor and deputy governor, with the governor acting as chairman of the *Policy Board* (policy council). The Board may have up to four interim members as necessary to study and discuss specific issues. With the approval of the Prime Minister and Minister of Finance, the Governor of DICJ will elect members and interim members for *The Policy Board* (Policy Council) of people with experience and expertise in finance. Selected members come from various sectors, including the financial industry, such as the chairman of the Japan Bankers Association, business, academia, and other communities.[20]

DICJ has carried out its function as a deposit insurance institution. One example is Ashikaga Bank, which reported in November 2003 that it had debts that exceeded its assets. This bank is considered to have failed because it has a capital adequacy ratio of 3.7 percent. In accordance with the requirements set by the Financial System Management Commission (*Financial System Management Council* or FSMC), DICJ acquired Ashikaga Bank. Ashikaga Bank must operate banking services as usual in accordance with Kemudinan's orders to the *Financial Service Agency* to reduce the effects of failure on the regional economy. In addition, it must provide liquidity to good and healthy borrowers.[21]

With the Prime Minister's Decree Number 218/1999 QD TTG dated November 9, 1999, the Vietnam Deposit Insurance Corporation or *The Deposit Insurance of Vietnam* (DIV) is designated as a state institution whose aim is to help maintain the stability and healthy development of banking institutions and support their growth. As said by the *International Association of Deposit Insurance (IADI)*, savings insurance coverage and coverage ratio/GDP per capita should be equal to 2 and equivalent to the average ratio in other countries with the same level of development. Fixed deposit insurance coverage is paid on all types of savings, including principal and returns (*return). A* deposit owner is 50 million Vietnamese Dong/VND. Savings insurance coverage in

[18] Grillian Gracia, (2022), *IMF Working Paper, Deposite Insurance and Crisis Management, Monetary and Exchange Affair Departemen*, Authorized for Distribution by Charles Enoch, March p. 6.
[19] M Purwanto et al, (2018). 'Analisis Perilaku Nasabah Penyimpan Dan Bank Terhadap Skema Penjamin LPS, Monograf Riset Stabilitas Sistem Keuangan', *IMF Working Paper*,
[20] DICJ, dic.go.JP/english/e_kikotoha/page_000064.html.accessed on 15 June 2024, at 14.50 WIB
[21] *Ibid.*

Vietnam is lower than the minimum level suggested by IADI, based on various criteria.[22]

Currently, seven Southeast Asian countries have official deposit insurance systems, namely Indonesia, Malaysia, the Philippines, Singapore, Thailand, Laos and Vietnam. Vietnam is included in the group of countries with the lowest deposit insurance coverage compared to recommendations from international organizations and other Southeast Asian countries. Bin Thi Thanh Dao cited information from the International Monetary Fund, stating that:

a. The Indonesian state covers deposit insurance of IDR. 2 billion ($174,000), with a guaranteed deposit percentage of 99%.

b. Malaysia provides coverage of MYR 250,000 ($77,000), with a guaranteed deposit percentage of 99%.

c. The Philippines covers deposit insurance up to PHP 500,000 ($11,500), with a guaranteed deposit percentage of 97%.

d. The State of Singapore covers up to USD 50,000 ($50,000) with a guaranteed deposit percentage of 90%.

e. Thailand covers up to THB 50,000,000 ($1,539,000) with a percentage of 99%.

f. Vietnam covers deposits of up to VND 50,000,000 ($2,300), with a guaranteed deposit percentage of 87%.

Countries have implemented deposit insurance systems for a variety of reasons, including to (1) protect small deposit holders through providing immediate payment mechanisms or transfer of guaranteed (insured) portions of savings; (2) increase public confidence and system stability by establishing a framework for resolving bank failures decisively and quickly, and preventing such failures from spreading; (3) increase the amount of savings and stimulate economic growth; (4) empowering small and new banks to be able to compete with large banks and/or state-owned banks; (5) determine the limits of the impact of failed bank losses on the government; and (6) demanding that a bank or group must assist in resolving a failed bank. Therefore, the main reason for using a guarantee system is to protect small deposit holders and increase stability by strengthening the intensive structure, which includes a strong exit frameworkt.[23]

Every country needs a clear framework to resolve problematic banks. If it doesn't already exist, the creation of deposit insurance provides an opportunity to create and enforce laws and institutional frameworks that will help authorities intervene, sell, or close down troubled banks. A clear legal framework will prevent costly delays and give banks more opportunities to resolve their issues to maintain financial system stability. However, it is important to ensure that the legal framework of the deposit insurance

[22] Binh Dao, (2014). 'Deposit Insurance and Bank Risks in Vietnam', *Available at SSRN 2543048*,
[23] Gillian G. H. Garcia, *Good Practices For Deposit Insurance, International Monetary Fund*, January 2000, https://www.imf.org/external/pubs/op/197/, accessed on 20 June 2024, at 15.50 WIB

system is adequately reflected in banking law and does not conflict with other laws, such as laws regarding companies and commercial and personal bankruptcy, as well as company regulations.[24]

A well-crafted deposit protection system can help run well while reducing government spending. If this system is implemented: (1) in situations where banks have sufficient ability to pay their debts (or perhaps restructure their debts); (2) through adequate and careful support and supervision; and (3) combined with policy *lender of last resort* (LDLR) that is properly designed by a central bank or other entity. The major scandals that occurred in the savings and loan industry in the United States in the 1980s demonstrated that faulty deposit insurance systems can weaken internal controls, hinder markets, and make supervision difficult.[25]

3.2. The Deposit Insurance Corporation in Indonesia

Public or community trust in the national banking industry is very important to keep the banking industry stable and prevent a recurrence of crises. The existence of legal certainty in regulation and supervision, as well as guaranteeing customer deposits, can increase this trust. During the monetary and banking crisis, public confidence in the banking industry was restored through policy *blanket guarantees* or guaranteeing all bank obligations. However, this very broad guarantee gives rise to *moral hazards (moral hazards*) for bank managers, customers, and the state budget. The nature of customer deposit guarantees carried out by LPS is limited but can cover as many customers as possible. Every bank operating in Indonesia is required to participate in this program and pay a guaranteed premium. [26]

According to Article 4 of Law no. 4 of 2004 concerning LPS, the functions of LPS are:

a. As guarantor of customer deposits; And
b. To actively participate in maintaining the banking system's stability in accordance with its authority.

The LPS Law also stipulates that the maximum deposit value for each customer at one bank is IDR 100 million. The current value of guaranteed savings has been changed to IDR 2 billion according to Article 1 of Government Regulation no. 66 of 2008 concerning the Amount of Deposit Value Guaranteed by LPS, which confirms that the value of deposits guaranteed for each customer at one bank, which was originally set at a maximum of IDR 100 million based on Article II paragraph (1) of the LPS Law, is now changed to a maximum of IDR 2 billion based on this government regulation. However, these regulations are implemented in stages with the following framework:[27]

a. During the first 6 (or six) months of LPS operations, namely from September 22 to March 21, 2006, all deposits, including checking deposits, certificates of deposit, time deposits, and the like, were guaranteed.

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[24] *Ibid.*
[25] *Ibid.*
[26] Penjelasan Umum Undang-Undang No. 24 Tahun 2004 tentang Lembaga Penjamin Simpanan.
[27] Adrian Sutedi, (2010). 'Aspek Hukum Lembaga Penjamin Simpanan (LPS)', *Sinar Grafika, Jakarta*

b. Furthermore, for the next six (six) months, from March 22, 2006, to September 21, 2006, the maximum guaranteed deposit amount is IDR 5 billion.
c. For the next six (six) months, from 22 September 2006 to 21 March 2007, the guaranteed deposits will be IDR 1 billion. Starting March 22, 2007, the maximum guaranteed deposit amount is IDR 100 million. However, according to Article 1 of Government Regulation no. 66 of 2008, which was stipulated based on Article 11 paragraph (1) of the LPS Law, the amount of deposits guaranteed for each customer at one bank, which was previously set at IDR 100 million according to Article 11 paragraph (1) of the LPS Law was changed to a maximum of IDR 2 billion according to the Regulation this government.

A guaranteed interest rate is required because LPS is an indirect mandate from the LPS Law, especially which contains provisions regarding claim payment requirements. Claims cannot be paid if: [28]

a. Deposits are not officially registered with the bank.

b. Customers receive special or unfair treatment regarding interest rates, and

c. Customers are the parties who cause bank problems.

About point (2) above, the LPS regulations explain that what is meant by the phrase unreasonable is when a customer receives a guaranteed interest rate that is the same as the highest deposit interest rate that the LPS can guarantee. The word guaranteed is defined as public savings that will not be lost even if the bank is closed.

President Franklin D. Roosevelt's statement, *"After all, there is an element in the readjustment of our financial system more important than currency, more important than gold, and that is the confidence of the people,"* shows how important public trust is in banks. In addition, the absence of a deposit guarantee system that guarantees customers holding deposits when a bank is liquidated reduces public confidence in banking institutions. [29]

Ben S. Bernanke, Douglas W. Diamond, and Philip H. Dybvig received the 2022 Nobel Prize in Economics for their research, emphasizing how important it is for bankers to maintain customer trust. Customers' distrust of bankers can have a domino effect on other banks. The importance of deposit insurance—or, more precisely, deposit insurance institutions—which almost all countries now have—is another important point of research conducted by Bernanke, Diamond, and Dybvig. [30]

Deposit insurance institutions must pay several fees to maintain their functions in the banking industry. The costs associated with the implementation of deposit insurance are divided into two categories: direct costs (*direct cost*), which include operational costs, payment costs (*payment cost*), opportunity costs (*opportunity cost*), and indirect costs (*indirect cost*). Indirect costs (*indirect cost*) are especially related to implementing deposit insurance in increasingly strict regulations. Several factors

[28] *Ibid.*
[29] Sitompul.
[30] Elyana Novira, (2022). 'Kepercayaan Nasabah Dan Risiko Sistemik, Dimuat Pada Koran Harian Singgalang', *Nobel Ekonomi*,

influence these costs, such as the possibility of bank failure, the concentration of funds in foreign banks or banks, and the public's respect for monetary authorities. [31]

LPS in Indonesia has an initial capital of at least 4 billion rupiah, with a maximum of 8 billion rupiah being separated state assets. LPS is responsible for managing all its businesses and investments.[32]

Article 8, paragraph (1) of the LPS Law mandates that every bank operating in the territory of the Republic of Indonesia must become a guaranteed participant. This mandate is contained in LPS Regulation (PLPS) no. 1 of 2023 concerning the deposit guarantee program, which states that every bank licensed to operate in the territory of the Republic of Indonesia is declared a guaranteed participant. However, the obligation to become a guaranteed participant does not apply to the Village Credit Agency.[33] On January 12, 2023, Financial Law Number 4 of 2023, which aims to develop and improve the financial sector, was promulgated, and PLPS Number 1 of 2023 was issued in connection in addition to that. Several changes in regulations affect LPS institutions and operations in guaranteeing deposits from deposit-holding customers. These changes include guaranteeing premiums, handling deposit insurance claims, and handling objections complained about by customers who own deposits.

According to the provisions regarding minimum capital requirements set by the OJK, the membership contribution is 0.1% of the bank's paid-up capital. This premium is given to banks, which are branch offices of banks domiciled abroad. The balance guaranteed by LPS is 2 billion rupiah. Payment of guarantee claims to customers holding deposits is based on deposits eligible to be paid according to the reconciliation results. Payment is made in cash or by other means equivalent to deposits that are eligible to be paid. Each claim is paid using rupiah currency. Suppose the guarantee claim is in foreign currency. In that case, payment is made in the equivalent of rupiah based on the currency value issued by Bank Indonesia on the date the bank's business license is revoked.

Suppose the deposit date of the depositing customer is not recorded at the bank. In that case, the depositing customer is the party who benefits unfairly, or the bank's condition is unhealthy, so the guarantee claim is not worth paying.

When the COVID-19 pandemic hit the world in 2020, the Indonesian government issued Law No. 2 of 2020 to address financial system stability issues by LPS. Government Regulation (PP) no. 33 of 2020 establishes implementing regulations to deal with threats that endanger the economy and financial system stability. Article 2 Government Regulation no. 33 stipulates that the scope of the PP includes handling financial system stability issues by LPS. Furthermore, Article 11 Paragraph (1) states that LPS is given new authority to place funds during the economic recovery due to the Covid-19 pandemic. [34]

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[31] Sjafruddin Sjafruddin, 'Sistem Penjaminan Simpanan (Deposit Insurance System) Pada Industri Perbankan Indonesia', *At-Tijarah*, 1.2 (2019), 77–90.
[32] Article 81 no. (1), (2), (3) UU LPS
[33] Article 2 no. (2) dan (3) PLPS No. 1 of 2023.
[34] Novira, 'Restrukturisasi Bank Gagal Oleh Lembaga Penjamin Simpanan Dalam Sistem Perbankan Nasional'.

LPS's authority was expanded by Law No. 9 of 2016 concerning the Prevention and Handling of Financial System Crisis (UU PPKSK), as regulated in Article 15. Article 15 as a whole states that the Financial System Stability Committee reports to the president regarding:

a. Financial system stability conditions every 3 (three) months;

b. How to handle a financial system crisis;

c. Resolving Systemic Bank problems and/or

d. Implementation of the banking restructuring program by the Deposit Insurance Corporation.

To safeguard the country's economic interests and resilience, KSSK prevents and handles financial system crises. KSSK has members consisting of (a) the Minister of Finance as coordinator and a member who has voting rights, (b) the Governor of BI who has voting rights, (c) the Chairman of the OJK Board of Commissioners who does not have voting rights, and (d) the Chairman of the Board of Commissioners LPS has voting rights. The report provided by the KSSK to the President regarding the implementation of the PRP by the LPS is the same report regarding the LPS that has been evaluated and recorded by the KSSK.[35]

Furthermore, Article 38 of the PPKSK Law concerning banking restructuring in the financial system crisis provides the following explanation:

a. KSSK advises the President to decide on implementing the PRP in the event of a financial system crisis and banking sector problems that endanger the national economy.

b. One of the recommendations provided by KSSK is suggestions or recommendations regarding implementing PRP.

c. LPS is responsible for organizing the PRP.

3.3Banking Restructuring by LPS

Say "*restructure*" comes from the word "restructuring," which means "rearranging something into a system or reorganizing a company in a different way than before or rearranging something into a system. According to the Big Indonesian Dictionary, "restructuring" means "rearranging (so that the structure and the order are good)." Click or tap here to enter text.

This program includes economic stabilization and recovery packages in various countries with effective banking restructuring. The fact that microbanking restructuring also requires controlling significant macroeconomic impacts supports the motivation underlying this strategy. By recognizing that there are many macro and monetary elements, including efforts to prevent national payment systems from collapsing due to systematic savings flight, which often requires emergency action in the form of

[35] Explanation Article 15-d, UU PPKSK.

providing liquidity by the central bank as *lender of the last resort* (lender as a last resort? Therefore, banking restructuring in the countries mentioned above is usually planned comprehensively and includes efforts taken to make each bank and banking system healthy and consider how this will impact microeconomic recovery. Conflict is often unavoidable when achieving micro and macro goals. However, experience in the countries mentioned above shows that conflict can be avoided by minimizing instruments of *moral hazard* (danger), taking advantage of limited costs, and creating a healthy, intensive system for bank owners and managers to get used to consistently maintaining bank health. [36]

It is known that many countries implement three aspects as a banking destructuring strategy: [37]

a. Strategy to immediately stabilize the banking and financial system to reduce the crisis, restore depositor confidence, and protect the payment system. However, when there is a systemic crisis with significant savings flight, the policy options and tools available are very limited. Therefore, in many countries, the Central Bank functions as a *last-resort lender and provides* other emergency liquidity, such as convenience *overdrafts* for banks, when traditional liquidity facilities are inadequate. Extensive guarantee schemes have been implemented for creditors and depositors to stabilize the financial system in several countries, such as Sweden, Turkey, Finland, Thailand, and Korea. However, this strategy will depend heavily on the ability to reduce moral risk through non-monetary penalties such as management replacement, seizure of assets and bank ownership, and so on.
b. Strategy for resolving bank solvency (stock) problems. After the crisis has been resolved, banking restructuring aims to restore banking financial health by carrying out financial restructuring, which includes restructuring assets and liabilities. In many countries, the instruments used differ greatly depending on the source and intensity of the problem. They also differ in how they influence monetary and fiscal conditions, distribute losses imposed on governments, bank owners, creditors, and depositors, and how effective the recovery of non-performing loans is (*loan recovery*). This will be very important for reducing *moral hazard* (moral hazard) and independent monetary control.

c. Strategy to resolve bank solvency (stock) problems. Once the crisis is under control, banking restructuring is directed at restoring the health of the banking financial position through financial restructuring (*financial restructuring*), both on the asset and liability side. The instruments used in many countries vary greatly depending on the source and intensity of the problems faced, namely the impact of the instruments used on monetary and fiscal conditions, the distribution of losses borne by the government, bank owners, creditors, and depositors, as well as the effectiveness of recovering problematic loans (*loan recovery*). These will be critical for independent monetary control and reduction of *moral hazard*.

[36] Halim Alamsyah, (1998), 'Restrukturisasi Perbankan Dan Dampaknya Terhadap Pemulihan Kegiatan Ekonomi Dan Pengendalian Moneter', *Bulletin of Monetary Economics and Banking*, 1.3 121–45.
[37] Zulfi Diane Zaini, (2012), 'Lembaga Penjamin Simpanan Dan Fungsinya Terhadap Penyelesaian Bank Gagal Di Indonesia', *KEADILAN PROGRESIF*, 3.2 40–41.

d. Strategies to help banks run well again. Restructuring a bank's financial position can only be done with operational restructuring, namely improving the bank's external environment. Therefore, the banking restructuring strategy at the operational restructuring stage aims to correct deficiencies in the accounting system, banking sector configuration, and legal framework that could influence banking operations in the future. The actions taken in many countries are related to efforts to build banking systems that can encourage market discipline (*market discipline*) through competition and firm policies. This will also involve improving elements of the legal framework *supervision* banking from the perspective of banking authorities.

For example, Sweden succeeded in restructuring its banks quickly and cheaply thanks to strong political and legal support. In other cases, the resolution of banking crises is often delayed due to the need for a shared vision and an independent and strong banking restructuring control body. Seeing these findings, Andrew Sheng (1992) concluded that the following general conditions are necessary for the success of banking restructuring:

a. The realization of stable macroeconomic conditions and a competitive real sector.
b. Strong political will to carry out effective banking changes or restructuring.
c. Legal provisions (*legal framework*) which can create financial discipline.

These four aspects indicate that the consistency of the banking restructuring program with the micro, institutional, and legal regulations that underlie the banking system will determine the smoothness and success of the program. Two indicate how important political and legal support is in banking and restructuring. Click or tap here to enter text.

Reported by the Indonesian Information Portal: Indonesia.GO.ID, Indonesia still maintains macroeconomic stability and liquidity amidst global economic uncertainty. Indonesia's Balance of Payments (NPI) recorded a surplus of USD 6.5 billion in the first quarter of 2023, up from a surplus of USD 4.7 billion in the fourth quarter of 2023. The balance of payments consists of five main components: the current account balance, capital balance, and balance sheet. Financial, net calculation differences, and monetary traffic balance. The balance of payments is a record that summarizes transactions carried out by residents of one country with residents of other countries during a certain period.[38]

Indonesia can grow by 5.05% (yoy) in 2023, higher than the general estimate (*consensus forecast*) of 5.05%, driven by trade, domestic demand, and the processing industry. During the general election campaign, consumption of LNPRT (Household Non-Profit Institutions) also increased. Indonesia's general inflation of 2.57 percent is quite controlled and remains within the target range of 2.5-1%. Indonesia's inflation has been well controlled over the last five years, being below the average for ASEAN-5,

[38] Indonesia.GO.ID, *Portal Informasi Indonesia*, https://Indonesia.go.id, accessed on 17 July 2024, at 15.22 WIB.

developing, and developed countries. There are two main indicators for Indonesia's macroeconomy: economic growth and inflation.[39]

Law Number 4 of 2023 concerning Financial System Stability, an Omnibus Law for the financial sector, states that the PRP established as a mandate shows the readiness of the Indonesian state to implement a banking restructuring program if restructuring is necessary. Article 41 Chapter XXI of the Law states:

1) When implementing PRP, LPS has the authority to:

a) Take over and exercise all rights and authority of organs equivalent to shareholders and the GMS.

b) Take over and exercise all rights and authority of the Bank's directors and board of commissioners or other equivalent organs.

c) Postponing payment of certain obligations from the bank.

d) Selling, auctioning, or transferring bank assets directly or abroad through a public offering.

e) Selling, auctioning, or transferring bank bills and/or handing over management to another party without requiring the debtor's customer's approval.

f) Transfer the management of all or part of the bank's assets, activities, and/or management to another party.

g)) Make temporary capital investments in banks directly or through converting LPS claims to banks into shares.

h) Converting bank obligations to certain creditors into capital.

i) Collect bank receivables that are certain through issuing a forced letter.

j) Taking over land and buildings belonging to banks that other parties, either alone or with the assistance of authorized state law enforcement control.

k) Study and check to obtain necessary information from and about banks, both independently and with the assistance of authorized state law enforcement agencies.

l) Calculate and determine the losses experienced by the bank and charge the losses to the capital of the bank concerned. Suppose the losses in question occur due to errors or negligence of members of the Board of Directors. In that case, members of the board of Commissioners or equivalent organs, and/or shareholders, then the losses in question will be charged to those concerned.

m) Bank shareholders must increase capital using the additional capital set by LPS.

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[39] *Kementerian Koordinator Bidang Perekonomian Republik Indonesia*, "Siaran Pers: Pemerintahan Optimis Indonesia Tumbuh Solid di 2024 dan Lebih Baik Lagi di 2025", Jakarta, 29 February 2024, https://www.ekon.go.id, accessed on 04 August 2024, at 11.25 WIB

n) Freeze assets belonging to bank managers, bank shareholders, and/or its members who are proven to have committed actions that cause losses to the bank, both domestically and abroad.

o) Transfer some or all of the bank's assets and/or liabilities to the Recipient or Intermediary Bank.

p) M Sell the bank to a buyer willing to take over all obligations.

q) Guarantee certain loans from banks.

r) Giving loans to banks, and

s) Carry out other tasks determined by KSSK.

Article 4 paragraph (3) Law no. 4 of 2023 concerning Development and Strengthening of the Financial Sector states that the Chairman of the LPS Board of Commissioners as a member has voting rights. In contrast to the PPKSK Law, Article 4 paragraph (3) states that the Chairman of the LPS Board of Commissioners, as a member of the KSSK, does not have voting rights. This is different from the Minister of Finance (KSSK member and chairman), Chairman of the OJK Board of Commissioners (member), and BI Governor (member), all of whom have voting rights on the KSSK. The increasingly extensive authority of the LPS requires the granting of voting rights to the Chairman of the Board of Commissioners within the KSSK.

4. CONCLUSION

This research analyzes the role of the Deposit Insurance Corporation (LPS) in implementing the Banking Restructuring Program (PRP) to maintain the stability of the Indonesian financial system. The main findings show that LPS's authority in handling problematic banks, such as taking over assets, providing liquidity, and implementing restructuring, contributes significantly to national banking stability. However, moral hazard remains a major challenge affecting the effectiveness of this program. This research answers its main objective by showing that LPS has a strategic role in mitigating systemic risk and restoring public trust in the banking system. Theoretically, this research enriches deposit insurance and banking restructuring literature with a data-based policy perspective in Indonesia. Practically, the results of this research guide the government and financial authorities to optimize LPS authority through stricter regulations and an integrated supervisory system. The limitation of this research lies in the use of secondary data, which may include something other than the latest developments. Therefore, it is recommended that further research use primary data through interviews with stakeholders, such as regulators and banking industry players, to gain deeper insights. This research contributes by providing recommendations to strengthen collaboration between LPS and other financial authorities and increase transparency in PRP implementation. The results of this research can become a reference for policies that support the stability and sustainability of the Indonesian economic system.

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