

Analysis of Prudential Principles in Financing Feasibility Assessment for Micro Entrepreneurs at BPRS Taman Indah Darussalam

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Abstract

This study examines the implementation of prudential principles in the financing feasibility assessment for MSMEs at BPRS Taman Indah Darussalam. The research is based on the increasing trend of Non Performing Financing (NPF), which rose from 0,06% in 2021 to 1,11% in 2024. Although this figure remains below the threshold set by OJK (5%), it reflects a growing risk that deserves critical attention. This study adopts a normative empirical approach using descriptive qualitative methods, combining primary data from in depth interviews and field observations with secondary data from internal documentation and legal literature. The finding reveal that BPRS Taman Indah Darussalam applies the 5C framework (Character, Capacity, Capital, Collateral, Condition of Economy) as the foundation for assessing financing feasibility. The implementation of prudential principles is supported by a layered organizational structure involving the Risk Management Unit, Financing Committee, and a four eyes principle system. However, field implementation still encounters challenges such as the lack of an early warning system, reliance on manual assessment, and difficulties in evaluating MSMEs lacking formal financing records. The study concludes that while the 5C framework serves as a robust structure for risk assessment, its effectiveness needs to be enhanced through the intergration of analytical technology, strengthening of real time monitoring systems, and development of assessment models that are more adaptive to the dynamic nature of the MSMEs segment.

Keywords: *Prudential Principle, Financing Feasibility Assessment, MSMEs, BPRS, Risk Management*

Introduction

The banking sector plays a strategic role in improving public welfare and promoting national development by mobilizing and channeling funds to those in need of financial support. Islamic commercial banks and Islamic financial institutions (IFIs), including Islamic microfinance institutions, contribute significantly to this process by offering financial products based on Sharia principles. To ensure that financing remains profitable

and avoids the risk of becoming non-performing, these institutions are required to adopt prudential principles as part of a broader risk management framework.¹

The application of prudential principles in managing Islamic banks and Islamic microfinance institutions is essential to ensure that the funds distributed can be repaid to depositors, along with profit, in accordance with the profit-and-loss sharing mechanism. These principles, as outlined in Law No. 21 of 2008 on Islamic Banking, play a key role in maintaining financial system stability, safeguarding public trust, and minimizing the risk of rising Non Performing Financing (NPF).² A practical implementation of prudential principles is the financing feasibility assessment based on the 5C framework: Character, Capacity, Capital, Collateral, and Condition of Economy. However, in practice, several Islamic financial institutions still face challenges with problematic financing, often due to inadequate application of these principles especially the assessment of character.³

Neglecting prudential principles exposes Islamic banks to substantial financial risks. This is particularly critical in Sharia contracts such as *muḍārabah* and *mushārahah*, where no collateral is typically required. In such cases, repayment depends solely on the success of the customer's business (the "first way out"), requiring the bank to exercise a higher level of caution and selectivity. Proper assessment of financing prospects, business viability, continuous monitoring, and business mentoring are all crucial to prevent defaults and maintain a sound financing portfolio.⁴

Stakeholders in the Islamic banking industry must be capable of managing various risk factors that could jeopardize institutional stability, especially risks stemming from opportunistic behavior by owners or executives who prioritize short-term profits.

¹ Lindryani Sjoftan, "Prudential Banking Principle in Islamic Financing as an Effort to Maintain the Health Level of Islamic Banks," *PALAR (Pakuan Law Review)*, Vol. 4, No. 1, 2023.

² Law No. 21 of 2008 on Islamic Banking.

³ Wiwit Kuswahiriani, Hendro Siregar, and Fachrudin Syarifuddin, "Analysis of Non Performing Financing (NPF) in General and Micro Segments at Three National Islamic Banks in Indonesia," *Journal of Business and Management Applications*, Vol. 6, No. 1, 2020.

⁴ Gregorius Prima Langi and Imron Mawardi, "Risk Management of Musyarakah Mutanaqisah Financing at Bank Muamalat Indonesia KC Mas Mansyur Surabaya," *Journal of Islamic Economic Theory and Application*, Vol. 6, No. 1, 2020, pp. 188-197.

Therefore, Islamic banks and Islamic microfinance institutions are under the supervision of Bank Indonesia (BI) and the Financial Services Authority (OJK), while adherence to Sharia principles is monitored by the National Sharia Board – Indonesian Ulema Council (DSN-MUI). These oversight mechanisms ensure that Islamic financial institutions operate within legal and ethical boundaries, thereby promoting sustainable economic development and improving public welfare through productive and responsible financing, particularly to micro-enterprises.⁵

BPRS Taman Indah Darussalam, a relatively young institution established four years ago, continues to expand its financing and funding activities. A critical component of its operations is the assessment of financing feasibility for micro-enterprise applicants. Beyond verifying administrative documentation, the institution must ensure that prospective borrowers genuinely meet the eligibility criteria for receiving financing. The 5C framework remains central to the bank's assessment process.

The feasibility assessment procedures at BPRS Taman Indah Darussalam include in-depth interviews, document validation, character evaluation, SLIK (Financial Information Service System) checks, and on-site surveys. Despite these efforts, the institution has recorded a rising trend in NPF between 2021 and 2024. Internal data show an NPF ratio of 0.06% in 2021, dropping slightly to 0.02% in 2022, then rising sharply to 0.86% in 2023, and reaching 1.11% in 2024. While this remains below the 5% threshold set by OJK, the consistent increase signals potential issues in the current feasibility assessment system and the overall implementation of prudential principles in risk management.

This study, therefore, seeks to examine the application of prudential principles in the financing feasibility assessment at BPRS Taman Indah Darussalam, with a specific focus on micro-business financing. The research aims to evaluate the effectiveness of the

⁵ Putra Rulanda S., Dianie Zaini., and Safitri M., "Legal Position of Islamic Bank Supervision Conducted by the Financial Services Authority (OJK) and the National Sharia Board of the Indonesian Ulema Council (DSN-MUI)," *Supremasi Journal*, Vol. 10, No. 2, 2020, pp. 36-51.

bank's current risk assessment methods and identify both preventive and evaluative strategies employed to maintain a healthy Sharia-compliant financing portfolio.

Method

This study employs an empirical normative approach by examining the implementation of prudential principles at BPRS Taman Indah Darussalam in the provision of financing to UMKM (micro, small, and medium enterprises) in order to prevent problematic financing, particularly those arising from the inability of debtors to fulfill their obligations. The type of research applied is qualitative with a descriptive-analytical specification, aiming to provide a comprehensive and systematic overview of the application of prudential principles and to analyze the root causes of problematic financing, thereby supporting sustainable development in both financing and funding aspects. The data sources used in this study consist of primary and secondary data. Primary data were obtained directly from the field through interviews and documentation studies, including audio recordings. Meanwhile, secondary data were sourced from library materials, such as legal textbooks, fiqh literature, legal dictionaries, language dictionaries, legal encyclopedias, scholarly articles, and legal journals.

Discussion

1. Prudential Principles in Financing Distribution

The application of prudential principles in banking management is essential to ensure that banking operations comply with prudential standards, thereby maintaining financial stability, institutional integrity, and safeguarding third-party funds. In the context of Islamic banking, prudential principles are not only normative but also rooted in ethical values derived from Sharia, such as justice (*'adl*), trustworthiness (*amanah*), and the avoidance of uncertainty (*gharar*). As noted by Hulster and Montes-Negret, prudential banking represents a framework that guides banks to operate in a safe, controlled, and responsible manner in

managing business risks. These principles encompass operational measures aimed at preventing losses and fraud while ensuring long-term business continuity.⁶

In Indonesia, the application of prudential principles is a key component of Islamic banking, supported by a strong legal foundation under Law No. 21 of 2008. Article 2 stipulates that Islamic banking operations must adhere to sharia principles, economic democracy, and prudence.⁷ Article 23 (2) emphasizes the necessity of a thorough evaluation of prospective clients, covering aspects such as character, capacity, capital, collateral, and business prospects. In addition, Article 37 introduces limits on financing exposure to prevent risk concentration, while Articles 50 to 54 outline the responsibilities of supervisory and regulatory authorities in overseeing and guiding banking activities.

In addition to being regulated by law, prudential principles are also reinforced through various derivative regulations issued by the Financial Services Authority (OJK) and Bank Indonesia (BI). OJK Regulation (POJK) No. 65/POJK.03/2016 mandates Islamic banks to implement comprehensive and integrated risk management across all activities.⁸ POJK No. 8/POJK.03/2014 serves as the legal basis for assessing the soundness of Islamic banks, reflecting the effectiveness of prudential principles through evaluations of assets, management, liquidity, and market risk sensitivity. Additional regulations such as POJK No. 16/POJK.03/2014 on asset quality and POJK No. 24/POJK.03/2015 on Sharia bank products and business activities further support the implementation of prudential principles. Moreover, POJK No. 46/POJK.03/2017 and Bank Indonesia Regulation (PBI) No. 12/2/PBI/2011 require the establishment of compliance units to ensure operations remain aligned with applicable laws and Sharia principles.⁹ Regarding non-performing financing,

⁶ Hulster, Katia H., and Fernando Montes-Negret. *Micro-Prudential Supervision: A key FinSAC Business Line*. Washington, DC: Financial Sector Advisory Center World Bank Group, 2015, pp. 1-2.

⁷ Law No. 21 of 2008 on Islamic Banking.

⁸ Financial Service Authority Regulation No. 65/POJK.03/2016 on Implementation of Risk Management for Sharia Business Units.

⁹ POJK No. 46/POJK.03/2017 on Compliance Function and PBI No. 13/2/PBI/2011 on Implementation of Compliance Function for Commercial Banks.

PBI No. 10/18/PBI/2008 on Financing Restructuring regulates rescue measures aimed at minimizing loss risks.¹⁰

Islam teaches the importance of careful attitude in all aspects of life, including muamalah and worship, as a form of approach to Allah and for the common good. This careful attitude is also emphasized in the Quran in Surah Al-Maidah (5) verse 49:

وَأَنْ أَحْكُمَ بَيْنَهُمْ بِمَا أَنْزَلَ اللَّهُ وَلَا تَتَّبِعْ أَهْوَاءَهُمْ وَأَحْذَرُ لَهُمْ أَنْ يَقْتُنُوكَ عَنْ بَعْضِ
مَا أَنْزَلَ اللَّهُ إِلَيْكَ فَإِنْ تَوَلَّوْا فَاعْلَمُوا أَنَّمَا يُرِيدُ اللَّهُ أَنْ يُصِيبَهُمْ بِبَعْضِ ذُنُوبِهِمْ وَإِنَّ كَثِيرًا
مِّنَ النَّاسِ لَفَاسِقُونَ¹¹

“And judge between them by what Allah has revealed, and do not follow their desires. But beware of them, lest they turn you away from some of what Allah has revealed to you. And if they turn away, then know that Allah intends to afflict them for some of their sins. And indeed, most of the people are defiantly disobedient.”

In Islamic banking, prudential principles serve not only as regulatory requirements but also as an embodiment of key Islamic values amanah (trustworthiness) and justice—implemented through rigorous professional risk-management practices. Their application ensures that every financing decision is grounded in objective analysis and supported by adequate risk control mechanisms.

The concrete implementation of prudential principles in Islamic banking is reflected in the application of the 5C approach: Character, Capacity, Capital, Collateral, and Condition of Economy, which serves to comprehensively assess customer eligibility. Character evaluates the customer's integrity and commitment to fulfilling financial obligations. Capacity measures the borrower's ability to manage and repay financing based on business performance. Capital assesses the financial strength and resilience of the business. Collateral involves evaluating assets pledged as guarantees. Condition of Economy considers broader macroeconomic factors that may impact the sustainability of

¹⁰ Bank Indonesia Regulation No. 10/18/PBI/2008 on Financing Restructuring.

¹¹ Ministry of Religious Affairs, Al-Quran and Its Translation, (Bandung: Al-Bayan, 2017).

the customer's business. This holistic approach is particularly vital in financing micro-enterprises, which often lack formal financial documentation or structures.¹²

As a complement to the 5C approach, the implementation of prudential principles is also manifested through Know Your Customer (KYC) policies, which oblige banks to thoroughly understand the identity, background, and transaction patterns of their customers. Effective KYC implementation requires standardized operational guidelines to ensure consistency and reliability in risk mitigation. By analyzing customer backgrounds and transactional behavior, banks can identify and mitigate potential risks at an early stage.¹³ Furthermore, regulations concerning the Maximum Financing Provision Limits (Batas Maksimum Pemberian Pembiayaan/BMPP) play a critical role in preventing risk concentration in specific sectors or individual customers. Periodic evaluations of customer business performance, financial statements, and future prospects are conducted to ensure that emerging risks can be anticipated and managed proactively.¹⁴

Prudential principles are also reflected in contract selection. For asset-based financing, murabahah contracts are used, while mudharabah and musharakah contracts are chosen for partnership-based financing with higher risks. Contract selection considers the suitability of customer needs while maintaining bank risk management capacity to remain in accordance with sharia principles.

Overall, the application of prudential principles obliges Islamic financial institutions to operate with caution, responsibility, and objective analysis, supported by risk control systems that comply with prevailing regulations. These principles aim to ensure that BPRS remain liquid, solvent, and capable of managing public funds in a safe, transparent, and productive manner. The values embedded in prudential principles are also aligned with

¹² Asmi, "Implementation of Prudential Principles in Murabahah Financing at PT. BNI Syariah Micro Bank Masamba", *Thesis*, State Islamic Institute (IAIN) Palopo, 2019, pp. 29-31.

¹³ Veithzal Rivai et al., *Socializing Islamic Economics and Islamizing Community Economics* (Jakarta: Raja Grafindo Persada, 2007), p. 619.

¹⁴ Muhammad Arafah Yusmad, *Legal Aspects of Islamic Banking: From Theory to Practice*, (Jakarta: Prenadamedia Group, 2017), pp. 29-30.

Islamic teachings that emphasize justice (*'adl*), trustworthiness (*amānah*), and the avoidance of uncertainty (*gharar*) and gambling (*maysir*).¹⁵

The comprehensive implementation of prudential principles enables Islamic banks to maintain financial resilience and operational sustainability. Research conducted by Bismi Khalidin affirms that the quality of Islamic bank financing is highly dependent on the consistent application of prudential principles, particularly in customer selection, contract structuring, and effective risk management.¹⁶

2. Financing Feasibility Assessment System at Microfinance Institutions

Micro, Small, and Medium Enterprises (MSMEs) hold a strategic position in the Indonesian economy. According to data from the Ministry of Cooperatives and SMEs (2023), there are 64.2 million MSME actors who contribute 60.51% to the national Gross Domestic Product (GDP) and absorb 97% of the total workforce. Despite this significant contribution, MSMEs often face barriers in accessing financing, primarily due to low financial literacy, the absence of formal accounting records, and the lack of legal business documentation. These limitations make the MSME sector inherently high-risk and complex in terms of financing. Therefore, BPRS (Islamic Rural Banks) must adopt contextual and adaptive feasibility assessment approaches that are tailored to the unique characteristics of micro-scale entrepreneurs.¹⁷

To address the challenges in MSME financing, conducting a feasibility study becomes a crucial element in risk mitigation. This assessment not only encompasses technical and financial aspects, but also evaluates the character of business actors, business prospects, and operational sustainability. As an integral component of risk management in Islamic banking, feasibility studies are carried out prior to financing decisions to ensure the prudence of fund distribution. The 5C approach—comprising Character, Capacity, Capital,

¹⁵ Ascarya, *Islamic Bank Contracts and Products*, (Jakarta: Rajawali Pers, 2015), p. 15.

¹⁶ Bismi Khalidin, "Money Policy, Macroeconomic Variables, and the Performance of Islamic Banks Financing," *Journal of Islamic Monetary Economics and Finance*, Vol. 6, No. 3, 2020, p. 545.

¹⁷ Ministry of Cooperatives and SMEs of the Republic of Indonesia, *MSME Data 2023*, accessed at <https://kemenkopukm.go.id> on May 16, 2025.

Collateral, and Condition of Economy—serves as the primary framework in assessing the eligibility of prospective customers.¹⁸

The urgency of conducting feasibility studies is supported by data from the Financial Services Authority (OJK) in 2023, which recorded that the Non-Performing Financing (NPF) ratio in the micro sector reached 4.2%, exceeding the industry average of 3.2%. This indicates that deficiencies in feasibility assessments can directly contribute to a rise in financing problems. Consequently, feasibility studies should not be perceived as mere administrative procedures, but rather as strategic instruments to uphold the stability of microfinance institutions and the broader financial system.

From a sharia perspective, feasibility assessments reflect the bank's moral obligation to safeguard the trust placed in it by managing ummah funds responsibly. Antonio (2001) underscores that financing disbursed without proper feasibility considerations may result in harm (*ḍarar*), which is contrary to the objectives of *maqāṣid al-syarī'ah*, particularly *ḥifẓ al-māl* (protection of wealth).¹⁹ Furthermore, legal business status and the completeness of administrative documents are essential components that significantly influence the success and sustainability of MSME financing.²⁰

Therefore, Islamic microfinance institutions must adopt feasibility assessment systems that extend beyond administrative formality and are adaptive to the dynamics of micro-scale businesses. The assessment approach should comprehensively evaluate financial viability, legal status, business prospects, and alignment with sharia principles. Feasibility studies serve not only as instruments for risk mitigation, but also as strategic tools to achieve social impact, economic justice, and business sustainability in accordance with Islamic values. Technically, this approach is operationalized through various components of feasibility assessments, as elaborated below.²¹

¹⁸ Muhammad, *Islamic Bank Risk Management*, (Yogyakarta: UII Press, 2016), pp. 61-64.

¹⁹ M. Syafi'I Antonio, *Islamic Banks: From Theory to Practice*, (Jakarta: Gema Insani, 2001), p. 287.

²⁰ Rodhiatul Aslamah, et al., "Analysis of the Impact of Islamic Bank Financing Feasibility on MSMEs," *Edunomika Journal*, Vol. 7, No. 1, 2023, pp. 123-124.

²¹ Julkarnain Situmorang, "Feasibility Study Analysis of MSME Financing at LKMS Padang Sidempuan City," *Journal of Sharia and Islamic Finance*, Vol. 9 No. 2, 2021, p. 450.

a. 5C and 7P Approaches as Basic Evaluation Framework

The 5C evaluation framework comprising character, capacity, capital, collateral, and condition of economy is employed to assess customer integrity, business competence, capital readiness, risk mitigation capacity, and macroeconomic influences. Within a sharia framework, this method incorporates moral considerations and compliance with Islamic business ethics. In parallel, the 7P approach Personality, Purpose, Prospect, Party, Payment, Profitability, and Protection offers a complementary evaluation, particularly suited for informal sector customers. This framework emphasizes contextual and qualitative aspects such as entrepreneurial motivation, business prospects, and mechanisms to safeguard against default risk.

b. Legality Assessment and Sharia Compliance

Business legality is a vital component in the feasibility assessment process—not merely as an administrative requirement, but as an indicator of business maturity and readiness to compete in formal markets. Key legal documents such as the Business Identification Number (NIB), Taxpayer Identification Number (NPWP), and Trade Business License (SIUP) serve as evidence of legal compliance and operational legitimacy. The assessment of legality involves verifying the authenticity and completeness of formal documents, including halal certification, which reflects the business owner’s commitment to good governance and adherence to Islamic values. In addition, the evaluation of sharia compliance ensures that all business activities align with Islamic principles. This involves screening to avoid elements of *riba* (usury), *maysir* (gambling), and *gharar* (excessive uncertainty), as well as prohibiting products or services that are haram in substance or benefit. The Sharia Supervisory Board (Dewan Pengawas Syariah, DPS) plays an active role in this process, from determining appropriate contract types to evaluating transactions to ensure compliance with sharia guidelines.

c. Financial and Strategic Analysis (SWOT)

Although many micro-entrepreneurs lack formal financial statements, feasibility assessments are still conducted through direct observations and structured interviews. These qualitative methods provide valuable insights into business operations, cash flow

patterns, and managerial capacity. To complement this, a SWOT analysis assessing Strengths, Weaknesses, Opportunities, and Threats is utilized to evaluate the business's competitive position, potential risks, and growth prospects. This approach not only supports more accurate financing decisions but also helps identify areas where business coaching is needed, contributing to better risk mitigation strategies in microfinance operations.

d. Integration of Maqasid Sharia Values in Feasibility Evaluation

The feasibility assessment system is further enhanced through integration with the objectives of Islamic law (*maqāṣid al-syarī'ah*), encompassing the protection of religion (*ḥifẓ al-dīn*), life (*al-nafs*), intellect (*al-'aql*), lineage (*al-nasl*), and wealth (*al-māl*). Business ventures that contribute to social empowerment, environmental sustainability, and poverty alleviation are given positive consideration in the evaluation process. This value-based approach transforms feasibility assessments from being solely profit-oriented to becoming instruments of ethical intermediation. Such comprehensive evaluation not only strengthens risk mitigation but also supports Islamic microfinance institutions in maintaining a sound financing portfolio while promoting equitable and sustainable economic development in line with sharia principles.

3. Implementation of Prudential Principles in Financing Feasibility Assessment for Micro Entrepreneurs at BPRS Taman Indah Darussalam

BPRS Taman Indah Darussalam is a Sharia Rural Bank that offers financial services based on Islamic principles, with a primary focus on supporting Micro, Small, and Medium Enterprises (MSMEs). In its financing distribution, the bank applies a comprehensive feasibility analysis that goes beyond merely assessing profit potential. The evaluation ensures that financing is viable, secure, and aligned with sharia values. This rigorous process demonstrates the concrete implementation of prudential principles in day-to-day banking operations.²²

²² Lastuti Abubakar, "Implementation of Prudential Principles Through the Obligation to Prepare and Implement Bank Credit or Financing Policies," *Rechtidee*, Vol. 13. No. 1, 2018, pp. 200-202.

As an Islamic microfinance institution, BPRS Taman Indah Darussalam is not merely responsible for distributing funds to micro-entrepreneurs, but also for ensuring that the entire financing process adheres to both sharia principles and banking prudential standards. This dual responsibility demands an evaluation system that transcends profit-oriented assessments, incorporating the ability to detect potential risks from the earliest stages of financing applications. One of the initial manifestations of this system is the enforcement of administrative and business legality requirements for every prospective financing customer.²³

Implementation of prudential principles at BPRS Taman Indah Darussalam begins with an organizational structure designed to support risk control systems. The Risk Management Unit is tasked with overseeing the application of prudential principles in all operations. This unit is under the President Director and operates independently in evaluating risks and monitoring financing, without intervention from business units.

BPRS also establishes a financing committee comprising the President Director, Director, Financing Manager, and Risk Management Unit representative to decide on financing above Rp50 million. Proposals must include a comprehensive presentation of 5C analysis results, risk assessments, and recommendations from Account Officers and Legal Officers. Decisions are final and require majority approval. The four-eyes principle is strictly applied; Account Officers, who conduct field analyses, are not authorized to decide independently, and must escalate proposals through the Financing Manager to the Director level based on financing tiers.²⁴

This system is implemented through the Financing Policy Guidelines, which have been in effect since 2021 and updated in 2024. The document serves as the main reference in financing activities, combining practical experiences with adjustments to the latest regulatory developments. In practice, financing officers are required to use feasibility assessment sheets that are designed systematically and measurably, covering aspects such

²³ Rahma Yudi Astuti, "Implementation of Prudential Principles in Financing and Credit Distribution at Microfinance Institutions (Multi-Site Study at BMT Hasanah Mlarak and BRI Unit Mlarak, Ponorogo)," *Al-Tijarah*, Vol. 2, No. 1, 2016, pp. 119-145.

²⁴ Interview with Ariswan, Director of BPRS Taman Indah Darussalam, Banda Aceh, May 26, 2025.

as personality, business capacity, capital ownership, collateral, and economic conditions. Each component is assigned a specific weight based on past financing risk analysis and the characteristics of micro-scale customers.²⁵

Implementation of this guideline is reinforced by Risk Acceptance Criteria (RAC), which consist of quantitative provisions and clearly defined risk thresholds. These include, among others: a maximum installment to net income ratio of 30% to ensure repayment capacity, a minimum of two years of business experience as a track record indicator, and adjusted collateral value deductions based on liquidity and price stability considerations. These criteria are applied through a multi-stage assessment system, involving validation by units with relevant expertise. The initial screening is conducted by customer service officers, who verify the completeness and eligibility of submitted documents and are authorized to reject applications that fail to meet the minimum requirements.²⁶

The next stage involves field analysis through a minimum of two on-site visits at different times to verify business continuity and prevent data manipulation by prospective customers. Each visit follows a standardized assessment form and observation checklist, covering physical aspects of the business (equipment, infrastructure, layout), estimated daily transactions, customer interactions, and surrounding business environment (competition, accessibility, growth potential). All data are thoroughly documented, including photos and GPS coordinates. These observations serve as the basis for financing managers to conduct technical evaluations, including cash flow simulations under optimistic, moderate, and pessimistic scenarios, feasibility score validation, and risk profile adjustments aligned with the bank's risk tolerance.

This assessment is reinforced by legal and compliance reviews conducted by legal officers, including validation of collateral legality and marketability through official institutions such as BPN or the Transportation Department, as well as conformity of contract structures with sharia principles, guided by MUI fatwas and the Sharia Supervisory

²⁵ Interview with Zukhrufin Ikhda, Financing Manager of BPRS Taman Indah Darussalam, Banda Aceh, May 27, 2025.

²⁶ Interview with Qaulan Tsaqila, Account Officer of BPRS Taman Indah Darussalam, Banda Aceh, May 26, 2025.

Board. Comprehensive regulatory compliance checks are also carried out, covering OJK, BI, and relevant sectoral rules. To anticipate potential financing quality deterioration, an Early Warning System is employed using 15 indicators 10 quantitative, such as payment delays, declining balances, reduced transaction frequency, debt service ratios, and working capital turnover; and 5 qualitative, including shifts in operating hours, customer health, family stability, environmental dynamics, and behavioral changes.

Regular monitoring is conducted through a three-layer system: (1) weekly reviews by headquarters based on transaction and payment behavior, (2) field visits every three months for current customers and monthly for those requiring special attention, and (3) continuous communication via phone, WhatsApp, and informal visits to monitor business conditions in real time. Monthly Portfolio Review Meetings involve AOs, managers, and risk units to evaluate customer conditions using early warning indicators and monitoring data. Customers are classified using a traffic light system green (performing), yellow (needs attention), and red (problematic) with tailored follow-up plans such as enhanced monitoring, restructuring, or other recovery strategies.

This entire process is reinforced by integrated technology systems that detect unusual payment patterns, calculate financial ratios (e.g., current ratio, debt-to-equity), and generate management reports. AOs use mobile apps for field reporting, uploading documentation with automatic time and location stamps, and accessing customer history. BI Checking and OJK SLIK are also used to review the credit history of prospective customers. As part of quality control, 10% of approved financing is randomly tested each month by independent teams not involved in the assessment process to ensure compliance and support ongoing improvement in procedures and risk management.

To comprehensively apply prudential principles, BPRS Taman Indah Darussalam adopts the 5C approach in assessing financing feasibility. Each aspect is thoroughly evaluated through observation, interviews, and field analysis to ensure financing aligns with the customer's actual capacity and needs, while reducing the risk of future defaults.

a. Character

Character assessment is carried out by Account Officers (AOs) through direct interviews that go beyond administrative checks, focusing on honesty, business ethics, motivation, and behavioral consistency. AOs also observe non-verbal cues such as facial expressions and tone when discussing sensitive topics, and validate information with external parties like neighbors, suppliers, or partners. Internal records of post-disbursement behavior, such as avoidance or bad faith, also inform the assessment. To mitigate risks, AOs regularly visit business locations during the initial three months.²⁷

b. Capacity

Capacity aspects are viewed from prospective customer abilities in managing businesses. Since most micro entrepreneurs do not have formal financial records, AOs apply direct observation for at least two days to business locations, observing transaction numbers, operational rhythms, and daily cash flow management. Mystery customer approaches are also used to see how customers serve clients. AOs adjust visit times to cover busy and quiet hours, to know business resilience and fluctuations. AOs also insert simulation-based questions such as, "What would you do if raw materials suddenly become scarce and prices rise?", to measure resilience in facing risks.

c. Capital

Capital aspects not only assess amounts owned by prospective customers, but also their origins, whether from personal funds, inheritance, or other loans. BPRS requires minimum self-capital of 30% of total financing, except for customers with very good track records. AOs conduct verification through field reviews, asset verification, and transaction tracking through suppliers. The main challenge in this aspect is customer tendencies to mix business and household finances. Therefore, before financing is disbursed, AOs provide basic financial education and request written commitments to separate both finances.

d. Collateral

²⁷ Wawancara dengan Qaulan Tsaqila, AO BPRS Taman Indah Darussalam, Banda Aceh, 26 Mei 2025

Collateral is assessed based on legal completeness, physical condition, and market value. AOs verify ownership documents—such as land certificates or vehicle registrations—through official sources. Asset values are determined using haircuts based on type and liquidity, then adjusted to market prices via surveys and local broker input. High-value assets are revalued every three months. BPRS Taman Indah Darussalam also performs liquidity simulations to estimate how quickly collateral can be liquidated in the event of financing problems.

e. Condition of Economy

Business and economic environment conditions are assessed directly in the field, focusing on location, ecosystem, and market potential. AOs visit business sites for at least two days to evaluate visitor traffic, visibility, accessibility, and proximity to economic hubs like markets or terminals. They also observe surrounding competitors—both in number and type—to assess the level of competition and the resilience of the prospective business in the medium term. From the external economic side, the head office financing team monitors staple prices, raw material fluctuations, and local policies (e.g., road projects or market relocations) that may affect micro businesses. This information helps determine appropriate tenors and margins, although it is not yet structured into formal scenarios (optimistic, moderate, pessimistic) as commonly practiced in large-scale banks.

The 5C implementation at BPRS Taman Indah Darussalam has progressed, yet challenges persist in anticipating complex MSME financing risks. Despite cross-divisional synergy—Account Officers, risk management, and legal units—gaps remain between ideal procedures and unpredictable field realities. The informal nature of MSME customers often forces assessments to rely on qualitative, subjective judgments rather than measurable data, making risk identification less structured and increasing uncertainty in feasibility analysis.²⁸

²⁸ Interview with Qaulan Tsaqila, Account Officer of BPRS Taman Indah Darussalam, Banda Aceh, May 26, 2025.

In character assessment, challenges arise when post-disbursement customer behavior deviates from initial evaluations. These behavioral shifts highlight the need for early detection systems that are more responsive to signs of deviance, allowing earlier mitigation of financing risks. In assessing capacity, current methods still rely on short-term projections from field observations. However, high micro business volatility—driven by seasonal trends, local purchasing power, and competitor shifts—makes these projections often inaccurate. As a result, discrepancies frequently occur between predetermined installment schemes and customers' actual cash flow patterns.

Assessment of capital aspects faces challenges due to the prevalent commingling of personal and business finances among MSMEs, complicating the identification of capital truly available for operations. This often leads to misestimations of actual capital strength and working capital requirements. In collateral assessment, although multi-layer verification is implemented, practical issues persist, such as document authenticity, ambiguous ownership, or assets acquired through inheritance without formal certificates. These conditions pose legal risks during collateral execution. Moreover, limited access to external databases and delayed data updates further reduce the accuracy of collateral evaluations.

In assessing economic conditions, challenges arise from the intricate interplay between micro and macroeconomic factors. Micro businesses remain highly vulnerable to fluctuations in raw material prices, local purchasing power, and fiscal policies such as minimum wage adjustments or subsidy changes. Limited access to real-time economic data weakens the accuracy of risk assessments. The COVID-19 pandemic, for instance, demonstrated the inadequacy of conventional models in anticipating major disruptions. Although BPRS has developed early warning and monitoring systems, these remain heavily reliant on manual observations and subjective judgments. Quarterly monitoring often fails to capture gradual deteriorations or sudden shocks, while reliance on AO reports risks information asymmetry and delays in mitigation responses.²⁹

²⁹ Interview with Thona Mutuah Myco, Internal Control Manager of BPRS Taman Indah Darussalam, Banda Aceh, May 25, 2025.

Conversely, the relationship-based approach, which is a strength of the socio-cultural model at BPRS, faces scalability and standardization challenges. Overreliance on interpersonal ties may lead to inconsistent treatment among customers and officers. Thus, a balance must be maintained between personal engagement and professional objectivity in financing decisions. While the 5C principle remains a robust foundational framework, its technological integration is still limited. Significant gaps exist in information systems, particularly in enabling real-time monitoring, automated risk scoring, and predictive analytics. As a result, decision-making continues to rely on manual processes and AO discretion, potentially causing inefficiencies and inconsistencies in risk evaluation.

Overall, the 5C principle remains an effective framework for structured risk assessment. However, its implementation requires ongoing refinement to adapt to the evolving characteristics of the MSME segment. A hybrid approach combining systematic procedures with adaptive flexibility to field realities is a strategic step to enhance the risk management performance of BPRS.³⁰

Empirical data on Non-Performing Financing (NPF) trends at BPRS Taman Indah Darussalam during 2021–2024 confirms the complex challenges in implementing the 5C principles as highlighted in previous analyses. The data includes total financing and details of NPF based on collectibility levels 3 (substandard), 4 (doubtful), and 5 (loss):

Tabel. 1

BPRS TID Financing Collectibility (2021-2024)

| Year | Collectibility 3 (Substandard) | Collectibility 4 (Doubtful) | Collectibility 5 (Loss) |
|-------------|---|--|------------------------------------|
| 2021 | Rp 0 | Rp 0 | Rp 26.336.000 |
| 2022 | Rp 0 | Rp 0 | RP 11.059.000 |
| 2023 | Rp 7.768.000 | Rp 18.000.000 | RP 576.000.000 |

³⁰ Lubis, R., & Sahlan, M., "Implementation of 5C Approach in Problematic Financing Distribution at BPRS," *Scientific Journal of Islamic Economics*, No. 7 Vol. 3, 2022, p. 347.

| | | | |
|------|--------------|---------------|----------------|
| 2024 | Rp 4.422.122 | Rp 87.838.136 | RP 657.791.007 |
| | | | |

Source: Compilation of BPRS TID productive asset quality data based on OJK annual reports, 2021-2024.

Tabel. 2

BPRS TID Financing Amount and NPF Ratio Data

| Year | Financing | Total Financing | NPF Percentage |
|-------------|------------------|------------------------|-----------------------|
| 2021 | Rp 26.336.000 | Rp 47.819.711.000 | 0,06% |
| 2022 | RP 11.059.000 | Rp 55.721.000.000 | 0,02% |
| 2023 | RP 576.000.000 | Rp 69.926.620.000 | 0,86% |
| 2024 | RP 657.791.007 | Rp 67.631.809.313 | 1,11% |

Source: Compilation of BPRS TID productive asset quality data based on OJK annual reports, 2021-2024.

Based on the 2021–2024 financial reports of BPRS Taman Indah Darussalam, the Non-Performing Financing (NPF) ratio experienced notable fluctuations. In 2021, the NPF stood at 0.06%, declining to 0.02% in 2022, indicating relatively stable and controlled financing conditions. However, this trend reversed in 2023, with the NPF rising sharply to 0.86%, and further increasing to 1.11% in 2024.³¹

During 2021–2022, NPF was predominantly categorized under collectibility 5 (loss) with relatively low amounts. However, starting in 2023, systemic issues began to emerge across various collectibility levels. The appearance of collectibility 3 (substandard) amounting to Rp7,768,000 and collectibility 4 (doubtful) reaching Rp18,000,000 in 2023

³¹ BPRS Taman Indah Darussalam, Annual Financial Reports 2021-2024, accessed through internal data compilation and OJK annual publications.

then shifting to Rp4,442,112 and Rp87,838,000 respectively in 2024 reflects a progressive deterioration in assessment and monitoring quality. This trend aligns with previously identified weaknesses in the early warning system and the limitations of quarterly monitoring practices.³²

The increase in NPF during 2023–2024 is closely linked to lagging effects of global economic shocks, particularly in the post-pandemic recovery phase, which significantly influenced the accuracy of capacity assessments and macroeconomic condition analyses. Existing economic models at BPRS demonstrated limitations in anticipating and integrating the complex interplay between micro and macroeconomic variables. Furthermore, excessive reliance on short-term, observation-based projections contributed to a systematic underestimation of the inherent volatility within the MSME segment.³³

Although the 1.11% NPF ratio remains well below the 5% regulatory threshold set by OJK through POJK Number 16/POJK.03/2014, the upward trend over the past two years necessitates comprehensive strategic intervention. These developments highlight that while compliance-based risk management approaches fulfill regulatory standards, they remain insufficient in anticipating the unique characteristics and dynamic behavior of the MSME segment.

The empirical evidence underscores the urgency of transitioning from compliance-oriented frameworks to adaptive risk management systems that are responsive to sector-specific volatility. Addressing the identified implementation gaps requires the integration of analytical technologies, enhancement of financing feasibility assessment methodologies, and reinforcement of early warning systems. The development of dynamic risk models capable of synthesizing diverse risk indicators in real-time is crucial to effectively mitigate the escalation of Non-Performing Financing (NPF) in the future.³⁴

³² *Ibid.*

³³ Ahmad Ripai Saragih and Sugianto, "Analysis of Operational Risk Management for MSME Financing at KSPPS UB Amanah Syariah During the COVID-19 Pandemic," *Iqtishaduna*, Vol. 13, No. 1 June 2022.

³⁴ Akbar, Fachri. *Analysis of Operational Risk Management Process at BNI Syariah KC Micro Rungkut Surabaya*: UNAIR Repository, 2016, pp. 67-68.

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In the long term, sustaining the quality of BPRS's financing portfolio requires a more comprehensive approach through the strategic integration of prudential principles into inclusive financing frameworks. This includes formulating a risk appetite tailored to the unique characteristics of the MSME sector and applying pricing mechanisms that accurately reflect the actual risk profile. Such measures are essential to maintain a balance between institutional financial sustainability and the fulfillment of social objectives. Moreover, close collaboration with supporting ecosystems such as government agencies and business development service providers must be continuously strengthened to enhance the resilience of micro entrepreneurs while mitigating sector-specific risks.

Conclusion

BPRS Taman Indah Darussalam has demonstrated a clear commitment to implementing prudential principles in financing feasibility assessments through the integrated use of the 5C approach, supported by an independent Risk Management Unit, a structured financing committee, and the four-eyes principle. Despite the NPF ratio remaining below the OJK threshold at 1.11% in 2024, the significant rise from 0.02% in 2022 highlights unresolved risk management issues, especially in micro business financing.

This study identifies key obstacles in 5C implementation, such as subjective character assessment, limited formal financial data, capital estimation errors, and collateral verification difficulties. These findings underscore the need for more adaptive and field-responsive assessment systems. High dependence on manual judgment and limited technological support further constrain early risk detection. A shift is therefore needed—from compliance-based approaches to more inclusive frameworks that integrate prudential principles, sharia values, and contextual realities. This study offers a practical reference for developing more effective Islamic microfinance policies in Indonesia.

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