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Governance of Village-Owned Enterprises-Village Financial Institutions (BUMDesma-LKD) from a Sharia economic perspective: Analysis of institutional readiness

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ABSTRACT

Introduction

Village-Owned Enterprises–Village Financial Institutions are expected to strengthen village economic independence, expand financial inclusion, and improve community welfare through the collective management of local resources. However, in Central Buton Regency, these institutions remain dependent on revolving funds, have limited business diversification, and face weaknesses in administration, transparency, financial reporting, and community participation. Sharia economic governance offers an alternative framework based on justice, accountability, transparency, sustainability, and public benefit; however, its implementation depends on adequate institutional readiness.

Objectives

This study examines the institutional readiness of Village-Owned Enterprises (VOEs) and village financial institutions (VFIs) in Central Buton Regency to implement governance based on a Sharia economic perspective. It also formulates policy recommendations to support gradual, accountable, and sustainable institutional transformation.

Method

This study used a descriptive qualitative design. Primary data were collected through in-depth interviews, focus group discussions, triangulation, and open-ended questionnaires involving managers, supervisors, religious leaders, beneficiaries, local government representatives, and representatives of Islamic financial institutions. Secondary data were obtained from institutional regulations, administrative documents and financial reports. The data were analyzed using thematic analysis supported by qualitative data

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analysis software and a strengths, weaknesses, opportunities, and threats analysis.

Results

The findings show that institutional readiness is partial and uneven. Values such as fairness, transparency, deliberation, and concern for beneficiaries are informally present, but formal Sharia governance mechanisms have not been established. Savings and loan activities still use interest-based arrangements, while sharia contracts, standard operating procedures, supervisory structures, and compliance systems are largely absent. Limited managerial knowledge and inadequate community education also prevent stakeholders from distinguishing Sharia-based governance from conventional practices. Nevertheless, strong religious and cultural acceptance and available institutional partnerships create favorable opportunities for transformation.

Implications

The transition toward Shariah-based governance requires coordinated reforms in regulation, managerial competence, supervision, financial administration, digitalization, business diversification, and community participation.

Originality/Novelty

This study contributes to the literature by integrating institutional theory with Sharia economic governance and treating Sharia transformation as a multidimensional readiness process rather than merely a change in financing contracts.

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INTRODUCTION

Indonesia's national goal is a just and prosperous society based on Pancasila, as stated in Article IV of the 1945 Constitution. This aims to improve people's welfare. Economic development is a crucial pillar of this effort. Rural areas, rich in resources and untapped potential, are the key to national development. They facilitate comprehensive and long-term economic progress (Sukmani, 2025; Takhumova, 2020; Tshikovhi et al., 2023). Rural revitalization is no longer seen as less important in national development plans; it is now a vital pillar supporting the country's social and economic order (Cai et al., 2024; Dewi, 2017; Zhan et al., 2022).

BUMDesma-LKD is an important tool for encouraging economic independence in villages (Devananda & Darmawan, 2024; Harinurdin et al., 2025; Hidayat & Hidayah, 2023; Widowati et al., 2026). These businesses are managed cooperatively by villages to improve community welfare by optimizing existing resources. According to

Indonesian law (Law No. 6 of 2014 concerning Villages and Regulation of the Minister of Home Affairs No. 39 of 2016), village governments oversee economic organizations known as state-owned enterprises (BUMN). To manage local potential in areas such as agriculture, trade, and services, BUMNs function as business entities cooperatively managed by the community (Ameridyani et al., 2025; Masripah & Primasari, 2025). The government's efforts to improve village financial capacity to assist administration and encourage increased community income through various economic activities in rural areas are reflected in the formation of state-owned enterprises (Mundus et al., 2025; Saepudin & Yusuf, 2022). Microfinance services are the main focus of Village Financial Institutions (LKD) and Village Joint State-Owned Enterprises (BUMDesma), two specific types of BUMN that aim to assist economic activities in villages.

Preparing financial reports in accordance with Decree of the Minister of Villages, Disadvantaged Regions, and Transmigration 136/2022 and the State-Owned Enterprise Financial Accounting Standards (*Standar Akuntansi Keuangan Entitas Privat* abbreviated SAK EP in Bahasa Indonesia) is one of the new challenges posed by BUMDesma-LKD, which is a transformation from the previous PNPM UPK project. Field evidence shows that numerous issues remain in the governance of BUMDesma-LKD. These issues include a lack of human resources, which makes it difficult to prepare financial reports independently (Politeknik Keuangan Negara STAN, 2025). Another problem is the lack of professionalism (Ridzal & Sujana, 2023). In addition, there is a lack of community involvement and village officials regarding BUMDes management, as well as leadership and management problems (Jayadi et al., 2024), and the vulnerability of the principles of transparency and accountability (Anora & Mawardi, 2025), which can lead to operational failure and misuse of funds.

In Indonesia, a country with one of the largest Muslim populations in the world, Sharia economics can be a powerful tool to increase public trust, attract Sharia investment, and help achieve the Sustainable Development Goals (SDGs), especially goals 1 and 8, namely, ending poverty and promoting decent work and economic growth (Kalsum et al., 2025; Khan & Haneef, 2022). However, the institutional readiness of BUMDesma-LKD to implement sharia governance remains a major question, given that many villages lack adequate organizational structures, such as a sharia supervisory board or sharia audit mechanism, as is the case in Central Buton Regency. In this context, a Sharia economic perspective offers an alternative governance system based on the principles of justice, transparency, and sustainability, as stipulated in the Qur'an and Hadith. Sharia economics emphasizes the prohibition of riba (interest), *gharar* (excessive uncertainty), and maisir (speculation), as well as the promotion of zakat, infaq, and halal investments (Amirul Syah, 2025; W. Saputra, 2025).

Sharia-based economic management in BUMDesma-LKD offers a new approach to improving the welfare of village communities by emphasizing the principles of justice, sustainability, and public benefit (*maslahah*) (Kamal et al., 2025; Rahmani et al., 2023), which is more in line with the culture and religion of rural communities. Some recent studies that discuss the transformation of conventional Village-Owned Enterprises (BUMDes) into a Sharia-based model include research showing that the practice of

Sharia BUMDes in Mataram contributes to increasing income through savings and loan units (murabahah) and rice business (A. M. Saputra & Samsahudi, 2025; Syabilla et al., 2025). However, its implementation still faces obstacles, including minimal access to financing and less-than-professional management. Further studies indicate that the empowerment of the role of BUMDes in South Sumatra through Islamic social entrepreneurship has succeeded in increasing transparency and inclusiveness with instruments such as mudharabah, increasing profitability by 25% post-transformation (Fahmi & Panorama, 2025; Yasmeen, 2026). Further studies show that implementing Sharia principles in the management of BUMDes in Ketapang Regency, Pontianak, East Kalimantan, through a profit-sharing system (mudharabah), trustworthy buying and selling (murabahah), and productive zakat management has built a just and inclusive village economic ecosystem, as evidenced by the decline in poverty rates from 25% to 12% in three years (Nasfi et al., 2023; Sartomi, 2025).

Although various studies have shown the success of BUMDes transformation into a Sharia model in various regions of Indonesia, different conditions occur in Central Buton Regency, where BUMDesma-LKD in the region still reflects conventional operations that rely on revolving funds, thus opening opportunities for innovative adaptations to overcome similar challenges, such as a lack of business diversification and administrative transparency. BUMDesma-LKD in Central Buton Regency shows the potential of the rural economy; however, challenges such as dependence on the former PNPM revolving fund, lack of business diversification, and incomplete administrative governance are the main problems that hinder the optimization of the role of BUMDes in empowering the community. Therefore, an in-depth study is needed on the application of the concept of sharia economics to overcome these weaknesses and increase sustainability and economic inclusion in this region.

In this regard, the BUMDesma-LKD government should adhere firmly to the principles of good governance based on Sharia. In Central Buton Regency, good governance based on Sharia principles is a management system that is rooted in Islamic values. It ensures that all business and government activities are fair, transparent, accountable, responsible, professional, independent, reasonable, and compliant with Sharia laws. The primary goal is to create justice, prosperity, and sustainability (Ayub et al., 2024; Gunawan et al., 2021), which aligns with the objectives of Sharia (*maqashid Sharia*) (Iqbal et al., 2024; Zain & Zakaria, 2022). This principle complements and strengthens conventional Good Corporate Governance (GCG). This study is also based on the globalization of the Islamic economy, where countries such as Malaysia and the United Arab Emirates have successfully integrated Islamic principles into local business entities. In Indonesia, previous research has shown that Village-Owned Enterprises (BUMDesma) often fail due to weak governance, such as corruption and a lack of accountability. Therefore, analyzing institutional readiness is crucial for identifying strengths and weaknesses in organizational structure, human resources, internal control systems, and Sharia compliance, allowing for policy recommendations for village and central government.

This study aims to: 1) analyze the institutional readiness of BUMDesma-LKD in implementing governance based on a Sharia economic perspective to support sustainable and equitable village economic development; and 2) provide policy recommendations to improve BUMDesma-LKD governance to align it more closely with Sharia economic principles. A more explicit examination of institutional readiness is necessary because the transition from conventional BUMDesma-LKD governance to Sharia-based governance is not merely a technical change in financial contracts but a broader institutional transformation. In the context of Central Buton Regency, the main issue is not only whether Sharia principles are normatively desirable, but whether existing institutional structures, human resources, regulations, accounting practices, community literacy, and supervisory mechanisms are sufficiently prepared to support such transformation. Therefore, this study positions institutional readiness as a multidimensional construct consisting of regulatory readiness, organizational capacity, human-resource competence, financial-system preparedness, Sharia-compliance mechanisms, and community acceptance. By focusing on these dimensions, this study moves beyond the general claim that Sharia governance can improve village economic institutions and investigates the actual institutional conditions that may enable or constrain its implementation. This focus provides the study's novelty, especially in the specific context of BUMDesma-LKD transformation in Central Buton Regency.

LITERATURE REVIEW

BUMDesma-LKD Institutional Governance

Good governance is a manifestation of the acceptance of the importance of a set of regulations or good governance to regulate the relationships, functions, and interests of various parties in business and public service. Good governance is also defined as the managerial ability to manage a country's resources and affairs in an open, transparent, accountable, equitable, and responsive manner to the needs of the community (Daempal et al., 2022; Mason, 2020; Salehi et al., 2023). Institutional governance in this study refers to the theory of Sharia-based institutional management, which is integrated with institutional theory (Jakobsen, 2015). These elements include regulatory, normative, and cultural-cognitive elements, combined with the concept of Sharia-based management. Regulatory elements encompass rule-setting, monitoring, and sanctioning activities. In this context, the regulatory process encompasses the capacity to create rules, oversee their appropriate implementation, and impose sanctions (rewards or punishments) to influence behaviors. Normative elements refer to the rules that introduce the dimensions of prescription, evaluation, and obligation into social life. Normative elements encompass values and norms. Values refer to conceptions of what is most desirable or desirable. Cognitive-cultural elements refer to shared conceptions that shape the nature of social reality and the framework through which individuals derive meaning from it (Breemer et al., 2022; Buyukyazici et al., 2025).

Village-Owned Enterprises are commercial enterprises that receive recognition and support from local governments to improve the local economy and overall welfare of the community. BUMDesma-LKD aims to improve the village economy, optimize village assets, increase community efforts in managing village economic potential, develop business cooperation plans between villages, create opportunities and market networks that support the general needs of residents, open up employment opportunities, improve community welfare, and increase village community income and original income (P. B. Nasution et al., 2023). BUMDesma-LKD will transform into a pillar of national independence (Hilmawan et al., 2023; Indriana & Husen, 2025) and, at the same time, become an institution or unit that accommodates the economic activities of the community that grow in accordance with the nature of the village to improve the village economy (Purnamawati et al., 2023). Village financial institutions (LKD) are a form of business unit under BUMDesma or stand-alone (such as village granaries, BKD, and BPR Desa), which function as financial intermediary institutions in rural areas (Muharajabdinul et al., 2025; Salsabila & Kosasih, 2024). The institutional transformation of the Joint Village-Owned Enterprises (BUMDesma) and Village Financial Institutions (LKD), as a follow-up to Government Regulation (PP) Number 11 of 2021, requires a financial reporting system that is more accountable, transparent, and in accordance with applicable regulations.

Institutional Governance Based on Sharia Economics

Sharia-based Economic Institutional Governance is a system for managing economic institutions based on Islamic Sharia principles, which aims to achieve justice, transparency, and welfare in accordance with the maqasid of Sharia, including the protection of religion, soul, mind, descendants, and property (Kamal et al., 2025; Parasmono et al., 2022). This concept integrates the principles of good corporate governance (GCG), namely transparency, accountability, responsibility, independence, and fairness (Fadilah et al., 2025; Jan et al., 2021) with Islamic values such as tauhid, namely the oneness of Allah, as the basis of economic ethics (Fadhilah et al., 2026), *shura* (trust and integrity in carrying out responsibilities) (Aprilya & Tohawi, 2024; Taufik, 2021), *amanah* (deliberation for collective decision making) (Nisa et al., 2025; Wulandari & Fatimah, 2022). In practice, institutions such as Islamic banks implement halal contracts such as mudharabah (trust-based profit sharing), musyarakah (fairness-based partnership), and ijarah (rent) to avoid usury, with strict supervision by the Sharia Supervisory Board (*Dewan Pengawas Syariah*, abbreviated as DPS in Bahasa Indonesia).

Shariah-based economic institutions play a crucial role in improving people's welfare. First, these institutions, such as Islamic banks and Islamic operations, provide access to financing in accordance with Sharia principles, enabling communities to develop businesses and increase their incomes. Through halal financial products, these institutions help communities, especially those in the lower middle class, escape poverty and improve their quality of life. Sharia-based economic institutions function not only as financial institutions but also as financial institutions (Aditya et al., 2024;

Yahya et al., 2023) as well as agents of social change, promoting sustainable and equitable economic development (Lestari et al., 2024). In addition, Islamic economic institutions play a role in managing zakat and infaq, which are important instruments for the redistribution of wealth and economic empowerment of the people (Khaerunnisa et al., 2025; Razak, 2020).

Sharia BUMDes-LKD must adhere to specific operational guidelines. First, justice is achieved through profit sharing based on actual sales, considering the contributions and risks of all parties. Second, partnerships are formed where customers, investors, fund users, and financial institutions have equal standing as business partners working together for profit generation. Third, transparency is achieved when Sharia financial institutions openly and continuously share financial reports. This allows investors and clients to track the status of their funds. Fourth, generality means that there is no discrimination based on race, religion, or social groups. This follows Islamic principles such as *rahmatan lil aalamin* (Amar & Alaoui, 2023; Ibrahim et al., 2022; Sundari & Syarifudin, 2022).

Institutional readiness in Sharia-based BUMDesma-LKD governance can be understood by integrating institutional theory and Islamic governance principles. Scott's institutional theory explains institutional stability and change through three pillars: the regulatory pillar, which refers to rules, sanctions, procedures, and formal compliance; the normative pillar, which concerns values, obligations, ethical expectations, and social legitimacy; and the cultural-cognitive pillar, which reflects shared understanding, knowledge, and taken-for-granted meanings among organizational actors. In Sharia governance, these pillars can be linked to maqasid al-sharia, accountability, justice, transparency, amanah, shura, and the prohibition of riba, gharar, and maisir. Regulatory readiness includes regional regulations, standard operating procedures, Sharia contracts, reporting systems, and supervisory arrangements. Normative readiness includes commitment to fairness, trustworthiness, social responsibility, and public benefits. Cultural-cognitive readiness includes managers' and beneficiaries' understanding of Sharia finance, their ability to distinguish Sharia from conventional mechanisms, and their acceptance of institutional change. This integrated framework strengthens the study's analytical basis.

Research Gap and Justification

Previous studies on Village-Owned Enterprises and Village Financial Institutions have largely focused on business performance, village income, poverty reduction, and community empowerment. Research on sharia-based village enterprises has also shown that Islamic contracts, profit-sharing mechanisms, and social finance instruments can improve inclusion and public welfare. However, limited attention has been paid to the institutional conditions required for the effective implementation of such systems. In particular, few studies have examined how regulations, organizational structures, managerial competence, financial reporting, supervisory mechanisms, and community understanding interact to determine readiness for Sharia-based governance. This gap is particularly evident in the context of BUMDesma-LKD institutions in Central Buton Regency.

This study addresses this gap by treating sharia transformation as a multidimensional institutional process rather than merely a change in financing contracts. It integrates Scott's regulatory, normative, and cultural-cognitive pillars with Islamic governance principles, including justice, transparency, accountability, amanah, shura, and Maqasid al-Sharia. This framework makes it possible to distinguish religious-cultural acceptance from actual operational readiness. This study is significant because it provides a structured basis for identifying institutional strengths, weaknesses, opportunities, and barriers before the transformation begins. The findings also support policymakers and managers in designing regional regulations, training programs, supervisory arrangements, and community education strategies that can guide a gradual, accountable, and sustainable transition toward Sharia-based village economic governance.

METHOD

Research Design

This study employed a descriptive qualitative design to examine the institutional readiness of Village-Owned Enterprises–Village Financial Institutions (BUMDesma-LKD) in Central Buton Regency to adopt governance based on Sharia economic principles. The qualitative approach was selected because the research focused on organizational practices, stakeholder understanding, regulatory preparedness, and community acceptance rather than measuring relationships among numerical variables. This study investigates how existing governance arrangements support or constrain the transition from conventional financial management to a Sharia-based model. Institutional readiness is a multidimensional condition involving regulatory support, organizational capacity, human resource competence, financial and administrative systems, Sharia-compliance mechanisms, and public understanding. This design enabled the researchers to capture both formal institutional arrangements and the practical experiences of managers, supervisors, beneficiaries, government representatives, and Islamic financial actors involved in village economic governance.

Research Setting and Units of Analysis

The research was conducted in Central Buton Regency, where BUMDesma-LKD institutions continue to manage village-level financial and economic activities that developed from former community empowerment programs. The setting was selected because these institutions possess considerable potential to support rural economic development but continue to face dependence on revolving funds, limited business diversification, incomplete administrative systems, and governance weaknesses. The primary unit of analysis was the institutional readiness of BUMDesma-LKD rather than the performance of the individual managers or beneficiaries. Readiness was examined through existing regulations, organizational structures, operational procedures, financial practices, supervisory mechanisms, managerial knowledge, and community attitudes toward Sharia governance. Particular attention was paid to whether current practices reflected principles such as justice, transparency, accountability, deliberation, public benefit, and the avoidance of riba, gharar, and maisir.

Research Participants

The study involved stakeholder groups whose roles provided different perspectives on BUMDesma-LKD governance and the prospects for Sharia-based transformation. Administrators and managers served as key informants regarding institutional policies, daily operations, financial arrangements, contracts, reporting practices and organizational constraints. Supervisors, supervisory board members, and local religious leaders contributed to the assessments of institutional accountability, social legitimacy, and conformity with sharia principles. Beneficiaries, including borrowing members, micro, small, and medium enterprise operators, farmers, and fishermen, provided information on financial access, service experiences, economic inclusion, income-related effects, and perceptions of Sharia-based financing. Representatives of the local government, particularly those from offices responsible for village empowerment and cooperatives, offered regulatory and policy perspectives. Representatives of Islamic rural banks and Islamic microfinance institutions were also included to explore possible partnerships, access to halal financing, technical assistance and supervisory support.

Data Sources and Collection Procedures

This study used both primary and secondary data to obtain a detailed picture of institutional conditions. Primary data were collected through in-depth interviews, focus group discussions, and open-ended questionnaires administered to the participants. These methods allowed participants to explain their understanding of Sharia economics, describe current savings and loan practices, identify institutional weaknesses, and assess the feasibility of adopting Sharia-based governance. Data collection began with triangulation across stakeholder groups to compare accounts and identify areas of agreement or inconsistencies. Open-ended questions were used to explore issues that required further clarification, including perceptions of interest, public acceptance, regulatory support, training needs, and operational readiness. Secondary data were obtained through a review of institutional documents, including joint regulations, articles of association, and internal regulations, supporting administrative records, and available BUMDesma-LKD financial reports. Documentary evidence was used to verify the interview findings and examine whether formal procedures corresponded with actual practices.

Thematic Data Analysis

Qualitative data from interviews, focus group discussions, questionnaires, and institutional documents were analyzed through thematic analysis supported by the NVivo software. The analysis began with the organization and coding of the data according to recurring concepts, statements, practices, and institutional concerns. Related codes were grouped into broader themes, including regulatory readiness, organizational capacity, human-resource competence, financial administration, Sharia literacy, public acceptance, supervision, and operational compliance. Word patterns and relationships among themes were examined to identify how stakeholders understood Sharia principles and how these understandings were reflected in institutional practice. The analysis also distinguished between values that were already informally present, such as fairness and transparency, and formal mechanisms that remained absent, such as Sharia contracts, standard operating procedures, supervisory structures, and compliance systems. This process enabled the study to explain the gap between the community's religious receptiveness and the institution's limited operational readiness.

SWOT Analysis and Strategic Formulation

A SWOT analysis was conducted to assess the internal and external conditions affecting the proposed transformation of BUMDesma-LKD into a Sharia-based institutional model. Internal strengths and weaknesses were identified from organizational resources, governance practices, financial systems, managerial competence, existing social values and administrative capacity. External opportunities and threats were examined through community support, government policy, potential partnerships with Islamic financial institutions, digital financial development, market opportunities, and possible resistance arising from limited literacy or conventional habits. The SWOT findings were interpreted alongside the thematic results rather than being treated as a separate numerical exercise. This integration allowed researchers to connect field evidence with strategic options and determine which institutional reforms were most feasible. The combined analysis provided the basis for recommendations concerning regional regulation, Sharia training, standard operating procedures, financial partnerships, digitalization, business diversification, social finance instruments, regular monitoring, and broader community participation.

Research Credibility and Interpretation

The credibility of the findings was strengthened by source and method triangulation. Information from managers, supervisors, beneficiaries, religious leaders, government officials, and Islamic financial representatives was compared to reduce the dependence on a single viewpoint. The interview and discussion data were also checked against open-ended questionnaire responses and institutional documents. Differences between formal rules and actual practices were treated as important analytical evidence rather than inconsistencies to be removed. The interpretation was guided by an integrated framework that combined institutional theory with Shariah economic governance. Regulatory, normative, and cultural-cognitive dimensions were used to explain whether institutional rules, shared values, and stakeholder understanding supported the transformation. Therefore, this study assessed readiness as a staged institutional process, not merely as the acceptance of Islamic terminology or the replacement of interest with alternative contracts. The findings were interpreted to produce practical recommendations that reflected the actual capacities, constraints, and opportunities of BUMDesma-LKD in Central Buton Regency.

RESULTS AND DISCUSSION

Sharia Elements in Bumdesma-LKD Practices

The results of the data analysis using a word tree indicate that the implementation of Sharia principles in BUMDESMA-LKD in Central Buton Regency is still in its early stages and has not yet become an established system. The narrative emerging in the Word Tree based on the informants' responses states that so far, there has been no effort to implement Sharia policy principles in savings and loan practices. However, several respondents' answers stated that sharia values such as justice, transparency, and non-oppression, which reflect the normative principles in the sharia system, are only partially present in practice, for example through transparent annual reports or communication with customer families in the event of a disaster, but have not been accompanied by a financing and administration system that truly adheres to sharia principles. In fact, several informants emphasized the persistence of elements of usury through the setting of loan interest rates of around 1%, which they believe cannot be categorized as a Sharia principle, so that the current practice still tends to be conventional. This is supported by the statement (Prayudi et al., 2020; Utami et al., 2023). The minimal understanding of Islamic economics in society influences people's mindsets, as there is not much difference between Islamic and conventional economic systems.

Furthermore, the data analysis shows that the community and some administrators do not yet understand the concept of Sharia, and there has been no adequate outreach from the institution to explain the mechanisms of Sharia. This means that the implementation of Sharia is not only not yet effective, but also has not yet become a necessity or a matter of collective awareness for either the administrators or the village community. Overall, the Word Tree maps language patterns that represent the real conditions on the ground: Sharia principles are understood as ideal values, but there is no policy foundation, SOPs, or operational systems to support their implementation. Informants reinforce and clarify the context, namely that the absence of specific regulations, persistence of old habits, lack of understanding, and absence of outreach are factors that prevent the full implementation of Sharia principles. This aligns with previous research stating that Sharia-compliant village-owned enterprise (BUMDes) management can increase community income, but its implementation faces obstacles, including a limited understanding of Sharia principles, which results in the suboptimal management of Sharia-compliant village-owned enterprises (A. M. Saputra & Samsahudi, 2025). The study also shows that the absence of specific regulations, persistence of old habits, lack of understanding, and absence of outreach are factors that prevent the full implementation of Sharia principles. The existence of regional regulations that adopt Sharia principles is related to the governance of village institutions or limited regulations (S. Nasution & Mu'arrif, 2025; Syujai, 2025), adequate understanding (Alamsa et al., 2025), socialization are importfactorsctor in optimizing the principles of Islamic economics in society (Musyafa, 2025).

Public Response to Sharia Concept

Village communities in Central Buton Regency have a strong religious foundation, as reflected in the responses of informants who stated that the villages in this region are known as religious communities. For example, one informant stated that "If the concept of sharia is introduced, the community is expected to accept it well, because villages in Central Buton are known as religious communities." This indicates that, culturally, the community is more receptive to and applies Sharia principles in its economic and social activities. However, community acceptance of the application of Sharia concepts in daily economic life through BUMDesma-LKD still runs counter to deep misunderstandings and a lack of adequate socialization. The lack of understanding of the differences between Sharia BUMDES and conventional BUMDES, as well as how Sharia principles should be applied in community economic activities, is quite significant. This is in line with the findings of previous studies that the lack of public knowledge about the principles of Islamic economics, such as the prohibition of riba (interest), gharar (uncertainty), and maysir (speculation), is the main reason why the public does not support institutions that implement governance policies in accordance with Islamic law (Andatu et al., 2025; Harahap et al., 2023).

The research also shows that the community and some administrators do not yet understand the concept of sharia, and there has been inadequate outreach from the institution to explain the mechanisms of sharia programs. This means that not only has sharia not been implemented, but it has also not become a necessity or a collective awareness for either the administrators or the village community. Furthermore, the lack of outreach regarding the concept of Sharia in the community also contributes to the low public response to Sharia-based institutional management (Aassouli & Ahmed, 2023; Surur & Aufa, 2020). This is supported by previous research stating that more inclusive and equitable economic development can be achieved through the socialization of the concept of Sharia economics, which also increases public knowledge about Sharia-based transactions (Sativa & Rinaldi, 2025).

Challenges and Opportunities for Implementing Sharia Concepts in BUMDesma-LKD

The results of the research data analysis indicate that stakeholders, including managers and beneficiaries, still lack an understanding of Sharia concepts. Sources from various Village-Owned Enterprises (BUMDesma) in Central Buton Regency stated that although they support the concept of sharia economics, its implementation has not been fully implemented due to a lack of adequate mentoring and outreach programs. One source emphasized, "socialization about Sharia economics must be carried out first." Although the community in this area is religiously open to the application of Sharia principles, they still have difficulty distinguishing between conventional and Sharia financial systems, especially when it comes to financing. One major misunderstanding concerns the concept of interest, which in the conventional economic system is often considered the same as usury, which in Sharia is considered a prohibited practice. This indicates that an educational approach is crucial for the community to understand the differences between Shariah and conventional BUMDes. This is in line with previous research stating that education can be a strategy to increase public trust in the management of an institution (Marshelynda & Nisa, 2024).

An interview with one source revealed that many people "still associate the word interest with usury," reflecting that despite explanations of the concept of Islamic economics, a deeper understanding of how Islamic economic principles are applied in the financing system remains lacking. This echoes the sentiment expressed by findings stating that reality on the ground shows that the public's understanding of the Islamic financial system is still far from ideal (Kafabih & Manzilati, 2018; Prabowo & Fitri, 2025). This means that even though Islamic economics does not consider interest as usury, people still consider it usury because they are familiar with conventional economic terminology. Overall, the interviews revealed that the biggest challenge in implementing the Sharia-based BUMDesma-LKD concept in Central Buton Regency is the lack of literacy and in-depth knowledge regarding the differences between the application of Sharia principles and conventional management principles. The principles of justice and sustainability within the Sharia-based institutional management concept present a significant opportunity for the development of Sharia-based BUMDesma-LKD in Central Buton Regency, given that public acceptance of this concept has shown positive value, as indicated by increased public awareness of the Sharia economy. Despite these numerous opportunities, BUMDesma-LKD faces technical weaknesses, such as a lack of Sharia training.

Buton Tengah Regency BUMDesma-LKD (Village-Owned Enterprise) in the SWOT matrix is in the Strength–Opportunity (S–O) quadrant. This means that its internal strengths are relatively dominant compared to its weaknesses, and its external opportunities outweigh its challenges. Overall, the institutional performance of BUMDesma-LKD should be viewed as a result of the interaction between the regulatory and normative pillars. The transformation to a Sharia economy will be successful if institutional regulations and norms are simultaneously strengthened. Islamic values and policy support (strengths and opportunities) must be mutually reinforcing.

Therefore, to support the optimal governance of BUMDesma-LKD in Central Buton Regency in accordance with Sharia principles, several strategic recommendations can be made: 1) Creating Regional Regulations: The transformation of Sharia Bumdesma-LKD in Central Buton needs to be strengthened through legal instruments in the form of Regent/Regent regulations or Regional Regulations; 2) Holding Sharia Training and Literacy for BUMDesma-LKD administrators through collaboration with local governments, universities, and Sharia financial institutions; 3) Establishing Sharia Bank partnerships with the aim of strengthening formal cooperation with Sharia banks or financial institutions for access to halal capital and technical assistance; 4) Providing digitalization services through the development of Sharia digital platforms such as Sharia fintech applications to manage village finances and reach more participants, while increasing transparency in governance; 5) Diversifying Sharia Businesses through the development of new business units based on the halal real economy as an effort to utilize the Sharia market as well as social capital to reduce dependence on conventional savings and loans; 6) Providing productive social funds through a productive waqf scheme or inter-village *qardh hasan*; 7) Publish SOPs and Sharia-based Internal Compliance for all business units by utilizing government support from Sharia financial mentors to ensure usury-free and accountable processes; 8) Conduct regular monitoring, which is a form of routine evaluation mechanism involving village stakeholders to ensure the implementation of Sharia strategies is in accordance with regulations (optimizing regulatory pillars) and dynamically adjusting policies; and 9) Expand community participation through deliberations to increase business capital and foster shared ownership in line with opportunities to strengthen the local Sharia economy. The application of Sharia principles in economic and business activities is believed to benefit all stakeholders and positively impact community development (Putri et al., 2024).

The findings indicate that the institutional readiness of BUMDesma-LKD in the Central Buton Regency remains partial and uneven. Three main patterns emerged from the field data. First, there is no formal Sharia governance system, as reflected in the absence of specific regulations, Sharia-based SOPs, Sharia supervisory mechanisms, and standardized contracts. Second, Sharia values such as justice, transparency, deliberation, and concern for beneficiaries are already present in limited forms, but they remain informal and have not been translated into binding institutional procedures. Third, conventional practices still dominate, particularly in savings and loan activities that continue to use interest-based mechanisms. These findings suggest that the challenge is not simply low literacy but a deeper institutional gap between religious-cultural receptiveness and operational readiness. Theoretically, this study extends institutional readiness analysis by showing that sharia-based transformation requires the simultaneous strengthening of regulatory, normative, and cultural-cognitive pillars. Practically, this implies that training, local regulation, sharia supervision, and community education should be implemented as a staged transformation roadmap rather than as isolated recommendations.

CONCLUSION

The study finds that the BUMDesma-LKD institutions in Central Buton Regency are not yet fully prepared to implement sharia-based governance. Although values such as fairness, transparency, deliberation, and concern for beneficiaries already appear in several practices, they remain informal and are not supported by legally binding procedures. Savings and loan activities still rely on interest-based mechanisms, while sharia contracts, supervisory arrangements, standard operating procedures, and compliance systems are largely absent. Limited managerial knowledge and inadequate public socialization also prevent stakeholders from distinguishing Sharia finance from conventional arrangements. These conditions show that institutional readiness is partial, uneven, and constrained by weaknesses in both governance infrastructure and collective understanding of the issue.

These findings imply that Sharia transformation cannot be achieved by merely replacing financial terminology. This requires coordinated reforms across regulatory, organizational, financial, and cultural dimensions. Regional regulations, structured training, Sharia supervision, digital reporting systems, partnerships with Islamic financial institutions, and broader community participation must be developed as mutually reinforcing components. The Strength–Opportunity position identified through the SWOT analysis suggests that Central Buton possesses a favorable religious culture, local support, and potential institutional partnerships that can sustain reforms. However, these advantages will produce limited results unless they are translated into formal rules, managerial competencies, diversified halal business activities, and accountable financing procedures that can reduce dependence on conventional revolving funds.

This study contributes to the literature by framing sharia-based transformation as a multidimensional process of institutional readiness, rather than a narrow change in contracts or financial products. By integrating Scott's regulatory, normative, and cultural-cognitive pillars with Islamic governance principles, this study explains why favorable religious attitudes do not automatically generate operational compliance. This study also provides a context-specific roadmap for strengthening village economic institutions through regulation, literacy, supervision, and organizational development. Its significance lies in showing that sustainable Sharia governance depends on the alignment of formal structures, ethical commitments, and a shared understanding. Further research should test this framework across multiple regions, compare different institutional models, and evaluate the long-term economic and social outcomes of the implemented reforms.

Limitations of the Study

This study is limited by its focus on BUMDesma-LKD institutions in Central Buton Regency, where the social, religious, economic, and administrative environments may differ from those in other Indonesian regions. Therefore, the findings reflect a specific institutional context and should not be generalized to all village-owned enterprises or village financial institutions. The qualitative design also prioritizes stakeholder interpretations and institutional narratives over statistically measurable patterns. Although interviews, focus group discussions, questionnaires, and documents provided rich information, this study does not quantify the level of readiness, compare readiness scores among institutions, or estimate the economic effects of adopting Sharia governance on income, repayment, profitability, or financial inclusion.

Another limitation concerns the developmental stage of the sharia transformation in the research setting. Because formal Sharia governance had not yet been fully implemented, the analysis evaluates preparedness and perceived opportunities rather than the actual performance of an established Sharia-based system. Participants' support for the proposed model may not accurately predict their behavior once new contracts, reporting requirements, supervision or profit-sharing mechanisms are introduced. The available institutional documents and financial reports may also vary in completeness and quality, which limits the detailed assessment of administrative and accounting readiness. In addition, the study does not include longitudinal observation; therefore, it cannot determine how institutional understanding, community acceptance, regulatory compliance, or operational capacity may change during and after implementation.

Recommendations for Future Research

Future research should examine BUMDesma-LKD institutions across several regencies and provinces to determine whether the readiness patterns identified in Central Buton also appear in areas with different religious cultures, market structures, administrative capacities and regulatory environments. Comparative studies can distinguish contextual barriers from problems that are common across village economic institutions. Researchers should also develop measurable indicators of regulatory readiness, managerial competence, sharia literacy, financial system preparedness, supervisory capacity, and community acceptance. A quantitative or mixed-methods design could then be used to test the relationships among these dimensions and produce a more precise readiness index. Such an approach would help governments and institutional managers identify priority areas, allocate training resources, and compare progress across institutions over time.

Further studies should evaluate BUMDesma-LKD institutions before and after the introduction of Sharia-based regulations, contracts, training programs, and supervisory systems. Longitudinal research could assess whether these reforms improve transparency, repayment quality, business diversification, public trust, financial inclusion, institutional sustainability, and beneficiary welfare in the future. Future analyses should also compare specific financing instruments, including murabahah, mudharabah, musyarakah, ijarah, and qardh hasan, to determine which arrangements are most suitable for village enterprises, farmers, fishermen, and microbusinesses. Research on digital Sharia platforms, productive Waqf, and partnerships with Islamic banks or microfinance institutions would further clarify viable implementation models. Community-based participatory research can ensure that institutional reform reflects local needs while remaining consistent with Sharia principles and public accountability.

Author Contributions

Conceptualization	I.W.S. & N.A.R.	Resources	I.W.S. & N.A.R.
Data curation	I.W.S. & N.A.R.	Software	I.W.S. & N.A.R.
Formal analysis	I.W.S. & N.A.R.	Supervision	I.W.S. & N.A.R.
Funding acquisition	I.W.S. & N.A.R.	Validation	I.W.S. & N.A.R.
Investigation	I.W.S. & N.A.R.	Visualization	I.W.S. & N.A.R.
Methodology	I.W.S. & N.A.R.	Writing – original draft	I.W.S. & N.A.R.
Project administration	I.W.S. & N.A.R.	Writing – review & editing	I.W.S. & N.A.R.

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Informed Consent Statement

Informed consent was not required for this study.

Data Availability Statement

The data presented in this study are available upon request from the corresponding author.

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Conflicts of Interest

The authors declare no conflicts of interest.

Declaration of Generative AI and AI-Assisted Technologies in the Writing Process

During the preparation of this work, the authors used ChatGPT, DeepL, Grammarly, and PaperPal to translate from Bahasa Indonesia into American English and to improve the clarity of the language and readability of the article. After using these tools, the authors reviewed and edited the content as needed and took full responsibility for the content of the published article.

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