Profit and Loss Sharing Application in Islamic Banking

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Abstract

The rapid development of Islamic banking in Indonesia is still faced with the fact that public knowledge about Islamic banking is still low, thus affecting public interest in becoming customers. One of them that must be understood is the procedure for profit and loss sharing in the Islamic banking system. This study aims to determine the application of profit and loss sharing in Islamic banking in Indonesia. This study uses a qualitative approach with a literature review method. The results showed that the agreed profit sharing contract was the proportion of profit sharing (called profit sharing) in terms of the percentage of possible real productivity results with a profit sharing system based on two models, namely the mudharabah and musyarakah models. This study also explains the basic differences between profit and loss sharing (PLS) and the interest system between Islamic banks and conventional banks.

Keywords: Profit and Loss Sharing, Islamic Banking, Conventional Banking.

A. INTRODUCTION

The banking sector is the most important medium in the economy because the bank is a business entity whose main task is a financial intermediary. As financial intermediaries, banks function to channel funds from parties that have excess and (idle funds/surplus units) to parties who need funds or lack funds (deficit units) at a specified time (Simatupang, 2019). The function of the bank was initially limited to exchanging and lending money. No one can tell exactly when banking institutions and financial systems emerged. But some argue that the use of the banking system is a legacy of the Roman Empire. The banking and financial affairs system in Western countries originated from the trading system brought by people from the East through mainland India to West Asia (Saraswati, 2016).

A bank is a financial institution used as a place for depositing or storing money, distributing credit, and payment traffic (Widyastuti & Armanto, 2013). Islamic banks first appeared in Egypt without using Islam for fear of being considered a fundamentalist movement. The pioneer of this business was Ahmad El Najjar, who had the idea of a savings bank based on profit sharing or profit-sharing, which operated in Mit Ghamr in the 1963 period. Furthermore, operations continued until the 1967 period until nine banks with the same system in Egypt. This interest-free
concept becomes the operational basis of this bank, so the scheme used is by way of investment in cooperation or partners (Ismail, 2017).

Indonesia first had a bank that used sharia principles in 1991, namely Bank Muamalat Indonesia. The establishment of Islamic banks in Indonesia in 1991 was at the initiative of the Indonesian Ulema Council (MUI) supported by the government plus the Indonesian Muslim Intellectuals Association (ICMI) without the exception of Muslim entrepreneurs. Even though it was affected by the monetary crisis, Bank Muamalat Indonesia remained standing even though its equity was only 1/3 of the initial capital. In 1999-2002 Bank Muamalat Indonesia rose and was able to make a profit after being assisted by the Islamic Development Bank. Initially, Islamic banks in Indonesia were regulated for their existence and operations in Law no. 10 of 1998 from the Amendment to Law no. 7 of 1992 concerning Banking.

Furthermore, Law Number 21 of 2008 concerning Islamic banking until now has been enforced. Bank Muamalat Indonesia, Bank Syariah Mandiri, and Bank Mega Syariah were Islamic banks until 2007 with three institutions. Meanwhile, there are 19 sharia business units (Main, 2018).

Profit-sharing has been known by the people in Indonesia for a long time, although it is not as busy as it is now. The profit-sharing system has been applied for generations, for example, in cultivating rice fields where the owner of the field allows people or laborers to work on the fields until harvest, then the results are divided according to the agreement from the beginning, and this practice has been going on for a long time. And even now. The agreement in profit sharing is not always 50-50 but can be done with another agreement, for example, 70-30, or 60-40 according to the agreement of both parties (Afkar, 2011).

Profit share is definitely defined as 'distribution to the employees of a firm of some percentage of the earnings.' The bonus might be a yearly cash bonus based on previous-year earnings, or it can be paid weekly or monthly. Islamic financial institutions or profit-sharing profit sharing income applies to investment products, total and partial participation, or corporate business forms (Yuliana, 2013). Being fair is one of the challenges in running a business. Still, every believer must try to obey it so that business cooperation brings safety in the world and the hereafter.

Sharia principles prohibit business activities that contain gharar, haram objects, usury, maisir, and injustice to society in general. Economic democracy is a business activity that prioritizes equity, benefit, justice, and togetherness. Islamic banking takes the initiative to support national development by moving in the real sector, not financial. Islamic banks in providing service fees that have been collected from the public are not in the form of a percentage of interest but provide benefits based on a profit-sharing system, namely the profits given to customers following the ratio or portion set by the bank. The profits obtained are based on the distribution of funds (credit) to the public. Sharia principles are used as the basis of sharia banking business

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activities in addition to economic democracy and the principles of prudence and togetherness (Marimin & Romdhoni, 2015).

The practice of profit sharing is packaged by Islamic banks in profit-sharing with various schemes using applicable sharia contracts and adjusted to financial policies. Islamic bank operations by sharing the results between customers and Islamic banks. In this case, customers who deposit their money in Islamic banks are treated as owners of funds that invest funds in Islamic banks. Furthermore, Islamic banks manage these public funds by investing in productive sectors that generate profits. Profits obtained from managing these funds are then shared with a profit-sharing system with various levels of agreement (Harahap & Siregar, 2020).

It is vital to investigate, in Indonesia, how Islamic banking shares profit and loss. Based on the explanation above. The aim of this research was to discover how the public knows how Islamic Banking profits and losses in Indonesia are distributed. It is hoped that this research would be a public benchmark and knowledge on Islamic banking, which will definitely impact Islamic banking's own development. This study can perhaps be a reference for other scientists and practitioners in the development of Islamic banking in Indonesia.

B. METHOD

Research on profit-sharing and loss-sharing in Islamic banking in Indonesia blends the literary review with a qualitative method. Qualitative research is a sort of study whose results are not produced by statistical or other methods of computation. In such cases, he attempts to comprehend and to interpret the significance of an occurrence in the light of the researcher's point of view (Gunawan, 2013). Qualitative techniques aim to comprehend and understand in particular conditions the significance of an event for human behavior interaction from the point of view of the investigator. Qualitative research is aimed at understanding the thing under examination in depth (Somantri, 2010).

Secondary data sources used in this investigation. Secondary data are collected or collected by third parties indirectly by means of intermediate media. Secondary data from books, papers, past research, and other publications have been gathered in this study. The examination of the study results carried out using descriptive analysis contains two categories of secondary data, i.e. internal and external data. Data supporting the research will be collected and evaluated through the description or description of the actual condition of the object. This analysis of the data is essential since the data acquired can be beneficial in solving research issues by means of that analysis.
C. RESULT AND DISCUSSION

Sharia prohibition is the result of a complete removal of interests. Sharia interest prohibition PLS theory is constructed as a new offers outside the interest system, not reflecting the justice system (injustice/dzalim) since it discriminates against the risk and profit-sharing by economic actors. Muslim financial principles have been established based on a ban on usury, a ban on *ghararar*, halal management of business, shared corporate risk, and economic transactions, based on fairness). Sharing profit-loss is sharing of earnings or losses resulting from economic/corporate activity. There is no set and definite profit as interest in the attribute of profit sharing, but profit and loss share is dependent on the actual productivity of the product (Maswedah, 2014).

In fact, in the modern economy, financing with the PLS system is common in various business equity financing activities. Share ownership in a company is a popular example of equity participation. Shareholders will receive profits in the form of dividends and bear the risk if the company suffers losses (Abbas & Arizah, 2019).

The capital price is established by the function of entrepreneurship in the profit-loss sharing system. In establishing the price of the components of production, capital prices and entrepreneurship is an integrative unit. In the Sharia’s view, only true productivity can generate money. The concept that produces no production is not supplemented (Setiono, 2018).

The negotiated profit-sharing agreement is the percentage share (called the profit sharing ratio) of the potential actual productivity outcomes. The nominal value of the agreed profit sharing can only be recognized when the results are available (ex-post phenomenon, not ex-ante). The profit-sharing ratio is established on the basis of a consensus between the parties. The proportion amount is normally affected by taking account of each party’s commitment to cooperation (sharing and partnership) and the profit perspective (anticipated return), and the level of risk that might arise (expected risk).

The agreement on a ratio level must first consider these three factors. The first factor, share on the partnership has been real and measurable. Consequently, extra attention is not needed. Special attention is required for the last two criteria, anticipated return and projected risk. The capacity to assess the benefit and risk in collaboration with PLS is therefore important, in particular in the face of potential hazards. Firstly, this is because risk hurts the business—the greater the risk, the lower the value of business profits. Second, risk has a source, scope, and nature that often do not consider the data carefully. Third, estimates of profits usually include calculating risk variables (Maisur & Shabri, 2015).

Risk arises because there is uncertainty in the future. Van Deer Heijden (1996) divides uncertainty into three categories:
1. Risks. Its occurrence may have historical precedent, and a probability estimate can be made for each possible outcome.

2. Structural uncertainties. The likelihood of an outcome occurring is unique, having no precedent in the past. However, it is still possible in the logic of causality.

3. Unknowables. The occurrence of extreme events was unimaginable before.

In this category, the risk is a term for the probability of an event with historical precedent and follows a probability distribution. Therefore, the actual risk can be estimated -- at least theoretically. Meanwhile, Tri Mulato (2017) uses the word risk for everything that happens uncertainly in the future. Risk is divided into two aspects, namely:

1. Passive risk is a risk and no computations and the reply is uncertain. 1. 1. A risk is passive. Estimates of this danger depend solely on luck, as one can only remain passive.

2. Responsive risk is a risk whose cause and probability distribution have been explained. Certain approaches can be used to quantify this risk. Estimating responsive risk is frequently referred to be a game of competence as it is based on a certain competency.

Within certain limits, the risk can be estimated so that a person’s acceptance of the profit-sharing ratio is not merely speculative. Risk is a consequence of productive activity. Risks that need to be avoided cannot be predicted, such as passive risks or unknowns. This kind of risk in the terminology of fiqh mu’amalah is called gharar, which is truly speculative. Gharar occurs because someone does not (can) know the possibility of something happening, so it is gambling or a game of chance. If one party receives a profit, then the other party must suffer a loss. This means that there has been a win-lose solution. Sharia transactions reflect a positive-sum game or win-win solution as in the teachings of profit-loss sharing theory.

Based on the theoretical framework of mu’amalah fiqh (sharia), it can be stated that the interest system is included in the category of gharar scope. This is because, in the process, it has a game of chance nature. PLS theory was developed in two models, namely the mudharabah and musharaka models. A kind of economic collaboration between two parties is referred to in the Mudharabah model. The first party offers the entire capital (Shaibul maal). The other party is the fund manager; the musyarakah model is a collaboration agreement between two or more parties that run a certain business. The other party is the fund manager. Each side provides funding to agree on the sharing of advantages and risks after the agreement (Jaffar, 2010).

This model is called mudharabah because, at the time of the business cooperation agreement, one party contributes capital. In contrast, the other party contributes to entrepreneurship in energy, thought, or management. The first party is called sahib al maal (financier), while the second party is called mudharib (entrepreneur). In this
scheme, 100% of capital is borne by 

sahib al maal. Meanwhile, management is entirely the responsibility of the mudharib. Meanwhile, the Musyarakah model scheme shows that each party contributes to the capital. They agreed to do profit-loss sharing.

An institution that plays a part in taking deposits from other customers who require money is one of the important tasks of the bank. For conventional banks, the main source of profit is the gap between the interest payable to borrowers and the interest payable to depositors. Meanwhile, the Islamic banking system is different from the conventional banking system, because it is a subsystem of a larger Islamic economic system. Islamic banking is therefore necessary not just to create economic profit, but also to show seriously how Sharia ideals are being achieved (Lestari, 2015) (Lestari).

Profit-sharing is determined based on the ratio agreed between the bank and the customer. In sharia, it is not stated how much the profit sharing ratio between the customer and the bank. The rapid development of Islamic banking in Indonesia is still faced with public knowledge about Islamic banking. Because public knowledge about banks in general and Islamic banks will affect the public's interest in becoming their customers. One of the knowledge that must be understood is the procedure for distributing profit and loss. Therefore, this study aims to determine the implementation of profit and loss sharing in Islamic banking in Indonesia. This study uses a qualitative approach with a literature review method. The study results show that the agreed profit-sharing agreement is the proportion of profit sharing (called profit sharing ratio) in percentage size of possible real productivity results with a profit-loss sharing system based on two models: the mudharabah musyarakah models. This study also explains the basic differences between PLS and the interest system between Islamic banks and conventional banks.

The determination of the amount of the ratio is determined based on the agreement of each contracting party. Still, in practice in modern banking, the bargaining ratio between the owners of capital (i.e., investors or depositors) and Islamic banks only occurs for depositors/investors with large amounts because they have relatively high bargaining power. This condition is known as a special ratio, while for small depositors, bargaining does not occur. Sharia banks will include the ratio offered, and depositors may agree or not. If he agrees, he will continue to save; on the other hand, he is welcome to look for another sharia bank that offers a more attractive ratio if he does not agree.

There is no clear reference regarding the determination of the profit-sharing ratio in Islamic banking. The determination is only influenced by calculating and using the market interest rate method as a reference. So that in practice, there are still many Islamic banks that use the pattern of conventional banks in determining the ratio. This raises criticism regarding the consistency of Islamic banks in applying Islamic principles in their banking activities. If the contract in sharia banking still refers to the interest mechanism in conventional banking, sharia banking is not yet 100%
sharia-based. So that it can cause injustice to certain parties, even though Islam is against injustice and exploitation.

Determination of the ratio results from thoughts/ideas made by humans, not from teachings/orders from Allah SWT. Determination of the ratio that refers more to the conventional bank mechanism is evidence that the capitalist economic system still greatly influences the economic system in general and as a whole. But at least with Islamic banking, there have been efforts to avoid usury in banking activities gradually.

Perwataatmadja & Antonio (1992) formulate the difference between profit sharing and interest as follows:

1. Determination of the interest percentage does not take into account the possibility of profit and loss. In contrast, the determination of the profit-sharing ratio takes into account the possibility of profit and loss.
2. The interest rate is based on the amount of the loan, but the profit-sharing ratio is based on the real profit amount.
3. Payment of interest is not related to the profit or loss of the project concerned, while the distribution of results is related to the profit or loss of the project concerned.
4. Even if the number of profits or the financial position doubles, the quantity of interest payments does not rise, but the profit participation increases with the expansion of revenues.
5. All religions, at least as written in the holy books, doubt or even blame the existence of interest, while the validity of the profit-sharing no one doubts or even blames.

Profit-sharing and interest both provide benefits but have a fundamental difference due to the difference between investment and money interest. The law is clear that Islam forbids interest because it equates it with usury. On the other hand, Islam justifies profit sharing because the profit-sharing system reflects the principle of justice in every activity (Chapra, 2000).

Islamic banking provides the best solution to eliminate interest (usury) in various transactions and financing activities, which are based on Islamic law. The profit-sharing system in Islamic banking is very different from the interest system in conventional banking. The difference between Islamic banks and conventional banks can be compared as follows:

1. A bank with Sharia principles is a bank, while a traditional bank is a bank whose operations are not based on Sharia rules. Sharia.
2. Sharia Bank is a financial institution whose main purpose is to provide payment and other services using sharia principles, whereas regular banks are the reverse. Sharia Bank.
3. Sharia banks in their business activities are carried out based on Islamic law, which prohibits the element of interest/usury, while conventional banks are the opposite.

4. Islamic banks in obtaining profits with the principle of large profit-sharing, the profit-sharing ratio is made at the time of the contract based on profit and loss. In contrast, conventional banks earn profits using the interest/usury principle, whose interest determination is made at the time of the contract with the assumption that it must be profitable.

5. Islamic banks in their business activities, both in accommodating customer money and distributing their money, are based on the investment principle. Business activities contain risks because they face uncertain elements, the profits of which are uncertain and not fixed. Meanwhile, conventional banks in their business activities are based on the principle of interest in money, whose business activities are less risky because the profits are relatively certain and fixed.

Based on some of the differences above, it can be seen that the development of Islamic banking in Indonesia has its advantages, namely, in addition to relying on the financial sector, it also relies more on the real sector, which aims to prosper the community and improve the economic system. In addition, there is an advantage in the structure of the authorized institution in the development of sharia banking, namely the existence of a National Sharia Council, which is in charge of overseeing the operations of banks and their products so that they are following shariah lines. So that makes Islamic banking in Indonesia still feasible to continue to grow.

**D. CONCLUSION**

Profit-sharing is a fair and clean business. It gives satisfaction to both parties because the results received by each are following the contributions that have been given to customers. The method of sharing operating results follows the contribution by following the ups and downs of operating results through income. The application of the profit-sharing instrument reflects fairness more than the interesting instrument. Profit-sharing sees the possibility of profit and risk as a fact that may occur in the future. At the same time, interest-only follows the certainty of profit on the use of money.

The basic principles of profit-sharing in Islamic banking consist of: the Principle of Cooperation, the Principle of Trust, the Principle of Prudence, the Principle of Responsibility, and the Principle of Justice. The comparison between the profit-sharing system in Islamic banking and the interest system in conventional banking lies in the concept of getting the benefits. The determination of the interest percentage does not take into account the possibility of profit and loss. In contrast, the determination of the profit-sharing ratio takes into account the possibility of
profit and loss. Sharia banking can play more of an investment banking role with a profit-sharing system, while conventional banking always uses a money-interest system.

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