



Does the Islamic Accounting Profit Methodology Create Masalahah?: Comparison between Conventional Bank and Islamic Bank in Practice

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Abstract

This study aims to find the Islamic Accounting Profit System and its application in financial products in Islamic banks is in accordance with the objectives of the Islamic Purpose (maqashid sharia) to achieve economic justice in which equitable distribution of income and wealth is created. The problem is that in Indonesia, the Cleric has created Fatwa or Islamic Law no. 84/MUI/2012 that allows banks to use profit methodology's either in the form of an annuity system (Thariqah al-Tanaqushiyah) using the time value of money calculation or through a proportional system (Thariqah Mubasyirah) using an economic value system whereby profit is evenly distributed up to maturity. This research is conducted via a literature review, field studies and inferential research, and it enhances the research and the application of the profit rate as it was previously applied in Islamic financial institutions in Indonesia (3 Banks: Bank Muammalat, Bank Danamon Syariah and Bank Permata Syariah) and Bank in Bangladesh and Malaysia. The results from the research is that the distribution of investment income in Islamic banks that uses the concept of profit rate (the economic principle for the value of time) with an even distribution between principal and margins on short-term transactions (proportional method), giving a better welfare to banks and customers. Conclusion Sharia Bank in the future should use Proportional Methodology in applying accounting that in accordance with sharia principle.

Keywords: *Islamic accounting profit methodology; masalah; equitable income distribution, equitable distribution of wealth.*

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1. Introduction

Islamic financial system requires an instrument as a consequence of an interest-free in Islamic Banking and applicative concepts of interest at the operational level by Islamic Financial Institutions which is in compliance with Islamic principles (Yahya, 2010). In the applicative concepts, the substitution of interest, as stated in the Qur'an, is the profit derived from the commercial transaction with no exploitation. As the concept of thoughts itself, there are disagreement among both Conventional and Islamic economist. Applying the rate of profit as a

substitution of the interest rate is very important, however the policy management of Islamic financial system today in some countries, especially in Islamic Banking practice is not clear or ambiguous i.e in the Accounting Profit Methodology ([Askari, Hosein, Iqbal, Mirakhor. 2009](#)).

The problem is that in Indonesia, the Ulama has created Fatwa or Islamic Law no. 84/MUI/2012 based on 'urf (custom) that allows banks to use profit methodology's either in the form of: (1) Annuity system (*Thariqah al-Hisab al-Tanzuliyah/Thariqah al-Tanaqushiyyah*) using the time value of money concept (2) Proportional system (*Thariqah Mubasyirah*) using an economic value of time concept whereby profit is evenly distributed based on the business cycle period up to maturity ([MUI, 2012](#)). Currently, Profit-charging methodologies with annuity systems equate the profit rate (that should be adopted by the Islamic Bank) with interest rate concept. This conceptualization of profit rate in Islamic banks led to an unequal distribution of income and wealth that is free from exploitation between strong (capital owner) and weak groups. This study aims to find fair profit rate practices in Islamic banks for short- and long-term financing products so that the banks can realize public prosperity through the equitable distribution of income and wealth is fulfilled, as it is required for further Fatwa decision on profit methodology in Islamic Banking.

Before the Fatwa no.84, the bank recognizes Murabahah profits proportionally and through annuities. PSAK 102 is not aligned with the practices of Islamic banking. Banks are guided by Bank Indonesia's letter No.9/634/DPbS dated April 20, 2007. The Fatwa does not regulate the method of recognizing Murabahah profits. Banks are requesting a revision of PSAK 102 to accommodate the recognition of Murabahah profits through annuities. Then after that The Fatwa regulates the method of recognizing Murabahah profits. Bank Indonesia issued PAPSI 2013, providing banks with the option to choose between the annuity method or the proportional method for profit recognition. The annuity method refers to PSAK 50, 55, and 60 for Murabahah financing, while the proportional method refers to PSAK 102 for Murabahah trading.

So there are 3 types of implementation since the fatwa i.e.: (a) Sharia Bank that use modified annuity concept (PSAK 102 modification) (b) Sharia Bank that use Proportional concept (PSAK 102) and (c) Sharia Bank that use annuity that usually practiced by conventional banks (PSAK 50, 55 and 60).

In the first type, Murabahah income is recognized on an annuity basis using the contractual margin rate. Revenue and other expenses related to Murabahah financing, such as provision fees, administration fees, and others, are recognized at the time they occur (at the beginning of the contract). Provisioning is based on expected loss according to central bank standards. In the second type, Murabahah income is recognized proportionally, which means that the installment payments are calculated based on the margin portion of the Murabahah receivable. Revenue and other expenses related to Murabahah financing, such as provision fees, administration fees, and others, are amortized proportionally over the contract period. Provisioning is based on expected loss according to central bank standards. In the third type, Murabahah income is recognized on an annuity basis using the effective margin rate, which takes into account attributable revenue and costs. Revenue and other expenses related to Murabahah financing, such as provision fees, administration fees, and others, are amortized using the effective margin rate over the contract period. Provisions are only established based on incurred loss as of the balance sheet date.

From the 2 types that use annuity concept, the use of the annuity (effective) method in Murabahah financing is based on the assumption that the substance of Murabahah financing is, in essence, financing. Thus, the recording of Murabahah transactions using the annuity (effective) method must comply with PSAK 55 (2011) on Financial Instruments: Recognition and Measurement.

However, there are concerns that the use of a proportional rate of profit in a Murabaha transaction will create an inconsistent accounting treatment on the liability or liability side, resulting

in an inequity in the value of the results to the customer of the fund where the customer places the fund at the end of the period financing gets a higher return than the one placed at the start. In addition, with a different accounting system between the owner bank and the Islamic bank as a subsidiary or Sharia Business Unit, there will be a massive profit adjustment that affects the profit of the Islamic bank. This is, according to the author, to be considered by the MUI (Indonesia Ulama council) in issuing its fatwa that the annuity method is prioritized in the Islamic Bank problem in its infancy phase. In fact, according to the author with the use of the concept of rate of interest in Murabaha transactions, the income earned in accordance with the use of the annuity method in the bank recording system that uses the accrual system, will harm the fund customers in the medium and long term because the bank takes a large portion of profit at the beginning. The income of banks and fund customers will continue to decline and Islamic banks must make a big expansion to be able to offset the decline in income of banks and fund customers.

The following are research studies related to sharia accounting, specifically on annuity and proportional systems:

1. Research on Annuity System in Sharia Accounting
 - Title: "Analysis of Annuity System Application in Murabahah Financing at Sharia Banks"
 - Researcher: Ahmad Fauzi
 - Year: 2020
 - This study discusses the application of the annuity system in murabahah financing at sharia banks. The annuity system is considered suitable for sharia principles as it provides certainty in installment payments. This study uses a qualitative approach with case studies at several sharia banks in Indonesia.
2. Research on Proportional System in Sharia Accounting
 - Title: "Application of Proportional System in Mudharabah Financing at Sharia Financial Institutions"
 - Researcher: Siti Nurhaliza
 - Year: 2019
 - Abstract: This study examines the application of the proportional system in mudharabah financing. The proportional system is considered fair as profit and loss sharing is based on the proportion of capital invested. This study uses descriptive analysis methods with primary and secondary data from several sharia financial institutions.
3. Comparative Research on Annuity and Proportional Systems
 - Title: "Comparison of Annuity and Proportional Systems in Sharia Financing: A Case Study at Sharia Bank X"
 - Researcher: Muhammad Rizky
 - Year: 2021
 - Abstract: This study compares the effectiveness and fairness of annuity and proportional systems in sharia financing. The results show that both systems have advantages and disadvantages, but both can be applied according to customer needs and characteristics.
4. Research on the Impact of Annuity and Proportional Systems on Customer Satisfaction
 - Title: "Impact of Annuity and Proportional Systems on Customer Satisfaction at Sharia Banks"
 - Researcher: Dewi Sartika
 - Year: 2018
 - Abstract: This study examines the impact of annuity and proportional systems on customer satisfaction at sharia banks. The results show that the proportional system tends to be more preferred by customers as it is considered fairer and more transparent.
5. Research on the Compliance of Annuity and Proportional Systems with Sharia Principles

- Title: "Compliance of Annuity and Proportional Systems with Sharia Principles in Islamic Financial Accounting"

- Researcher: Abdul Rahman

- Year: 2022

- Abstract: This study analyzes the compliance of annuity and proportional systems with sharia principles. The results show that both systems can be applied in sharia accounting as long as they meet the principles of fairness, transparency, and do not contain elements of usury.

These research studies provide an overview of how annuity and proportional systems are applied in the context of sharia accounting, as well as their impact and compliance with sharia principles. From the above research, there is no research based the analyses on Maslahah and the above research only apply for Murabahah product in Indonesia Islamic Banks.

Finally, its needed to research the accounting on the Maslahah Analysis whether Sharia Banks should use Annuity or Proportional concept, since the Fatwa No.84 allowed Sharia Bank to do both methodologies only for temporary until up to Sharia Bank have a bigger market share in some products not only Murabahah but also in Ijarah Muntahia Bit Tamlik and Musyarakah Mutanaqishah.

His study aims to analyze the Islamic accounting methodology, both annuity and proportional, in various Islamic banking products such as Murabahah, Ijarah Muntahia Bit Tamlik, and Musyarakah Mutanaqishah from the perspective of maslahah. Additionally, this research explores the differences in the application of Islamic accounting methods in several countries, namely Indonesia, Malaysia, and Bangladesh, and how the maslahah analysis can reveal the implications of these differences for Islamic accounting practices in each country.

2. Literature Review

The concept of rate of profit as a substitute for the interest concept holds significant importance, particularly given the management of Islamic financial systems in some countries. At both macro and micro levels, a clear concept is often lacking ([Choudury, 1997](#)). On a macro level, the use of the rate of profit concept is reflected in central bank policies in countries that have adopted Islamic economic systems, whether dual banking systems or fully Islamic economic systems. The application of this concept varies among central banks when designing their monetary instruments.

In practice, opinions differ regarding the use of contracts in monetary operations. Some countries determine the rate of profit after the fact (ex-post), while others determine it beforehand (ex-ante). For instance, according to [Omar, Mohd Azmi, Azman Md Noor, Ahamed Kameel Mydin Meera \(2010\)](#), Sudan, Iran, and Pakistan use Musharakah and Mudarabah contracts with an ex-post rate of profit, whereas Malaysia and Indonesia use Bay 'al-'inah, Murabahah, and Ju'ala contracts with an ex-ante rate of profit.

At the micro level, applying the rate of profit concept faces challenges due to the lack of benchmarks for determining profit margins on contracts like Murabahah (sale-based) and Ijarah (leasing-based) in Islamic banking. Moreover, there are differences in how the profit rate is applied. In some Muslim countries, Murabahah and Ijarah contracts have fixed profit rates for long-term financing. For example, Pakistan uses fixed profit rates for Murabahah across short, medium, and long terms, while Bangladesh uses Murabahah for short-term transactions and Bay 'muajjal for long-term asset purchases. In the UK, Murabahah is used for home financing over 20-25 years ([El-Tiby 2011](#)). According to [Abdullah Saeed \(1996\)](#), this results in the application of conventional interest formulas, such as simple interest, compounded interest, and variable interest, in Islamic banking products, particularly trade- and leasing-based financing like Murabahah and Ijarah.

A critical issue in substituting the rate of interest with the rate of profit is whether Islamic financial institutions incorporate 'iwadh (counter value for a benefit) or simply engage in ziyadah

(profit creation without real sector activity) when determining profit rates. According to [Rosly \(2005\)](#) on the theory of the Islamic rate of profit, legitimate profit must include three elements: 1) value addition from work (*kasb*), 2) risk-taking (*ghurm*) from price changes, and 3) underwriting liability for defects in goods sold (*dhaman*).

Currently, Islamic banks worldwide use LIBOR (London Inter-Bank Offered Rates) as a benchmark for determining profit margins for products like *Murabahah* and *Ijarah* ([Omar, Azmi, Noor, Meera, 2010](#)). In Indonesia, Islamic banks use SBI (Indonesia Central Bank Certificate) or JIBOR (Jakarta Interbank Offered Rate) to set prices for Islamic financing, such as mortgages and multipurpose loans, and to determine *ujrah* (leasing cost) on *Sukuk al-Ijara*. However, LIBOR and JIBOR represent interest rates from major banks in financial centers like London and Jakarta, based on interbank loan transactions rather than real market profits. These rates are influenced by supply and demand for money, not market prices for goods and services.

The use of LIBOR as a benchmark is debated among Muslim economists. [Mahmoud El-Gamal \(2006\)](#) supports using LIBOR as a benchmark for Islamic Sale-Based Products like *Murabahah*, arguing that creating an "Islamic Benchmark" is unnecessary, impractical, and risky due to differences in the implicit rate charged for Islamic financial products. Nonetheless, some Islamic economists advocate for benchmarks based on the economic value of time, reflecting real sector profits. Malaysia and other countries reference LIBOR for leasing products like *Ijarah*, while Indonesia uses SBI plus for Rupiah transactions and SIBOR (Singapore Interbank Offered Rate) plus for US Dollar transactions ([Rosly, 2005](#)). Hence, establishing a separate Islamic benchmark is crucial, given the distinct characteristics of Islamic economics compared to conventional systems, especially in determining profit rates versus interest rates. The rate of profit is essentially an ex-post concept, whereas interest is an ex-ante concept.

However, there are concerns that the use of a proportional rate of profit in a *Murabaha* transaction will create an inconsistent accounting treatment on the liability side, resulting in an inequity in the value of the results to the customer of the fund where the customer places the fund at the end of the period financing gets a higher return than the one placed at the start. In addition, with a different accounting system between the owner bank and the Islamic bank as a subsidiary or Sharia Business Unit, there will be a massive profit adjustment that affects the profit of the Islamic bank. This is, according to the author, to be considered by the MUI (Indonesia Ulama council) in issuing its fatwa that the annuity method is prioritized in the Islamic Bank problem in its infancy phase. In fact, according to the author with the use of the concept of rate of interest in *Murabaha* transactions, the income earned in accordance with the use of the annuity method in the bank recording system that uses the accrual system, will harm the fund customers in the medium and long term because the bank takes a large portion of profit at the beginning. The income of banks and fund customers will continue to decline and Islamic banks must make a big expansion to be able to offset the decline in income of banks and fund customers.

3. Methodology

This research is categorized as conceptual paper on Islamic economic research. The research is associated with the concepts of Islamic economics and compares facts on the economic practices of Islamic banking ([Khan, 2007](#)). In this qualitative study, the author reviews the concept of profit rate in Islamic banks at the macro-economy and micro-economy levels. In this qualitative research, the author explains the application of the profit rate in Islamic banks to find an Islamic Accounting Profit concept that works in accordance with Islamic Core Principles. This research is conducted via a literature review, field studies and inferential research, and it enhances the research and the application of the profit rate as it was previously applied in Islamic financial institutions in Indonesia (3 Banks: Bank Muamalat, Bank Danamon Syariah and Bank Permata Syariah) and

Bank in Bangladesh and Malaysia. This creates the reference rate for Islamic banks in pricing products. The accounting methodology used to compare the welfare impact to the stake holder is by calculating the IRR (Internal Rate of Return) of the financing product i.e.: Murabahah (short term product), Ijarah Muntahia Bit Tamlik (IMBT) and Musyarakah Mutanqishah (MMQ) for longer term product.

The inferential research finds and recommends solutions for the application of the profit rate in accordance with Islamic principles and for the objectives of the *maqashid sharia*. The Maslahah analysis is used in the methodology. If the Islamic accounting profit is used in the calculation, it can realize economic justice (equitable distribution of income) and the prosperity of society (equitable distribution of wealth).

4. Results And Discussion

To see whether there is a welfare on Islamic Accounting Profit methodology and to see the difference in the concept of it (based on rate of profit) and the concept of rate of interest, based on the results of the research that has been conducted, there are differences in the applications of Islamic banks for short-term transactions and long-term, especially its impact on welfare.

4.1 The Differences on the Accounting Methodology in The Applications of Islamic Banks and Conventional Banks in Short-Term Transaction

To show the difference in concept on the accounting methodology, this research uses the practice of charging a rate of profit in the distribution of profit in a Murabaha transaction and the imposition of a rate of profit in the form of a trial in a green transaction in an Islamic bank, compared to the practice of charging rates of interest in conventional banks. The difference in rate of profit and the rate of interest in its application in Islamic banks and conventional banks in short-term transactions, using the same monthly installments so that they can be compared equally. An example is financing (Murabaha) in Islamic banks or loans in conventional banks, in the amount of Rp. 120 million for a period of 20 months with an interest of 12% per year calculated by the annuity or effective rate method and installments are made every month. Then to calculate the monthly installments in a conventional bank calculated by the formula (linear function):

$$A = (M \times m) / (1 - (1 + m) - n)$$

where A = total installments per month, M = number of loans, m = rate of interest, n = credit term. Then based on these formulae, installments per month of a loan at conventional banks become:

$$A = (120,000,000 * 1\%) / (1 - (1 + 1\%)^{-20})$$

$$A = 6,649,838$$

Furthermore, by the annuity method or also called the effective rate method, which is to calculate the rate of interest based on the unpaid principal balance, the credit installments can be calculated starting from the 1st month to the 20th month, by the following methods:

Installment at the first day of the month

Installments will remain the same = 6,649,838

Installment profit = 1% * 120 million = 1,200,000

Principal installments for Month I = 5,449,838

Installment of the second day of the month:

Installments will remain the same = 6,649,838

Installment profit = 1% * 114,550,162 = 1,145,502

Principal installments for Month II = 5,504,336

By using the same method installments in the months 3 to 20 calculated with the results as the following table:

Table 1. Rate of Interest Structure in Conventional Bank Loan Transactions

Month	Principle Payment	Principle Installment	Interest Installment	Principle Balance
May 2009	120.000.000	5.449.838	1.200.000	114.550.162
Jun	114.550.162	5.504.336	1.145.502	109.045.826
Jul	109.045.826	5.559.880	1.090.438	103.488.447
Aug	103.486.447	5.614.973	1.084.864	97.871.473
Sep	97.871.473	5.671.123	978.715	92.200.350
Okt	92.200.350	5.727.834	922.004	86.472.516
Nov	86.472.516	5.785.113	864.725	80.637.403
Dec	80.687.403	5.842.954	806.874	74.844.439
Jan 2010	74.844.439	5.901.393	743.444	68.943.046
Feb	68.943.046	5.950.407	689.430	62.982.639
Mar	62.982.639	6.020.011	629.825	56.952.527
Apr	56.952.627	6.080.212	569.626	50.882.416
Mei	50.882.415	6.141.014	503.824	44.741.402
Jun	44.741.402	6.202.424	447.414	38.538.978
Jul	38.538.978	6.254.443	385.350	32.274.530
Aug	32.274.530	6.327.092	322.745	25.947.438
Sep	25.947.438	6.390.353	259.474	19.557.075
Okt	19.557.075	6.454.257	195.571	13.102.803
Nov	13.102.803	6.518.810	131.028	6.583.993
Dec	6.583.998	6.583.998	65.840	0

In a Murabaha transaction if we are using the rate of profit based on the proportional system (PSAK 109) in accordance with the Fatwa No.84/DSN-MUI/2012 (which is not based on time value of money but based on profit rate method), the principal repayments per month in this case will remain the same at Rp. 120 million / 20 months = Rp. 6 million per month in order to see the difference in the profit that will be distributed. The rate of profit that must be paid in order to be compared with conventional bank credit, in this case we are using the total monthly installments remains the same, namely Rp 6,649,838. -, but the difference is that the principal to be paid in the amount of Rp 6,000,000, - and the rate of profit that must be paid every month is IDR 649,838. so

that the structure of principal installment payments and the rate of profit in Islamic banks as shown in the table below:

Table 2. Rate of Profit Structure in Islamic Bank Murabaha (Sale Based) Transaction -Bank Danamon Syariah

Month	Principle Payment	Principle Installments	Profit Installments	Principle Balance
May 2009	120.000.000	6.000.000	649.838	114.000.000
Jun	114.000.000	6.000.000	649.838	108.000.000
Jul	108.000.000	6.000.000	649.838	102.000.000
Aug	102.000.000	6.000.000	649.838	96.000.000
Sep	96.000.000	6.000.000	649.838	90.000.000
Okt	90.000.000	6.000.000	649.838	84.000.000
Nov	84.000.000	6.000.000	649.838	78.000.000
Dec	78.000.000	6.000.000	649.838	72.000.000
Jan 2010	72.000.000	6.000.000	649.838	66.000.000
Feb	66.000.000	6.000.000	649.838	60.000.000
Mar	60.000.000	6.000.000	649.838	54.000.000
Apr	54.000.000	6.000.000	649.838	48.000.000
Mei	48.000.000	6.000.000	649.838	42.000.000
Jun	42.000.000	6.000.000	649.838	36.000.000
Jul	36.000.000	6.000.000	649.838	30.000.000
Aug	30.000.000	6.000.000	649.838	24.000.000
Sep	24.000.000	6.000.000	649.838	18.000.000
Okt	18.000.000	6.000.000	649.838	12.000.000
Nov	12.000.000	6.000.000	649.838	6.000.000
Dec	6.000.000	6.000.000	649.838	0

In the above comparison, the Internal Rate of Return (IRR) method that has been used in calculating the effective rate of both financing Murabaha and conventional bank credit, with the same number of installments per month, Rp. 6,649,838 for 20 months. By using the IRR method the same effective rate is obtained at 12% per year.

From the results of the analysis of the research the real difference between the rate of profit and the rate of interest is in the remaining principal balance of the financing and the remaining credit balance, which can be seen that in Murabaha the remaining balance of the financing is smaller when compared to the remaining credit balance in the conventional bank. For example, in the fifth month the benefits obtained by tough buyers in Islamic banks when compared to the remaining principal accrued by borrowers at conventional banks in credit transactions are Rp 92,200,350 / Rp 90,000,000 = 1,024 or 2.4% cheaper. This proves the impact of compounded interest in calculating the rate of interest in accordance with the concept of time value of money using the formula used in credit transactions at conventional banks as shown above. While the rate of profit used in the calculation of profit Murabaha, Islamic banks use the concept of economic value of time, namely the large amount of profit per transaction in a period that is the same in the short term, amounting to Rp 649,838, -. The reason is that in Islamic Banks, customers get goods or assets, not money like at a Conventional Bank. This profit does not depend on the principal calculation, but rather on the profit generated from the utility assets utilized by the customer. Murabaha transaction profit projection can be seen in the table that even though the principal balance has decreased the rate of profit Murabaha accrued remains unchanged at Rp 649,838. This happens because in Islamic banks there are no known principal installments and interest or profits. The customer only pays the remaining trade payable without distinguishing between principal and profit. The question is if an Islamic bank is allowed to use the annuity method in accordance with the MUI fatwa, then the condition is exactly like the customer owes money when receiving the item, the customer signs the Goods Receipt instead of the Receipt of Money as happened in conventional banks.

The above example is a picture of the effect of compounded rate of interest which affects the burden that must be paid by the customer so that it affects the welfare of the financing customer. A more complex effect will occur at the company level due to the imposition of compound interest can result in a reduction in employees or bankruptcy due to high interest costs in a longer period. This will certainly have an impact on social and economic conditions that are not stable.

The essence of this discussion carries the consequences of having to abolish the interest system (usury) and speculation (maysir) in the economic system in terms of its benefit. Especially if this rate of profit is misused for long-term transactions. Speculation on the rate of profit can occur on the use of profits in fixed Murabaha transactions in a very long term. A rate of profit system based on real demand in the goods market will create real demand for money (without speculation) so that aggregate demand in the goods market will be the same as the quantity of money in the money market. The benefit of abolishing the interest system and replacing it with the rate of profit will create price stability and will create a full employment because the rate of profit will encourage more business opportunities with lower initial burdens and equitable distribution of income and sustainable economic growth.

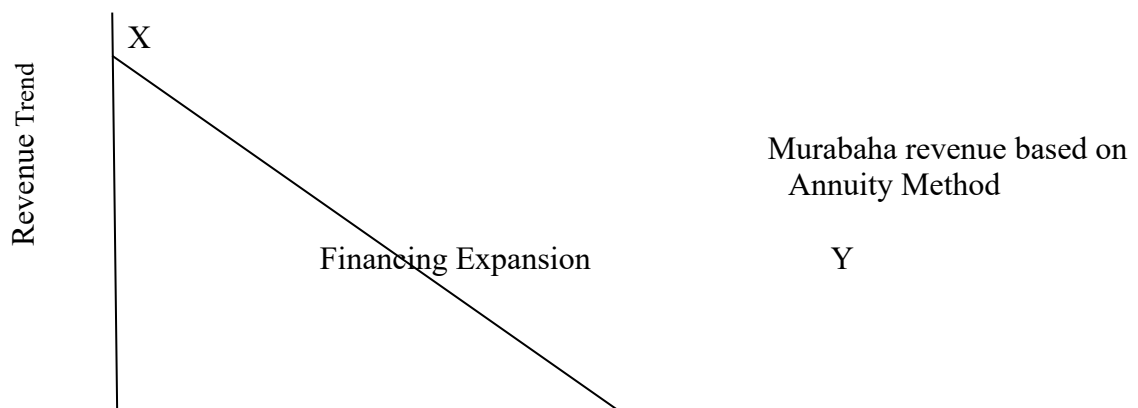
However, there are concerns that the use of a proportional rate of profit in a Murabaha transaction will create an inconsistent accounting treatment on the liability or liability side, resulting in an inequity in the value of the results to the customer of the fund where the customer places the fund at the end of the period financing gets a higher return than the one placed at the start. In addition, with a different accounting system between the owner bank and the Islamic bank as a subsidiary or Sharia Business Unit, there will be a massive profit adjustment that affects the profit of the Islamic bank. This is, according to the author, to be considered by the MUI (Indonesia Ulama council) in issuing its fatwa that the annuity method is prioritized in the Islamic Bank problem in its infancy phase. In fact, according to the author with the use of the concept of rate of interest in Murabaha transactions, the income earned in accordance with the use of the annuity method in the bank recording system that uses the accrual system, will harm the fund customers in the medium

and long term because the bank takes a large portion of profit at the beginning. The income of banks and fund customers will continue to decline and Islamic banks must make a big expansion to be able to offset the decline in income of banks and fund customers ([Wirosa, 2005](#)).

In the distribution of principal and profit that is even or proportional in accordance with the principle of economic value of time, even though the bank does not expand, bank revenue does not change so that bank management and customers are not disadvantaged. Whereas in the distribution of principal and profits on an annuity basis (based on time value of money), the revenue to be shared only provides benefits to the bank management and customers who place funds in the Islamic bank at the beginning, while in the end it will harm the customer because income continues to decline. With the increase in distribution of funds the income from the equitable pattern (rate of profit) will be greater than the decrease in annuity income (rate of interest).

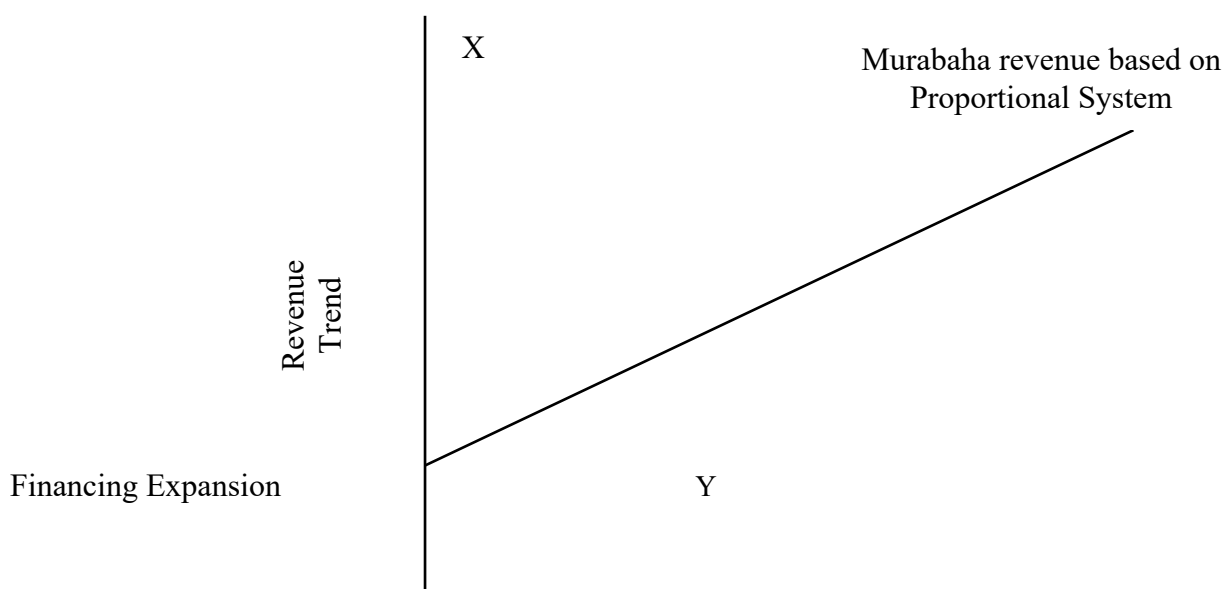
In the annuity method, income trends decline from time to time, so that fund customers are more disadvantaged. Whereas with the proportional method income will continue to increase, especially if banks expand, customers will increasingly get increased income so that Islamic banks do not need to worry if at the beginning of the replacement method the income decreases, but gradually there will be an increase in line with the distribution fund.

Figure 1. Masalah analysis based on Annuity concept (*Time Value of Money*)



With the proportional method, the financing customer also pays a smaller fee according to the proportion of profit compared to the annuity method where a large portion of the profit will be more burdensome to the operating expenses. Problems often arise in the field when financing customers are not notified or Islamic banks do not provide payment schedules according to the principal and profit proportions. When an accelerated payment occurs, the financing customer will be surprised because the calculation of the remaining principal debt to be paid will be different from the remaining principal debt in the Islamic bank because the Islamic bank uses the annuity method. Some cases even reached the court's claim for differences in the calculation of this method because they considered the Islamic banks were not transparent in providing actual information about the remaining principal debt contained in the bank notes using the annuity method. This, according to the author, must immediately be completed with a clear concept of rate of profit so that the application does not cause problems and high distrust of Islamic banks. Graphically it can be illustrated the benefit comparison between the proportional method (economic value of time) and the annuity method (time value of money).

Figure 2. Maslahah Analysis on Islamic Accounting Profit Distribution (Proportional System)
 Based on the concept of *Economic Value of Time*



In addition, Islamic banks that use the annuity method experience difficulties when restructuring because the customer's liability balance in the form of principal debt must be recalculated using the annuity method if the bank wants to calculate bank income using the effective (rate of interest) method. With the annuity system, the principal portion is still large when compared to the proportional method with the economic value of time system so that the only beneficiary is bank management and fund customers who place their funds first in the case of Islamic banks. Whereas in conventional banks this annuity system only benefits the bank while the interest income fund customers do not increase because it has been determined in advance and has nothing to do with credit benefits. In other words, the interest system is more profitable for banks (big capital owners), disadvantages debtors and is unfair to third party fund owners.

In the proportional method, the debt for the purchase of goods is a trade debt, so it does not recognize the principal debt and profit debt. What must be paid by the customer is the total trade payable minus the outstanding payments made, there is no principal payment so the cost of the financing customer is smaller. In addition, in profit Murabaha paid by debtors, there are still fund customers' rights so that they are fairer to fund customers. On the other hand, financing customer debt is not distinguished between principal debt and profit debt, thus the burden of financing costs for debtors is lower, so that they can more quickly obtain profits and provide wider business opportunities for the welfare of the community (equitable distribution of wealth).

Although the rate of profit in muraba transactions is ex-ante, it is hypothetical and ex-post (cash basis) in the distribution of income to banks and fund customers. If the customer makes an installment payment less than his obligation, the customer who is reduced is the debt, while for the bank the distribution of the principal portion and profit portion will still be carried out proportionally according to the installment coming in (cash basis). Islamic banks do not recognize a reduction in principal or profit by Islamic banks on installment payments. This is clearly different from conventional banks, if customers make smaller installment payments, then they are treated as principal loan payments first and the rest are treated as interest payments.

In terms of pricing profit or rate of profit in Murabaha financing (by not existing risk premium and cost of funds), and by ignoring the effect of "time value of money" on financing income with a contract with a contract Murabaha, the burden of payment of the rate of the profit will be lower with the interest system. Based on this, according to the author, therefore financing Murabaha is only intended for short-term financing products. The longer the term and the greater the profit, the greater the burden on financing customers, especially at the beginning of the financing period. This annuity system uses compounded interest in the calculation and the effective income calculation uses the opposite of the compounded interest formula described earlier, which in the conventional financial system is called the discount rate: $V (\text{Value}) = C / (1 + R)^n$ where C is the installment amount and R is the interest rate used as a benchmark for assessing the effective rate on a given loan. So in conclusion the annuity method is the concept of time value of money which is worse than simple interest. In the long run, the effect of time value is even very persecuting (Toutouchian, 2009), as the table below.

Table 3. Growth of 10,000 Units of Money after 50 Years with Different Interest Rates

Rate of Interest (%)	Accumulation
3	4.4
6	18.4
9	74.4
12	290

With the use of the rate of profit concept with a proportional system (the level of profit taken periodically / circularly) without the use of the usurious time value of money concept, the benefits gained will be more: namely the stable prices of financial assets, full employment (due to the low capital costs with a non-compounded rate of profit and jointly borne expenses) and equitable distribution of income in investments in Islamic banks (equitable distribution of income). According to Sri Edi Swasono (2010), when a transaction carried out only benefits individuals, then this transaction is not in accordance with "economic democracy". He said that Indonesian social welfare was based on the understanding of Indonesia's "economic democracy," meaning that it was based on ideological demands that "... the prosperity of the people is the main thing, not the prosperity of the people ... prosperity for all people." per person. The principle of Indonesian economic democracy is basically the same as the concept of Maslahah in Islamic economics. Attributed to the method of profit distribution in accordance with the Sharia principle in the transactions of Murabaha it can be concluded that the proportional method in the long run is more prosperous to the community.

The following illustrates the effect of time value charging between the rate of interest and the rate of profit in long-term transactions in both conventional and Islamic banks for comparison.

4.2 The Differences in accounting methodology in the application of Islamic Bank and Conventional Bank in Medium Term Transaction in Bank Permata Syariah

To show the differential between the contracts in medium term (10-15 years), we compare the methodology used in the Islamic Bank, Ijarah Muntahia Bit Tamlik, or Sale and Lease Contract (in conventional Leasing Company) and in the end the customer will own the property. As a consequence, the Bank will have to depreciate the property as in the inception the Bank has to buy the property and hold it up to the maturity and finally sell it to the customer. So the main difference between the conventional bank and Islamic Bank, is in the depreciation cost that has to be charged to Islamic Bank as it is reflected in the table below.

Table 4. Home Ownership Financing with Ijarah Muntahia Bit Tamlik (IMBT) with a Rate of profit in the form of Rent Payment with an Equivalent Rate of 12% for a period of 12 years

JADWAL ANGSURAN PEMBIAYAAN IMBT		IJARAH MUNTAHIA BI TAMLIK		KPR								
NAMA		DESIGN PRODUK IMBT										
HARGA BARANG	1,500,000,000.00											
UANG MUKA	-											
BESAR PEMBIAYAAN	1,500,000,000.00											
JANGKA WAKTU (BLN)	12											
PRICING	12%											
ANGS	TGL. ANGSURAN	OUTSTD POKOK	KEPEMILIKAN			MARGIN (%)	PORSI UJRAH	PORSI POKOK	12.00% IRR			
			NASABAH (NILAI)	NASABAH (%)	BANK (NILAI)				BANK (%)	ANGSURAN PERBULAN	BIAYA DEPRESIASI	SELISIH ANGS POKOK DAN DEPRESIASI
							\$118,273,183.00	(1,500,000,000.00)				
1	2013-02-21	1,500,000,000.00	118,273,183.00	7.88%	1,381,726,817.00	92.12%	15,000,000.00	118,273,183.00	133,273,183.00	125,000,000.00		(6,726,817.00)
2	2014-03-21	1,381,726,817.00	237,729,098.00	15.85%	1,262,270,902.00	84.15%	13,817,268.00	119,455,915.00	133,273,183.00	125,000,000.00		(5,544,085.00)
3	2015-04-21	1,262,270,902.00	358,379,572.00	23.89%	1,141,620,428.00	76.11%	12,622,709.00	120,650,474.00	133,273,183.00	125,000,000.00		(4,349,526.00)
4	2016-05-21	1,141,620,428.00	480,236,551.00	32.02%	1,019,763,449.00	67.98%	11,416,204.00	121,856,979.00	133,273,183.00	125,000,000.00		(3,143,021.00)
5	2017-06-21	1,019,763,449.00	603,312,100.00	40.22%	896,687,900.00	59.78%	10,197,634.00	123,075,549.00	133,273,183.00	125,000,000.00		(1,924,451.00)
6	2018-07-21	896,687,900.00	727,618,404.00	48.51%	772,381,596.00	51.49%	8,966,879.00	124,306,304.00	133,273,183.00	125,000,000.00		(693,696.00)
7	2019-08-21	772,381,596.00	853,167,771.00	56.88%	646,832,229.00	43.12%	7,723,816.00	125,549,367.00	133,273,183.00	125,000,000.00		549,367.00
8	2020-09-21	646,832,229.00	979,972,632.00	65.33%	520,027,368.00	34.67%	6,468,322.00	126,804,861.00	133,273,183.00	125,000,000.00		1,804,861.00
9	2021-10-21	520,027,368.00	1,108,045,541.00	73.87%	391,954,459.00	26.13%	5,200,274.00	128,072,909.00	133,273,183.00	125,000,000.00		3,072,909.00
10	2022-11-21	391,954,459.00	1,237,399,179.00	82.49%	262,600,821.00	17.51%	3,919,545.00	129,353,638.00	133,273,183.00	125,000,000.00		4,353,638.00
11	2023-12-21	262,600,821.00	1,368,046,354.00	91.20%	131,953,646.00	8.80%	2,626,008.00	130,647,175.00	133,273,183.00	125,000,000.00		5,647,175.00
12	2024-01-21	131,953,646.00	1,500,000,001.00	100.00%	(1.00)	0.00%	1,319,536.00	131,953,647.00	133,273,183.00	125,000,000.00		6,953,647.00

Attributed to the method of profit distribution in accordance with the Sharia principle in the transactions of IMBT it can be concluded that the proportional method in the medium-term contract is also more prosperous to the community since the depreciation cost is hold by the Islamic Bank

4.3 Differences in Rate of profit and Rate of Interest in The Applications of Islamic Banks and Conventional Banks in Long-Term Transactions with the contract Musharakah Mutanaqishah in Malaysian, Bangladesh and Bank Syariah Indonesia

To show the operational differences the concept of rate of profit in Islamic banks and the concept of rate of interest in conventional banks is used in long-term contracts to use housing finance in Islamic banks with the contract Musharakah Mutanaqishah or House Ownership Credit in banks conventional long-term 30 years. Musharakah mutanaqishah contract, like a loan agreement at a conventional bank, also uses a down payment as a customer's initial ownership stake of 10%, while Islamic banks provide the remaining 90%, so initially the contract was syirkah inan where the customer has 10% of home ownership, while banks own 90%. At the beginning of this transaction there is no interest or compensation charged to the customer, but if the customer occupies the house, the customer must pay rent to the owner, namely the bank and the customer according to the portion of ownership of the house. Of course, because the customer also owns 10% of the house, the customer will also receive a rent back in proportion to his ownership. In addition, customers are also allowed to increase the portion of their shares gradually with additional periodic payments until all ownership becomes the property of the customer (100%). Therefore, different from mortgage loans in conventional banks, in Table 4 seen in MMQ transactions in Islamic banks that the rent payments made by customers are different from conventional banks because there is an element of acceptance of customer leasing rights from customers which increases periodically as a co-owner of the house the. So that the total efficiency becomes $2,377,404,000/2,310,183,000 = 1,029$ or 2.9% more efficient when compared to mortgages at conventional bank

Table 5. Home Ownership Loans at Conventional Banks with an 8% Rate of Interest with a 30-Year Term

Instalment	Monthly Payment	Interest Payment	Principle	Remaining Principle Balance
1	6.603.900	6.600.000	603.900	899.396.100
2	6.603.900	5.996.000	607.900	898.788.200
3	6.603.900	5.991.900	612.000	898.176.200
12	6.603.900	5.954.200	649.700	892.481.300
...				
120	6.603.900	5.271.300	1.331.600	789.518.400
...				
240	6.603.900	3.848.300	2.955.600	544.289.800
...				
359	6.603.900	87.000	6.516.900	6.530.900
360	6.603.900	73.000	6.530.900	0
Total	2.377.404.000	1.477.404.000	900.000.000	

In contrast to home ownership loans in conventional banks, in Islamic banks home ownership financing is very structurally different even though the number of installments is the same. This is due to the use of the construction contract cooperation agreement (shirkah ‘inan), where in each installment payment there is a customer's right in the percentage of ownership that continues to increase in accordance with the number of installments. Structurally, the pattern of installments and changes in home ownership ([Faruk, 2010](#)), such as the table below:

Table 6. Home Ownership Financing with Musharakah Mutanaqisah (MMQ) with a Rate of profit in the form of Rent Payment with an Equivalent Rate of 8% for a period of 30 years.

Rent	Monthly Payment	Customer Ownership	Bank's Ownership	Customer's Equity Portion	Customer Equity %	Bank's Equity Portion	Bank's Equity %
				100.000.000	0%	900.000.000	90%
1	6.603.900	660.400	5.943.500	100.660.400	0.07%	899.339.600	89.93%
2	6.603.900	669.100	5.939.100	101.325.200	0.13%	898.674.800	89.87%
3	6.603.900	669.100	5.934.800	101.994.300	0.20%	898.005.700	89.80%
...							
24	6.603.900	768.300	5.835.600	117.113.400	1.71%	882.886.600	88.29%
...							
120	6.603.900	1.445.400	5.158.500	220.309.400	2.03%	779.690.600	77.97%
...							
240	6.603.900	3.184.300	3.419.600	485.362.400	8.54%	514.637.600	51.46%
...							
359	6.603.900	6.525.200	78.700	994.613.700	9.46%	5.386.300	0.54%
360	6.603.900	5.386.300	35.600	1.000.000.000	00%	0	0%
Total	2.310.183.000	900.000.000					

Source: [Abu Umar Faruq \(2010\)](#)

From Table 6, it can be seen that with the principle of risk sharing through joint ownership (shirkah ‘inan), the rental expense to be paid by customers is cheaper when compared to the interest expense to be paid on mortgages at conventional banks by 2.9%. This burden will be even greater in the conventional bank if the rate of interest used as a measure is higher and results in higher interest payment burdens, causing income inequality in the community. A clearer benefit will be seen if the customer is unable to pay according to the agreed rental and ownership payment schedule, so there is no process of closing the transaction with a one-sided sale from an Islamic bank bearing in mind the contract used is a joint ownership agreement (shirkah 'inan), then the bank has no priority in forcibly selling assets that are jointly owned. Banks and customers will look for asset buyers

together so that the best-selling prices for assets will be found. When compared to conventional bank credit, the contract at an Islamic bank with MMQ will create harmony and a just society because there is no conflict created between creditors and debtors who forcibly execute assets and income inequality in society.

The MMQ transaction with this pattern of ownership cooperation is basically in line with the thinking of the structural economists mazhab who tend to demand actors as homo ethics' and to oppose neoclassical economists who take the starting point of humans as homo economicus. Sri Edi Swasono in offering a restructuring of structural inequalities advocates an equitable distribution of wealth. Every economic endeavor must be able to increase ownership (entitlement) not just increase public income equally. This restructuring is directed to form a "Triple Co", namely: 1) co-ownership, 2) co-determination and 3) co-responsibility. These Triple Co are all contained in MMQ transactions on Islamic bank products described above. Co-ownership is reflected in joint ownership (shirkah 'inan) assets that are transacted with the principle of risk sharing. Co-determination can be seen in the event that if the customer is unable to pay according to the agreed rental and ownership payment schedule, then there is no forced closure of the transaction from the Islamic bank because with the cooperation agreement, the bank has no priority in forcibly selling assets that are jointly owned. Forced restructuring can be avoided such as deprivation (savage acquisition), cannibal redistribution or wild take over as happened in conventional banks with riba loan transactions. Co-responsibility will be reflected in the maintenance of shared assets and discipline in paying according to schedule so that togetherness and kinship can be achieved. These principles of Islamic economics are not in line with the capitalist economic system in transactions that are individualistic (only benefit certain groups) and exploitative riba.

Comparison of the imposition of the rate of profit in Islamic banks with the MMQ contract and the rate of interest in conventional banks in the housing loan agreement, basically is a comparison of the concepts of economic value of time and time value of money. The concept of compounded time value of money will burden customers more than the concept of economic value of time, in transactions with additional (ziyadah) that are fixed in the longer term. The inclusion of the risk premium element will increasingly burden the debtor and benefit the capital owner. If payment is made according to schedule, then this additional belongs to the owner of capital and is not returned to the debtor. At a macro level, riba additions will create distributive inequities in income resulting in widespread economic (injustice) injustice.

The element of riba on the use of a fixed and long-term of ujarah, also creates instability in the financial system, because an additional element is charged based on the element of time (usury al-nasi'ah). To avoid this element of riba, some MMQ contracts were modified using a price-adjusted ujarah (reprice), but this adjustable test currently still uses the 6-month LIBOR benchmark. This agreement follows the fatwa issued [by Muhammad Taqi Usmani \(1998\)](#), who said that the ujarah can be set according to different time periods, but the benchmarks must be set ahead with certainty. The use of the 6-month LIBOR benchmark is set so that there are no elements of jihadism, gharar and al-shurut-al-mufsidah (corrupt conditions) in accordance with Wahbah Zuhayli's opinion of ujarah in ijarah transactions. In practice, the use of the LIBOR benchmark will actually create an element of evil because this LIBOR is determined every day (daily basis) for the future, for example 3% for a period of 6 months. During the next 6 months, customers and banks also do not know the LIBOR rate for 6 months because it is only set on the same day. In the crises period, like currently covid-19 pandemic, whereas the LIBOR near to zero the benchmark could be misled, since the rental rate still well above zero.

So that, the use of LIBOR does not eliminate the element of mischief (Ujarah uncertainty). In fact, according to the author, the use of LIBOR as a benchmark will violate the mark to the market principle recommended by the Prophet to avoid usury al-fadl because of the use of unequal

benchmarks. Ujrah at the core basically follows the rate of profit in the real sector (in this example the price of a rental house), while LIBOR basically follows the price on the money / monetary market based on the rate of interest. This shows in the development of the Islamic financial system, the need to create a rental index in the real sector both regionally and nationally, to reflect the real rate of profit. The making of this index can also be developed for other industries, so that Islamic banks have a benchmark in the goods and services market, so that the elimination of interest and its calculation method (annuity) as a whole in the Islamic financial system can be achieved.

Risks Arising in Musyarakah Mutanaqishah

C.1. Ownership Risk

In Musyarakah Mutanaqishah financing, the ownership status of the goods remains joint ownership between the Islamic bank and the customer. This is a consequence of Musyarakah Mutanaqishah financing, where both parties contribute funds to purchase the goods. During the transfer of ownership, the customer can fully own the goods after paying the Islamic bank's share along with the agreed rental amount.

C.2. Regulatory Risk

The practice of Musyarakah Mutanaqishah for financing goods is subject to applicable regulations. One regulation relevant to Musyarakah Mutanaqishah is the imposition of Value Added Tax (VAT) on goods ownership. The VAT imposition is based on Law No. 18 of 2000, an amendment to Law No. 8 of 1983. The delivery of taxable goods and services is subject to tax under the VAT and Sales Tax on Luxury Goods Law. This law states that all types of goods, tangible or intangible, movable or immovable, are subject to VAT. This regulatory requirement will increase the cost of doing the MMQ Transaction.

C.3. Market Risk

Market conditions can lead to fluctuations in the price of goods. Regional differences in Musyarakah partnerships can result in price variations, meaning that Islamic banks cannot standardize prices across different areas. Additionally, Musyarakah Mutanaqishah financing involves joint purchasing of goods by the Islamic bank and the customer. The bank's ownership decreases in proportion to the installments paid by the customer towards the bank's principal capital. Besides the installments, Musyarakah Mutanaqishah includes a rental fee that the customer must pay monthly as the bank's profit compensation. The rent can fluctuate based on the situation and conditions during the collaboration agreement. The rent for the goods is influenced by: [1] the time of agreement, [2] location/region, [3] supply and demand for the goods.

C.4. Credit (Financing) Risk

Musyarakah Mutanaqishah financing involves monthly installments, exposing it to credit risk. There is a possibility of default if the customer fails to meet their monthly payment obligations. The customer's inability to pay installments each month can lead to contract failure, potentially causing financial losses for the Islamic bank.

5. Conclusion

There are three primary findings from the research regarding the distribution of investment income, the elimination of the usury and speculation (maysir), and the pricing of sharia financing products. Firstly, the distribution of investment income in Islamic banks that uses the accounting methodology (the economic principle for the value of time) with an even distribution between principal and margins on short-term transactions, giving a better welfare to banks and customers. Banks that use profit rates are fairer compared to those that use interest rates (regarding the concept of the time value of money). This is especially true when there is a large share of interest in the initial period of the loan when it is more profitable for capital owners such as Islamic banks and fund customers. The *masalah* that is to be achieved is in accordance with the Islamic concept of

time, specifically in Islamic transactions where there is economic value (profit rate) of time (economic value of time). The lower cost burden at the beginning of the contract in the sale and purchase transaction can overcome poverty by providing more equitable business opportunities through this Islamic bank financing product (equitable distribution of wealth). This is in line with the Islamic theory of the legitimacy of profit-making called the 'iwad' theory.

Secondly, the elimination of usury and maysir on long-term sale and purchase transactions with a fixed rate system using an alternative MMQ (Musharakah Mutanaqisah) or IMBT (Ijarah Muntahia Bittamlik) with an adjusted profit rate that aligns with the business cycle (price adjustment method), creates a more stable Islamic financial system. The stable systems allow for distributive equity in investment income (equitable distribution of income) to be realized. This prohibition of usury and maysir is a basic concept of Islamic transactions contained in the theory of profit-taking that must originate from tijarah (trade) transactions and not from tabarru transactions (loans with interest).

Finally, the implementation of the Musyarakah Mutanaqishah contract has several advantages as a form of Sharia-compliant financing, including: (1) Joint Ownership: Both the Islamic bank and the customer have ownership of the asset that is the object of the agreement. Since it is a shared asset, both parties will take care of the asset (2). Profit Sharing: Both parties share the profit from the rental margin agreed upon for the asset (3). Adjustable Rent: Both parties can agree to adjust the rent price according to predetermined times, in line with market prices (4) Minimized Financial Cost Risk: It helps minimize the risk of financial costs in the event of inflation and rising market interest rates in conventional banking (5) Unaffected by Market Interest Fluctuations: It is not affected by fluctuations in market interest rates in conventional banks or price fluctuations during inflation.

However, there are also weaknesses in the Musyarakah Mutanaqishah contract when applied as a form of Sharia financing, such as : (1) Transaction and Tax Burden Risk: The risk of transferring transaction costs and tax payments, including taxes on secured rights or building taxes, and other potential costs that may burden the asset (2) Reduced Bank Income: The income for the Islamic bank from the rental margin charged on the asset may decrease (3) Heavy Initial Installments: The installments in the first few years can be burdensome for the customer and will become lighter in subsequent years.

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