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Analysis of the Profit and Loss Sharing Principle in Islamic Banking Investment Deposits (A Comparative Legal Study of Several Countries)

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Abstract

The growth of Islamic banking in several countries especially Indonesian, Malaysian and Egypt is growing very rapidly, statistics show that Indonesian and Malaysian have become one of the centre of the development of the Islamic financial industry. Indonesian and Malaysian as countries in this region which are the dynamo of the development of the Islamic banking industry among ASEAN countries, this condition encourages other Southeast Asians to participate in the development of the Islamic banking industry. Based on this study examines 2 (two) problems namely how the principle of profit and loss distribution of investment funds of Islamic banking deposits in comparative studies of laws of several countries and how the settlement of disputes of investment funds of Islamic banking deposits in comparative studies of laws of several countries. Both of these constraints are examined using legal comparison theory and solutions to resolve if Islamic banking disputes occur in several countries. The approach used is normative with a comparative method of law in data collection techniques, namely by analyzing documents that are relevant to the research topic. The conclusion in this study is that Islamic banking deposit investment funds in several countries especially in Indonesian, Malaysian and Egypt still use the principle of profit sharing and dispute resolution of Islamic banking deposit investment funds arising from Islamic financial transactions in Indonesia, Malaysian and Egypt certainly needs sufficient attention from their respective governments.

Keywords

Islamic Bank, Profit and Loss Sharing, dispute resolution of Islamic banking.

I. Introduction

Indonesia, as the largest Muslim-populated country in the world,¹ has implemented Shariah-compliant economics, which allows for the social function of acting as a Baitul Maal institution. This institution functions to receive funds from the community derived from zakat (obligatory alms), infak (voluntary donations), sedekah (charitable giving), hibah (gifts), or other social funds, as well as wakaf uang (endowment funds) whose management is carried out in accordance with the regulations.

One of the most dominant and essential business activities in this context is the operations of Islamic financial institutions, primarily banking institutions. These institutions play a crucial role as fund collectors in supporting the economic growth of a nation. As fund aggregators, these financial institutions facilitate development by channeling funds to various important projects in different sectors managed by the government. They provide funding to private entrepreneurs or economically vulnerable individuals who require financial assistance for their businesses, among other functions, such as facilitating smooth national and international money circulation and transactions.²

However, the operations of banking institutions become problematic when connected to Islamic legal provisions, not from the institution's function but rather from the concept of their business activities. Banking activities are crucial for the community's business operations to thrive, particularly through the utilization of credit interest obtained by lending the community's savings with additional interest. Some people perceive that the credit system with interest has long been prohibited not only by Islamic teachings but also by other religions. The conventional banking system's interest-based mechanism can prove detrimental to both the banks themselves and their customers. Since then, Islamic banking systems offer profit-sharing models that are free from interest (riba).

International economists have empirically acknowledged that the interest-based system entails harm. This is due to the profit gained without bearing the risk, which results in borrowers not receiving proportional benefits relative to the interest they have to pay. Consequently, various economic crises occur, especially affecting impoverished countries worldwide.³

The development of Shariah-compliant financial institutions, both in the banking sector and other sectors such as insurance, has been rapid. This is primarily driven by the realization among Muslims that Islamic teachings contain universal principles and have two balanced dimensions: worldly (duniawi) and spiritual (ukhrawi). As a manifestation of Islam's teachings that emerged in this world as a mercy to all of creation (rahmatan lil 'alamin), the teachings and

¹ <https://dataindonesia.id/ragam/detail/populasi-muslim-indonesia-terbesar-di-dunia-pada-2022>

² Gemala Dewi, *Aspek-Aspek Hukum Dalam Perbankan & Perasuransian Syariah Di Indonesia*, Edisi Ketiga, Prenadamedia Group, Jakarta, 2019, hlm. 49.

³ Ibid, hlm. 50

guidelines regarding Shariah economics foster the awareness that conventional banking systems are laden with elements of maysir (gambling), gharar (uncertainty), riba (interest), and falsehood (bathil), which should be avoided in every transactional activity.

The development of Islamic banking after the issuance of Law Number 7 of 1992 concerning Banking, in conjunction with Law Number 10 of 1998 concerning Amendments to Law Number 7 of 1992 concerning Banking, implicitly indicated that banks were allowed to operate based on profit-sharing principles. The operational foundation of the Islamic banking system was further strengthened with the issuance of Government Regulation Number 72 of 1992, which was replaced by Government Regulation Number 30 of 1999 concerning Banks based on profit and loss sharing (Mudharabah), and Law Number 21 of 2008 concerning Islamic Banking, in conjunction with Law Number 4 of 2023 concerning the Development and Strengthening of the Financial Sector. Subsequently, with the enactment of Law Number 3 of 2004 concerning Amendments to Law Number 23 of 1999 concerning Bank Indonesia, two systems were implemented in banking: conventional banking and banking based on Sharia principles (dual banking system), with Islamic banks exclusively operating on Sharia principles.

The characteristics of the Sharia banking system, which operates based on profit-sharing principles, provide an alternative banking system that benefits both society and banks. It emphasizes fairness in transactions, ethical investments, the promotion of solidarity and brotherhood in production, and the avoidance of speculative activities in financial transactions. With a diverse range of products and services and more varied financial schemes, Islamic banking has become a credible alternative banking system that can be enjoyed by all segments of Indonesian society.⁴

One of the products offered by Islamic banking is Sharia deposits, a fixed-term savings product based on the Mudharabah principle, where depositors grant full freedom to the bank to manage their investments. The profits or gains from the management of these investment funds are distributed according to the agreed-upon ratio or share.⁵

Islamic banks, based on profit and loss sharing principles, do not charge interest but instead invite participation in funded business ventures. Depositors also share in the bank's profits according to pre-determined ratios. There is a partnership between Islamic banks and depositors on one side and between banks and investment customers as managers of the depositors' funds in various productive ventures on the other side.

Islamic banking provides interest-free services to its customers, free from unproductive speculative activities such as gambling (maysir), free from unclear and doubtful transactions (gharar), and free from transactions that are invalid or unlawful (bathil).

4 Ibid, hlm. 63

5 <http://www.simulasideposito.com/dp-deposito-syariah.php>

The concept of the profit and loss sharing system requires new approaches to develop the Islamic market in Indonesia. This system is an important element of Sharia principles that have long been implemented in Asian and European countries. The rapid growth of Islamic banking in Indonesia enters a new phase in the Indonesian banking industry with the enactment of Law Number 21 of 2008 concerning Islamic Banking, in conjunction with Law Number 4 of 2023 concerning the Development and Strengthening of the Financial Sector.

Based on the main ideas above, the following issues can be identified:

1. How does the Profit and Loss Sharing Principle of Shariah Banking Investment Deposits work in a comparative legal study of several countries?
2. What are the solutions for resolving disputes related to Shariah Banking Investment Deposits in a comparative legal study of several countries?

II. METHOD

The research methodology employed in this study is normative research, which includes the examination of legal principles, systematic legal research, vertical and horizontal synchronization research, legal comparison, and legal history research.⁶

The legal writing in this study adopts a descriptive research method, considering that the issues under investigation revolve around legal regulations. These legal regulations aim to provide a systematic, factual, and accurate description of the facts and nature of the research object. The research object chosen for this legal writing is the comparison and resolution of disputes related to the Profit and Loss Sharing Principle of Shariah Banking Investment Deposits. To support the research, secondary data sources are needed. These sources consist of literature or secondary data such as legal regulations, which are categorized as primary data (basic data) that have been compiled by previous researchers. These sources are readily available, in terms of their form and content, without time or place constraints. The data sources used in this study include: a. Primary Legal Materials: relevant legal regulations. b. Secondary Legal Materials: draft laws, research findings, legal works, particularly those related to the issues addressed in this legal writing. c. Tertiary Legal Materials: dictionaries, encyclopedias, cumulative indexes, and so on.

Iii. Results and Discussion

The Profit and Loss Sharing Principle of Shariah Banking Investment Deposits in a Comparative Legal Study of Several Countries

The Profit and Loss Sharing Principle of Shariah Banking Investment Deposits in Indonesia

The principle of Islamic banking is a part of Islamic teachings related to

⁶ Soerjono Soekanto dan Sri Mamudji, *Penelitian Hukum Normatif: Suatu Tinjauan Singkat*, cetakan XIV, Raja Grafindo Persada, Jakarta, 2012, hlm. 14

economics. One of the principles in Islamic economics is the prohibition of usury (riba) in various forms and the use of profit and loss sharing principles. Through profit and loss sharing, Islamic banks can create a healthy and fair investment climate where all parties can share both the profits and potential risks, thus achieving a balanced position between the bank and its customers. This will contribute to the long-term economic equality in the country because the profits are not only enjoyed by the capital owners but also by the capital managers.

Islamic banking, as one of the national banking systems, requires various supporting facilities to contribute maximally to the development of the national economy. One vital supporting facility is adequate regulation that aligns with its characteristics. One such regulation is enshrined in the Sharia Banking Law. The establishment of the Sharia Banking Law is a necessity and inevitability for the development of Islamic banking institutions. The regulation concerning Sharia banking in Law Number 7 of 1992 concerning Banking, as amended by Law Number 10 of 1998 and amended by Law Number 11 of 2020 concerning Job Creation, and further amended by Government Regulation Substitute for Law No. 2 of 2022 concerning Job Creation, and transformed into Law No. 4 of 2023 concerning the Development and Strengthening of the Financial Sector, is not specific enough and fails to accommodate the operational characteristics of Islamic banking, despite the rapid growth and business volume of Islamic banks.

The referred Islamic banking institution in this context is Bank Muamalat Indonesia in Jakarta, which conducts its business activities based on Sharia principles and implements them through the use of mudharabah contracts.⁷

Mudharabah is a business cooperation agreement between two parties, where the first party (shahibul maal) provides the entire (100%) capital, while the other party becomes the manager. The profits from the business under mudharabah are shared according to the agreement stated in the contract, whereas if there are losses, they are borne by the capital owner as long as the losses are not due to the negligence of the manager. If the losses are caused by fraud or negligence on the part of the manager, then the manager is responsible for those losses.⁸

In Bank Muamalat Indonesia in Jakarta, mudharabah contracts are implemented in the form of Islamic deposit products. According to Article 1 number (22) of Law Number 4 of 2023 concerning the Development and Strengthening of the Financial Sector in the Islamic Banking section, a deposit is a savings based on mudharabah or other contracts that are not contrary to Sharia principles, where withdrawals can only be made at specific times based on agreements between depositors and the Islamic bank and/or Sharia Business Units (UUS).

In practice, the choice of the mudharabah type mentioned above is closely related to the amount of deposit made by the depositor. If the amount is significant

⁷ <https://www.bankmuamalat.co.id/index.php/profil-bank-muamalat>

⁸ Muhammad Syafi'i Antonio, *Bank Syariah Dari Teori Ke Praktek*, Gema Insani, Jakarta, 2001, hlm. 95.

enough, usually the depositor imposes certain restrictions or conditions that the bank must fulfill in managing their funds.

The mudharabah muthlaqah contract has been allowed by Sharia principles because it is clearly stated in Article 233 of the Compilation of Sharia Economic Law (KHES) that the agreement regarding the field of business can be absolute/free or limited to a specific field, place, and time.⁹

The mudharabah mutlaqah contract is implemented in the Islamic deposit product. In Bank Muamalat Indonesia in Jakarta, the deposit product with mudharabah contract is called iB Hijrah Muamalat deposit. The Bank Muamalat Indonesia in Jakarta is managed in the form of a project or business using the principle of profit and loss sharing. This means that the profits and losses from the income generated by the business are shared accordingly. The advantages of the iB Hijrah Muamalat deposit at Bank Muamalat Indonesia are:¹⁰ a. Profitable: Optimal profit sharing. b. Peace of mind: Investments are managed in a Sharia-compliant manner, providing inner peace. c. Flexibility: Choose the term that suits your needs, whether it's 1, 3, 4, 6, or 12 months. d. Collateral: iB Hijrah deposit can be used as collateral for financing if needed.

When compared to fixed-interest deposit accounts, deposits based on the principle of profit sharing are significantly different from those without interest. In an interest-based system, deposit owners receive a certain fixed and periodic interest, regardless of the efforts made by the Islamic bank, whether it incurs losses or profits. In a mudharabah deposit, the return received by the deposit owner depends on the business results generated by the bank, namely a certain ratio or percentage of the total business outcome obtained by the bank. The bank, acting as the mudharib, is not obligated to provide a specific return but depends on the business results. This contract is more appropriate because it aligns with the characteristics of a business that has potential for profit or loss.¹¹

The distribution of business outcomes among the parties in a cooperative business venture can be based on the principle of Profit Sharing, which calculates the share of profits from revenue after deducting management costs, or it can be based on the principle of Revenue Sharing, which calculates the share of profits from the total revenue of fund management. Each has its advantages and disadvantages.¹²

In a mudharabah contract, the capital owner or shahibul maal provides the principal capital to be managed by the entrepreneur or mudharib. The capital owner is not authorized to intervene in the business decision-making process and acts as a sleeping partner.

⁹ Kompilasi Hukum Ekonomi Syariah, Pasal 233, Mahkamah Agung Republik Indonesia Direktorat Jenderal Badan Peradilan Agama Tahun 2011, <https://perpustakaan.mahkamahagung.go.id/assets/resource/ebook/02.pdf>

¹⁰ <https://www.bankmuamalat.co.id/index.php/deposito-consumer/deposito-ib-hijrah>

¹¹ Rachmadi Usman, *Produk dan Akad Perbankan Syariah di Indonesia, Implementasi dan Aspek Hukum*, PT. Citra Aditya Bakti, Bandung, 2009, hlm. 169.

¹² Ahmad Ifham, *Ini Lho Bank Syariah, Memahami Bank Syariah Dengan Mudah*, Gramedia Pustaka Utama, Jakarta, 2015, hlm. 46.

In an agreement based on profit sharing, the basis for distribution can vary based on profit and loss or revenue sharing. The main issue in choosing between the two is the recognition of costs that arise during the business process, where accounting standardization will be one of the primary considerations. When accounting standards are well-implemented, the application of profit and loss sharing becomes easier. The choice of the profit-sharing basis also depends on the risk preferences of the contracting parties.

In transactions based on revenue sharing, the income of the capital holder depends only on the level of business uncertainty, while the income of the mudarib depends on the level of uncertainty regarding business conditions and the costs that arise during the realization of the business activities. Agreements based on revenue sharing have a lower level of uncertainty or risk compared to profit and loss sharing contracts, from the perspective of the capital owner. The cost structure and profit-sharing for both types of arrangements can be described in the following table:¹³

Table 2. Profit and Loss Sharing and Revenue Sharing

	Profit and Loss Sharing		Revenue Sharing	
	Entrepreneur	Fund Owner	Entrepreneur	Fund Owner
Gross Receipts	X		X	
Cost	C		C	
Profit and Loss Ratio	a	(1-a)	β	(1-β)
Nominal Value of Profit and Loss	a (X - C)	(1-a) (X- C)	(βX-C)	(1-β)X

Source: Akad dan Produk Bank Syariah: Konsep dan Praktek di Beberapa Negara by Ascarya.

There has been a debate regarding whether profit and loss sharing or revenue sharing should be used for the distribution of returns in Mudarabah financing contracts. Scholars and academics prefer profit and loss sharing. However, due to the persistent issue of moral hazard and the challenges in monitoring and controlling costs, current banking practices still use revenue sharing for profit distribution.

In practical terms, as long as an Islamic bank is in operation, customers will continue to receive positive returns. The only potential loss for customers occurs during the liquidation process (when an Islamic bank's financial performance is poor and can cause systemic effects) when customers are in a first come first served position. When third-party fund repayment guarantees are implemented by the government, Islamic banking customers effectively remain in a position of never experiencing losses. This surplus allocation concept clearly shows that Islamic banking in Indonesia currently adopts a hybrid contract concept to attract

¹³ Ascarya, *Akad dan Produk Bank Syariah: Konsep dan Praktek di Beberapa Negara*, Bank Indonesia, Jakarta, 2006, hlm. 213.

and protect risk-averse depositors.

In practice, at Bank Muamalat Indonesia, customers do not need to worry too much about the profit and loss sharing calculations. Customers simply need to inquire about the indicative rate of iB Hijrah Mudarabah deposits they are interested in. This indicative rate represents the equivalent rate of investment income that will be distributed to customers, expressed as a percentage, such as 11% or 12%.¹⁴ The profit and loss sharing calculation commonly used by Bank Muamalat Indonesia is based on business income without subtracting business expenses, allowing the public to save and invest easily in Islamic banks.

In managing customer funds with the principle of profit and loss sharing in the business distribution carried out by the Islamic bank, there can also be the risk of business losses. The risks of business losses can be categorized into several types as follows:

- a. Credit risk This risk arises when a debtor defaults or fails to fulfill their obligations.
- b. Market risk This risk can occur when mudarabah financing is provided in foreign currencies, specifically the risk of exchange rate fluctuations.
- c. Operational risk (internal fraud) This risk includes incorrect recording of position values, bribery or corruption, intentional tax misreporting, manipulation and mark-up errors in accounting or record-keeping, or reporting.

To minimize these risks, Bank Muamalat Indonesia, as the mudarib (fund manager), implements risk management by conducting a series of procedures and methods to identify, measure, and control the bank's business activities with reasonable and sustainable risk levels. Regarding the implementation of risk management, Law Number 21 of 2008 concerning Islamic Banking has been amended to Law Number 4 of 2023 concerning the Development and Strengthening of the Financial Sector, Article 38 paragraph (1) states that: "Islamic Banks and Islamic Business Units are obliged to apply risk management, know-your-customer principles."¹⁵

b. Profit and Loss Sharing Principle in Islamic Banking Investment Deposits in Malaysia

The application of Sharia principles in Islamic banking can vary depending on the understanding and opinions of scholars. For example, according to the opinion of Malaysian scholars, cash flow is considered equivalent to debt and property. For instance, a receivable worth Rp. 1000 can be sold at a discounted price of Rp. 800. This opinion has implications for the contract of Islamic financial products and instruments used in Malaysia, such as allowing Bai' Al-Inah (sale and buyback) and Bai' Al-Dayn (debt trading or discounting).

¹⁴ Ahmad Ifham, *Op.Cit.*, hlm. 48.

¹⁵ Undang-Undang Nomor 4 Tahun 2023 tentang Pengembangan dan Penguatan Sektor Keuangan, Pasal 38 ayat (1).

Various popular Islamic financial products and instruments in Malaysia use contracts or contain elements of Bai' Al-Inah and Bai' Al-Dayn. By applying these contracts, Islamic financial products and instruments can resemble conventional financial products and instruments. If conventional banking has credit cards, Islamic banking has Islamic credit cards. If conventional banking has overdraft facilities, Islamic banking has Islamic overdraft facilities. If conventional banking has short-term money market instruments, Islamic banking has short-term Islamic money market instruments.

Islamic banking in Malaysia uses unique contracts that are only used in Malaysia and may not be used in other countries, namely BBA, Bai' Al-Inah, Bai' Al-Dayn, and Variable Rate Ijarah. Islamic banking in Malaysia does not utilize profit-sharing contracts (musyarakah and mudarabah) to provide financing, which is the main characteristic of Islamic banking. Additionally, the contracts of salam and istisna are also not popular in Malaysia.

The Islamic banking referred to in this research is Bank Islam Malaysia Berhad, which offers deposit products such as current accounts (demand deposits) and savings accounts (time deposits) with the concept of Wadiah (guaranteed custody), as well as investment deposits with the concept of mudarabah (profit sharing). Islamic banks and conventional banks with Islamic branches or windows in Malaysia offer deposit facilities that rely on profit-sharing, i.e., returns. BIMB itself offers current accounts and savings accounts with the concept of guaranteed custody (wadiah) and investment deposits with the concept of profit sharing (mudarabah). Essentially, BIMB's financial instruments are based on three main sources of funds: current accounts, savings accounts, and deposits.

The deposit mentioned in this research refers to investment deposits in Islamic banks with the concept of profit sharing (mudarabah). The difference between investment deposits in Islamic banks and fixed deposits in conventional banks is that this type of account is not considered a liability or debt but rather a participatory account. In this case, the bank invests the customers' funds with their general or specific consent, depending on the deposit contract, in various projects. Based on the agreement, the profit distribution is shared between the bank and the customers using pre-agreed ratios.

c. Principles of Profit and Loss Sharing in Islamic Banking Investment Deposits in Egypt

The system of Islamic banking in Egypt operates according to the concept of partnership that arises between the bank and the depositor. This relationship is based on the principle of profit and loss sharing, which enables both parties to participate in the ownership of physical assets and engage in trading processes. Depositors in Islamic banking are recognized as entrepreneurs through various Islamic financial contracts such as mudharabah, musyarakah, murabahah, ijarah, Bai Muajal, salam, and prepaid purchases, which are considered the best alternatives to conventional banking to avoid interest (riba) that is explicitly

prohibited in Islam. The four main rules that govern investment behavior are as follows:

1. Prohibition of interest-based transactions (riba).
2. Avoidance of economic activities involving speculation (ghirar).
3. Introduction of Islamic tax, Zakat.
4. Avoidance of production decisions and services that contradict Islamic principles (Haram).

Investment financing is carried out through several methods, as follows:¹⁶

Musyarakah: Banks can join with other entities to establish joint ventures, where each party can participate in various aspects of the project at different levels. Profits are shared based on predetermined ratios, and any losses are shared proportionally according to the contribution of capital.

Mudharabah: Banks can provide financial contributions while the client provides expertise, management, and labor. Profits are shared between both partners based on pre-agreed proportions, but when losses occur, the bank bears the total loss.

Murabahah: This is a transaction in which a trader purchases goods required by an end-user. The trader then sells these goods to the end-user at an agreed-upon price calculated with an agreed-upon profit margin on the cost incurred by the trader. To comply with the principles of Islamic finance governing exchange transactions, each Murabahah transaction must meet certain conditions. Murabahah transactions can only be carried out if the bank's client wants to purchase the commodity. To make it a valid transaction, it is necessary for the commodity to be actually purchased by the bank and come into the ownership and possession (physical or constructive) of the bank so that it can bear the risk of the commodity. After acquiring ownership and possession of the commodity, it must be sold to the client through a valid sale.

Ijarah: Ijarah can be defined as a process where "specific property is transferred to another person in return for rent claimed from the customer." In many ways, Ijarah resembles leasing as practiced in the commercial world. The distinguishing feature of this mode is that the fixed asset remains the property of the Islamic bank to be leased each time the lease period ends so that it is not used for a long period. The bank or leasing company bears the risk or decreased demand for these assets.

Istishna: It is the second type of sale where a commodity is transacted before it comes into existence. For Istishna to be valid, the price should be agreed upon by the parties, and the required specifications of the commodity must be fully settled between them.

Salam: It is a sale where the seller supplies specific goods to the buyer in the future, in exchange for a down payment and full payment on the spot. Salam sales are suitable for agricultural operational financing, where banks provide great

¹⁶ *Comparative Performance Study of Conventional and Islamic Banking in Egypt*, http://www.scienpress.com/Upload/JAFB%2fVol%203_2_1.pdf.

services to farmers in their efforts to achieve production targets. Salam sales are also used to finance commercial and industrial activities, especially in the pre-production and export phases of commodities, by purchasing them in Salam and marketing them at favorable prices.

Resolution of Disputes in Sharia Banking Investment Deposits in a Comparative Legal Study of Several Countries.

Resolution of Disputes in Sharia Banking Investment Deposits in Indonesia

In Indonesia, there are two mechanisms for resolving disputes in Sharia banking, namely through Litigation and Non-Litigation. The resolution through the litigation process involves handling each case or matter presented to the opposing party, where the judge must carefully study the case beforehand. This is necessary to determine the direction of the examination of the case in the subsequent litigation process. In relation to Sharia economics, particularly Sharia banking cases, there are several important steps that need to be taken before the litigation process begins, including:

First, make sure that the case is not an agreement dispute containing an Arbitration clause.

It is important to ascertain whether the case involves a dispute over an agreement containing an arbitration clause or not. This is to ensure that the religious court does not examine and adjudicate a case that falls outside its absolute jurisdiction. The absolute jurisdiction of the religious court does not cover disputes or cases involving agreements that contain arbitration clauses. If the case is indeed a dispute over an agreement containing an arbitration clause, the judge does not need to proceed with reconciliation efforts because it is clear that the case falls outside the absolute jurisdiction of the religious court.

If the agreement contains a clause stating that in the event of a dispute between the parties regarding the agreement, it will be resolved through an arbitration body determined by them, then the agreement clearly contains what is known as an arbitration clause.

Carefully study the underlying agreement (contract) that governs the cooperation between the parties.

Every case in the field of Sharia economics, particularly in Sharia banking, involves disputes between the Islamic bank and its customers regarding a cooperation or business activity conducted by the parties themselves. The cooperation or business activities undertaken always have an underlying agreement or contract that has been made and agreed upon by the parties beforehand. The focus of the examination in this regard is the agreement or contract of the parties, and the reference for examining these agreements or contracts is the law of contracts.

The provisions of the contract law, in their application, must be relevant to

the provisions of Islamic contract law, whether regulated in the Qur'an, Sunnah, or the opinions (fatwas) of scholars in that field. If the provisions of the contract law, in their application, are contrary to the provisions of Islamic law, the judge must prioritize the provisions of the contract law that are in accordance with Islamic contract law.

The resolution of Sharia banking disputes through Non-Litigation or through reconciliation requires the judge or the court to make efforts to reconcile the disputing parties before handling a case. Efforts to reconcile the disputing parties in the court are imperative (mandatory). Failure of the judge to make reconciliation efforts for the disputing parties can result in the cancellation of the examination of the case for legal reasons.

Mediation, as applied in the judicial system according to Article 1 paragraph 1 of the Supreme Court Regulation (PERMA), is defined as "a dispute resolution process through negotiations to reach an agreement between the parties, assisted by a mediator."

If the reconciliation efforts are successful, either through the basis of Article 154 R.Bg/130 HIR paragraph (1) or through mediation with the assistance of a mediator as regulated in PERMA Number 1 of 2016, the resolution can occur in two possibilities. The parties, through the mediator, can submit a peace agreement to the examining judge to be strengthened in a peace deed as stipulated in Article 27 paragraph (4) of PERMA. Alternatively, if the parties do not wish for the peace agreement to be confirmed in a peace deed, the peace agreement must include the withdrawal of the lawsuit as outlined in Article 154 R.Bg/130 HIR paragraph (2) in conjunction with Article 27 paragraph (5) of PERMA.

The institution that provides non-litigation dispute resolution services in Indonesia is carried out internally within the Islamic banking sector, namely the National Sharia Arbitration Body (BASYARNAS), the Financial Services Authority (OJK), and the Indonesian Alternative Dispute Resolution Institution for Banking (LAPSPI). The dispute resolution process at BASYARNAS prioritizes efforts for reconciliation or *islah* as intended by Surah Al-Hujurat verse 9 and Surah An-Nisa verse 128. BASYARNAS does not set a limit on the disputed object's value.

The resolution of Sharia banking disputes is also handled by the Financial Services Authority (OJK) in this Indonesian Financial Institution. In 2014, the banking supervision functions, tasks, and authorities of Bank Indonesia, including mediation functions, were transferred to OJK following the issuance of OJK Regulation (POJK) Number 1/POJK.07/2014 concerning Alternative Dispute Resolution Institutions in the Financial Sector, which is mandated by Law Number 21 of 2011 regarding the Financial Services Authority.

b. Resolution of Sharia Banking Investment Deposit Disputes in Malaysia

In Malaysia, there are two mechanisms for resolving Sharia banking disputes, namely through litigation and non-litigation. Dispute resolution through

litigation falls under the jurisdiction of the Civil Court. Sharia banking in Malaysia conducts business transactions based on muamalah principles because the law applied in civil courts is common law or customary law.

Based on this legal system, court decisions in a particular case become a reference and binding rule for all subsequent court decisions related to the issue. It has been decided that the resolution of Sharia banking disputes in Malaysia falls within the jurisdiction of the civil court and not the jurisdiction of the Sharia court.

An example of an Islamic banking case in Malaysia is the case of Bank Islam Malaysia Berhad vs. Adnan Bin Omar (1994).¹⁷ In this case, the court recognized the Bai Bithaman Ajil (BBA) contract entered into by the parties. This means that the BBA contract is a separate contract, although it is relatively new compared to contracts commonly used in conventional banking. The court believed that the intention of the parties in entering into the agreement was to provide and obtain a loan, rather than engaging in a genuine sale and purchase. The court also did not question matters related to interest.

To address these issues and rulings, several actions need to be taken, including amending existing laws, including amendments to the Federal Constitution concerning various aspects of the implementation of Islamic law.

The resolution of Islamic banking disputes in Malaysia has an alternative financial dispute resolution institution called the Ombudsman, previously known as the Financial Mediation Bureau (BPK). The mechanism applied by the Ombudsman, similar to the BPK, involves functioning as a counselor, conciliator, and arbitrator. This institution will not handle disputes that have exceeded the expiration period stipulated by the law or disputes that have been submitted to the court or arbitration institution. The decisions issued by the Ombudsman must be complied with by financial institutions, but they are not mandatory for customers.

The resolution of Islamic banking disputes in Malaysia also has its own arbitration regulations, which are modifications of the UNCITRAL Arbitration Rules on International Trade Law. The regional center for arbitration in Kuala Lumpur, known as the Kuala Lumpur Regional Centre for Arbitration (KLRC), provides facilities for conducting arbitration on international commercial transactions. This non-profit and independent institution serves financial disputes, including Islamic banking disputes in Malaysia, through mediation, adjudication, and arbitration mechanisms. The approximate duration of the case examination process until the decision is made is about six months.

Resolution of Disputes on Sharia Banking Investment Deposits in Egypt

The resolution of disputes regarding Sharia banking investment deposits in Egypt is conducted through the use of arbitration. Arbitration has become an increasingly important means to settle investment and commercial disputes in

¹⁷ Bank Islam Malaysia Berhad vs Adnan Bin Omar dalam *All Malaysia Reports* (1994).

Egypt. The Arbitration Law No. 27 of 1994 is a significant milestone in providing a comprehensive framework for the arbitration process in the country. The law regulates the rules governing the formation and validity of arbitration agreements, the arbitrability of legal disputes, the composition of the arbitral tribunal, the arbitration process, and the enforcement of arbitral awards. Judicial precedents from the Supreme Constitutional Court and the Court of Cassation have played an important role in complementing the provisions of the Arbitration Law.

The Arbitration Law is the primary source for regulating dispute resolution mechanisms outside the legal process. Concerns within the country over the past three years have led to the emergence of faster and more flexible mechanisms for the settlement of investment disputes. Egypt has also acceded to several international conventions governing the arbitration process, and these provisions have been incorporated into its national legal system.

The Arbitration Law sets forth procedural rules governing the arbitration process in Egypt, based on the UNCITRAL Model Law on International Commercial Arbitration. The Arbitration Law is aligned with applicable international arbitration standards. Egypt's approach to arbitration includes the following noteworthy specific rules:¹⁸

1. Application Article 1 of the Arbitration Law states that the law applies to any arbitration proceedings taking place in Egypt or to international commercial arbitration taking place outside Egypt if the parties involved have agreed to submit their dispute to Egyptian law as the *lex arbitri*.

In 1997, Article 1 of the Arbitration Law was amended to require the validity of arbitration clauses in government contracts to receive explicit approval from the relevant minister or head of the government agency. Arbitration clauses in government contracts made between government institutions and individuals are valid only upon the approval of the respective minister or the head of the contracting authority if the agent is not subject to a specific minister.

2. Egypt's Legal Approach to Arbitration Arbitration, as an unconventional method for resolving disputes within the Egyptian legal system, has seen the traditional jurisdiction of state courts transferred to newly organized arbitration courts.
3. Arbitration Courts and Process An arbitration court must consist of an odd number of arbitrators. In the absence of a specific agreement to the contrary, the court will consist of three arbitrators, with the claimant and respondent each appointing one arbitrator, and the two arbitrators thus appointed selecting the third arbitrator and the chairman. If one party fails to appoint its arbitrator or the two appointed arbitrators fail to agree on the appointment of the presiding arbitrator, the competent court must intervene and appoint the arbitrator. The competent court is considered to be the Cairo

¹⁸ Egypt: Legal Framework For Arbitration, <https://www.loc.gov/law/help/arbitration/egypt.php>.

Court of Appeal in the case of international commercial arbitration.

The Arbitration Law does not require arbitrators to hold a law degree or any specific academic qualifications. An arbitrator must not be a minor, under guardianship, or deprived of civil rights due to a conviction for a crime or offense involving dishonesty or a declaration of bankruptcy, unless their civil status has been restored. Unless otherwise agreed by the parties, arbitrators may be of any nationality or gender.

Once the arbitration process commences, the arbitral tribunal must render a final award within the period agreed upon by both parties. In the absence of such an agreement, the award must be rendered within twelve months from the date of commencement of the arbitration process. In exceptional cases, the arbitral tribunal may decide to extend this period, provided that the extension does not exceed six months, unless both parties agree to a longer period. Failure to comply with this maximum time limit gives each party the right to resort to the competent court to request the termination of the arbitration process, bringing the dispute under the jurisdiction of the competent court.

Egyptian litigation is influenced by the Arbitration Law, which adopts a civil law system primarily based on the philosophy of codified law. Judicial precedents from the Court of Cassation enjoy a high level of persuasive effect, but they do not have de jure binding effect on lower courts, which are generally bound by codified laws issued by the legislature. On the other hand, when the Constitutional Court declares a law as unconstitutional, that law is considered void from the date of the Court's decision, and therefore, the courts are bound by this decision and cannot further apply the law. The Court of Cassation has also established some judicial principles regarding the application of the Arbitration Law, which are consistently followed by lower courts.

The International Islamic Center for Reconciliation and Arbitration (IICRA) is an independent international nonprofit organization that aims to regulate the settlement of various types of financial, commercial, banking, investment, and real estate disputes in compliance with Sharia law through institutional reconciliation and arbitration. IICRA was established based on an international agreement dated April 5, 2005, corresponding to Safar 26, 14 Hijriah.

IV. CONCLUSION

A. Conclusion

Based on the main issues discussed, the following conclusions can be drawn:

The principle of Profit and Loss Sharing in Islamic Banking Investment Deposits in Indonesia applies the principle of al-mudharabah, while in Malaysia, it can be identified as the core of equity relationships. Equity relationships are built on capital and labor contributed by partners. The mechanism of profit and loss distribution is facilitated through syirkah and mudharabah investment capital, while the Islamic banking system in Egypt operates according to the partnership concept

that emerges between the bank and the depositor.

The resolution of Islamic banking disputes in Indonesia and Malaysia consists of litigation and non-litigation pathways, while the resolution of Islamic banking disputes in Egypt is done through arbitration.

B. Recommendations

Based on the main issues discussed, the following recommendations can be made:

The principle of profit and loss sharing in Islamic banking investment deposits in Indonesia and Malaysia needs to improve the service of a specific Shariah deposit product, especially the profit-sharing principle between the two countries, to make its implementation more structured. Associations in Egypt need to acquire a certain level of professionalism for the enforcement of such regulations and standards, and there must be coordination among all Islamic and non-Islamic banking units operating in Islamic and non-Islamic countries regarding how to address knowledge and informative advertising issues. The current Islamic banking infrastructure can be utilized, such as the General Council for Islamic Banks and Financial Institutions, the Islamic Development Bank, and the Islamic Financial Services Board in Malaysia.

Malaysia should consider adopting the institutional framework for resolving Islamic banking disputes that exists in Indonesia, which specifically grants authority to handle Islamic banking disputes to Religious Courts, ensuring that the judges handling such cases are more competent in the field, which significantly affects the quality of case decisions. Support from policy stakeholders is needed in terms of operational costs and the development of human resources for judges, arbitrators, and mediators. As for Egypt, efforts should be made to improve the existing economic conditions to make it less vulnerable to international claims before the ICSID.

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