Financing Schemes and Lost Profit Sharing in Islamic Banking: Challenges and Opportunities

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ABSTRACT: A and lost profit sharing system is an agreement between a financier (Shahibul mall) and a capital manager (mudharib) to run a business with a particular economic and risk loss of profit sharing scheme. At this time a lot of literature encourages PLS schemes as the main mode of Islamic banking system, but in practice it is avoided. The research aims to theoretically Evaluate the causes of the PLS in Islamic banking contracts fail to be fully accepted and be excellent for investors in Islamic Banking. The results Showed that the use of PLS (mudaraba and musharakah) schemes in Islamic (sharia) Banking in Indonesia, Malaysia, Pakistan, Turkey and Morocco did show a low percentage of total financing. There are internal factors and external factors that hinder the development of PLS schemes. Internal factors include moral hazard concerns from partners, low trust in partners, weak monitoring systems, weak capabilities and collateral from partner companies. While external factors include; public literacy on Islamic banking products, government support, and supervision from regulators. Some of Reviews These factors Arise because of a misunderstanding of the PLS system. Therefore, it is Necessary to reprogram the perception of Shahibul mall and mudarib in the PLS scheme. This research is expected to Contribute to the development and improvement of PLS schemes in Islamic Banking it is Necessary to reprogram the perception of Shahibul mall and mudarib in the PLS scheme. This research is expected to Contribute to the development and improvement of PLS schemes in Islamic Banking it is Necessary to reprogram the perception of Shahibul mall and mudarib in the PLS scheme. This research is expected to Contribute to the development and improvement of PLS schemes in Islamic Banking

Keyword: Lost Profit Sharing; Shahibul mall; Mudharib: Mudarabah: musharakah

Introduction

Practice flower that is currently the basis of the practice of conventional banking services, it has been determined by Islamic scholars as usury. Riba has been forbidden by the Qur’an as mentioned in Surah Al Baqarah verse 275
People who eat (take) usury can not stand but as stands one whom possessed devil because the (pressure) insanity. Their circumstances were such that, is because they say (argued), the actual buying and selling the same as usury, but Allah has permitted trading and forbidden usury. People who receives an admonition from his Lord and stops (from taking usury), then for him what he has taken in advance (before coming ban); and affairs (up) to Allah. The returnees (usury), then it is the dwellers of Hell; they will abide therein .

This verse is the basis of bank interest Prohibition of conventional banking practice. As an alternative, the Muslims establish banks and financial institutions that are free practices by raising interest Islamic banking products. Profit-sharing scheme and commonly referred to as a model risk and lost profit sharing. Model and lost profit sharing is considered as a concept that truly reflects the values of Islam. Term profit sharing in the science of accounting is the distribution of some part of the profits of a company to another party (Hajj, 2015). Shafi Antonio (2001) and Aziz and Suharyanti (2013) explains that profit sharing is a distribution of profits among the owners of capital (shahibul maal) and manager (mudharib) on the results of operations. System and lost profit sharing agreements that are bound to form a business contract between the investor (Shahibul mall) and managers of capital (mudharib) to carry out an economic business activities. In the management of economic enterprises are run, the benefits will be shared with both parties in accordance with the agreement in the early covenant ratio. Similarly, if the business suffered a loss, it will be on the responsibility together according to each serving. Losses incurred financiers is not the return of investment capital as a whole or overall. As for managing capital (mudharib), the losses in the form of loss of the right to a wage / results of his efforts towards the work done (Hafid, Majid, and Juardi, 2018).

In the Islamic banking system and lost profit sharing is a form of intermediation services. Model and lost profit sharing is generally known as mudharabah and musharakah and is a form of reward-sharing and risk-sharing between the parties to a transaction known as a profit and loss sharing. Profit and loss sharing schemes are considered to promote honesty and fairness (Bakhtiar, Sugema, & Irfany, 2014). In addition, the profit and loss sharing is claimed to improve the well-being and more equitable than the interest-based banking system (Sugema, Bakhtiar, & Effendi, 2010). According Sugema, et al.

The justice system on the model of profit and loss sharing banking is due to the elimination of the element of interest in a partnership contract and depositors earn a
return (return) over the real economy (from the business). It is certainly an impact on the preparation conditions in accordance with the monetary and financial market developments and more suitable for the implementation of investment project financing schemes (Bidabad & Allahyarifard, 2016). Model of profit and loss sharing avoid investment financing of debt and encourage the use of the concept of partnership in equity financing. The scheme is similar to venture capital scheme (Astrom, 2012).

And lost profit sharing concept applied to mudharabah and Musharaka. Mudharabah explained that the owners of capital to provide funds (principal) to users of capital or entrepreneurs (agent) for some businesses or productive activities. The provision of such capital is done with the proviso that the resulting gains and losses will be shared among them (and lost profit sharing). If any damage occurs in the normal process or business activity that caused not due to negligence or fault of the employer, then it will be borne by the investors (Shahibul mall). Employers in this context only invest in human capital. The ratio of income distribution is ex-ante. In the event of a loss, capital providers will lose their money to a certain extent and businessman (agent) will lose all of its workforce (Sarker, 1999). Although there are some parties do not agree with the ex-ante scheme and considers that the truly Islamic PLS and sharing is determined after they are collected. Musharaka contract is an agreement of cooperation between two or more parties to a particular where each party contributes funds to the agreement that the benefits and risks will be shared in accordance with the agreement (Joseph, 2005).

Model risk mitigation profit and loss sharing is done by managing risk together and both parties will bear and manage risks together so that no party has been harmed because they have to bear the risk alone. The concept of different profit and loss sharing with the business model that raises risk transfer schemes win-lose situation. In the scheme of win-lose situation was explained that one of the parties to avoid the risk (win) and the other party to bear the risk (lose). This will open a boost for the insurer to risk to make efforts in order not to experience any losses, including the justified the means. Furthermore, the risk transfer scheme, there is still a risk of not being managed. One party simply move the risk to other parties that may result in a loss to him. Risk transfer is a zero-sum forms of activity which benefit one party to a transaction resulting in a loss for the opponent transaction. Whereas Islam teaches that commerce must be principled love-at-love (win-win situation) between parties to a transaction, tijaaratan antaradhin minkum (QS. An-Nisa : 29) (Tutuko, 2018). While the concept of profit and loss sharing is risk sharing. The concept of profit and loss sharing scheme will lead to a win-win situation because of the benefits and risks will be shared by both parties. Whereas Islam teaches that commerce must be principled love-at-love (win-win situation) between parties to a transaction, tijaaratan antaradhin minkum (QS. An-Nisa : 29) (Tutuko, 2018). While the concept of profit and loss sharing is risk sharing. The
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Application of profit and loss sharing scheme turns into reality is not easy because of some constraints in Islamic banking. Application of profit and loss sharing models could potentially lead to conflict Agency. One example is in mudharabah and Musharaka. Agency conflicts likely to occur on profit and loss sharing contract relating to the interests of both parties are different (M. Muhammad, 2008). Management (mudharib) as a fiduciary of the principal (Shahibul mall) on several reality shows their effort to minimize losses is given as; condition because it can not reach a specified target principal (Rama, 2012). Another concept that is offered to enhance profit and loss sharing application in practice is the perfection of the contract process in order to provide a security guarantee to both parties through contract-contract agreement sharia. Clauses in the contract reflect the risk mitigation shariah performed by the provider contract. But the model shows that in fact the two sides do not trust each other. This condition is seen that the concept of profit and loss sharing is still not reflect the spirit of sharia (Islamic) and away from the concept taawun (helping) you desire sharia (Suryanto, 2015). Sugema et al., (2010) proposed a mechanism that would increase the transparency of the system of profit and loss sharing from the perspective of the owners of capital is through risk pooling bank. Bank will absorb all the risks faced by owners of capital and then maintain their income distribution and at the same time reducing the risks faced by the borrower. However, this concept still needs improvement to be elaborated in a practical level.

Mudharabah explained that the other person is a party to the insider (active) identified as the agent (mudharib) who has knowledge of an investment project that is risky, but profitable. Agents hope to jump in it, but he did not have the initial funds to finance the project. Parties to the outsider as funders (Shahibul mal), which provide all initial funding for the establishment of the project. In this case sometimes the agents tried to take advantage of the information it has. It can trap funders (Shahibul mall) in losses. Shahibul mall (lenders) are likely to provide a wide range of requirements in akadnya as a form of protection for the granting of these funds. So that the practice is often seen as another form of conventional practice (Khoiruddin and Noekent, 2011). Therefore, according Khoiruddin and Noekent, sharia contract needs to be reviewed and refined in order to truly reflect Islamic concepts in business / business. So as to generate a large maslahah for all parties. Therefore, researchers try to summarize the
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weaknesses of the implementation of the PLS system over the years, as well as opportunities for further improvement.

Until now, few studies have tried to dissect the shortcomings of profit and loss sharing scheme. One is research Dar and Presley (2000) who studied the weaknesses of the control in the PLS in Islamic banking. Research Bank Indonesia (2009) on the entire Islamic banking in Indonesia highlighted several weaknesses in the scheme of profit and loss sharing, resulting in Islamic banks in Indonesia are reluctant to use the scheme of profit and loss sharing. Abdul Rahman et al (2014) writes about the challenges of profit and loss sharing scheme in the Malaysian Islamic banking. Research results also highlighted the reluctance of Islamic banking in Malaysia in the use of profit and loss sharing scheme. Then in 2019,

The phenomenon that occurs today is the Islamic financial institutions currently considered deliberately and systematically avoid financing model of profit and loss sharing (Nuddin & Ibrahim, 2019). This statement is motivating this study is to see how the challenges and opportunities faced by Islamic banking is not interested in using the scheme of profit and loss sharing in their intermediation services. Theoretically, this research evaluates the causes of profit and loss sharing contract in Islamic banking have failed to be accepted. The purpose of this evaluation is to draw a convincing theoretical arguments about the causes of profit and loss sharing scheme difficult to thrive in Islamic Banking.

Research Methods

This study collects some of the results of research from 2000 to 2019. Searches of articles using google scholar. The entire article was then analyzed to collect the red thread of any research results. Having collected then made systematic and formulation of the problem and then look for opportunities for improvement of the concept of profit and loss sharing. The analytical method used is qualitative research. Data analysis was performed using the literature (Sugiyono, 2010).

Result and Discussion

Results Analysis

The results of several studies to formulate some of the causes of profit and loss sharing schemes difficult to thrive in Islamic banking. Research Alyah, (2006) found that the burden of profit-sharing scheme is greater than the interest scheme. It is certainly weighing on the manager (mudharib). When running mudharabah Islamic banking and acted as financier (Shahibul mall), tend to charge a profit sharing rate is higher than the interest rate on conventional banking. Some cases show that the level of revenue sharing ratio of the predetermined agreement. Though sharing system should ensure a level of profit in the beginning. In the event of a loss, then the Bank will recover such losses. Customer (mudharib) will not benefit. However, the bank will continue to
investigate the causes of the loss. If the accidental loss or negligence of the customer, the customer must still bear the loss. Musharaka financing scheme, in case of loss then the loss will be shared based on the portion of capital agreed. Although sometimes paid customers more and more expensive. But it is still acceptable to Islamic law. This is because the customer and the bank has done a deal at the beginning of an agreement on revenue sharing PLS (Aliyah, 2006). Although sometimes paid customers more and more expensive. But it is still acceptable to Islamic law. This is because the customer and the bank has done a deal at the beginning of an agreement on revenue sharing PLS (Aliyah, 2006). Although sometimes paid customers more and more expensive. But it is still acceptable to Islamic law. This is because the customer and the bank has done a deal at the beginning of an agreement on revenue sharing PLS (Aliyah, 2006).

Research Bank Indonesia (2009) shows that shifting the problems faced by Islamic banks in implementing the scheme of profit and loss sharing. Islamic banking is an internal matter. Shift is from the human resource issues that are less in terms of quality and quantity and the impact on the occurrence of problems such as the technical aspects of information technology problems, weakness SOP, and top management commitment issues. While the external side, emerging issues related to lack of support and commitment of the government in the form of regulations and incentives that support the development of Islamic banking. In addition, there is still a lack of public confidence in Islamic banking. Policies developed by the regulator (FSA) should include not only market-driven policies, but also the professionalism of the perpetrators. Furthermore,

Research Abdul-Rahman, Latif, Young, & Abdullah, (2014) highlights the challenges faced by the scheme of profit and loss sharing financing in Islamic banking institutions in Malaysia, particularly mudaraba and musharakah. Results of some of the interview to the management of Islamic banks in Malaysia that offers financing profit and loss sharing shows that there are four main obstacle financing schemes profit and loss sharing. These barriers are; high investment risk, difficulty in choosing the right partner, the average customer (mudharib candidates) who are interested in having a low credit worthiness, and the lack of security guarantees on capital in Invest.

Research AM Muhammad (2014) also tried to summarize developments in Islamic banking PLS mode Pakistan. The results of the survey showed that only 0.2% who choose the scheme mudharabah and 8.6% of the overall scheme Musharaka contract sharia contract period January to March 2014 (Source State Bank of Pakistan). Research results suggest that some factors inhibiting the development of financing schemes profit and loss sharing in Islamic banks. He said there are three main categories that affect it is; internal factors, external factors, and communal factors. Internal factors include; Constraint Management monitoring and control systems, the effect of the role of top management, the effect of the application of risk management, and the influence
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of sharia supervisory boards (DPS). While external factors include; public preference towards Musharaka scheme and the lack of government policy support. While communal factors include; the risk of moral hazard, the high risk in this scheme, and the difficulty of operating the scheme Musharaka. The most influential factor for the low interest in the Musharaka contract is an internal factor that the strict application of risk management in Islamic banking that led to the emergence of a desire to protect any potential risks because they are potentially against moral hazard and failure of business.

Research Abdul-Rahman and Nor (2017) in the Islamic Bank Malaysia Bhd (BIMB) and Bank Rakyat (BR) find a low interest in the scheme and musharakah mudharabah. Results of interviews with respondents A (BIMB) shows that the number of applicants musharakah and mudaraba financing is still small. Akad offered are based construction musharakah financing such assets; building which was later sold, and the profits distributed among the businessmen and bankers accordance with sharia. Musharakah is also implemented in several venture capital by many companies with the support of the Malaysian Government. Mudaraba is also offered to the entrepreneurs. The scheme has been carried out BIMB is acting as Shahibul mall and the customer as an entrepreneur (mudharib) in a project. According BIMB, musharakah and mudaraba-based financing is not widely available to its customers because they both have a relatively high risk. Banks always want to find the most suitable candidates to provide funding based on profit and loss sharing.

Musharakah financing and mudaraba with profit and loss sharing scheme requires the customer (mudharib) to be able wisely to generate profits and not losses. This is due to the funds invested by the bank is owned by the depositors. Therefore, Islamic banks must be very careful in investing the fund because it is very risky to maintain the confidence of depositors. Research results and Nor Abdul-Rahman (2017) found that small companies that do not yet have the ability and strength adequate business will try to get financing through musharakah and mudaraba. While large companies such as Petronas and TNB, tend to avoid these financing schemes.

Results of research and Nor Abdul-Rahman (2017) specifically describes four barriers to implementation musharakah and mudaraba financing schemes in general. The first is a high chance of failure in this investment model. The second is the selection of a partner who will be invited to cooperate has high difficulty. This caused very difficult to assess the capabilities of a partner in a short time. It took a long time to really get to know potential customers. In fact, it is in some cases failed to assess the integrity of partners. All three are enthusiasts. The average interest PLS scheme are customers who have a profile that is vulnerable and at risk. The customers are generally individuals and small and medium businesses that do not have a strong business base. So it is likely to suffer losses. In addition, the costs for the control of individuals and small to medium sized companies, much bigger than the large companies. And the
fourth is a guarantee. Small and medium companies and individuals generally do not have a guarantee (collateral) is adequate to cover potential operating losses.

Orhan research (2017) conducted a survey of five Islamic banks in Turkey. The results of calculations based on the proportion of the participation of profit and loss sharing agreement against all assets and financing (credit) Islamic Bank. shows the ratio of profit and loss sharing (Mudharabah) to total deposits of 5.2%. While the ratio of profit and loss sharing (Musharaka) to total financing (loans) is only 0.4% and the total asset size is only 0.2%. The number shows the still low interest financing scheme of profit and loss sharing. According to Orhan (2017), there are several factors that lead to profit and loss sharing scheme is less developed, among other things 1) The lack of transparency in the company's balance sheet in particular sometimes do not reflect the reality or true value, 2) Balance of companies that do not reflect these realities lead to a lack of confidence in these partners, 3) Family Finance, a house special financial that started operations as Faisal Finans in 1984 and later merged with Anadolu Finans in establishing Turkiye Finans in 2005, has some experience in mudarabah, This raises the fear of loss sebagaiman then a previous bad experience. Example; Companies can declare bankruptcy forged in order not responsible for the risk of the partnership. 4) Lack of legal regulation in this scheme a specialized financial house as Faisal Finans started operations in 1984 and later merged with Anadolu Finans in Turkiye Finans founded in 2005, has some experience in mudarabah, This raises the fear of loss then a previous bad experience. Example; Companies can declare bankruptcy forged in order not responsible for the risk of the partnership. 4) Lack of legal regulation in this scheme a specialized financial house as Faisal Finans started operations in 1984 and later merged with Anadolu Finans in Turkiye Finans founded in 2005, has some experience in mudarabah, This raises the fear of loss then a previous bad experience. Example; Companies can declare bankruptcy forged in order not responsible for the risk of the partnership. 4) Lack of legal regulation in this scheme a specialized financial house as Faisal Finans started operations in 1984 and later merged with Anadolu Finans in Turkiye Finans founded in 2005, has some experience in mudarabah, This raises the fear of loss then a previous bad experience. Example; Companies can declare bankruptcy forged in order not responsible for the risk of the partnership. 4) Lack of legal regulation in this scheme

Badaj and Radi (2018) also conducted research with the same object in Morocco in 2018. The goal is to test the willingness of SMEs Morocco to wear PLS financing scheme. The results showed that there is a factor of cost considerations, reduced control of the business, limited access to conventional debt, financial feasibility, and religious beliefs have a significant impact on the willingness to use the model of profit and loss sharing. Additionally, normative beliefs (use by people close and influential people) also has significance. Neither the facilitation conditions, associated with government support, was found to have a significant effect on the control behavior has a significant impact on the intention to use PLS financing scheme. Badaj and Radi (2018) explains that turns profit and loss sharing models and business support has no effect on attitudes. Accessibility and independence to conventional debt has no effect on the control behavior of profit and loss sharing partners. Findings on religious beliefs and
subjective norms do not affect the intention to adopt the profit and loss sharing scheme because respondents were not given information about its function. These results illustrate that the principle of profit and loss sharing is still poorly understood. Therefore Badaj and Radi (2018) propose that more be disseminated more widely on Islamic financing scheme. Findings on religious beliefs and subjective norms do not affect the intention to adopt the profit and loss sharing scheme because respondents were not given information about its function. These results illustrate that the principle of profit and loss sharing is still poorly understood. Therefore Badaj and Radi (2018) propose that more be disseminated more widely on Islamic financing scheme. Findings on religious beliefs and subjective norms do not affect the intention to adopt the profit and loss sharing scheme because respondents were not given information about its function. These results illustrate that the principle of profit and loss sharing is still poorly understood. Therefore Badaj and Radi (2018) propose that more be disseminated more widely on Islamic financing scheme.

**Discussion**

Findings Alyah, (2006), Bank Indonesia (2009), Abdul-Rahman, Latif, Young, & Abdullah, (2014), AM Muhammad (2014), Abdul-Rahman and Nor (2017), Orhan (2017), Badaj and Radi (2018) shows that much work remains to be solved by experts of Islamic economics. There are four economic agents were concerned that the application of profit and loss sharing schemes can be successful. The party is; entrepreneurs, depositors, shareholders, and Islamic banks. Some researchers suggest to change the position and model of lending. Islamic banks have to escape from the shadow of a conventional bank conducting business through lending. Islamic banking intermediation services model rather than as lenders (creditors) but it should be the investor or manager (investment manager).

Errors that occur in the pengagas Islamic banking is the notion that adopting profit and loss sharing scheme is the replacement rate system for profit and loss sharing system is considered to meet the need to make a profit or make money without violating sharia. Though profit and loss sharing system is designed based on sharia have different goals with the system of interest in conventional banks. Rate system from the perspective of people see money as a form of a commodity (rationalistic). While the PLS from the perspective of universalism in creating maslaha and money is only a medium of exchange. The nature of the borrowing not for profit but please help (taawun) against fellow human beings. As stated by the Qur’an Surah Al Maidah verse 2, namely;

وتعاونوا علیالب‌وآلتقؤی ولا تعاونوا على الائتم والعدون وآتقوا الله إن الله شديد العقاب

This means:
"And please-menolonglah you in the (working) virtue and piety, and do mutual assistance in sin and transgression. And fear ye Allah, verily Allah is severe in punishment."

Fear shahibul mall will be the risk of non-performing loans, moral hazard, lack of partner capabilities and distrust against unwarranted actual partners. Fear Shahibil mall capital loss is the perspective of individuals who were looking for a profit is not the perspective of mutual help. Perspective attended parties are parties who do not have sufficient ability both in terms of capabilities, capital and collateral. Therefore, Islamic banking should act as a builder and raise the capability Shahibil mall. Supposedly the application of risk management to the feasibility of this mudharib (small and medium entrepreneurs) do not use the criterion of 5 C (capital, collateral, capabilitas, character, condition) and 7 P (personality, party, purpose, payment, profitability, and protection) because the average businessman who entered the category in need of help will not be able to meet these criteria. Assessments should be directed to the principles maslahah in society (protection of religion, life, intellect, lineage and property).

The argument that if Shahibil mall taawun apply the concept in his business schemes can trigger moral hazard of mudharib action should not have happened because the Islamic business based on the principles of trust and mandate. Mudharib which manages the mall shahibul capital required to hold the mandate and the parties are not able to hold the trust and cheating to others described in the Quran as the killing itself. When translated in a business context, undermine the mandate as damaging his own business. As mentioned Qur’an in Surah An-Nisaa verse 29;

يأيها الذين آمنوا لا تأكلوا أمولكم ببطل إلآ أن تكون تجرة عن ثراض منكم ولا تقتلوا أنفسكم إن الله كان بكم رحيما

This means:
"O ye who believe, do not eat each other neighbor's property by way of vanity, except by way of commerce that goes with the same love-love between you. And do not kill yourselves; surely Allah is Merciful to you."

Do vanity (cheating) is the same for fellow human beings kill themselves. It is these values that bind mudharib to maintain professionalism (belief and trust) in the capital entrusted to manage Shahibil mall. Therefore, both sides should depart from the intention of the net. Party Shahibil mall taawun departing from the concept and the mudharib departing from an attitude of trust. Context intention is important because it will determine the final results to be obtained by both parties. As the hadith of the Prophet narrated from Umar bin Khattab that;
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 وإنما الأعمال بالنيات وإنما لكل امرئ ما نوى فمن كانت هجرته إلى دنيا يصيبها أو إلى امرأة ينكحها فهجرته إلى ما هاجر إليه.

That is;

"All deeds depend intentions, and the (children) for each person (depending on) what is intended; Whoever intention of emigration since the world who want digapainya or for a woman who wants to marry, then emigration is to what he intended"

Source: (Hadith-Book Encyclopedia 9 Imam).

This hadith suggests that the intention is the factor that determines the assessment of an act. All kinds of worries Shahibul mall in terms of internal factors can be overcome. So that the financing scheme of profit and loss sharing can be a way out that is required by sharia.

Conclusions

The results of this study indicate that the use of the scheme of profit and loss sharing (Mudharabah and musharakah) in Islamic Banking (Shariah) Indonesia, Malaysia, Pakistan, Turkey and Morocco showed a low percentage portion of the total financing. Internal factors such as concerns the behavior of moral hazard of partners, lack of trust in the partner, the weakness of the monitoring system, the lack of capability, collateral from partner companies and external factors such as literacy community towards Islamic banking products, government support, supervision of the regulator is the cause of a scheme of profit and loss sharing to thrive. The results of this study suggest that the initiators of Islamic Banking considers that the scheme profit and loss sharing (Mudharabah and musharakah) designed based on the concept of mutual help (taawun) against fellow human beings and not just for profit. Shahibul mall and mudharib parties should depart from the intention of the net. Low literacy community causes people not able to distinguish between conventional and Islamic financing. Therefore, the support of the government as regulator, monitors and guards of Islamic banking business should be improved so as to encourage the development of Islamic banking.

Reference


