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# Strengthening Interest and *Riba* in Bank Financial Institutions

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***Abstract:*** *This research examines and substantially analyzes the problem of riba from a rational perspective, and at the end of this paper offers a profit-sharing system and profit-sharing system as an alternative solution to the interest system in the transaction system in banks (bank financial institutions). Interest in the study of riba has always been a topic that does not experience saturation and is still very hotly discussed in Islamic economics. This can be seen from the discussion of riba which has always colored the discourse of Muslim thought and debates that have barely found common ground. The results of the study display that the debate on thoughts about riba and bank interest shows that the issue of riba is very closely related to muamalah (economy) issues, especially those that occur in Bank financial institutions. The concept of riba turning into interest cannot be separated from the evaluation of the development of these financial institutions.*

*Keywords: Interest; Riba; Financial Institution; Bank; Islamic Economy*

## Penguatan Bunga dan Riba di Lembaga Keuangan Bank

**Abstrak:** Penelitian ini mengkaji dan menganalisis secara substansial masalah riba dari perspektif rasional, dan pada akhir tulisan ini menawarkan sistem bagi hasil dan sistem bagi hasil sebagai alternatif solusi sistem bunga dalam sistem transaksi di bank (lembaga keuangan bank). Minat kajian riba selalu menjadi bahasan yang tidak mengalami kejenuhan, bahkan masih sangat hangat dibicarakan dalam ekonomi Islam. Hal ini terlihat dari pembahasan riba yang selalu mewarnai diskursus pemikiran umat Islam dan perdebatan yang hampir tidak menemukan titik temu. Hasil penelitian menunjukkan bahwa perdebatan pemikiran tentang riba dan bunga bank menunjukkan bahwa persoalan riba sebenarnya sangat erat kaitannya dengan persoalan muamalah, terutama yang terjadi di lembaga keuangan bank. Konsep riba menjadi bunga tidak lepas dari evaluasi perkembangan lembaga keuangan tersebut.

**Kata Kunci:** Bunga; Riba; Lembaga Keuangan; Bank; Ekonomi Islam

## A. Introduction

The term *riba* (usury) is closely related to transaction activities. *Riba* is a concept that is one of the prohibitions in conducting transactions in the Islamic economic system, in addition to the implementation of zakat and the prohibition of *maisir* (gambling), *gharar* (obscurity), and falsity. In economy, the concept of prohibiting *riba* will have an impact on investment flows to be directed, then in the implementation of *zakat* (charity), it will generate aggregate demand and encourage wealth to flow into investments, while the prohibition of *maisir*, *gharar*, and falsity will ensure that investment flows into productive businesses and will produce productive goals as well, and ultimately will increase aggregate supply.[1]

The prohibition of *riba* is essentially the elimination of injustice and upholding justice in the economy. The elimination of *riba* in the Islamic economic system can be interpreted as the elimination of *riba* that occurs in the practice of buying and selling and debts. In this context, various speculative transactions containing elements of *gharar* must be prohibited. Likewise, interest, which is *riba nasi'ah* (taking or giving additional goods or capital which is deferred and ends with the payment) absolutely must be eliminated from the economic system.

Observing the issue of *riba* is very closely related to financial and banking issues. Not long ago we lost our memories, the tragedy of the 1997 monetary crisis where the Indonesian economy slumped, has even become a multidimensional crisis. It is suspected that the Indonesian economy has been dragged into this prolonged crisis as a result of ineffective monetary policy management. In addition, it was also triggered by the problem of foreign debt which had turned into a "time bomb" that devastated the Indonesian economy at that time. Conglomerate businessmen who are hailed as “the biggest taxpayers,” are in fact like “looters” at the national level. Banks are not used as institutions to assist the government and society in financing national development, but rather as tools for plundering government and public funds by conglomerates.[2]

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[1]Ascarya, *Akad dan Produk Bank Syariah* (Jakarta: Raja Grafindo Persada, 2007), 8.
[2]Mubyanti, *Membangun Sistem Ekonomi* (Yogyakarta: BPFE, 2007), 274.

The above facts show that conventional banking, which uses an interesting system, is very unstable and not strong in facing monetary turmoil conditions marked by higher interest rates so it experiences a negative distribution. However, the Islamic banking system has shown its existence as a system that is tough and free from negative distribution, because it is not based on an interesting system.

For this reason, this paper seeks to examine the problem of *riba* from a Sharia perspective. The discussion will start by raising the background of the emergence of *riba*, the concept of *riba* and interest in Islamic economics, profit sharing and sharing loss as a rational solution to interest, which includes the Islamic concept of money, money in the Islamic economic system, prohibition of *riba* in the Islamic financial system, how to be productive money that does not contain elements of *riba*, and at the end of the discussion this paper offers profit sharing and loss sharing as a solution to the interest or *riba* system.

## B. The Concept of *Riba*

*Riba* has been known for a long time and has experienced development. The study of *riba*, it turns out, is not only discussed by Muslims, but various groups outside of Islam also take this issue seriously. If traced back more than two thousand years ago, the study of *riba* has been discussed by non-Muslims, such as Hindus, Buddhists,[3] Judaism, Greek, Romans, and Christianity.[4]

The concept of *riba* for Jews, known as "Neshekh" is stated as something that is prohibited and despicable. This prohibition is found in many of their scriptures, both in the Old Testament and in Talmudic statutes. Many verses in the Old Testament prohibit the imposition of interest on loans to the poor and condemn the pursuit of wealth by burdening the poor with *riba* or interest, including the following:

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[3]Rivai Veithzal, et.al., *Bank and Financial Institution Manajemen Conventional and Shariah System* (Jakarta: Raja Grafindo Persada, 2007), 761.

[4]Muhammad Syafi'i Antonio, *Bank Syariah: Dari Teori ke Praktek* (Jakarta: Gema Insani Press, 2001), 42.

1. The Book of Exodus chapter 22 verse 25 states the following:

   "If you lend money to one of My people, a poor person among you, then do not act as a debt collector against him; do not charge interest on him."[5]

2. The Book of Deuteronomy chapter 23 verse 19 states the following:

   "You shall not charge interest on loans to your brother, interest on money, interest on food, interest on anything that is lent for interest."[6]

3. The Book of Leviticus chapter 25 verses 36-37 states the following:

   "Do not take interest or any profit from them, but fear your God, so that they may continue to live among you. [37] You must not lend them money at interest or sell them food at a profit."[7]

Meanwhile, during the Ancient Greek and Roman times, the practice of *riba* or interest was a common tradition.[8] In the Greek period, around the 6th century BC to 1 AD, several types of flowers varied in size.[9] Meanwhile, during the Roman era, around the 5th century BC to 4th AD, there was a law that allowed residents to take excess interest as long as the interest rate was under the "maximum legal rate." This interest rate varies according to the changing times, but the withdrawal is not justified through interest bearing or double countable.

In Roman times there were 4 types of interest rates, namely as follows: (a) maximum interest allowed: 8%-12%; (b) typical loan interest in Rome: 4%-12%; (c) interest in Roman possessions: 6%-100%; and (d) Byzantine special interest: 4%-12%.[10]

The concept of *riba* among Christians experiences different views, which in general can be grouped into three periods as follows: First, the views of the early Christian priests (I-XII centuries) prohibited *riba* by referring to the Old Testament and the laws of the church. In the IV century AD, the Roman Catholic church prohibited the practice of *riba* for priests, which was later extended to the laity in

[5]https://www.biblegateway.com/passage/, diakses 16 Juni 2022.
[6]*Ibid.*
[7]*Ibid.*
[8]Abdul Azim Islahi, *Economic Concepts of ibn Taimiyah* (London: The Islamic Fondation, 1988), 124.
[9]Antonio, *Bank Syariah,* 43.
[10]*Ibid.*

the fifth century AD. In the VIII century AD, under the reign of Charlemagne, the Roman Catholic church declared the practice of *riba* a criminal act.[11]

Second, the view of Christian scholars (XII-XVI centuries) who tend to allow interest, by making breakthroughs through efforts to legitimize law, interest is divided into interest and *riba*. According to them, interest is permissible interest while *riba* is excessive interest. Christian scholars who contributed to this floral thought were Robert of Courcon (1152-1218), William of Auxerre (1160-1220), St. Raymond of Pennaforte (1180-1278), St. Bonaventure (1221-1274) and St. Thomas Aquinas (1225-1274).[12]

Third, the views of Christian reformers (XVI-1836 century) such as Martin Luther (1483-1536), Zwingli (1454-1531), Bucer (1491-1551), and John Calvin (1509-1564) which caused Christianity to justify interest). During this period, King Henry VIII decided to break with the Roman Catholic Church, and in 1545 interest was officially allowed in England as long as it did not exceed 10%. This policy was again strengthened by Queen Elizabeth I in 1571.[13]

It was this history that gave rise to the practice of modern banking operations which began to grow and develop in the XVI century AD using the interest system. This interesting system has begun to grow, take root, and become ingrained in the modern banking industry, making it difficult to stop it. They even think that interest is the center of the banking system. If there is no interest, the banking system will become lifeless, and eventually. The economy will be paralyzed.[14]

Meanwhile, *riba* has been clearly and unequivocally prohibited in Islam. The prohibition of *riba* in the Qur'an was not revealed all at once but gradually, in line with the readiness of society at that time, such as the prohibition of liquor. The

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[11]Iqbal Zamir dan Mirakhor Abbas, *An Introduction to Islamic Finance* (Wiley: John Wiley and Sons (Asia) Pte, 2007), 71.

[12]Antonio, *Bank Syariah,* 47.

[13]Adiwarman Karim, *Ekonomi Islam: Suatu Kajian Kontemporer* (Jakarta: Gema Insani Press, 2001), 72.

[14]Muhammad Abdul Mannan, *Islamic Economic, Theory and Practice,* terj. Nastangin (Yogyakarta: Dana Bhakti Wakaf, 1997), 165.

stages of the prohibition of *riba* in the Qur'an can be explained as follows:

In the first stage, it is stated that *riba* will keep wealth away from God's blessings, while almsgiving will multiply blessings:

> That which ye lay out for increase through the property of (other) people, will have no increase with Allah. but that which ye lay out for charity, seeking the Countenance of Allah, (will increase): it is these who will get a recompense multiplied. (QS. Ar-Ruum/30: 39).[15]

In the second stage, at the beginning of the Medina period, the practice of *riba* was severely condemned, in line with the prohibition of previous books. *Riba* is equated with those who take other people's wealth improperly and threaten both parties with God's painful punishment:

160. For the iniquity of the Jews. We made unlawful for them certain (foods) good and wholesome which had been lawful for them in that they hindered many from Allah's Way.
161. That they took usury, though they were forbidden; and that they devoured men's substance wrongfully. We have prepared for those among them who reject faith a grievous punishment (QS. al-Nisa'/4: 160-161). [16]

In the third stage, *riba* is prohibited because it is associated with a multiplied addition (QS. Ali Imron/3: 130). This verse was revealed after the Uhud war, which is the 3rd year of Hijriyah. The term multiplied must be understood as a non-conditional characteristic so that the meaning is that what is forbidden is not only what is multiplied while a little is not *haram*, but the nature of *riba* that is generally accepted at that time is multiplied.[17]

The fourth stage is the final stage in which Allah firmly forbids *riba*, emphasizes the clear distinction between buying and selling and *riba*, and demands that Muslims write off all debts that contain *riba*:

278. O ye who believe! Fear Allah, and give up what remains of your demand for usury, if ye are indeed believers.

279. If ye, do it not, Take notice of war from Allah and His Messenger. But

[15]https://www.surah.my, diakses 12 November 2022.
[16]*Ibid.*
[17]Antonio, *Bank Syariah,* 49.

> if ye turn back, ye shall have your capital sums: Deal not unjustly, and ye shall not be dealt with unjustly (QS al-Baqarah/2: 278-279).[18]

## C. Views of Sharia Economics on Usury (*Riba*) and Interest

1. Definition of *Riba* and Its Types

Etymologically, the word *ar-riba* means *zada wa nama*, which means to increase and grow.[19] In the Qur'an, the word *ar-riba* and its various forms of derivation is mentioned twenty times; eight of them form the word *riba* itself. This word is used in the Qur'an with various meanings, such as growing, adding, nourishing, expanding, and becoming big and many. Although different, in general, it means an increase, both qualitatively and quantitatively.[20]

While terminologically, *riba* is generally defined as exaggerating profits or assets from one party to another in a sale and purchase transaction or exchange of similar goods without giving compensation for that excess.[21] In another expression, *riba* is understood as the payment of a debt that must be repaid by a person who owes more than the amount of the loan in return for an overdue grace period.[22] Ignoring the differences of opinion, in general, the jurists agree that there are two kinds of *riba*, namely *riba fadl* and *riba nasi'ah*.

However, Abu Zahrah and Rafiq Yunus al-Misri made a slightly different distribution of than other scholars. According to both, *riba* is distinguished from *riba* that occurs in debts called *riba nasi'ah* and *riba* that occurs in buying and selling, namely *riba nasa'* and *riba fadl*. Al-Mishri emphasized the importance of distinguishing between *riba nasi'ah* and *riba nasa'* to avoid confusion in identifying various forms of *riba*.

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[18]https://www.surah.my, diakses 12 November 2022.

[19]Abadi al-Fairuz, *Al-Qamus al-Muhit* (Beirut: Dar al-Fikr, 1998), 332.

[20]Saeed Abdullah, *Islamic Banking and Interest: A Study of Prohibition of Riba and its Contemporary Interprestetion* (Leiden: E.J. Brill, 1996), 20.

[21]Abdurrahman al-Jaziri, *Kitab al-Fiqh 'ala Mazahib al-Arba'ah* (Beirut: Dar al-Fikr, 1972), 221

[22]Muslim Muslihun, *Fiqh Ekonomi* (Mataram: LKIM, 2005), 128.

Table 1. Typology of *Riba* according to Abu Zahrah and Rafiq Yunus al-Mishri

| | **Transaction** | **Riba Types** | **Elements** | **Information** |
|---|---|---|---|---|
| Riba | Owe; lead | *Riba nasi'ah* | Delay and additionally | Agree about it is forbidden if it is tyrannical and exploitative |
| | Buy and sell | *Riba nasa'* | Delay | Still sincere |
| | | *Riba fadhl* | Addition | |

*Riba nasi'ah* in the definition as practiced by the Arab Jahiliyyah community with multiple and exploitative main characteristics has been agreed upon as forbidden by the scholars. Meanwhile, what is currently being debated is that *riba nasi'ah* is not multiplied and to a certain extent is seen as not exploitative, as has been widely discussed regarding bank interest. While *riba fadhl* is still being debated among Muslim scholars. Hassan is one of the scholars who disagree with his ban for various reasons.

The expert in interpretation who allows *riba fadhl* is at-Tabari (d.310 H). Meanwhile, a friend (*shahabat* Nabi saw.) and *tabi'in* (a disciple of the Prophet's companions) figure who allows *riba fadhl* is Ibn Abbas (d. 68 H, Ibn Umar (d.73 H), Zaid bin Arqam (d. 66 H), Usamah bin Zaid (d. 54 H), and Urwah bin Zubair (d. 94 H). The reason for these scholars is the hadith: لَا رِبَا إِلَّا فِي النَّسِيئَةِ (here is no *riba* except *riba nasi'ah*." According to these Islamic scholars, *riba fadhl* is the excess price of transactions of similar goods not due to delays or expediting payments. In their opinion, *riba* which is forbidden according to them is *riba* which contains additions due to delays in time (*nasi'ah*).

Table 2. Law of *Riba*

| ***Riba* Type** | **The *Illat* (Legal Basis) Law** | **Transaction Method and Type the Goods** |
|---|---|---|
| *Riba nasi'ah* | Modernist: *dzulm* (tyranny) | Borrow money |
| | Neo-Revivalism: *ziyadah* (addition) | Borrow money |
| *Riba fadhl* | Abu Hanifah: balance (*ittihad al-wazn*); Imam Malik, Syafi'i, and Ahmad: similar in price | Exchange (buy) gold and silver |
| | Abu Hanifah: *ittihad al-kail* (in size) Imam Malik: *ittihad al-jins* (a kind and includes food); Ahmad: food with conditions can weigh | Exchange (buy) wheat, dates, salt |

These differences are generally caused by various understandings of *riba*. Although *riba* in the Qur'an and hadith is strictly forbidden because it is not given clear boundaries, this has given rise to various understandings of *riba*, and in turn, this issue has had an impact on the understanding of Islamic scholars after generations of friends (*thabi'in*). In fact, until now the issue of *riba* is still a discussion that has not stopped.

2. Definition of Bank Interest

Etymologically, bank interest according to The American Heritage Dictionary of the English Language as quoted by Wirdyaningsih, 'interest is a charge for a financial loan, usually a percentage of the amount loaned.[23] In Oxford English Dictionary, 'interest is money that is paid for use of money lent (the principal) or for forbearance of a debt, according to a fixed ratio (rate percent). Meanwhile, the Legal Encyclopedia for Home and Business is defined as compensation for use of money that is due.[24]

In English, "*interest*" is often translated as "*riba*" which means the act of lending money at an exorbitant or illegal rate of interest.[25] Another definition in Oxford English Dictionary is interpreted as the fact or practice of lending money at interest; especially in later use, the practice of charging, taking, or contracting to receive, an excessive or illegal rate of interest for money for the loan. The Legal Encyclopedia for Home and Business is defined as an excess over the legal rate charged by the borrower for the use of money.[26]

European economic history distinguished between "*riba*" and "interest." *Riba* is defined as the activity of lending money "where more is asked than is given." Word "*riba*" comes from the Latin "*usura*" which means "*use*" which means use something. Therefore, *riba* is the price one has to pay for using money. While said "*interest*" comes from the Latin "*intereo*" which means disappear "*to*

[23]Wirdyaningsih, et.al, *Bank dan Asuransi Islam di Indonesia* (Jakarta, Kencana, 2005), 21.
[24]Tim Pengembangan Perbankan Syariah Institut Bankir Indonesia, *Bank Syariah: Konsep, Produk dan Implementasi Operasional* (Jakarta: Djambatan, 2001), 36.
[25]Wirdyaningsih, et.al, *Bank dan Asuransi,* 25.
[26]Tim Pengembangan Perbankan Syariah Institut Bankir Indonesia, *Bank Syariah,* 37.

*be lost.*" Others said *interest* comes from the Latin "*interesee*" meaning "to come in between" as loss compensation will appear in the middle of *aqad* (contract), "compensation or penalty for delayed repayment of a loan." Then next, "interest" is not only interpreted as compensation for late payment of the debt but also interpreted as compensation for lost opportunities.[27]

From this definition, it is clear that "interest" and "*riba*" what is currently developing the same, meaning additional money, the term "*riba*" emerged due to the unstable financial markets in the past so that the authorities had to set interest rates that were considered "reasonable." However, after the stability of financial institutions and markets, the term disappeared because there is only one interest rate in the market according to the law of supply and demand.

3. Criticism of Interest Theory

In the capitalist economic system, interest is a very important element. It can even be said that interest is the blood of the economy in the capitalist system. but the theory of interest is unable to explain with certainty whether interest is needed in the economic system or whether interest has a role in real investment and not for speculation. For this reason, it is necessary to carry out an in-depth analysis of interest theories in the financial system.

The development of interest theory can be grouped into 2 (two), namely the pure theory of interest and the monetary theory of interest. Economists who support the first group of theories include Adam Smith and David Ricardo, who are adherents of the classical (theory of interest), N. W. Senior was a pioneer of the abstinence theory of interest. Marshall was a pioneer of the productivity theory of interest and Bohm Bawerk was a pioneer of the Austrian theory of interest. Meanwhile, supporters of the second group of theories are A. Lerner was the pioneer of the loanable fund's theory of interest and Keynes was the pioneer of the theory of cash balance interest (Keynesian theory of interest).[28]

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[27]Veithzal, et.al., *Bank and Financial,* 762.

[28]Tim Pengembangan Perbankan Syariah Institut Bankir Indonesia, *Bank Syariah,* 41-42.

In the realm of classical economics, the most famous figures are Adam Smith and David Ricardo. Adherents of the classical interest theory view interest as compensation paid to the lender by the borrower as a service for the profits derived from the loan money. Then, interest can be regarded as remuneration for savings. Because people do not want to save without the expectation of a return from savings, this interest theory holds that an economy without interest cannot possibly work.[29]

Adam Smith also argues that interest is a special price issue and emphasizes the importance of interest with 2 (two) foundations, namely (1) to generate sufficient capital supply, and (2) because of the importance of profits that enable the sustainability of capital.[30] However, this theory has several weaknesses, one of which is that not all savers intend to lend money, so basically even without interest people will still save, and when banking lends money to customers it makes no sense at all if it is said to be a sacrifice.[31]

Then Marshall argues that the productivity interest theory is different from its predecessors. This theory treats productivity as a wealth contained in capital and the productivity of capital is influenced by interest rates. The interest rate itself is determined by the interaction of the supply and demand curves for savings. If the supply of savings is greater than the demand for savings, interest rates will fall and investment will increase. Conversely, if the demand for savings is greater than the supply of savings, interest rates will rise and investment will fall.[32]

Criticism of the theory of Adam Smith, Ricardo, and Senior can also be used to show the weakness of Marshall's theory. now what guarantees a balance between saving and investment is the level of income, not the interest rate. Changes in interest rates have very little effect on savings. An increase in savings is not always followed by an increase in investment or it can be said that

[29]Muhammad, *Teknik Perhitungan Bagi Hasil dan Profit Margin pada Bank Syari'ah* (Yogyakarta: UII Press, 2001), 13.

[30]Afzalur Rahman, *Economics Doctrines of Islam,* terj. Soeroyo dan Nastangin (Jakarta: Dana Bhakti Wakaf, 2002), 17.

[31]Muhammad, *Teknik Perhitungan,* 15.

[32]*Ibid.,* 13.

investment cannot be affected by high and low-interest rates. It can be proven that in a depression, for example, there is a decrease in interest rates, but the reality shows that investment does not increase. then the opinion that the interest rate is determined by the productivity of capital is inaccurate reason because the productivity of capital itself is determined by the interest rate.[33]

Meanwhile, Bohm Bawerk has developed the same theory of interest as that developed by Senior. This Austrian pioneer of the theory of interest argued that the marginal productivity of goods now is higher than the marginal productivity of goods in the future. This theory is generalized based on a very subjective psychological view that makes the understanding of the theory of interest misguided. First, most people do not save on the consideration that their savings in the future will be more than at present, but for specific purposes, such as school, marriage, retirement, and so on. Second, middle and upper-class people accumulate wealth with the aim of prestige and social position, so it's not because the marginal productivity of goods now is higher than goods for the future.[34]

Then the views of other theoretical groups, namely the theory of monetary interest, including Lerner who initiated the loanable fund's theory. This theory departs from the concept of interest that comes from savings and investment. This theory holds that interest is determined by the interaction of the supply and demand for loanable funds. Meanwhile, Keynesian interest theory argues that the interest rate is determined by the supply and demand for money. Therefore, Keynesians believe that saving and investment are always balanced in value. The first stream disagreed with this. According to him, assuming the planned savings will always be the same as the planned investment is baseless. According to him, interest rates are determined by the price of credit and are therefore governed by the interaction of supply and demand for capital. This theory is considered ambiguous,[35] because the analysis confuses the notion of supply with the flow.

[33]Tim Pengembangan Perbankan Syariah Institut Bankir Indonesia, *Bank Syariah,* 42.
[34]*Ibid.,* 43.
[35]Muhammad, *Teknik Perhitungan,* 14.

The last monetary interest theory was carried out by Keynes. Keynes viewed interest not as a price or remuneration for savings, but as a payment for borrowing money. In general, the theory of monetary interest views interest payments as an act of self-confidence to make a profit and an act of lending money. Therefore, Keynes called it a speculative motive. This motive is defined as an attempt to guarantee future profits. In this theory, speculative activities carried out by economic actors will affect interest rates one after another, and will ultimately affect investment, production levels, and employment opportunities.[36] Meanwhile, Islam prohibits all forms of speculation because it can be interpreted as *maysir*.

4. Fatwas of Ulama Regarding Bank Interest

The fatwa of the scholars regarding the prohibition of interest was stipulated in an Islamic research meeting which was attended by 150 leading scholars at its second conference in May 1965 in Cairo, Egypt. After that various International and National Ulema Forums also issued a fatwa forbidding bank interest. As for the decisions of international Islamic institutions, among others:

a. The al-Azhar Islamic Studies Council, Cairo, at the DSI al-Azhar conference in the month of Muharram 1385 H/May 1965 AD, decided that "interest in all forms of loans is *riba* which is forbidden"
b. The decision of the II Islamic Bank Conference, Kuwait, 1403 H/1983.
c. Majma' al-Fiqh al-Islami, Organization of the Islamic Conference, in Decree No. 10 Majma' Fiqh Islamic Council, at the 2nd OIC Conference in Jeddah, Saudi Arabia on 10-16 Rabi' ats-Tsani 1406 H/22-28 December 1985, which decided that “all additional and interest on loans due and the customer is unable to pay it, as well as the addition (interest) on the loan from the beginning of the agreement are two illustrations of *riba* which is forbidden in Shariah.
d. Rabithah al-'Alam al-Islami, in decision number 6th session of the 9th held in Mecca on 12-19 Rajab 1406 H, decided that "bank interest applicable in conventional banking is *riba* which is forbidden."

[36] *Ibid.,* 14-15.

e. Reply to the al-Azhar Fatwa Commission on 28 February 1988.[37]

Meanwhile, the decisions of Islamic institutions in Indonesia include:

a. Muhammadiyah in Lajnah Tarjih 1968 in Sidoarjo decided that "the law on government bank interest is deliberative.
b. Lajnah Ulama of the Fatwa Commission throughout Indonesia, the Indonesian Ulema Council, at the MUI's National Gathering on December 16 2003 decided that "bank interest is the same as *riba*."
c. Nahdhatul Ulama in Lajnah Bahsul Masa'il, National Conference of Bandar Lampung in 1992 issued a fatwa regarding bank interest by accommodating three decisions, namely bank interest is *haram* (forbidden), *halal* (clean, permitted), and *syubhat* (query).
d. The Indonesian Ulema Council at the Alim Ulama Workshop in Cisarua in 1991 decided that: (1) bank interest is the same as *riba*; (2) bank interest is not the same as *riba*; and (3) bank interest is classified as *syubhat*.
e. DSN Fatwa of the Indonesian Ulema Council (MUI) number 1 of 2004 concerning the prohibition of bank interest.
f. It turned out that the emergence of these fatwas caused various responses among the public, both pros and cons. Thus, it is clear that in dealing with the issue of bank interest there are various opinions among Muslims in Indonesia.[38]

## D. *Riba* in Islamic Financial Rationality

The differences of opinion among scholars regarding *riba* and bank interest show that the issue of *riba* is very closely related to financial matters. The change from the concept of *riba* to interest cannot be separated from the development of financial institutions. Financial institutions arise because of the need for capital to finance industry and trade. For this reason, it is necessary to examine in depth the issue of *riba* related to Islamic finance issues.

[37] Ascarya, *Akad dan Produk,* 15.
[38] *Ibid.,* 16.

Money is something that is generally accepted by a society that can be used as legal tender or medium of exchange, either used to pay for the purchase of goods and payment for services, or used as payment for debts. In other words, money is an integral part of human life because money is a means of traffic for payment of goods and services in all economic activities.

Money in its function or purpose of use can be interpreted as an object that can be exchanged with other objects, can be used as a means of storing wealth, and can also be used to pay debts in the future. Meanwhile, Samuelson in Ascarya put forward the definition of money as a modern medium of exchange and a standard unit for setting prices and debt. Lawrence Abbott defines money as anything that is generally accepted by certain economic areas as a means of payment for buying and selling or debt.[39]

Meanwhile, some conventional economic literature defines money from the role and function of money itself in the economy, namely money as (1) a medium of exchange; (2) a store of value; (3) a unit of account or measure of value; and (4) standard size for deferred payment. While the motive for holding money, according to Keynes in Karim, there are three motives, namely (1) transaction motive (the motive for transactions); (2) precautionary motive (motive to take precautions), and (3) speculative motives. From this third motive, the interest rate as an opportunity cost emerges, where the higher the interest rate, the lower the demand for speculative money, and vice versa.[40]

The conventional theory of money is somewhat different from the theory of money in Islamic economics, as a new paradigm in the world of economics. Islamic economics views the concept of money as very clear and firm that money is money, and money is not capital. In contrast, the theory of money put forward in conventional economics is often interpreted the same, namely money as money and money as capital.[41]

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[39] *Ibid.,* 22.

[40] Adiwarman Karim, *Ekonomi Makro Islam* (Jakarta: Raja Grafindo Persada, 2007), 182-183.

[41] *Ibid.*, 77.

According to Ibn Taimiyah in Islahi, money in Islam is a medium of exchange and a measure of value. Money is intended as a measuring tool for the value of an item, through money, the value of an item will be known and they do not use it for themselves or consume it. The same thing was stated by his student, Ibn Qayyim that money and coins are not intended for the object itself, but are intended to obtain goods (as a medium of exchange).[42] Concerning the concept of money, al-Ghazali in Muhammad revealed that: 'money is like glass, glass has no color, but it can reflect all colors. Money has no price, but money can reflect all prices.'[43]

From the definitions and theories regarding money above, in general money in Islam is defined as a medium of exchange and a measure of the value of goods and services to facilitate economic transactions. Thus, money is not a commodity. Therefore, the motive for holding money in Islam is for transactions and precautions only, and not for speculation.[44] Another difference between the theory of money in Islamic economics and conventional economics is that in Islamic economics, money is something that is a flow concept and capital is something that is a stock concept. Whereas in conventional economics there are 2 (two) views on the concept of money as follows:

First, the Irving Fisher concept as stated by Frederic S. Mishkin in Karim that the faster the velocity of money, the greater the income earned. This can be interpreted that money is a flow concept. In other words, there is no correlation between the need to hold money (demand for holding money) and the prevailing interest rate. This concept can be stated in the following equation: [45]

$$MV = PT$$

M = Amount of money
V = Money turnover rate
P = Price level of goods
T = The number of goods traded

[42]Islahi, *Economic Concepts,* 140.
[43]Muhammad, *Dasar-Dasar Keuangan Islam* (Yogyakarta: UPP AMP YKPN, 2005), 46.
[44]Ascarya, *Akad dan Produk,* 22-23.
[45]Karim, *Ekonomi Makro Islam,* 77.

Second, the concept of Marshall Pigou from Cambridge in Karim as expressed by Mishkin, is expressed in the following equation: [46]

$$M = kPT$$

| | | |
|---|---|---|
| M | = | Amount of money |
| k | = | 1/v |
| V | = | Money turnover rate |
| P | = | Price level of goods |
| T | = | The number of goods traded |

Marshall's mathematical equation above shows that the demand for holding money is a proportion (k) of total income (PT). The greater k, the greater the demand for holding money (M) for a certain level of income (PT). This shows that the Marshall concept states that money is a stock concept. Therefore, the Cambridge group said that money is one way to store wealth (store of wealth). In Islam, capital is private goods, while money is public goods. When money flows are public goods (flow concept) then settles into someone's ownership (stock concept) and the money becomes private property (private goods).

An explanation of the concept of money as a flow concept and public goods can be explained as follows:

1. Money as a Flow Concept

In Islam, money is a flow concept while capital is a stock concept.[47] The faster the velocity of money, the better. Money can be likened to water. If the water flows, then the water will be clean and healthy. However, if water is allowed to stagnate somewhere, the water will become cloudy (dirty). Likewise, with money, money that circulates for production will be able to lead to economic prosperity and public health. Meanwhile, if money is withheld (hoarding money), it can cause the wheel of the economy to jam it can cause an economic crisis. For that, the money needs to be used for investment in the real sector. If the money is

[46] *Ibid.,* 78.
[47] Muhammad, *Dasar-Dasar,* 71.

only saved, then not only will you not get a return, but you will also be subject to *zakat*.

2. Money as Public Goods

Money as a public good has the characteristics of being an item that can be used by the public without hindering other people from using it.[48] Money as public goods is likened to roads and capital as private goods are likened to vehicles. Roads can be used by anyone without exception, but people who have vehicles have a greater chance of using the roads compared to people who don't have vehicles.

Likewise with money. Money as public goods can be used more by richer people. This is not because of their savings in the bank, but because of their assets, such as houses, cars, stocks, etc., which are used in the production sector, thereby giving the person greater opportunities to earn more money. So, the higher the level of production, the greater the opportunity to benefit from the money (public goods). Therefore, hoarding is prohibited because it prevents other people from using these public goods.

Differences in the concept of money in conventional economics and Islamic economics can be explained in the following table 3.

Table 3. The Concept of Money according to Conventional Economics and Islamic Economics

| Money | Conventional Economics | Sharia Economics |
|---|---|---|
| Theory Money | 1. Money is synonymous with capital<br>2. Money (capital) is private goods<br>3. Money (capital) is a flow concept for Fisher<br>4. Money (capital) is a stock concept for Cambridge School | 1. Money is not synonymous with capital<br>2. Money is public goods<br>3. Capital is private goods<br>4. Money is a flow concept<br>5. Capital is a stock concept |
| Function Money | 1. Medium of Exchange<br>2. Store of Value<br>3. Unit of Account/Measure of Value<br>4. Standard for Deferred Payment | 1. Medium of Exchange<br>2. Unit of Account/Measure of Value |

[48]Karim, *Bank Islam,* 87.

These differences and similarities can be drawn from their respective theories about the demand for money. Departing from this difference in concept, the idea of interest emerged in conventional economics and profit sharing in Islamic economics which was then applied to the concept of banking.

3. Money in the Islamic Economic System

In the history of Islamic economic activity, the importance of the existence of money is emphasized by the opinion of Rasulullah saw. who advocated that better (fair) trade is a trade that uses the medium of money (dinars or dirhams), not the exchange of goods (barter) which can cause *riba* when there is an exchange of goods. of a different quality.

With the existence of money, the nature of the economy (in an Islamic perspective) can take place better, namely, it is maintained and the velocity of assets (velocity) among humans (economic actors) increases. With the existence of money, *zakat (alms), infaq (donation), sadaqah (alms), waqf* (property donated for religious or community use), *kharaj* (tax), *jizyah* (tax for non-Muslims), and other activities can be carried out more smoothly. With the existence of money too, private, public, and social sector activities can take place with faster acceleration.

The difference in the concept of money between conventional economics and Islamic economics has implications for the economy. In conventional economics, the system of interest and the function of money which can be equated with commodities results in the emergence of a separate market with money as the commodity and interest as the price.

This market is a monetary market that grows parallel to the real market (goods and services) in the form of a money market, capital market, bond market, and derivative market. As a result, in the conventional economy, a real and monetary sector dichotomy arises. Furthermore, rapid development in the monetary sector has sucked up money and productivity or added value generated by the real sector so the monetary sector has hampered the growth of the real sector, and has even narrowed the real sector, caused inflation and hampered economic growth.[49]

4. Prohibition of *Riba* in Islamic Finance

*Riba* according to Al-Qardhawi, has wisdom hidden behind its prohibition, namely the embodiment of fair equality between owners of assets (capital) and business, as well as taking risks and their consequences courageously and responsibly. The principle of justice in Islam is not in favor of one party, but both are in a balanced position.

The theory of the prohibition of *riba* in Islam can be explained by its economic superiority compared to conventional economic concepts. *Riba* economically is more of an effort to optimize the flow of investment by maximizing the possibility of investment through the prohibition of certainty (interest). The higher the interest rate, the greater the chance of unstoppable investment flows. This can be likened to a dam. The higher the dam wall, the greater the dammed water flow.[50]

With the prohibition of *riba*, the walls that limit the flow of investment do not exist so that the flow runs smoothly without hindrance. This was seen when Indonesia was hit by the financial and banking crisis in 1997-1998. At that time, bank interest rates soared to 60%. With such high-interest rates, it can be said that almost no one dares to borrow from a bank for investment.

Furthermore, when the interest-only covers *riba*, the focus of Islamic economic development will lead to the refinement and completeness of regulation of only Islamic economic infrastructure, which includes Islamic financial institutions (shari'ah banks, shari'ah insurance, shari'ah capital markets). uh, and so on). However, when *riba* is included in interest, the focus of Islamic economic development also leads to a macroeconomic order and monetary management based on gold (full-bodied money) in the long term.[51]

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[49] Ascarya, *Akad dan Produk Bank Syariah,* 25-26.
[50] Ascarya, *Akad dan Produk Bank Syariah,* 17.
[51] *Ibid.,* 21.

5. Development of *Riba* Free Money

*Riba* is a form of economic transaction whose prohibition is not due to its substance, but due to the transaction being carried out (*haram lighairihi*). Therefore, in essence, *riba* can be eliminated in the ways described in table 4 as follows:

Table 4. How to Eliminate *Riba*-Causing Factors

| ***Riba* Type** | **Causative Factor** | **How to Eliminate Causative Factors** |
|---|---|---|
| *Riba Fadl* | *Gharar* (uncertain to both parties) | Both parties must confirm the following factors: (1) quantity (2) quality |
| *Riba Nasi'ah* | Returns without risk, fee-free income | Both parties make a contract which details the rights and obligations of each to guarantee that no party will receive a return without bearing the risk or enjoying the income without bearing the cost |
| *Riba Jahiliyah* | Giving commercial voluntary loans because every loan that takes advantage is *riba* | Do not take any advantage of a kindness contract (*tabarru'*) Even if you want to benefit, use a business contract (*tijarah*) not a kindness contract (*tabarru'*) |

Islamic teachings prohibit the practice of *riba* (interest in money) and encourage people to invest because there is a fundamental difference between investing and lending money. According to Antonio, these differences can be studied from the definition to their respective meanings, namely:

a. Investment is a business activity that carries risks because it is faced with an element of uncertainty. Thus, the acquisition of returns is uncertain and not fixed.
b. Borrowing money is a business activity that contains less risk because the return is obtained in the form of interest which is relatively certain and fixed.[52]

This investment can be made through economic cooperation carried out in all lines of economic activity, both production, consumption, and distribution. One

[52]Antonio, *Bank Syariah,* 59.

form of cooperation in Islamic economic business is *musyarakah* or *mudharabah* (profit-sharing). Through these *musyarakah* and *mudharabah* transactions, the two partners will not receive interest but will receive profit sharing or profit and loss sharing from mutually agreed economic cooperation. This profit-loss sharing can be considered as a cooperation system that prioritizes justice in Islamic business so that it can be used as an alternative solution to the interest system.

## E. Profit and Loss Sharing as a Solution

As an alternative to the interest system in conventional economics, Islamic economics offers a profit-sharing system (profit sharing and loss sharing) when the owner of capital (surplus spending units) works with entrepreneurs (deficit spending units) to carry out business activities. If the business activity generates profit, the profits are shared and if the business activity suffers a loss, the loss is also shared. This profit-sharing system can be in the form of *mudharabah* or *musyarakah* with various variations.

In *mudharabah* there is business cooperation between two parties where one party: owner (*shahibul mal*) provides all the capital, while the other party acts as a *mudharib* (manager). Business profits on a *mudharabah* basis are divided according to the agreement outlined in the contract, whereas if the loss is borne by the owner (*shahibul mal*) of the capital as long as the loss is not due to the *mudharib's* negligence. However, if the loss is due to the *mudharib's* negligence, the *mudharib* must also be responsible for the loss.[53]

Another alternative to interest is capital participation (equity participation) through the expected rate of return which is referred to as *musyarakah*. The real sector is the most important sector highlighted in Islamic economics because it is directly related to increasing output and ultimately social welfare. All components

[53] *Ibid.,* 95.

in the economy are directed to encourage this real sector, both in motivating business people and in terms of financing.[54]

Expected returns, in contrast to interest rates, are always justified by the time value of money, but instead are linked to the economic value of money. Thus, the factor that determines the value of time is how one uses that time. The more effective and efficient, the higher the time value. With the best use of time to work and try to generate income that can be valued in money. This is contrary to the time value of money, which does not proportionally consider the probability of deflation, apart from inflation. Because in reality, uncertainty always occurs, and it would be very unfair if it only requires certainty, as is true in conventional economics through the concept of the time value of money. Therefore, investors in Islam have no right to ask for a fixed rate of return and no one has the right to get additional capital invested without participating in taking the risk.[55]

Thus, these two profit and loss sharing systems, both *mudharabah* and *musyarakah*, will be able to guarantee justice and no parties are exploited (unjust). Through this profit-sharing system, equality and togetherness will also be built and create a more equitable economic order.[56]

Whereas in the conventional economy, the *riba* system, fiat money, commodity money, and the permissibility of speculation will lead to the creation of money (currency and demand deposits) and the siphoning of money in the monetary sector to seek profit without the risk. As a result, most of the money or investment that should have been channeled into the real sector for productive purposes went to the monetary sector and hindered growth and even shrunk the real sector. Furthermore, the creation of money without added value will cause inflation. In the end, the economic growth that is the goal will be hampered.

[54]Masyhuri, et.al., *Teori Ekonomi dalam Islam* (Yogyakarta: Kreasi Wacana, 2005), 108-109.

[55]*Ibid,* 109-110.

[56]Ascarya, *Akad dan Produk Bank Syariah*, 26.

Thus, Islam encourages the practice of profit and loss sharing (profit sharing system) and forbids *riba* (interest). Even though both of them can provide benefits for the owners of capital, the two have very basic differences. The difference can be explained in table 5 below.

Table 5. Difference between Interest and Profit Sharing

| Interest | Profit Sharing |
|---|---|
| 1. Determination of interest is made at the time of the contract with the assumption that the business will always generate profits. | 1. Determination of the profit-sharing ratio (*nisbah*) is agreed upon at the time of the contract based on the possibility of profit and loss. |
| 2. The amount of percentage is based on the number of funds/capital lent. | 2. The amount of profit-sharing ratio is based on the amount of profit earned. |
| 3. Interest can be floating/variable, and the amount fluctuates according to the ups and downs of benchmark rates or economic conditions. | 3. The profit-sharing ratio remains unchanged as long as the contract is still valid unless it is changed by mutual agreement. |
| 4. Fixed interest payments as promised regardless of whether the business run by the borrower makes a profit or a loss. | 4. Profit sharing depends on the profits of the business being run. If the business loses money, the loss will be shared. |
| 5. The amount of interest payments does not increase even though profits have doubled. | 5. The number of profit-sharing increases according to the increase in profits. |
| 6. The existence of flowers is doubted (if not criticized) by all religions. | 6. No one doubts the legitimacy of profit sharing. |

Meanwhile, the profit-sharing system and the prohibition of *riba* in the Islamic economy will encourage an investment climate that will flow smoothly into the real sector for fully productive purposes. This will ensure the distribution of wealth and income and grow the real sector. With increased productivity and opportunities for work and business, in the end, economic growth will be encouraged and, in the end, people's welfare will be achieved.

The above description shows that the profit-sharing and loss-sharing model is a model of a *non-ribawi* (non-interest-based) Islamic financial system, which can be an alternative solution for the banking system. This model can have implications for the creation of fair, stable, and sustainable economic activities toward achieving social welfare.

## F. Conclusion

The title of *riba* has always been an issue that dominates the study of Islamic economics. The prohibition of *riba* as one of the main pillars of the Islamic economy aims to create a system that supports the investment climate. The implications of the prohibition of *riba* in the real sector include encouraging investment optimization, preventing the accumulation of wealth among a group of people, preventing inflation and decreasing productivity, and encouraging fair economic activity.

The presence of Islamic economics in society is to create economic justice and income distribution toward achieving social welfare. Islamic economics places justice for all business people and does not recognize the terms "creditor" and "debtor," but work partners who share the same risks with a full sense of responsibility. For this reason, the profit and loss sharing system can be used as an alternative solution to the interest system in a rational Islamic economic system.

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