The Practice of Islamic Contracts in Islamic Bank X

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Abstract. The aim of the research is to explore the practice of Islamic contracts at Islamic Bank X, particularly from a financial standpoint, as a preliminary to doing applied education research. The exploratory descriptive approach is used in this study, with data collected through interviews with employees of Islamic Bank X. The Bank utilizes Islamic contracts in its savings and financing products, including *Mudharabah* and *Wadiah* contracts for savings, and *Murabahah* and *Musyarakah* sale and buy contracts for financing. *Murabaha* contracts are the most frequently used in finance, although *Salam* contracts are not used. When making computations, Bank X follows specific procedures and adheres to Islamic principles.

Keywords: Islamic contracts · Islamic bank · Murabahah · Musyarakah

1 Introduction

The founding of Bank Muamalat Indonesia (BMI) in 1991 marked the beginning of the modern era of Islamic banking in Indonesia, which began in the country. The development of Islamic banking in Indonesia shows continuous growth but has not yet reached the expected market share target. There are 14 Sharia Commercial Banks operating until 2020. In 2021 there was an important milestone in the development of Sharia with the merging of three state-owned Sharia banks, namely Mandiri Syariah, BRI Syariah and BRI Syariah to become Bank Syariah Indonesia (BSI) with the aim of encouraging the growth of Islamic banking which operates based on sharia principles using various forms of contracts.

Profit sharing and buying and selling contracts are two types of contracts used in Islamic banks. *Mudharabah and Musyarakah* are the most frequently used contracts in profit sharing transactions. *Mudharabah* contracts are business collaboration agreements between a *shahibul maal* (fund owner) and a *mudharib* (fund manager), with a profit-sharing ratio agreed upon in advance [1]. In the event of a loss for a company, the fund owner is responsible for covering all costs unless the loss was caused by the fund manager's carelessness, error, or cheating. *Musyarakah* contract is a collaboration agreement between capital owners who all contribute capital to a specific business with

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the intention of profiting. *Musharakah* may be used to finance existing or new businesses. The return on capital is made in stages or all at once to the capital owners [1].

Sale and purchase contracts include *Murabahah*, *Istisna* and Salam contracts, where each contract has its own characteristics [1]. *Murabahah* contract is a contract for the sale and purchase of items that specifies the price of profit (margin) that has been agreed upon by the seller and buyer, whether the contract is based on an order or not [1]. Payments for *Murabahah* can be made in cash or in installments. The seller is entitled to a discount if the customer makes a faster payment (installment or settlement).

Istishna is a contract of sale and purchase between *Al-mustashni* (buyer) and *As-shani* (seller) (producer who also acts as seller). The buyer assigns the producer the responsibility of supplying *Al-mashnu* (ordered goods) in accordance with the buyer's specifications and selling them at the agreed price. Payment can be made in advance, in installments, or deferred for a specified period of time. The *Istishna* contract is irrevocable unless both parties agree to terminate it; and the contract is null and void if any legal conditions exist that would prevent the contract from being implemented or completed. *Istishna* payments must be agreed upon in the contract to be made in full or in part after the contract but before the goods are manufactured, or at the time of delivery/during the process of manufacturing the goods, or the payment must be deferred until after the goods are delivered. Payment options may also include a combination of the payment methods listed above. *Salam* is a *Muslam fiih* sale and purchase contract (ordered goods) in which the Muslam alaihi (seller) postpones delivery and the payment is made immediately prior to the ordered goods being received, subject to certain conditions [1]. In a *Salam* transaction, the bank acts as a buyer or seller; however, if the bank acts as a vendor and then instructs another party to deliver the ordered goods as a *Salam*, this is referred to as a parallel *Salam*.

In terms of contract implementation in Islamic banks, several studies have revealed that the *Murabahah* contract has become the most frequently used in Islamic banking due to its simplicity [2]. To mitigate the risk of *Mudharabah* and *Musyarakah* contracts, the Islamic bank has implemented proactive and reactive risk management strategies [3]. Moreover, according to a study carried out at the Bank Syariah Mandiri Malang Branch, the sharing mechanism is more beneficial to both parties and involves less risk than the system employed by traditional banks to compute interest [4]. With a particular emphasis on *Mudharabah* in Islamic banks, a standard formula was developed using mathematical and arithmetic equations to refine and improve the calculation method [5]. Another research focuses on the practice of *Murabahah* and the method used to determine the selling price for consumptive financing at Bank Syariah Mandiri. This research describes the practice of consumptive financing through the use of a *Murabahah wal wakalah* contract and the method used to determine the selling price for this consumptive financing through the annuity method [6]. Additionally, the *Mudharabah* savings equivalent rate method used at PT. Bank Mega Syariah Pekanbaru Branch has been consistent with the MUI Fatwa on *Mudharabah* savings, as illustrated by the author's case example, where both the bank and the customer benefit from the income obtained using the ratio agreed upon in the initial agreement [7]. In relation to the *Mudharabah* savings equivalent rate method used at the PT. Bank Mega Syariah Pekanbaru branch, it is determined that it is consistent with the MUI Fatwa on *Mudharabah* savings, as banks and customers both benefit from income generation at the ratio agreed upon in the initial agreement [8]. The BTN Syariah has complied with the DSN MUI Fatwa by implementing *Istisna's* contract [9].

These studies concentrate on a single contract at a single Islamic bank. As a result, it is necessary to conduct research to determine the status of all contracts in order to obtain a complete picture of a particular bank. The purpose of this study is to examine how profit-sharing contracts and buying and selling contracts are implemented and calculated at Islamic Bank X.

2 Methodology

This research uses descriptive research which seeks to describe the object of research based on facts and data and events; then it connects events or research objects as well as analyze them based on concepts that have been developed previously. Interviews with employees of Bank Syariah X were conducted to ascertain current practices in Islamic banking. On June 9, 2021, interviews with the Head of the Financing Section and a member of staff were conducted. The interviews were conducted to elicit detailed information about Islamic Bank X's contract implementation practices, particularly in the area of profit sharing and buying and selling contracts.

This research employs analytical techniques in the form of field data collection and processing, as well as the results of interviews and documentation, which include some activities associated with qualitative data analysis [10]. First, data reduction entails summarizing, selecting the essentials, concentrating on the critical, and searching for themes and patterns. Thus, the reduced data will provide a clearer picture and make it easier for researchers to collect additional data and locate it as needed. Researchers will be guided in their data reduction efforts by the objectives to be accomplished. Second, data were presented in the form of concise descriptions, in the form of descriptive and narrative text. The data presented explains how Mudharabah and Murabahah financing are calculated. The third and final step is to reach conclusions.

3 Analysis and Discussion

In general, Islamic Bank X provides two types of services: distribution of Sharia-compliant financing and fund depository. Corporate and retail/individual customers are financed through house purchase contracts or Home Ownership Credit (KPR) for both new and existing homes. The Islamic Bank X uses the following contracts:

- *Wakalah* and *murabahah* contracts for mortgage refinancing for customers who already own a home.
- *Musyaraqah Mutanaqisah* contract, which is applicable to KPR Savings-Based Housing Financing Assistance (BP2BT) with a down payment of up to Rp 40 million; payments are made in tiers, with the first three years paying the least. This contract has been in effect at this Syariah-compliant bank since 2018.
- The *Istisna'* contract is used by customers who purchase a mortgage-backed home on an indented basis.

- *Murabahah* contract for subsidized mortgages for the Housing Development Liquidity Facility (FLPP) program, which provides housing subsidies to low-income individuals earning less than Rp 8 million and up to Rp 150 million.

The vast majority of products (70%) are subsidized mortgage products (FLPP *Murabahah*), as this bank is a state-owned institution that specializes in public housing finance.

Along with financing products, this bank offers a variety of savings products under the following contracts:

- The *Mudharabah* contract is applied to Prima iB as a mandatory savings requirement for house financing customers and Time Deposit products.
- The *Wadiah* contract is applied to the Batara iB Savings contract. This bank does not offer profit sharing, only bonuses.
- Gold Savings, Hajj Savings, Junior Savings, and *Qurban* Savings are additional savings products.

In terms of financing, this has implemented an effective margin since 2010, which is calculated as a percentage of the remaining loan balance. Between 2005 and 2010, this bank maintained a flat margin. The following programs have an effective margin: FLPP Subsidized Mortgage with an effective margin of 5.77% for five-year financing, 5.25% for ten-year financing, and 5.01% for twenty-year financing.

Guaranteed financing is also available with the caveat that the amount of financing provided does not exceed 95% of the collateral value for new homes. Specifically for used house financing, financing is provided at 80% of the value of the collateral, namely the house, based on the results of an independent asset valuation (appraisal). Naturally, this still takes into account the customer's ability to pay in installments.

This bank utilizes only two types of contracts for sale and purchase transactions, namely *Murabahah* and *Istisna'*; the Salam contract is not utilized by this bank. *Murabahah* contracts are used to finance mortgage home purchases by providing the developer company with a total of 100% financing funds after deducting certain costs. The *Istisna'* contract is used for mortgages only with certain developer companies that work with this bank and meet the following criteria: the developer company has a good track record, the land area in each housing unit is at least 90 m^2, the number of houses is greater than 50, and the financing period is greater than two years. *Istisna* products are disbursed in stages of 30%, 40%, and so on.

Mudharabah and *Musyarakah* profit sharing contracts are used in this Bank. In particular, *Mudharabah* contracts are used by certain companies to finance working capital and investment in building construction. While *Musyarakah* contracts are used by housing development companies and carry an effective margin of 13% depending on the duration of the financing. Funds are disbursed to the developer company in stages, in accordance with the progress of house construction.

The bank recognizes that the banking industry is highly competitive, not only with other Islamic banks, but also with conventional banks. This occurs as a result of consumers failing to consider Sharia compliance when purchasing products. According to informants, the most formidable competitors are Bank Central Asia (BCA) and Bank Syariah Indonesia (BSI), both of which can offer lower margins.

3.1 Murabahah Contract

The following procedure is used to calculate the *Murabahah* sale and purchase contract at Sharia Bank X:

- Enter some basic information, such as the purchase price of the goods, the percentage of the down payment, the duration of the financing, and the profit margin.
- Calculate the bank's profit margin by estimating the bank's total financing for all customers, estimating the bank's annual operating costs, and estimating the financing period (in years)
- Calculating a bank's profit margin is a multi-stage process that includes cost recovery, profit margin in rupiah, determining the bank's selling price, calculating financing installments, and calculating the percentage margin.
- After calculating the annual margin, the monthly installments are calculated by inputting the loan term (in months), the maximum loan amount, and the down payment. Monthly installments are then calculated.
- In addition to monthly installments, customers must pay other bank-mandated fees.

The simulation of calculation based on the bank policy with tiered *ujroh* can be presented as follows:

a) House price: IDR 140 million
b) Family income: IDR 4 million
c) Minimal Down Payment from customer' saving: 1% $\times$ (A) = IDR 1,4 million
Smaller Down Payment support between D or E
d) funds based on group income: IDR 40
e) fund based on house price index: 45% $\times$ (A) = IDE 63 million
Maximum financing: (A-C-D) = IDR 98,6 million Installment for 240 months:
Installment Year I–III : IDR 95.511
Installment Year IV–XX : IDR 1.101.356

3.2 Istisna Contract

The calculation procedure in an *Istisna* contract is as follows:

- Enter basic data, such as the name of the goods, their specifications, the unit price of the goods, the quantity ordered, and the time period.
- Calculating customer financing requirements and bank fees
- Calculate the anticipated profit margin.
- Calculating monthly installments and calculating the initial payment.

3.3 Mudharabah Contract

The calculation procedure for *Mudharabah* contracts is as follows:

- Determine the profit sharing ratio (nisbah) between the customer and the bank in accordance with the contract's terms.
- Entering the average monthly balance for customer A.
- Calculate the monthly balances of all customers.
- Calculate the bank's monthly revenue.
- Using a percentage ratio to determine profit sharing between banks and customers.
- Calculate profit sharing for customer A and add it to the savings account for customer A at the start of the following month.

4 Conclusion

In its saving and financing products, the bank makes use of a number of Islamic contracts, including the *Mudharabah* and *Wadiah* contracts for saving products and the sale and purchase (*Murabahah*) and *Musyarakah* contracts for financing products. Despite the fact that the *Salam* contract is not utilized very often, it is the most commonly used contract in financing. While computing, this bank adopts precise procedures and adheres to Islamic principles. Therefore, it can be conclude that this bank has performed well in providing good services for all customers. Further research is recommended to go deeper into the operational aspects of Islamic banks and how Islamic contracts are implemented, as well as the obstacles associated with contract implementation.

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