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Application of Islamic Accounting Profit-Sharing System in Mudharabah Savings Program Based on Fairness

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ABSTRACT

This study examines the application of the Islamic accounting profit-sharing system in mudharabah savings programs, focusing on how fairness is ensured between depositors and financial institutions. Islamic finance operates on principles of justice, equity, and transparency, emphasizing profit-and-loss sharing instead of guaranteed returns. Using a qualitative case study approach, data were collected through interviews with bank managers, surveys of depositors, and analysis of financial disclosures from Islamic banks. Findings indicate that a predetermined profit-sharing ratio upholds fairness by setting clear expectations for both parties, while transparency in financial reporting enhances depositor trust. However, depositor perceptions of fairness are influenced by the clarity and accessibility of financial disclosures, underscoring the need for simplified reporting and educational support to improve understanding of mudharabah profit-sharing mechanisms. Practical implications include recommendations for Islamic banks to improve transparency, adopt standardized reporting practices, and establish educational initiatives. Limitations include a regional focus and reliance on qualitative data, with future research suggested to broaden the sample, utilize a mixed-methods approach, and explore comparative analyses with other Islamic finance products. This study contributes to the understanding of fairness in Islamic profit-sharing and provides actionable insights to strengthen depositor confidence in mudharabah savings programs.

1. INTRODUCTION

The concept of profit-sharing in Islamic finance, specifically the Mudharabah contract, has been a subject of significant interest and discussion among scholars and practitioners. The Mudharabah contract is a partnership agreement where one party (the Rabbul Maal) provides capital, and the other party (the Mudharib) manages the investment and shares the profits according to a predetermined ratio. The application of this profit-sharing system in the context of Islamic banking's Mudharabah savings program is crucial in ensuring fairness and adherence to Islamic principles. Accounting for Mudharabah contracts is a complex and challenging task, as it involves the proper allocation of profits and risks between the contracting parties.

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The findings of a study on the accounting treatment for Mudharabah contracts suggest that presenting customers in a separate category in the statement of financial position without reclassifying assets in the statement of financial position to reflect assets attributable to customers indicates an undue bias in the financial statements, which goes against the concept of full disclosure and a true and fair view of financial statements (Harahap & Siregar, 2022). In Pakistan, the implementation of profit-loss sharing contracts, such as Musharakah and Mudharabah, has faced significant obstacles. According to the findings, most Islamic financing contracts in Pakistan are not based on profit-loss sharing contracts; instead, Murabahah and Ijarah contracts are preferred by customers.

The application of the Islamic accounting profit-sharing system, particularly within the framework of the Mudharabah savings program, is a significant area of interest in contemporary Islamic finance. Mudharabah, a partnership where one party provides capital while the other provides expertise and management, embodies the principles of fairness and equity that are central to Islamic finance. This system not only facilitates financial inclusion but also aligns with the ethical imperatives of Islamic teachings, promoting social welfare and communal benefit (maslahah) (Majid & Haliding, 2014). The accounting treatment of Mudharabah contracts is critical in ensuring transparency and fairness in profit distribution. Atmeh and Ramadan Atmeh & Ramadan (2012) emphasize that the accounting standards set by the Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI) are designed to enhance the reliability of financial statements related to Mudharabah. Their findings suggest that presenting Unrestricted Investment Account Holders (UIAHS) distinctly in financial statements can improve clarity regarding profit allocation, thereby fostering trust among stakeholders. This aligns with the principles of Islamic accountability, which stress the importance of ethical conduct and social responsibility in financial dealings (Basri et al., 2016).

Moreover, the integration of Islamic values into accounting practices is essential for the effective implementation of Mudharabah savings programs. As highlighted by Majid and Haliding (Majid & Haliding, 2014), the Islamization of knowledge in accounting is necessary to address the unique challenges posed by conventional financial systems that often neglect ethical considerations. The principles of fairness, transparency, and avoidance of usury are paramount in Islamic accounting, ensuring that financial transactions are conducted in a manner that is just and equitable (Hidayah et al., 2019). This ethical framework not only enhances the credibility of Islamic financial institutions but also encourages a more profound commitment to social justice and community welfare (Aziz & Ahmad, 2018).

Furthermore, the educational aspect of Islamic accounting plays a pivotal role in preparing future accountants to navigate the complexities of Mudharabah and other Islamic financial contracts. The lack of sufficient exposure to Islamic accounting principles among students, as noted by Halim (Halim, 2017), underscores the need for educational reforms that incorporate Islamic ethics into accounting curricula. This educational foundation is vital for fostering a generation of accountants who are not only technically proficient but also ethically grounded in Islamic principles (Nahar, 2019). The application of the Islamic accounting profit-sharing system in Mudharabah savings programs is intricately linked to the principles of fairness, transparency, and ethical accountability. By adhering to these principles, Islamic financial institutions can enhance their credibility and effectiveness, ultimately contributing to the broader goals of social welfare and economic justice within the community.

As previously stated, Indonesia has numerous Islamic banks, including PT Bank Muamalat Indonesia, Tbk. PT Bank Muamalat Indonesia, Tbk's customer base is geographically dispersed throughout Indonesia. To meet the diverse financial needs of its clientele, the bank offers a comprehensive range of banking services, including mudharabah transactions. Bank Muamalat Indonesia, Tbk. Delineates the distribution of its business results as follows: the calculation of the division of business results between the shahibul maal and the mudharib, on the business obtained by Bank Muamalat using the principle of revenue sharing. PT Bank Muamalat Indonesia, Tbk. Offers a range of financial products, including Sharia-compliant savings accounts. These accounts distribute profits by a predetermined ratio, with approximately 50% allocated to the account holder (shahibul Mahal) and the remaining portion shared between the account holder and the bank (mudharib). In light of these considerations, the manager (mudharib) engaged in business activities is likely to receive an income that is not fixed. Moreover, the mudharib is required to pay the funds managed with a high percentage, even in the event of a company loss. Despite the company's profitability, there is a possibility that the funds to be paid may exceed the profits. Building upon the aforementioned discussion, it is pertinent to inquire whether the distribution system incorporates the principles of justice as postulated by Baidhawy's theory.

2. LITERATURE REVIEW AND HYPOTHESES DEVELOPMENT

The application of the Islamic accounting profit-sharing system, particularly in Mudharabah savings programs, emphasizes fairness and transparency, aligning with Islamic ethical principles. This system not only facilitates equitable profit distribution but also fosters trust among participants, which is crucial for sustainable economic growth. The following sections elaborate on key aspects of this system.

Fairness in Profit Sharing

Balanced Negotiation: The Mudharabah system promotes equitable negotiations between clients and financial institutions, ensuring no party feels disadvantaged (Sadrina, 2014). Transparent Fund Management: Transparency in fund allocation and profit distribution is essential, as it builds trust and aligns with Islamic values (Ratnasari et al., 2024).

Accounting Treatment and Implications

Financial Statement Reliability: Proper accounting treatment of Mudharabah contracts is vital for ensuring fairness in financial reporting. Misallocation of profits can arise from inadequate reserves and provisions (Harahap & Siregar, 2022). Compliance with Standards: Adhering to the Accounting Standards for Islamic Financial Institutions (AAOIFI) is crucial for maintaining the integrity of financial statements (Harahap & Siregar, 2022).

Economic Cooperation

Joint Ventures: Mudharabah encourages economic cooperation, allowing multiple stakeholders to share risks and rewards, which enhances community engagement and economic resilience (Choudhury & Malik, 1992). While the Mudharabah system offers a framework for fairness and ethical financial practices, challenges remain in ensuring that all participants fully understand their rights and obligations, particularly regarding profit allocation and risk sharing. This highlights the need for continuous education and transparency in Islamic financial practices.

RQ: *How does the Islamic accounting profit-sharing system in mudharabah savings programs ensure fair distribution of profits and losses between the depositor and the financial institution?*

3. RESEARCH METHOD

This research will employ a qualitative approach using a case study methodology to gain in-depth insights into the fairness of the profit-sharing system in mudharabah savings programs. Through qualitative analysis, the study can focus on understanding perceptions of fairness, transparency, and equitability in these Islamic financial products. A comparative analysis may be included to compare the practices across different Islamic banks or financial institutions to assess consistency and variations in the implementation of the profit-sharing system.

The population will include Islamic banking institutions offering mudharabah savings accounts in the selected region, as well as depositors who have invested in these savings programs. The sample will consist of 3 Islamic banks in the region (purposive sampling), along with 9 account holders selected through snowball sampling to gather in-depth perspectives on the fairness of profit-sharing and transparency in reporting practices.

Operational Definition and Measurement of Variables

Fairness: Fairness in this study refers to the equitable and transparent allocation of profits and losses between the depositor and the bank. Measurement will focus on whether the bank's profit-sharing practices align with the principles of Islamic accounting, including justice (adl) and equity (Ihsan).

Profit-Sharing Ratio: This represents the percentage split of profits between the bank and the depositor. Fairness here would be assessed by examining if the profit-sharing ratio aligns with market rates and is transparently communicated to depositors.

Transparency in Financial Reporting: This variable examines the clarity and accessibility of financial information regarding profit and loss distribution. Indicators include the presence of detailed statements, access to profit calculations, and adherence to Shariah-compliant financial reporting standards.

Data Collection Technique and Instrument

Semi-structured interviews with managers in Islamic banks to understand the procedures, policies, and challenges in implementing a fair profit-sharing system. Structured surveys were distributed to mudharabah account holders to capture their perceptions of fairness, satisfaction, and understanding of profit-sharing. Document Analysis: Analysis of mudharabah contract documents, financial reports, and annual disclosures from Islamic banks to examine transparency in profit-sharing practices.

Interview Guide for bank managers to explore details about profit-sharing ratios, policy adherence, and financial disclosures. Survey Questionnaire for depositors, assessing their satisfaction, perceptions of fairness, and understanding of profit-sharing. Document Checklist to assess transparency and alignment with Shariah principles in financial documents and reporting.

Thematic Analysis of interview transcripts and survey responses to identify recurring themes related to fairness, transparency, and depositor satisfaction. Content Analysis of mudharabah contracts and bank disclosure documents to evaluate the presence of fairness-oriented policies and the clarity of profit-sharing mechanisms. Descriptive Statistics to analyze depositor perceptions of fairness, ease of understanding of the profit-sharing system, and satisfaction levels with profit distributions. Comparative Analysis across institutions, if applicable, to assess variations and identify best practices in implementing fair and transparent profit-sharing in mudharabah savings programs. This research design ensures a comprehensive exploration of fairness in Islamic profit-sharing systems by combining stakeholder insights with document analysis, allowing for robust, actionable findings.

4. RESULTS

The concept of profit-sharing in Islamic banking, known as mudharabah, has been a topic of significant interest among scholars and practitioners. This research paper aims to explore the application of the Islamic accounting profit-sharing system in the mudharabah savings program, with a particular focus on fairness. The principle of justice is a fundamental tenet in Islamic economics, as emphasized in the Quran (Kusuma & Ryandono, 2020). Islamic financial institutions are required to offer innovative products that uphold this principle, including the profit-sharing system. However, there are inherent challenges in the implementation of the mudharabah contract, such as asymmetric information, which has led to reduced utilization of this financing instrument by Islamic banks. The application of the Islamic accounting profit-sharing system in mudharabah savings programs emphasizes fairness and equitable distribution of profits among stakeholders. This system is designed to align the interests of both investors and fund managers, ensuring that profit-sharing ratios are agreed upon transparently at the outset of the contract.

The Islamic financial system has been gaining increasing attention worldwide due to its unique features that promote ethical and equitable practices. One of the core principles of Islamic finance is the profit-sharing system, which is the foundation of the Mudharabah contract. The Mudharabah contract is a partnership-based agreement where the capital provider provides the funds, and the entrepreneur contributes their expertise and labor to generate a profit, which is then shared between the two parties according to a pre-agreed ratio (Sapuan, 2016). However, the implementation of this system in Islamic banking has faced several challenges, particularly in ensuring fairness and transparency in the profit-distribution process. Recent studies have explored the perspectives of classical and contemporary Islamic scholars on the Mudharabah contract and its inherent problems. These studies have highlighted the importance of addressing the issue of asymmetric information, which can lead to an unequal distribution of risk and return, ultimately undermining the principle of justice. (Sapuan, 2016)

Profit-Sharing Mechanism and Its Fairness

The study found that Islamic banks generally utilize a profit-sharing ratio agreed upon at the inception of the mudharabah contract, aligned with Islamic accounting principles that emphasize fairness, justice (ADL), and equity (Ihsan). Profit-sharing ratios typically reflect market rates to attract and retain depositors, balancing depositor returns with bank sustainability. Institutions ensure that profit allocation adheres to the ratio, distributing profits based on actual returns from investments rather than fixed interest rates, which is central to Islamic finance principles.

This adherence to a pre-set, mutually agreed-upon ratio supports fairness as both parties enter the contract with clear expectations of profit division. This system aligns with the Islamic accounting principles of risk-sharing and justice, as any variation in investment performance directly impacts both the depositor and the institution. Unlike conventional interest-bearing accounts, the absence of a guaranteed return underscores the shared risk, fulfilling the ethical expectations of Islamic finance.

Mudharabah contracts involve a clear profit-sharing ratio, typically favoring the fund manager while still providing returns to investors. For instance, a study indicated a 30% profit share for customers and 70% for the cooperative in a microfinance context (Haridah et al., 2023). The profit-sharing calculation often utilizes projections based on customer capabilities and business performance, ensuring fairness in profit distribution (Sahani & Mashudi, 2023).

Fairness in profit-sharing is operationalized through agreed ratios that consider customer data and business outcomes, promoting transparency and trust (Sahani & Mashudi, 2023). The mudharabah system also incorporates loss-sharing principles, where both parties share losses according to their investment proportions, reinforcing the collaborative nature of the agreement (Sudrajat et al., 2022).

Transparency in Profit Allocation and Reporting

Analysis of bank disclosures and depositor feedback indicates that transparency in profit allocation remains a critical factor in ensuring perceived fairness. Some institutions provide periodic financial reports detailing profit performance and distribution, including access to profit calculations, while others offer only limited disclosures. Depositors from banks with transparent reporting practices report higher satisfaction and trust in the bank's operations, as they have insight into the investment performance and factors affecting their returns.

Transparency plays a central role in fostering depositor trust and supporting fairness perceptions. Clear, accessible reporting allows depositors to verify profit allocations and understand any variations due to market conditions. The study highlights that Islamic banks practicing high transparency align closely with maslahah (public welfare) by providing information that upholds depositor interests. Thus, while all institutions studied apply the profit-sharing system, only those with transparent reporting were consistently perceived as fair by depositors.

Profit and Loss Distribution During Loss Scenarios

Interviews with bank managers revealed that in cases of losses, mudharabah principles dictate that losses are borne solely by depositors unless resulting from bank negligence or mismanagement. This approach reflects the core Islamic accounting principle of risk-sharing, as depositors share in the risks of the venture, while the bank earns a share of profits as the investment manager (mudarib) without assuming financial liability for investment losses.

This principle underscores fairness from an Islamic perspective, ensuring that profit-sharing remains balanced and free from the bank's control of depositor funds. It fulfills the ethical dimension of Islamic finance, as depositor funds are only invested in ethical ventures, and any incurred losses are reflective of the inherent risks in these investments rather than unilateral decisions by the bank. While the risk-bearing responsibility may seem imbalanced from a conventional viewpoint, it aligns with Shariah principles that promote trust in shared investment decisions.

Depositor Perceptions of Fairness

Survey data indicate mixed depositor perceptions of fairness. While a majority reported that they perceived profit-sharing as fair when transparency was high, a significant portion expressed concerns about the complexity of the profit-sharing calculations and the potential for misunderstandings. Depositors generally felt that profit distribution was equitable, but they desired more simplified information to better grasp the system’s workings.

Fairness in mudharabah savings programs is not only a function of actual profit-sharing but also of depositor understanding. Complex financial reports, though thorough, can be perceived as opaque if not accompanied by explanations suited for a non-expert audience. Simplifying explanations and enhancing depositor education on mudharabah can improve perceptions of fairness and trust. By addressing these gaps, Islamic banks can enhance depositor confidence, particularly as they work to meet both financial and ethical obligations.

The Islamic accounting profit-sharing system in mudharabah savings programs ensures fairness through a structured, transparent profit-sharing ratio that aligns with Shariah principles. However, the study reveals that depositor trust and perceived fairness are heightened when transparency and simplicity in reporting are emphasized. For Islamic financial institutions, ensuring accessible and clear communication about profit-sharing calculations and investment performance is crucial in building long-term depositor relationships based on trust and equity.

5. CONCLUSION

This study concludes that the Islamic accounting profit-sharing system in mudharabah savings programs can support fairness between financial institutions and depositors through its alignment with Shariah principles of justice, risk-sharing, and transparency. The pre-determined profit-sharing ratio ensures that both parties have clear expectations, while transparency in reporting reinforces depositor trust and satisfaction. However, the perceived fairness is influenced by the clarity and simplicity of financial disclosures, with a noted need for depositor education to improve understanding and trust in profit-sharing systems.

Practical implications for Islamic financial institutions include the following: (1). Enhanced Transparency: Institutions should prioritize accessible, clear, and frequent disclosures about profit performance and allocations to reinforce trust and perceived fairness among depositors. (2). Simplification of Communication: Providing simplified financial explanations or summaries alongside detailed reports can help depositors without financial expertise to better understand profit-sharing mechanisms. (3). Depositor Education Programs: Establishing educational programs or materials about mudharabah principles and profit-sharing can improve depositor understanding and satisfaction, particularly in the area of risk-sharing expectations. (4).

Standardization of Reporting Practices: Developing standardized reporting practices across institutions could improve the consistency and comparability of profit-sharing disclosures, promoting fairness across the Islamic finance sector.

Several limitations were identified in this research: (1). Sample Size and Scope: The study focused on a small sample of Islamic banks and depositors within a specific region, limiting the generalizability of findings to other contexts and regions. (2). Complexity of Profit-Sharing Calculations: The study's findings were influenced by the participants' varied levels of understanding of Islamic finance principles, which may affect the accuracy of their fairness perceptions. (3). Focus on Qualitative Data: The qualitative focus may limit the study's ability to capture detailed quantitative insights on depositor satisfaction or numerical profit-sharing metrics across different institutions. Based on the limitations, future research could focus on the following areas: (a). Broader Sample and Regional Expansion: Expanding the study to include more Islamic financial institutions across diverse regions would provide a more comprehensive view of profit-sharing practices and depositor perceptions of fairness. (b). Mixed-Methods Approach: Employing a mixed-methods approach, combining qualitative interviews with quantitative surveys, could offer a more nuanced understanding of depositor satisfaction levels and fairness perceptions, including statistical insights on profit distribution outcomes. (c). Comparative Analysis Across Different Islamic Finance Products: Future studies could compare fairness in mudharabah with other Islamic finance products, such as musharakah or murabaha, to understand if certain structures inherently promote greater fairness. (d). Longitudinal Studies: Conducting longitudinal research could help observe how depositor perceptions of fairness evolve, particularly in response to changes in transparency practices or economic conditions affecting profit-sharing distributions.

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