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Analysis of interest theory and profit-sharing in the Islamic financial system

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Abstract

This article examines the comparison between interest theory in conventional financial systems and profit-sharing theory in Islamic financial systems by integrating religious and economic perspectives. The purpose of this study is to gain a more comprehensive understanding of the practical and ethical implications of both financial systems and how they can be applied to support fair and sustainable economic development. The methodology used is a literature review with in-depth content analysis related to the concepts of interest and profit-sharing from various religious perspectives, including Islam, Christianity, and Judaism. The results show that interest theory dominates conventional financial systems with its various applications, while profit-sharing theory in Islamic financial systems offers a fairer and more efficient alternative with profit and loss distribution based on the actual contributions of each party. This study provides significant insights into understanding the fundamental differences between interest and profit-sharing and offers recommendations for creating a more inclusive and sustainable financial system. However, this research has limitations in terms of empirical analysis and variations in the implementation of the profit-sharing system that need to be further explored in future studies.

Keywords: interest theory; profit-sharing; conventional finance; Islamic finance; religious perspective.

Introduction

Riba has long been recognized as an economic disease in human civilization. Several economic experts estimate that riba has existed since the advent of money (gold and silver) (Bradley, 2023; Olechnowicz, 2011; Shahar, Mohamad Zan, & Wan Hassin, 2016). Riba was known during the civilizations of the Pharaohs in Egypt, the Sumerians, Babylonians, and Assyrians in Iraq, as well as the Hebrew Jewish civilization. In the Old Testament, it is stated that Jews are forbidden to take riba from fellow Jews, but they are allowed to take riba from non-Jews (Al-‘Umrānī, 2010).

Riba, known in the conventional world as interest, is not only a problem within Islamic society but is also seriously addressed by various circles outside of Islam. Therefore, research on the issue of riba has existed for over 2000 years. The issue of riba has been a topic of debate among Jews, Greeks, and Romans. Christians also have their views on riba (Harahap & Risfandy, 2022; Olechnowicz, 2011).

Although the accuracy of estimates about the history of riba cannot be confirmed, except for its existence in Jewish civilization, the Quran explains that the Israelites (the people of Prophet Moses) practiced riba and that Allah forbade them from consuming riba. Subsequently, the Jews introduced riba to the Arabs in the Arabian Peninsula, particularly in the cities of Taif and Yathrib (Madinah). In these two cities, Jews managed to reap significant profits, causing many ignorant Arabs to pawn their children, wives, and themselves as collateral for riba debts. If they were unable to repay the debt, they became slaves of the Jews (Tarmizi, 2016).

The Quran and Hadith clearly state that riba is haram. Interest and riba essentially share the same nature, making them both haram. However, some economic theories justify riba, as if riba is necessary to create justice (Haymon, 1958). These theories were proposed by Western economists because, in the early Middle Ages, the Catholic Church prohibited the practice of usury in European society (Noor, 2024).

Research on interest must consider the non-Muslim perspective for several reasons. First, Muslims, like Jews and Christians, believe in and respect the prophets Abraham, Isaac, Moses, and Jesus. Islam also recognizes Jews and Christians as People of the Book, who were given the Torah and the Gospel. Second, Jewish-Christian thought should be considered because many writings on interest were produced by their religious leaders. Third, Greeks and Romans contributed to human civilization, so their opinions must also be considered. Their views influenced many Jews, Christians, and Muslims in the debate over interest (Haroen, 2000).

Discussing interest applied in conventional banks, which base most of their operations on interest, Islam recognizes a profit-sharing system that is significantly different from the interest system. The profit-sharing system is an essential alternative consumer financing scheme as a manifestation of justice (Yahya & Agunggunanto, 2012). The nature and characteristics of profit-sharing applied in Islamic banks to avoid riba practices have their appeal. These differing views and practices present challenges and opportunities in integrating ethical principles into the global financial system.

This study focuses on a comparative analysis of interest and profit-sharing theories, integrating religious and economic perspectives. This approach aims to achieve a more comprehensive understanding of the practical and ethical implications of these two systems and how they can be applied to support equitable and sustainable economic development.

The objective of this research is to conduct a comparative analysis of interest and profit-sharing theories, integrating religious and economic perspectives. The novelty of this research lies in its holistic approach, combining theoretical and practical analyses of two different financial systems: interest in the conventional system and profit-sharing in the Islamic system. The study's scope includes a literature analysis of religious views on interest and profit-sharing, as well as case studies of the application of these two systems in banking practices. With this approach, this research aims to provide deeper insights into the ethical and practical implications of these financial systems and offer recommendations to support more equitable and sustainable economic development.

Literature review

Interest theory

Usury (riba) has been recognized as an economic malady in society since ancient human civilizations. Some economists estimate that usury has existed since humans first used money (gold and silver) (Bradley, 2023; Olechnowicz, 2011; Shahar Mohamad Zan & Wan Hassin, 2016). Usury was known during the civilizations of the Pharaohs in Egypt, the Sumerians, Babylonians, and Assyrians in Iraq, and the Hebrew Jews. In the Old Testament, it is stated that Jews were forbidden to take usury from fellow Jews but were allowed to take usury from non-Jews (Al-‘Umrānī, 2010).

In the conventional world, known as interest, usury is not only an issue within Islamic communities but also taken seriously by various non-Islamic circles. Therefore, research on usury has been ongoing for over 2000 years. It has been a topic of debate among

Jews, Greeks, and Romans. Christians also have their perspectives on usury (Harahap & Risfandy, 2022; Olechnowicz, 2011).

Although the historical accuracy of usury, except in Jewish civilization, cannot be confirmed, the Quran explains that the Israelites (followers of Moses) engaged in usury, and Allah prohibited them from consuming it. Later, Jews introduced usury to the Arabs in the Arabian Peninsula, especially in the cities of Taif and Yathrib (Medina). In these cities, Jews gained substantial profits, causing many pre-Islamic Arabs to pawn their children, wives, and themselves as collateral for usurious loans. If they could not repay the debt, they became Jewish slaves (Tarmizi, 2016).

The Quran and Hadith clearly state that usury is forbidden. Interest and usury, in essence, are similar, hence both are prohibited. However, some economic theories justify usury as if it is a necessity for creating fairness (Haymon, 1958). These theories were proposed by Western economists because, in the early Middle Ages, the Catholic Church prohibited the practice of usury in European societies (Noor, 2024).

Research on interest must consider the non-Muslim perspective for several reasons. First, Muslims, like Jews and Christians, revere and respect prophets such as Abraham, Isaac, Moses, and Jesus. Islam recognizes Jews and Christians as People of the Book who were given the Torah and the Gospel. Second, Jewish-Christian thought must be considered as many writings on interest have been produced by their religious leaders. Third, the Greeks and Romans contributed to human civilization, so their views must also be considered. Their opinions influenced many Jews, Christians, and Muslims in the debate over interest (Haroen, 2000).

Interest in conventional finance

Interest is the main instrument in conventional banks. Investments and financing cooperation in conventional banks are always measured by the interest rates offered to investors. The higher the interest rates on savings and deposits, the more interested people become in becoming bank customers or investors (Oleiwi, 2020; Heriyansyah, 2018). Conversely, the lower the interest rates on loans and credits, the more interested people are in applying for financing and credit from conventional banks. The interest system is considered simpler and more practical than the profit-sharing logic. Until now, the interest system still dominates financing carried out by banks, cooperatives, insurance companies, and other financial institutions, leading not to fortune but to loss and difficulty (Suretno, 2018). This occurs because people are still unfamiliar with the substance of interest and the interest system.

Linguistically, bank interest is a translation of the word "interest." Technically, interest is the cost of a financial loan, usually expressed as a percentage of the amount loaned (Muhammad, 2005). There are many definitions of interest: it is the price paid by depositors to banks, the liability on money loans usually expressed as a percentage, or calculated for the use of capital. The percentage associated with it is called the capital interest rate. Interest is reasonable compensation given to depositors to prevent loss (Syamsuddin, 2003). Interest is also monetary compensation provided by banks to their customers for a certain period (Muhammad, 2004).

In banking, two types of interest are given to customers (Rahim, 2020): (1) Savings interest: Incentives or compensation for customers who deposit their money in the bank, such as giro services, savings interest, and deposit interest, (2) Loan interest: Interest given to borrowers or the price paid by borrowing customers to the bank, such as credit interest.

These two types of interest are the main components of bank costs and income. High savings interest automatically raises loan interest and vice versa (Kasmir, 1999).

Classical interest theory.

The classic interest theory states that interest is compensation given by the debtor to the money owner as profit from the borrowed money. The money owner deserves profit for saving their money (Muhammad, 2012). Then came the abstinence interest theory, which tries to refine the classic interest theory. This theory suggests that interest is given because of restraint, meaning that the lender has refrained from consumption or production (Suretno, 2019).

Next, productivity interest theory developed by Marshall differs from previous theories. Marshall argues that interest is given on supply due to the sacrifice of waiting. Bohm-Bawerk's theory states that people prefer present goods to future goods, so it is reasonable for lenders to be given interest (Suretno, 2019).

Monetary interest theory

The monetary interest theory states that interest is determined by savings and investment. Interest is a guarantee of future profit. This theory views interest payments as opportunistic acts to gain profit when borrowing money (Ohlin, 1937; Lerner, 1938). It arises from the concept of interest from savings and investment, believing that savings and investment are always balanced (Sanusi, 2004).

Keynes (1936) perceived interest not as a price or reward for savings but as a payment for borrowing money. Interest compensates for not holding money in liquid form for a specific period. Thus, interest rates balance the desire to hold money with the available cash. Interest payments are seen as borrowing and an opportunity for future profit. Keynes called it speculation motivation, encompassing efforts to gain future profits, affecting interest rates, production levels, investment, and employment. Market instability can be caused by speculative motives (Sanusi, 2004).

Literature on interest theory shows fundamental differences between religious views and conventional financial systems. Interest, as the main instrument in conventional financial systems, has various definitions and applications depending on its context. Classic, abstinence, productivity, and monetary interest theories provide different frameworks for understanding how interest works in the economy. While these theories offer valuable insights, it is essential to consider the social and religious contexts underlying views on interest in different societies.

Profit-sharing theory

Profit-sharing, or known in English as profit sharing, is defined as "the distribution of some portion of profits to employees of a company" (Muhammad, 2001). According to Antonio (2001), profit-sharing is a system of managing funds in the Islamic economy involving the distribution of business results between the owner of the capital (ṣāhib al-māl) and the manager (muḍārib). In Islamic economics, profit-sharing theory emphasizes cooperation between the capital provider (investor) and the capital user (entrepreneur). The prohibition of interest in Sharia entails the absolute elimination of interest. Profit-sharing in Islamic banking is a characteristic offered to the public (Ilyas, 2014).

The profit-sharing system provides competitive advantages for customers and banks and can enhance financial efficiency. The profit-sharing concept can also maximize profits (Kurniawansyah, 2016). The agreed profit-sharing calculation uses the revenue sharing and profit and loss sharing methods.

Revenue sharing means distributing revenue without deducting costs, so revenue is divided from gross profit. This gross profit method only applies to business managers, while Islamic banks receive a share of gross profit becoming net profit. Profit and Loss Sharing, on the other hand, is a profit-sharing calculation system where profits are taken from total revenue minus capital and costs, making profits net profit (Suretno, 2019).

The profit-and-loss sharing theory was built as an alternative outside the interest system, which tends to be unfair as it discriminates against the distribution of risk and profit among economic actors (Yahya & Agunggunanto, 2011). Islamic financial principles are based on the prohibition of riba, gharar prohibition, halal business guidelines, shared business risks, and economic transactions based on considerations of fairness (Gait & Worthington, 2008).

Profit-loss sharing means that profits and/or losses that may arise from economic/business activities are shared. In profit-sharing attributes, there are no fixed and definite returns like interest but profit and loss sharing based on the actual productivity of the product (Adiwarman Karim, 2001).

Islamic financial institutions (Lembaga Keuangan Syariah, LKS) can use the revenue-sharing or profit-and-loss sharing principles in sharing business results with partners (customers) following the agreement made by both parties. If one party determines the profit-sharing pattern to be used, the other party must also agree. The allowance of both systems is because no scriptural basis has been found that prohibits these principles (Suretno, 2019).

This profit-sharing concept is very different from the interest concept applied by the conventional economic system. The funding sources consist of deposits, namely savings and term deposits; capital, namely principal savings, mandatory savings, other funds, and debts from other parties.

In Islamic economics, the profit-sharing concept can be described as follows (Ma'ruf & Cahyoningtyas, 2023):

1. Fund owners invest their funds through financial institutions that act as fund managers.
2. Managers manage these funds in a system known as the pool of funds (fund aggregators), then invest these funds in feasible and profitable projects or businesses that meet all Sharia aspects.
3. Both parties make an agreement *(ʻaqd, ʻuqūd*) that contains the scope of cooperation, nominal amount of funds, and the duration of the agreement.
4. Forms of profit-sharing cooperation in Islamic economics can generally be done in four contracts, namely *mushārakah*, *muḍārabah*, *muzāraʻah*, and *musāqah*. However, in practice, the principle used in the profit-sharing system generally uses mushārakah and muḍārabah contracts.

Muḍārabah (trustee profit-sharing) is one form of *shirkah* (partnership) contract. The term *muḍarabah* is used by the Iraqis, while the Hijaz people call it *qirāḍ*. Thus, *muḍarabah* and *qirāḍ* are terms with the same meaning (Syafei, 2001). The *muḍārabah* model refers to a business partnership between two parties. The first party (*ṣāḥib al-māl*) provides all the capital, while the other party becomes the fund manager (*muḍarib*). The *muḍarabah* model is a business partnership contract where one party contributes capital while the other party contributes entrepreneurship in the form of labor, thought, or management. In this scheme, capital is 100% the responsibility of *ṣāhib al-māl*, while management is entirely the responsibility of the *muḍarib* (Arifin, 2000). *Shirkah muḍārabah* is a partnership between a capital owner and a worker in a specific trade where profits are shared according to mutual agreement, while losses are borne solely by the capital owner (Ghazali, 2010).

Mushārakah (joint venture profit and loss sharing) is a partnership contract between two or more parties for a specific business where each party contributes funds with the agreement that profits and risks will be shared according to the agreement. Manan (2001) explains that *mushārakah* is a partnership between a company and consumers for a limited period on a project where both the company and consumers invest capital in different proportions and agree on a pre-determined profit. Manan further states that this system is also based on the principle of reducing the likelihood of final partnership participation by consumers by giving the company or business partner the right to repay the company's shares in installments or all at once from part of the net operating income. *Mushārakah* involves mixing one type of asset with another so that they cannot be distinguished among a partnership between two or more parties for a specific business where each party contributes funds with the agreement that profits and risks will be shared according to the agreement (Antonio, 2001). The musyarakah model is a partnership contract between two or more parties to run a particular business. Each party contributes funds with the agreement that profits and risks are shared according to the agreement (Arifin, 2000).

In the profit-loss-sharing system, capital prices are jointly determined with the role of entrepreneurship. Price of capital and entrepreneurship is an integrative unit that must be considered in determining the price of production factors. In the sharia view, money can only be developed through actual productivity. There is no additional amount on the principal of money that does not produce productivity (Yahya & Agunggunanto, 2011).

In the agreed profit-sharing agreement, the share proportion (called *nisbah*) is expressed as a percentage of the possible actual productivity outcome. The nominal value of profit-sharing received can only be known after the actual utilization of the funds (ex post phenomenon, not ex ante). The profit-sharing proportion is determined based on the mutual agreement of the parties involved. The proportion is usually influenced by considerations of each party's contribution to the cooperation (share and partnership), the prospect of profit (expected return), and the risk level (expected risk) (Anto, 2003). Mathematically, it can be formulated as follows:

BH=f(S,p,r)BH = f (S, p, r)BH=f(S,p,r)

Explanation: BH = profit-sharing; S = share on partnership; p = expected return; and r = expected risk

An agreed proportion must consider these three factors. The first factor, share on partnership, is something already certain and measurable, thus requiring no special attention. The last two factors, expected return and expected risk, require special attention. Therefore, the ability to estimate potential profits and risks in profit-loss-sharing based cooperation is essential, especially regarding potential risks. Risks have a negative effect on business; the greater the risk, the more it reduces business profit. Risk also has sources, scopes, and characteristics that often do not carefully consider data.

Third, profit estimation usually includes risk variables (Yahya & Agunggunanto, 2011).

Fundamentally, a risk arises because of future uncertainty. Van Deer Heidjen categorizes uncertainty into three: Risk, Structural Uncertainties, and Unknowables. Within certain limits, risk can be estimated so that someone's acceptance of a profit-sharing proportion is not always speculative. Risk is a consequence of productive activities. Risks to be avoided are those that cannot be estimated, like passive risks or unknowables. Such risks, in fiqh muamalah terminology, are called *garar*, truly speculative. Garar occurs because one cannot predict the occurrence of something, thus becoming gambling or a game of chance. If one party gains, the other party must suffer a loss. This implies a win-lose solution. Sharia transactions reflect a positive-sum game or win-win solution as in the profit-loss sharing theory (Yahya & Agunggunanto, 2012).

Research methods

The research method used in this study is qualitative, with data collection techniques through library research. Library research is a data collection technique by analyzing secondary data needed to complete this study. The secondary data used comes from various relevant sources, such as books, dictionaries, journals, documents, and other sources related to the discussion of interest and profit-sharing concepts from various religious perspectives.

Data collection in this study was conducted by thoroughly reviewing literature related to interest and profit-sharing concepts from various religious perspectives, including Islam, Christianity, and Judaism. The literature used includes published and validated scholarly works, whether from books, scientific journals, articles, or other official documents relevant to the research topic. The data analysis technique used in this study is content analysis. Content analysis was chosen because it can comprehensively describe the principles of ethics and justice in heterogeneous global financial practices.

Data analysis steps include data collection, data classification, data analysis, data interpretation, and data validation. Data collection was done by gathering all literature relevant to the research topic. After that, the data was classified based on specific categories relevant to the research topic, such as religious views on interest, profit-sharing concepts in Islam, and comparisons between interest and profit-sharing. Data analysis focused on the content and context of each reviewed source. This analysis aims to find relevant patterns, themes, and relationships between interest and profit-sharing concepts from various religious perspectives. The analysis results were then interpreted to produce comprehensive conclusions about the principles of ethics and justice in heterogeneous global financial practices. Data validation was done by comparing the analysis results with other relevant literature, ensuring the validity and consistency of the data used.

Results and discussion

Interest in Judaism

Jews were forbidden to practice usury, and this prohibition is found in their scriptures, both in the Old Testament and the Talmudic laws. Exodus 22:25 states: "If you lend money to one of my people among you who is needy, do not be like a moneylender; charge him no interest."

Deuteronomy 23:19 states: "Do not charge your brother interest, whether on money or food or anything else that may earn interest."

Leviticus 25:36-37 states: "Do not take interest or any profit from them, but fear your God, so that they may continue to live among you. You must not lend them money at interest or sell them food at a profit." (Antonio, 2001).

Interest in Greek and Roman Civilizations

Around the 6th century BCE to the 1st century CE, Greeks implemented several types of interest, varying depending on their use, as described in Table 1.

Table 1. The application of interest among the Greeks

No	Type of Loan	Interest Rate
1	Ordinary loans	6% - 18%
2	Property loans	6% - 12%
3	Intercity loans	7% - 12%
4	Trade and industry loans	12% - 18%

During the Roman era, from the 5th century BCE to the 4th century CE, laws allowed citizens to charge interest as long as it did not exceed the maximum legal rate. Interest rates fluctuated over time. Although laws permitted charging interest, double counting was not allowed (Ipandang, 2020; Yuliana & Hidayat, 2018).

In 342 BCE, the Genucia administration prohibited interest practices. However, in 88 BCE, the Unciaria administration allowed it again. Table 2 describes some interest regulations during the Roman era.

Table 2. The application of interest among the Romans

No	Type of interest	Interest rate
1	Maximum legal interest rate	8% - 12%
2	Ordinary loan interest rate in Rome	4% - 12%
3	Interest rate for conquered regions	6% - 100%
4	Special interest rate in Byzantium	4% - 12%

Not all Greek philosophers agreed with these interest regulations. Two prominent Greek philosophers, Plato (427-347 BCE) and Aristotle (384-322 BCE), criticized interest practices. Plato believed that interest caused social division and dissatisfaction and was a tool for the wealthy to exploit the poor (Kasdi, 2016). Aristotle argued that money's function is as a medium of exchange, not to generate additional money through interest. He considered interest to be unnatural and unjust (Sutjipto, 2017).

In addition to Plato and Aristotle, Cato (234-149 BCE) and Cicero (106-43 BCE) shared similar views. Cicero advised his son to avoid two professions: tax collecting and lending with interest. Cato illustrated the difference between trade and lending with interest. According to him, trade involved risk, while lending with interest was inappropriate. In their tradition, there was a comparison between a thief and an interest taker; a thief would be fined twice, while an interest taker would be fined four times (Ipandang, 2020; Yuliana et al., 2018).

Interest in Christianity

Some Christians believe that Luke 6:34-35 prohibits interest practices, although the New Testament does not explicitly address this issue. These verses state: “And if you lend to those from whom you expect repayment, what credit is that to you? Even sinners lend to sinners, expecting to be repaid in full. But love your enemies, do good to them, and lend to them without expecting to get anything back. Then your reward will be great, and you will be children of the Most High, because He is kind to the ungrateful and wicked." (Hidayatullah, 2021).

The lack of clarity in this verse has led to diverse reactions and interpretations among Christian leaders regarding whether Christians may practice interest. The differing views among Christian leaders can be divided into three main periods: early Christian leaders who prohibited interest (1st to 12th centuries), Christian scholars who sought to allow interest (12th to 16th centuries), and Christian reformers who led to the legalization of interest by Christianity (16th century to 1836) (Ipandang, 2020; Yuliana et al., 2018).

In the early Christian era (1st to 12th centuries), collecting interest was generally prohibited. They referred to the Old Testament on usury, and Christians also believed it. St. Gregory of Nyssa (335-395) criticized usury as immoral. St. Ambrose condemned interest takers as deceivers and usurers. St. Augustine argued that imposing interest on the poor was more cruel than a robber taking money from the rich. The prohibition of interest was also issued in Canon Law (Kasdi, 2013).

Interest among Christian scholars (12th-16th centuries)

During this period, there was rapid development in economics and trade. Money and credit became essential elements of society. In the early 12th century, credit was introduced to provide working capital for traders. Money markets gradually formed, facilitating the realization of various market interest rates. Christian scholars of the time discussed interest not only from a moral perspective, referring to the Old and New Testaments, but also connecting it to other aspects, including the nature and legal form of human rights over property, the nature and meaning of justice, forms of interest, intentions and actions of humans, and the difference between individual and group sins.

Christian scholars who contributed significantly to the discussion of interest include Robert of Courcon (1152-1218), William of Auxerre (1160-1220), St. Raymond of Peñaforte (1180-1278), and St. Bonaventure (1221-1274). St. Thomas Aquinas (1225-1274) argued that the intention or act of profiting by providing security was contrary to the ideals of justice, and taking interest on loans was permissible but dependent on the lender's intention (Antonio, 2001).

Interest in christian reformers' views (16th century - 1836)

Reformers' views shaped new perspectives on interest. Reformers included John Calvin (1509-1564), Charles du Moulin (1500-1566), Claude Saumaise (1588-1653), Martin Luther (1483-1546), Melanchthon (1497-1560), and Zwingli (1484-1531). Calvin's views on interest included that it was a sin if it caused money to multiply without contributing to productive use, it should not become a profession, and interest should not be taken from the poor (Ghafur, 2018).

Du Moulin argued that small interest practices were allowed if the interest was used for productive purposes. Saumaise, a follower of Calvin, justified all interest practices, even from the poor. He believed that selling money for money was the same as a regular transaction, and there was no reason to prohibit using money to make money. He argued that religion should not interfere with interest matters (Oleiwi, 2020; Yuliana et al., 2018).

Interest in Islamic views

Usury and interest have been intriguing topics in Islam. The prohibition of usury is perhaps final, but interest remains a subject of discussion. Controversies among Muslim scholars on the technical interpretation of usury have persisted since the 18th century. Pragmatic views prevailed during the second half of the 19th century to the early 20th century, represented by prominent scholars, including Al-Azhar Mosque imams. Islamic jurists supporting the permissibility of bank interest include Muhammad ‘Abduh, Rashīd Ridā, Maḥmūd Shaltūt, ‘Abd. al-Wahhāb al-Khallāf, and Ibrāhīm Z. al-Badawī (Antonio, 2001; Hak, 2011).

In Islam, interest is known as riba. Linguistically, riba means “increase” or “growth.” Technically, riba means taking additional money from the principal or capital unjustly (Antonio, 1999). The Quran has several verses on usury, and Islamic scholars throughout history from various fiqh schools have conveyed the prohibition of usury for everyone.

Pragmatic views

According to pragmatic views, the Quran prohibits usury practiced before the Islamic era but does not prohibit interest in modern financial systems (Hak, 2011). They base their opinion on QS. Āli ‘Imrān [3]:130: “O you who have believed, do not consume usury, doubled and multiplied, but fear Allah that you may be successful.”

Therefore, transactions based on interest are considered lawful. Interest becomes legally prohibited if the added amount to the loaned funds is excessively high, intending to exploit the borrower. In Indonesia, exorbitant interest charges by loan sharks are known to impoverish borrowers (Hak, 2011).

Pragmatic views argue that there is no strong evidence in the Hadith that Islam prohibits interest according to the modern financial system. Reports on usury in the Hadith are considered ambivalent and inconsistent. Furthermore, pragmatic views suggest that imposing interest is necessary for the economic development of Muslim countries. Interest is intended to encourage savings and provide capital for productive investments (Hak, 2011).

Conservative views

In contrast to pragmatic views, conservative views argue that riba should be interpreted as both interest and usury. They claim that this interpretation is supported by the Quran and Hadith. Any predetermined return on a loan is riba. In Islam, this form of riba is called riba *al-nasī’ah*, derived from the root *nasa’a*, meaning “delay” or “wait,” referring to the deferment of the loan repayment, compensated by an “addition” or “premium” (Chapra, 2000). In other words, riba al-nasī’ah is the compensation given by the borrower to the lender for the deferment of repayment.

Chapra, a proponent of conservative views, asserts that riba al-nasī’ah also refers to interest applied in modern banking systems (Chapra, 2000). According to him, riba in this sense is mentioned in QS. al-Baqarah [2]:275: “Those who consume usury cannot stand except as one stands who is being beaten by Satan into insanity. That is because they say, 'Trade is just like usury.' But Allah has permitted trade and has forbidden usury. So, whoever has received an admonition from his Lord and desists may have what is past, and his affair rests with Allah. But those who return to usury are the companions of the Fire; they will abide eternally therein.”

In addition to the legal perspective, the reason why interest is forbidden by orthodox legal scholars is their reluctance to provide intellectual arguments supporting Islamic provisions. One scholar stated, “When the Creator Himself has forbidden something, that should be the highest intellectual opinion supporting it” (Muslehuddin, 1990).

Socio-economic views

Recently, some Muslim economists have offered socio-economic reasons for the prohibition of interest. The most important view is that interest tends to accumulate wealth in the hands of a few. Interest suppliers should not rely on the speculation faced by borrowers. Transferring risk from one party to another violates the law. Such agreements are unjust and foster selfishness, which contradicts Islamic principles of brotherhood. According to Islamic financial principles, both lenders and borrowers should face risks (Muslehuddin, 1990).

Another reason for the prohibition of interest is that, in Islamic economic terms, capital is not a separate factor of production but part of other factors, i.e., the enterprise. This means that taking profit from providing capital without personal involvement in the risk by the financier is undesirable in Islam. Furthermore, Islam views that everything in this world is subject to the natural law of depreciation. All money should depreciate over time (Hak, 2011).

Based on several opinions about riba, it generally produces additional income in both sales and lending transactions without being balanced by justified transactions. The purpose of exchange or mutual annulment is a business or commercial transaction that justifies an addition: sales, pawn rights, rent, or profit-sharing projects. For example, in a sale, the buyer pays for the received goods. Even in profit-sharing projects, partners are entitled to profits because, besides investing capital, they also bear the risk of loss that may occur at any time (Antonio, 2001).

In traditional borrowing and lending transactions, lenders typically receive additional interest without providing any compensation to the borrower other than the opportunity factor or time taken during the borrowing process. What is unjust is that the borrower is always obliged to provide additional benefits to the lender, while the lender takes advantage of this opportunity (Antonio, 2001). Fiqh scholars unanimously agree that muamalah (transactions) involving riba are haram (forbidden) (Haroen, 2000).

Comparison of interest theory and profit-sharing theory

Islam encourages profit-sharing practices and prohibits riba. Both provide benefits to fund owners but have very distinct differences. The fundamental difference between Islamic and non-Islamic financial institutions lies in the returns and profit distribution provided by customers to financial institutions and/or provided by financial institutions to customers. Hence, the terms interest and profit-sharing exist (Antonio, 2001).

The issue of bank interest, referred to as riba, has been a subject of debate among Islamic thinkers and fiqh scholars. It seems this issue will never end but will continue to be discussed from time to time. To address this issue, Muslims have tried to develop an old economic paradigm that will continue to evolve to improve the ummah's economy and welfare. Its realization is the operation of Islamic banks in various regions, operating not based on interest but on profit-sharing systems (Muhammad, 2012).

Table 3. Differences between interest and profit-sharing

No	Interest	Profit Sharing
1	Interest is determined at the time of the contract, assuming it always generates profit.	The profit-sharing ratio/nisbah is determined at the time of the contract, considering the possibility of profit or loss.
2	The percentage is based on the amount of money (capital) borrowed.	The profit-sharing ratio is based on the profit obtained.
3	Interest payment is fixed as promised, regardless of whether the project undertaken by the customer is profitable or not.	Profit-sharing depends on the project's profit. If the business suffers a loss, the loss is borne by both parties.
4	The amount of interest payment does not increase even if the profit doubles or the economy is booming.	The amount of profit distribution increases with increased income.
5	The existence of interest is doubted (if not condemned) by all religions, including Islam.	No one doubts the validity of profit-sharing. Profit-sharing is a halal instrument used for *shirkah* cooperation, both *muḍārabah* and *mushārakah*.
6	Interest contains elements of injustice that harm others.	Profit-sharing contains elements of justice that bring peace and prosperity.
7	Interest makes the economy dominated by the wealthy, widening the gap between the rich and the poor.	Profit-sharing extends to the real sector, increasing gross domestic product.

Source: Antonio (2001)

The table 3. clearly shows the fundamental differences between interest and profit-sharing applied in Islamic banks for profit-sharing and conventional banks for interest, both structurally and procedurally. Although both have similarities in collecting and distributing funds from the public (Hak, 2011).

However, the implementation of profit-sharing in Islamic banks is not yet optimal and faces difficulties. These difficulties are mainly due to strict mechanisms. Ideally, the profit-sharing model is applied to *muḍarabah* and *mushārakah* products, where the bank, as the shāḥib al-māl, provides business funding, while the second party, the customer as the mudharib, runs the business with profit or loss shared by both parties. In practice, if the second party incurs a loss, both parties should bear it, but in reality, the bank bears the loss. Conversely, if the second party gains substantial profit, it should be shared between both parties, but in reality, the profit only benefits the second party. This is the difficulty of the profit-sharing model (Hak, 2011).

The tendency of people to use the interest system (interest or usury) is more to optimize personal interests, neglecting its social impact. In contrast, the profit-sharing system (profit sharing) is oriented towards fulfilling the welfare of humanity (Sudarsono, 2003).

Conclusion

This study has conducted a comparative analysis between the interest theory in conventional financial systems and the profit-sharing theory in Islamic financial systems. The analysis found that interest theory dominates conventional financial systems with its various applications, focusing on interest rate determination based on loans and deposits, as well as interest as compensation for investment risk. Conversely, the profit-sharing theory in Islamic financial systems offers an alternative centered on the principle of justice, with profit and loss distribution based on the actual contributions of each party in economic activities.

The study also indicates that while the concept of interest has been widely recognized and utilized across various civilizations, there are differing religious views on the legality and morality of interest. From an Islamic perspective, interest is considered haram due to its elements of riba, whereas profit-sharing is deemed more just and in line with Sharia principles. This profit-sharing approach not only supports justice but also promotes economic efficiency through a more equitable distribution of risk between the capital owner and the entrepreneur.

However, this study has several limitations that should be noted. First, it focuses more on theoretical analysis rather than empirical analysis, thus providing less practical insight into the application of both systems in real economic contexts. Second, it does not consider the variations in the implementation of the profit-sharing system across different Islamic financial institutions. For future research, it is recommended to conduct in-depth empirical studies on the effectiveness and efficiency of the profit-sharing system in various economic contexts and to identify the factors influencing the success of its implementation. Additionally, exploring the integration of Sharia principles with conventional finance to create a more inclusive and sustainable financial system is necessary.

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