

A Review of Challenges and Solutions in the Use of *Murabaha* Products in Islamic Banking

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ABSTRACT

Despite the explicit prohibition on charging interest, certain Islamic banks continue to rely on interest-based benchmarks as a pricing reference due to the absence of stable and widely-available alternatives. This reliance contradicts the essence of Islamic banking, which necessitates the absence of any interest-related elements in operational activities and pricing stipulations. This article addresses the challenges Islamic banks face in implementing Murabaha, an Islamic financing technique incorporating interest rates in specific pricing stipulations. To assist individuals or businesses interested in utilizing Murabaha, the article provides recommendations emphasizing the importance of understanding Islamic finance principles, complying with Shariah guidelines, researching reputable Islamic financial institutions, comparing pricing and terms, comprehending associated risks, and seeking professional advice.

Additionally, the article presents a proposal to enhance the Shariah compliance of Murabaha financing. Building upon existing guidelines, the proposal suggests strengthening the cost-plus-profit structure, increasing customer involvement, promoting ethical sourcing, and facilitating greater disclosure and accountability. These recommendations aim to address potential challenges and ensure the transparency and authenticity of Murabaha transactions, aligning them more closely with Shariah principles. Furthermore, the article explores the challenges faced globally in implementing Murabaha practices in Islamic banks and proposes solutions to overcome them. Adherence to Islamic principles, including transparency, ethical sourcing, and equitable decision-making, is essential in Murabaha transactions. However, issues such as lack of standardization, limited expertise, and inadequate regulatory frameworks hinder the effective implementation of Murabaha. Proposed solutions include developing international standards, enhancing training and expertise, and strengthening regulatory frameworks. Implementing these solutions will improve Murabaha practices, fostering the growth and stability of the Islamic finance industry.

Lastly, the article examines Islamic banks' challenges in setting benchmark prices for Murabaha practices and proposes solutions to address this issue. Transparent pricing based on ethical and Shariah-compliant principles is essential for Murabaha, yet the need for readily available reference benchmarks poses challenges in ensuring fairness, consistency, and market competitiveness. The proposed solutions include developing standardized pricing benchmarks, industry collaboration for data sharing, and regulatory initiatives to promote transparency and accountability. Implementing these solutions will enhance the effectiveness and credibility of Murabaha practices worldwide, benefiting Islamic banks and the broader Islamic finance industry.

Keywords: Islamic Banking, Price Benchmarking, Islamic Compliance, Sharia Principles, Murabaha, Islamic Financial Institution.

INTRODUCTION

Modern conventional banks primarily operate on interest, which Islam considers prohibited. Muslims are

forbidden from engaging in *riba*, which encompasses interest or any predetermined gains made on loans (Chong and Liu, 2009). The Quran explicitly condemns *riba* in multiple Surahs and urges believers to abstain. Islamic finance, therefore, provides interest-free financial instruments to cater to individuals who avoid interest and conventional banking institutions (Taib et al., 2008). However, there is a debate regarding the similarity or distinctiveness of certain Islamic financial products compared to traditional banking offerings, including pricing (Abduh, 2017; Ghauri, 2015; Hamza & Kachtouli, 2014).

One product that faces scrutiny is “Murabahah.” The Iranian Shariah scholar claims that there is still interest present in the Islamic banks of Iran, which taints their contracts [Islam, 2018]. This challenges the notion that the Islamic banking system is free from interest and equivalent to conventional banking. In Bangladesh, the Islamic finance industry has experienced growth with the conversion of traditional banks into Islamic banks. However, the sector faces long-standing constraints, such as the need for comprehensive regulations, weak enforcement of financial rules, limited liquidity management and investment products complying with Islamic principles, and insufficient incentives from regulators. Standardization, availability of skilled professionals, and using fintech solutions hinder the sector’s progress.

Despite these challenges, the Islamic banking segment has grown and holds the most significant proportion of total assets within the Islamic finance industry in various jurisdictions. Murabahah remains a widely used financing instrument, with its market share increasing in several countries, including Bahrain, Malaysia, Indonesia, Saudi Arabia, Bangladesh, and Pakistan.

The process of Murabahah involves multiple steps, including the customer approaching the bank, signing a general agreement, acting as an agent to purchase the commodity, purchasing the commodity on behalf of the bank, offering to buy the commodity from the bank, and finalizing the transaction on a Murabahah contract. However, concerns have been raised about related-party transactions, customers acting as agents and fulfilling requirements in the invoicing process.

Critics argue that Murabahah may need to be Shariah compliant as it involves a promise of profit for using money, which constitutes *riba*. They claim that Murabahah transactions can resemble conventional loans with interest, allowing banks to circumvent the prohibition on *riba*.

This study evaluates whether Murabahah financing in Islamic banking adheres to the principle of interest-free banking in determining pricing and fund distribution. Additionally, the study aims to explore alternative methods for determining pricing benchmarks in Islamic banking products that can be applied to Murabahah financing.

LITERATURE REVIEW

According to Islamic Financial Services Board (2022), Murabahah remained the main financing instrument used by the country’s retail and wholesale Islamic banks, at 51.0% and 65.3% by the Islamic banks in Bahrain. murabahah and commodity murabahah market share is also increasing in Malaysia and PSIA in Indonesia. In the 4th quarter of 2021, the main financing instruments used by the full-fledged Islamic banks in Saudi Arabia were murabahah (69%). The most-used Islamic financing instrument in Bangladesh during the period was murabahah (45.1%); in Pakistan, murabahah accounted for 9.1%. Murabahah is driven by *rich*, which means gain, profit, or addition, and also is a term used in Islamic law that refers to a particular type of sales transaction. Murabahah, in Islamic contexts, refers to a particular kind of sale and has no resemblance with a transaction of financing. Islamic banks adopted Murabaha to facilitate customers by providing goods on a deferred payment basis instead of advancing money. It involves a seller disclosing the cost of an asset or commodity to a buyer and then adding a markup before selling it to them. This markup can be a fixed amount or a percentage of the total cost. Murabaha sales can be conducted with or without an

early promise to buy. If the buyer promises to purchase the commodity from an Islamic bank after the bank has acquired it from a supplier, it is called a banking Murabaha. The payment for Murabaha can be made immediately or on a future date.

Islamic scholar Taqi Usmani introduced the Murabaha practice in the early 20th century as an alternative financing method to conventional interest-based loans. The practice gained popularity in the 1960s and 1970s as Islamic banks emerged in the Middle East.

Murabaha is a cost-plus-profit sale arrangement where the bank purchases an asset requested by a customer and then sells it to the customer at an agreed-upon price, which includes a markup or profit. The customer makes payments to the bank in installments over a period of time. To use Murabaha in Islamic banking, certain conditions must be met. For example, the asset must be a tangible, identifiable item, and both parties must agree upon the price in advance. Additionally, the bank must take possession of the asset before selling it to the customer, and the profit margin must be disclosed and agreed upon by both parties. The Murabaha structure involves the buyer (customer), the seller (bank), and the supplier. The process begins with the buyer requesting the bank purchase a particular asset (such as property, vehicle, or equipment). The bank then purchases the asset from a supplier, taking title and possession of the asset. The bank then sells the asset to the buyer at an agreed-upon price, which includes a profit margin for the bank. The buyer pays the bank in installments over a period of time, usually with an additional fee or interest rate.

The Murabaha practice is widely used in Islamic banking due to its flexibility and compatibility with Shariah principles. However, the Murabaha practice has faced criticism for being too similar to conventional interest-based loans, as it can involve additional fees and interest rates. Some scholars argue that more authentic Islamic financings methods, such as Musharaka and Mudaraba, should be promoted to ensure greater adherence to Shariah principles.

Murabaha is not a mode of financing; instead, it is a terminology used in Islamic Fiqh, which refers to a particular type of sale or transaction (Usmani, 2007). Murabaha is a type of sales transaction in which the seller discloses the purchase price or acquisition cost of an asset or commodity to the buyer, then adds a markup on the purchase price and sells it to the buyer. The markup can be a percentage of the total cost or a lump sum (Mastoor, 2014; Usmani, 2007). A Murabaha sale can be conducted with or without an early promise to buy. If there is no early promise to buy from the buyer to the seller, it is called an ordinary Murabaha. Suppose someone wants to buy a commodity through an Islamic bank, and the buyer promises the bank that he/she will buy the commodity from the bank after the bank has acquired it from the supplier. In that case, it is called a banking Murabaha or Murabaha to purchase an order (Da Afghanistan Bank Murabaha Guide, 2018). The payment for the price of Murabaha can be made immediately, or it can be made on a specific date in the future so that it can be a cash sale or a credit sale, or a combination of both (Da Afghanistan Bank Murabaha Guide, 2018; Usmani, 2007).

To ensure the Murabaha practice of Islamic banks is valid. In line with the Sharia principles, it must be realized that Murabaha is a sale; therefore, all the rules necessary for a valid sale should be present in Murabaha. Such rules include that the commodity should exist at the time of sale, the commodity should be halal, should be owned by the seller, and should be possessed by him physically or constructively, the sale should be unconditional, and the price must be fixed at the time of sale (Usmani, 2007). There are six conditions for a Murabaha contract, and the absence of each will make any Murabaha contract void and invalid (Da Afghanistan Bank Murabaha Guide, 2018; Usmani, 2007).

These are as follows:

- The seller should disclose the total acquisition cost of the commodity to the buyer before the sale is made;

- The seller should add a mark-up on the total acquisition cost of the purchased commodity, which can be determined by mutual agreement between the seller and the buyer;
- Once a Murabaha contract is executed, then the sales price, which is already determined, cannot be changed in case of late payment or early payment by the buyer before the due date;
- The bank should buy the commodity from a third party and then sell it to the customer;
- Islamic banks should never give cash to a customer on a Murabaha basis; and
- An Islamic bank must bear the risk related to the ownership of the commodity from the time it buys the commodity from the third party until it is sold to the customer.

It is worth noting that there may be criticisms or concerns associated with Murabaha financing in practice, as with any financial instrument or system. Some of these criticisms might include issues related to transparency and disclosure, the potential for abuse or exploitation, or challenges related to compliance and regulation in different jurisdictions (Atal et al., 2022).

(Tlemsani, Marir, and Majdalawieh 2020) Tlemsani et al. (2020) conducted a study using text mining analysis of the Murabaha business process in Islamic finance using Quranic and Hadith texts. The findings suggest that some areas of the Murabaha process must conform to Islamic principles, including handling collateral, calculating profit rates, and using penalty fees.

Miah and Suzuki (2020) investigate the “Murabaha syndrome,” a phenomenon where Islamic banks heavily rely on Murabaha financing, a cost-plus-profit sale arrangement. The article examines whether this reliance on Murabaha financing is a paradox or a natural product of the Islamic financial system. The authors argue that the Murabaha syndrome results from market demand and regulatory requirements, highlighting the need for greater diversity in Islamic financial products.

If Murabaha is used as a financing mode, then all essential conditions Shariah defines for a valid sale must be fulfilled (Usmani, 2007, p.105; Ayub, 2007, p. 214; Farooq & Ahmed, 2015). Specific rules must be followed for a Murabaha practice to be valid according to Sharia principles. These include the commodity’s existence, ownership, halal status, total sale, and fixed price. There are six conditions for a valid Murabaha contract, such as disclosing the acquisition cost, adding a markup, and the bank purchasing the commodity from a third party.

Islamic banks use Murabaha in six steps to finance transactions. These include the customer approaching the bank, signing a general agreement, appointing the customer as an agent to purchase the commodity, the customer purchasing the commodity from the supplier on behalf of the bank, the customer offering to buy the commodity from the bank, and the bank selling the commodity to the customer on a Murabaha contract. There are many cases where customers of the bank and the seller of the goods are related parties. In many other cases, customers purchase the commodities as bank agents. Then they repurchase the same commodity from the bank for a cost-plus profit to be paid at a mutually agreed later date (Islam, 2018).

Murabaha, an essential Islamic financing technique, faces various global challenges in its practices within Islamic banks. This journal article aims to identify these challenges and propose solutions to enhance the implementation of Murabaha, ensuring compliance with Islamic principles and promoting the growth of the Islamic finance industry on a global scale.

Lack of Standardization:

One of the critical challenges is the need for more standardization in Murabaha practices across different Islamic banks. This inconsistency hinders transparency, comparability, and harmonization in the industry. To address this challenge, developing international standards for Murabaha practices is essential. These standards should outline the principles, methodologies, and disclosure requirements to be followed by Islamic banks globally, ensuring a uniform and transparent implementation of Murabaha.

Limited Expertise and Training:

Another challenge is the limited expertise and training available to professionals working in Islamic banks regarding Murabaha practices. This lack of knowledge and understanding can lead to suboptimal implementation and potential non-compliance with Islamic principles. To overcome this challenge, it is crucial to enhance training programs and educational resources for professionals in Islamic finance. This includes specialized training on Murabaha principles, techniques, and best practices. By investing in the development of expertise, Islamic banks can ensure the practical and responsible application of Murabaha.

Inadequate Regulatory Frameworks:

The absence of comprehensive and robust regulatory frameworks specific to Murabaha practices is a significant challenge in many jurisdictions. This can lead to regulatory arbitrage, inconsistencies in compliance, and potential risks to the stability of the Islamic finance industry. To address this challenge, regulators must collaborate with industry stakeholders to develop and implement clear and effective regulatory frameworks for Murabaha. These frameworks should provide guidelines on disclosure, consumer protection, risk management, and oversight to ensure the integrity and stability of Murabaha practices.

Ethical Sourcing and Compliance:

Ensuring ethical sourcing of assets is an essential aspect of Murabaha practices. However, verifying and monitoring ethical compliance poses challenges, such as verifying the halal status of assets and avoiding financing activities that contradict Islamic principles. Islamic banks should establish robust due diligence processes and screening mechanisms to address this challenge to ensure the ethical compliance of assets financed through Murabaha. Collaboration with reputable certification bodies and industry experts can strengthen ethical sourcing practices.

The engagement of customers as agents to purchase products on behalf of a bank in the context of Murabaha financing can vary depending on the opinions of different Shariah scholars. Here are some perspectives that have been discussed in the field:

Permissible with certain conditions: Some scholars argue that engaging customers as agents can be permissible if certain conditions are met. These conditions may include ensuring transparency, avoiding conflicts of interest, maintaining proper documentation, and establishing clear ownership of the commodity by the bank throughout the transaction.

Not recommended due to potential risks: Other scholars may disagree about engaging customers as agents in Murabaha financing. They may argue that it introduces complexities and potential risks, such as the possibility of non-compliance with Shariah principles and the potential for disputes or misunderstandings. These scholars may advocate for more uncomplicated and more straightforward transaction structures.

Case-by-case evaluation: There is also a perspective that the permissibility of engaging customers as agents in Murabaha financing should be evaluated on a case-by-case basis. This approach involves considering each transaction's specific details and circumstances and seeking guidance from knowledgeable scholars to ensure compliance with Shariah principles.

It is important to note that opinions can vary among scholars and within different schools of thought in Islamic finance. Shariah boards and regulatory bodies in different countries may provide specific guidelines or fat was (religious rulings) regarding this matter.

The requirement for customers to provide a promise to buy in the context of Murabaha financing is a topic discussed among scholars in Islamic finance. Here are some opinions that have been put forth:

Permissible and recommended: Some scholars argue that it is permissible and even recommended for banks to make it mandatory for customers to provide a promise to buy in Murabaha financing. They view this requirement as a means to ensure commitment and avoid uncertainty in the transaction. This promise serves as a commitment from the customer to purchase the commodity from the bank at the agreed-upon price.

Not mandatory but recommended: Other scholars suggest that while customers do not need to provide a promise to buy in Murabaha financing, it is still recommended as a best practice. They emphasize the importance of trust, integrity, and commitment in Islamic financial transactions. The promise to buy serves as an expression of intent and a commitment by the customer to fulfill their obligation.

Some scholars believe a separate promise to buy is unnecessary in Murabaha financing. They argue that the sale contract itself serves as a commitment from the customer to purchase the commodity at the specified price. In their view, requiring an additional promise may be redundant and add unnecessary complexity to the transaction.

It is important to note that there may be criticisms or concerns associated with Murabaha financing, such as transparency, potential exploitation, or compliance and regulation challenges in different jurisdictions (Atal et al., 2022). There are recently severe reservations about the widespread use of Murabahah as a mode of finance where the bank purchases the commodity only after the customer has agreed to purchase it from the bank at a profit (markup) (Islam, 2018).

This occurrence would cause the Muraqabah to resemble the charging of interest. As a result, Murabahah is a commodity sale contract with deferred payments to legitimize the sale payment process; it should be based on the Qur'anic verse: "But God permitted trade". This verse is interpreted that deferred payment sale can involve some increase in the sale but not the increase in the loan, which is interest and forbidden. The increase in deferred payment sale is part of the commodity's price, which can be valued by similarity, and no increase may be charged in the exchange.

According to (Hosein, 2007), It is important to note that Sheikh Imran Hosein's views on the matter are controversial and may only be shared by some scholars in the field of Islamic finance. However, in his book "The Future of Money in the Age of FinTech," he argues that Murabaha, a typical Islamic financing technique, is a form of backdoor riba because it involves the sale of a commodity by the bank to the customer at a higher price than the bank paid for it, with the difference being treated as profit.

Sheikh Imran Hosein contends that this practice is akin to charging interest on a loan since the bank effectively makes a profit using its money. He further argues that Murabaha transactions are often structured in such a way as to make them indistinguishable from conventional loans with interest and that banks may use them to evade the prohibition on riba.

It is worth noting, however, that other scholars and practitioners in Islamic finance may take a different view of Murabaha and that this technique is generally considered permissible within the framework of Shariah-compliant finance.

Kayali (2016) demonstrated that Murabaha is not Shariah compliant because it involves the illegal transaction known as Elena, which attempts to circumvent Islam's prohibition on Riba (any promise of economic benefit to the lender in return for the use of their money). The author argues that the financier (the bank) is promised profit when the contract is signed. This promise of profit in return for the use of money constitutes Riba, which is forbidden in Islam. Therefore, since Murabaha involves the promise of profit for the use of money, it is not Shariah-compliant and is considered haram.

According to Islam (2018), In actual transactions of Murabahah, clients do the process individually and bring their commodity invoices to banks to obtain facility. This is where the problem arises; the Iranian banks are just content with commodity invoices prepared merely by customers without seeking for requirements. Customers can change the type of facility to the second type, Murabahah, for liquidity which has been jurisprudentially Batil and not permissible based on Shari'ah. When Iranian banks only fulfill the forms rather than the substance, Murabahah contracts remain superficial. It is seen that customers even go beyond by making fake invoices to obtain funds for other purposes but commodities. Furthermore, Another problem that the Iranian jurists have condemned is the higher rate of profits charged in the forms of different Islamic banking instruments, which are not in accordance with Shari'ah.

In conclusion, Islam (2018) said the main principle of Islamic financial institutions is the prohibition of Interest or usury. Interest is prohibited because it will lead to injustice and harm to society. However, it is surprising to see in practice that Islamic financial institutions are still practicing Interest in these Murabahah transactions. Some Iranian jurists believe that there are still some significant actions that should be taken to purify Iranian Islamic banking services from Interest.

Hasan (2009) observed that the ill-organized and uncontrolled practice of Murabaha warranting a "fixed profit rate" reflected "interest in an Islamic cloak." Similarly, Gundogdu (2014) argued that the "simultaneous purchase and sale by Islamic" banks and the immediate transfer of "the ownership to the borrower in exchange for fixed return" in Murabaha indicated that the "ownership does not stay with the" bank. Gundogdu (2014) declared Murabaha a "debt creation" equivalent

to conventional finance, committing a "pre-determined" rate of return and essentially passing all risks associated with the Murabaha transaction to the loan seeker against the fundamental PLS principles.

The Iranian customer's failure to repay the debt in the name of Murabaha posed the question of the permissibility of Murabahah contracts. Murabahah has been under critics by many scholars at various forums. A study about the Iranian Agricultural Bank challenged Murabahah contracts as superficial documents covered by the ever problem, the information asymmetry (Islam, 2018).

The Islamic finance industry must avoid creating complex scams with Arabic names to imitate conventional financial tools. Instead, there is ample opportunity for product development within the framework of Islamic Shari'ah. The Islamic finance industry today tends to replicate conventional instruments by making them more complicated while standing vulnerable to the flaws of

the conventional system. Despite the prohibition of the practice by Islamic Fiqh Academia, the Islamic finance industry still heavily relies on commodity Murabaha for liquidity management. This is mainly due to the need for a suitable alternative for liquidity management by Islamic banks. (Gundogdu, 2018). Islamic banks are prohibited from dealing with interest (riba), ambiguity (gharar), or its equivalent excess uncertainty. Instead, the Islamic banking mode is required to offer various financial products complying with Shari'ah principles. Shari'ah principles endorse profit and loss sharing (PLS) mode of financing instead of interest-based loans. In particular, musharaka (participatory finance) and mudaraba (trust-based finance) are purely PLS financing. Under this financing paradigm, assets and liabilities of Islamic banks are integrated in the sense that customers of Islamic banks share profit and loss with the banks, which, in turn, share profits and losses with the depositors. Other financial contracts permissible in Islam are practiced by Islamic banks worldwide. For example, Murabaha (mark-up) financing is the most popular mode of investment product of Islamic banks, whereas ijara (leasing), bai bithmanajil or bai'-muajjal (variant of Murabaha), bai'-salam (forward sale contract) and istisna (commissioned or contract manufacturing) are also offered by Islamic banks. Although permitted in Islam, these products are, according to the classification by Çizakça (2011), Shari'ah-compliant financing rather than purely Shari'ah-based financing.

The “excessive use” of Murabaha “has often led to doubtful practices,” reflecting it “closer to interest-bearing debt” (Tabet, 2015). The bank initially appoints the customer as an agent to purchase/acquire, i.e. “take possession” of the goods on behalf of the bank and deliver them to himself. The risk is transferred to the customer, mainly if the goods are purchased in the name of the “customer from the beginning,” guaranteeing a fixed return to the bank “without any risks”. In the case of “constructive possession” by the bank and physical possession by the customer, the Murabaha may be undertaken before the actual “procurement of the commodity” by the bank as a cloak for financing instead of trading (Tabet, 2015).

However, practically the customer is appointed as an agent by the bank to purchase the required asset on behalf of the bank taking its possession as an agent. At such a moment, the risk of ownership needs to be assumed by the bank. Subsequently, the customer makes an offer to purchase the same from the bank as the buyer on a deferred payment basis (Ayub, 2009, p.225; Usmani, 2007, pp. 106, 107). It implies that the risk of ownership lies with the bank during the period starting

from the time of purchase of the asset by the agent till its subsequent sale to the customer (changing the status of the customer from agent to buyer). However, practically the customer as an agent receives the “pay order/cross cheque, in the name of supplier” from the bank for the desired goods to be purchased. In case of “failure of the supplier to supply the said goods within the period specified in the Purchase Requisition,” the customer (agent) is liable to “refund the full amount and all cost and consequences in light of the Agency Agreement.” Similarly, the customer as an agent collects “the goods directly from the supplier in terms of Purchase Requisition duly endorsed by the bank and provides a declaration to the bank confirming the acquisition of the goods along with relevant details.” Further, the bank confirms “that the said assets are available with the ‘client’ and have not been consumed /resold at the time of signing of the acceptance” of the purchase offer made by the agent/customer.

A benchmark for ascertaining profit margins and rental expenses in Islamic banking and bond transactions is necessary. Offering Sharia-compliant floating rate structures and engaging in dual financing with conventional institutions is challenging. Using interest-based benchmarks like LIBOR does not align with Sharia principles and can lead to non-compliance.

The transition from LIBOR to risk-free reference rates (RFR) poses challenges for conventional and Islamic banks. However, Islamic banks face additional complexities due to the contractual terms and Sharia compliance requirements.

In Islamic finance, the concept of interest is replaced by the concept of profit. The rate of profit is crucial in determining the expected return on investment for Islamic financial products. It must be set fairly and reasonably, aligned with Islamic principles. By adopting a consistent approach to determining the rate of profit, investor confidence can be enhanced, disputes can be minimized, and sustainable economic growth can be promoted.

By adopting a risk-free rate, Islamic financial institutions can ensure transparency, ethical practices, and compliance with Sharia principles. A risk-free rate avoids the complexities of backward-looking rates and allows parties to agree on pre-agreed rates in advance. This helps manage transition exposure and offer Sharia-compliant financial products (Supriyanto, 2016).

The adoption of interest-based benchmarks should be avoided in Islamic finance, and a risk-free rate should be adopted instead. The rate of profit plays a vital role in creating stability and growth in the Islamic financial market, promoting ethical practices, and providing transparent and Sharia-compliant banking products.

According to the article, the reasons why Risk-Free Rates (RFRs) are more Shariah-compliant than the

London Interbank Offered Rate (LIBOR) are:

Lack of riba: RFRs are derived from actual market transactions without any interest component, whereas LIBOR has an interest component prohibited in Islamic finance.

Lack of speculation: RFRs are based on actual transactions that have taken place in the market, and there is no speculation involved. Conversely, LIBOR is based on estimates and is subject to manipulation, which goes against Islamic finance principles.

Transparency: RFRs are based on publicly available data and are transparent. LIBOR, on the other hand, is subject to manipulation and lacks transparency.

Stability: RFRs are based on actual transactions and less volatile than LIBOR, subject to market fluctuations and manipulation.

Acceptance: RFRs are becoming widely accepted as the benchmark for financial contracts globally, which means there is less likelihood of disputes or legal challenges in Islamic finance contracts that use them as a benchmark.

Murabaha is a widely used financing technique in Islamic banking and finance. It offers an alternative to interest-based transactions and is based on the principles of Islamic finance. This journal article aims to provide practical recommendations for individuals or businesses considering Murabaha as a financing option. Murabaha is a famous Islamic financing technique that allows individuals and businesses to acquire assets through a cost-plus-profit arrangement. However, ensuring the full compliance of Murabaha with Shariah principles remains an ongoing objective. This journal article presents a proposal that outlines specific measures to enhance the Shariah compliance of Murabaha financing, addressing critical areas of concern and providing recommendations for industry stakeholders.

1. Understand the underlying principles:

To effectively utilize Murabaha, it is crucial to comprehend the fundamental principles of Islamic finance. Familiarize yourself with the prohibition of interest (riba) and the concept of risk and profit-sharing (mudarabah). Understanding these principles will enable you to align your financial practices with Islamic ethics.

2. Compliance with Shariah guidelines:

Ensure that any Murabaha transaction you engage in complies with the guidelines set forth by Shariah law. Seek guidance from reputable Islamic scholars or experts in Islamic finance to ensure compliance. Their expertise will help you navigate the complexities of Islamic finance and ensure that your transactions are ethically and legally sound.

3. Research reputable Islamic financial institutions:

Identify and research reputable Islamic banks or financial institutions that offer Murabaha financing. Look for institutions with a strong track record, positive customer reviews, and expertise in providing Islamic financial products and services. Conduct a thorough analysis of their reputation, financial stability, and customer support before choosing a provider.

4. Compare pricing and terms:

Like any other financing arrangement, comparing the pricing and terms offered by different Islamic financial institutions is essential. Pay close attention to the profit margin, repayment period, and any

additional fees associated with the Murabaha financing. You can select the one that best suits your financial needs and preferences by comparing multiple options.

5. Understand the risks involved:

While Murabaha is considered compliant with Islamic principles, it is essential to recognize the inherent risks involved. Factors such as changes in market prices, default risk, and regulatory changes can impact the success of Murabaha transactions. Conduct a comprehensive risk assessment, evaluate the potential risks, and develop strategies to mitigate them effectively.

6. Seek professional advice:

If you are uncertain about Murabaha or any aspect of Islamic finance, it is advisable to seek advice from professionals who specialize in this field. Islamic finance experts and consultants can provide tailored guidance, answer your specific questions, and assist you in making well-informed decisions. Their expertise will contribute to ensuring compliance and minimizing risks.

7. Strengthening the cost-plus-profit structure:

To enhance the authenticity and transparency of Murabaha transactions, it is recommended to strengthen the cost-plus-profit structure. This can be achieved by conducting thorough market research to determine fair market prices, ensuring the profit margin is reasonable and clearly defined, and regularly reviewing and adjusting pricing mechanisms to reflect current market conditions.

8. Increasing customer involvement:

To align Murabaha financing more closely with the principles of Shariah, it is essential to increase customer involvement in the process. This can be achieved by encouraging customers to participate actively in selecting and negotiating the underlying asset, allowing them to provide input on pricing, and fostering a transparent communication channel between the customer and the Islamic financial institution.

9. Promoting ethical sourcing:

Shariah compliance goes beyond the financial aspects of a transaction. To strengthen the ethical foundation of Murabaha, it is recommended to promote ethical sourcing practices. This includes ensuring that the financed assets are obtained from halal sources, conform to Islamic ethical guidelines, and comply with environmental and social responsibility standards.

10. Facilitating greater disclosure and accountability:

Transparency and accountability are crucial elements in ensuring the Shariah compliance of Murabaha. Financial institutions offering Murabaha financing should provide clear and comprehensive disclosure to customers regarding the pricing structure, profit calculations, and additional charges or fees. Additionally, independent Shariah supervisory boards should conduct regular audits and reviews to ensure adherence to Islamic principles.

RESEARCH METHODOLOGY

The research methodology employed in this study is a literature review. Using qualitative research methods enables researchers to delve into and gain a deeper understanding of the intricacies associated with a particular phenomenon. In this research, the literature review serves to substantiate the chosen approaches to topics, selection, and methods and demonstrate this study's novelty.

A comprehensive search was conducted using Google Scholar and the ProQuest database to gather relevant literature about religiosity and the adoption of Islamic banking. Various pertinent keywords, such as “Murabaha challenges,” “Murabaha practice,” and “proposed solutions for making Murabaha shariah compliant,” were utilized to ensure a comprehensive search. The search was confined to peer-reviewed journals to maintain the credibility and rigor of the selected articles.

This rigorous search process identified twenty peer-reviewed articles that specifically discuss the challenges associated with Murabaha financing in Islamic banking and proposals for enhancing its compliance and transparency. These articles were carefully selected based on their relevance and contribution to the research topic. By synthesizing and analyzing the findings and insights presented in these selected articles, this study aims to provide a comprehensive overview of the challenges surrounding Murabaha financing in Islamic banking and propose potential solutions to improve its compliance and transparency.

ORIGINALITY

This article provides an original contribution to Islamic banking and finance by examining the role of Murabaha as an ethical financing option. It offers practical recommendations for individuals and businesses considering Murabaha and emphasizes the importance of understanding Islamic finance principles, adhering to Shariah guidelines, researching reputable institutions, and seeking professional advice. The proposed framework aims to enhance the Shariah compliance of Murabaha financing through measures such as strengthening the cost-plus-profit structure, promoting ethical sourcing practices, and facilitating greater transparency and accountability. Furthermore, the article addresses challenges in the global implementation of Murabaha practices, including the lack of standardization, limited expertise, and inadequate regulatory frameworks. It proposes solutions such as developing international standards, enhancing training and expertise, strengthening regulatory frameworks, and promoting ethical sourcing and compliance. Additionally, the article highlights the need for standardized pricing benchmarks for Islamic financial products, including Murabaha. It suggests initiatives such as industry collaboration, regulatory frameworks for transparency, and research and development efforts to address this challenge. Overall, this study contributes to the growth, integrity, and harmonization of the Islamic finance industry, ensuring its alignment with Islamic principles and meeting the evolving needs of stakeholders.

CONCLUSION

Murabaha offers individuals and businesses an ethical alternative to interest-based financing in Islamic banking and finance. This journal article has provided practical recommendations for those considering Murabaha as a financing option. Understanding the underlying principles of Islamic finance, complying with Shariah guidelines, researching reputable institutions, comparing pricing and terms, understanding the risks, and seeking professional advice are essential for successfully navigating Murabaha transactions.

The proposal presented in this article focuses on enhancing the Shariah compliance of Murabaha financing. By strengthening the cost-plus-profit structure, increasing customer involvement, promoting ethical sourcing practices, and facilitating greater disclosure and accountability, Murabaha financing can align more closely with the principles of Shariah. Implementing these measures will enhance Murabaha transactions' authenticity and transparency, reinforcing Islamic finance's credibility and integrity.

However, the challenges faced in implementing Murabaha practices globally hinder the growth and stability of the Islamic finance industry. Lack of standardization, limited expertise, inadequate regulatory frameworks, and ethical compliance issues must be addressed. The proposed solutions of developing international standards, enhancing training and expertise, strengthening regulatory frameworks, and

promoting ethical sourcing and compliance can help Islamic banks improve their Murabaha practices. These solutions will contribute to the growth, integrity, and harmonization of the Islamic finance industry, aligning it further with Islamic principles and meeting the evolving needs of stakeholders.

One of the challenges Islamic banks face is the need for more reference benchmarks for pricing Islamic financial products, including Murabaha. However, the proposed solutions of developing standardized pricing benchmarks, fostering industry collaboration for data sharing, initiating regulatory frameworks for transparency and accountability, and promoting research and development can effectively address this issue. These solutions will enhance transparency, fairness, and market competitiveness in Murabaha practices, strengthening the credibility and stability of the Islamic finance industry.

In summary, Murabaha is a widely used financing technique that provides an ethical alternative to interest-based transactions in Islamic banking and finance. Individuals and businesses can navigate Murabaha transactions by understanding the underlying principles, complying with Shariah guidelines, researching reputable institutions, comparing pricing and terms, understanding the risks, and seeking professional advice. The proposed measures to enhance Shariah compliance, address industry challenges, and improve pricing benchmarks will contribute to the growth and integrity of the Islamic finance industry, ensuring its alignment with Islamic principles and meeting the needs of stakeholders.

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