
Empowering the Islamic Microfinance to Overcome Riba (Usury) based Economy

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Abstract. In order to have the success of economic policies to develop microenterprises and alleviate the problems of poverty in Indonesia over the past three decades, financing microenterprises was considered as an effective paradigm in the grass root economic sector and became the popular subject of study by a number of researchers in the past, particularly, after the proclamation of the year 2005 as the microfinance year by the United Nations (NU) and every July 12th is commemorated as the cooperative day in Indonesia. Therefore, this study aims to empower the Islamic microfinance system in order to overcome riba (usury) based economy in this country, besides to decrease the power of conventional banking and financial system, to abolish the moneylenders' system and to eradicate rural poverty and particularly to help Muslim micro entrepreneurs all over Indonesia. This article uses the library-based research method by analyzing relevant materials such as the Holy Quran, the Hadith, the traditional Islamic books and literatures, journals, academic textual materials as well as internet sources and afterwards followed by discussions based on Islamic law of financial transactions. As a result, the study found that the some of Islamic micro institutions such as Bayt Mal wa al-Tamwil (BMT) as a model of Islamic micro financial institution were problematic and not totally Islamic, although they are somewhat better, if compared to conventional products and services. The most reasonable arguments of the problem were derived from the operating system which is parallel to the conventional counterparts. Therefore, it is necessary to implement the pure Islamic microfinance products and services besides optimization of the Syarī'ah supervision (al-Raqabah Syar'iyyah) aspect. Currently, there are more than five thousand units of Islamic microfinance institutions scattered throughout the entire provinces and regions in Indonesia. Without efforts towards this direction, it will cause many problems and could affect the future of the Islamic microfinance institutions in Indonesia.

Keywords: Empowering, Islamic Microfinance, Riba (Usury), Syari'ah economy.

1. INTRODUCTION

In the last few years, microfinance has become one of the most popular strategies for developing microenterprise in developing countries. The establishment of microfinance institutions that can serve the needs of

micro entrepreneurs in obtaining fund is necessary. This fund is required to give them an opportunity to develop their business and enhance their quality of life. Professor mohammed yunus in bangladesh has become a leading figure in microfinance today. He successfully established the “grameen bank” or “village bank” which he has been striving to establish since 1976. This bank was founded on the principles of trust and solidarity to help the rural poor and lower income groups in running micro-businesses by offering them small loans, especially to poor women. This success has attracted the attention of the world to follow in his steps and he earned a nobel peace prize on 13 october 2006 as a result of his commitment and struggle. Moreover, the united nations (un) determined that the year 2005 should be the “international year of microfinance” [1].

Mohammed yunus [2] clarifies the definition of microfinance as “a kind of small financing and services based on the premise of solidarity, where the poor have skills which remain unutilized or underutilized. It is definitely not because of lack of skills which made poor people poor but charity is not the answer to poverty. It only helps poverty to be continued. It creates dependency and takes away the individual’s initiative to break through the wall of poverty. Unleashing of energy and creativity in each human being is the answer to eradicating poverty”.

The united nation (un)’s international labor organization (ilo) no. 57 act [none] on cooperative management and administration (geneva, report vii (1), 1964) defines microfinance as “ an association of persons, usually of limited means and small scales, who have voluntarily joined together to achieve a common economic end and through the formation of a democratically controlled business organization, making equitable contribution to the capital required and accepting a fair share of the risk and benefits of the undertaking”.

In this respect, besides refusing the conventional basis of accesses of the poor to financial services through riba based economy, many areas of commonality between conventional microfinance and the islamic microfinance could be pointed out. However, the islamic approach puts overwhelming emphasis on microenterprise development through financial and non-financial assistance and adherence to principles of transparency, empathy, cooperation, islamic ethics relating to aspects such as products and services, syarī’ah compliance, etc.

Ajaz ahmed khan [3], asserts the above definitions by saying that the different islamic lending methodologies which tend to be far more interesting and complex than techniques used in conventional “western” lending which largely rely on charging interest. The basic principles and practices upon which islamic financing is based date back to the early part of the seventh century-it is certainly not a new phenomenon.

Based on previous definitions, it may be noted here that islamic microfinance is a system or concept regarding the islamic modes of financing and services on a small scale such as, micro savings, micro equity, micro credit and micro insurance, provided that the islamic microfinance institutions should help the microentrepreneurs or poor households, especially if they are muslims, so that they can manage and improve their financial resources more effectively. Islamic microfinance is guided by the teachings of islamic law of financial transactions (fiqh al-mu’amalat al-maliyyah) and islamic ethics (al-akhlaq al-islamiyyah).

The objectives of this study are to define the terminology and verify the characteristics of islamic microfinance and conventional system. Furthermore, to empower the pure islamic microfinance institutions for the economic policies of the country in developing microenterprises and alleviating the problems of poverty especially in indonesia. Significance of the study will help islamic microfinance institutions all over indonesia to improve their performance and insure their products and services are in line with syari’ah islamiyyah. Moreover, it will contribute to integrate the islamic financial system in the scale of micro-finance as grass roots economy to overcome riba (usury) based economy.

2. MATERIALS AND METHODS

This article uses the library-based research method by analyzing relevant materials such as the Holy Quran, the Hadith, the traditional Islamic books and literatures, journals, academic textual materials as well as internet sources and followed by discussion based on Islamic law of financial transactions.

3. LITERATURE REVIEW

Microfinance and Islamic microfinance sector has been the spectacular subject of study by a number of researchers in the past. Most of previous studies were done in the 2000s, particularly after the labeling of the year 2005 as the Year of Microfinance by the United Nations (UN) and the awarding of the noble peace prize for the year 2006 to Professor Dr. Muhammad Yunus from Bangladesh as the Father of Micro Finance. This success indicates the growing importance accorded to microfinance as a tool of poverty alleviation and strategy to develop micro enterprises in developing countries.

These studies have covered topics like poverty alleviation, social solidarity and responsibility through the performance of microfinance. Important ones of these studies are conducted by Akhyar Adnan et al. [4]; Badru el-Din [5]; Ahmed [6]; Siswantoro [7]; Seibel [8]; Wahyuni [9]; Widiyanto [10]; and Obaidullah [11];

These studies merely focus on the performance of conventional micro finance system in poverty alleviation, social solidarity and responsibility. Some other studies focus on education and spirituality training for micro entrepreneurs, such as what are done by Mardhatillah and Rulindo [12]; and Waspodo [13]. A third group of studies has focused on models of microfinance institutions, such as what are performed by al-Asad [None]; Ahmed [3]; and Faruq Ahmad and Rafique Ahmad [14].

Lastly, some studies also were performed to highlight the role of government towards development of microfinance institutions in the country, such as what are accomplished by Muhtada [15]; and Siswantoro [16]. However, even though these studies were performed in the past, they were not focused on the topic of empowering pure Islamic microfinance institutions to overcome riba (usury) base economy.

4. RESULTS AND DISCUSSION

4.1 Characteristics And Structure Of Microfinance And Islamic Microfinance

In this section, we discuss the characteristics and structure of microfinance from the conventional microfinance point of view as well as the Islamic microfinance point of view as both share common basic principles and structures but sometimes differ in objectives. Al-Baltaji [17] has broadly identified five characteristics of microfinance system. They are as follows:

- i. The standard numbers of workers. Many countries have agreed on the identification of microfinance in accordance with the number of employees in each country. For example, Indonesia has identified small enterprises which do not exceed 20 workers. Japan and Korea set the number as 30 workers. Sudan has set the number of workers as 25 or less. Saudi Arabia set the number of workers less than 25. However, Western countries have set large numbers of maximum workers, such as 250 workers in United States of America (USA), 50 workers in Belgium and 200 workers in United Kingdom (UK).
- ii. The standard capital size of microfinance. The size of capital invested for quantitative criteria used in the identification of microfinance or small-sized enterprises, in addition to the value of fixed assets of the debtors, differs from one state to another, according to the economic development policies of each state. For example, in Egypt, the limit for microenterprises (without land and building) approximately is L.E. 700 thousand. This was classified by the General Authority for Industrialization in Egypt. As for Indonesia, the standard capital size of microfinance or small-sized enterprises is IDR 5 million (not including land and building).
- iii. The standard value of annual sales. Microfinance institutions use some criteria of the sales' value of enterprises with low volume of their production in terms of quantity and value, linked to local markets and their inability to market their products to international markets. Each country is different in estimating the volume of sales which are classified as small businesses. In Saudi Arabia for example, the annual sales of less than 3 million Riyals are classified as micro. In America, the figure is less than USD 1 million. Therefore, the identification of this standard depends on the circumstances of each country.
- iv. The quality of the technology used. In most cases, the use of advanced technology may lead to a reduction in employment and invested capital values, in the sense that small enterprises generally use modest technology in accordance with the investor.
- v. The legality standard of microfinance. The legal standard of microfinance depends on the legal nature of an enterprise such as the nature and magnitude of the capital invested in it and mode of their funding. According to this criterion, microfinance institutions are often founded with small installations according to the scope of individual business, family and solidarity with a simple recommendation.

Obaidullah [11] clarifies that one of the distinct characteristics of microfinance, that makes it more specialized components in economics and financial system today is the alternative approach to collateral that comes from the concept of joint liability or solidarity based on lending group scheme. He says:

Good microfinance programs are characterized by small, usually short-term loans; streamlined, simplified borrower and investment appraisal; quick disbursement of repeat loans after timely repayment; and convenient location and timing of services. Microfinance institutions thus have distinct characteristics that make them specialized components of the financial system. The main point of departure of microfinance from mainstream finance systems is its alternative approach to collateral that comes from the concept of joint liability. In this concept, individuals come

together to form small groups and apply for financing. Members of these small groups are trained regarding the basic elements of the financing and the requirements they will have to fulfill in order to continue to have access to funding. Funds are disbursed to individuals within the group after they are approved by other members in the group. Repayment of the financing is a shared responsibility of all of the group's members. In other word they share the risk. If one defaults, the entire group's members face a setback. This is a basic but effectual credit scoring mechanism that may mean a provisional suspension from the program and therefore no access to financing for the group or other penalties. In most cases, microfinance programs are structured to give credit in small amounts and require repayment at weekly intervals and within a short time period- usually a month or a few months. The beneficiary looks forward to repetitive financing in a graduated manner and this also helps mitigate risk of default and delinquency.

The model that has popularized the above methodology and has been replicated in many countries in a wide variety of settings is the Grameen Bank model. The model requires careful targeting of the poor through means tests comprising mostly of women group. The model requires intensive fieldwork by staff to motivate and supervise the borrower groups. Groups normally consist of five members, who guarantee each other's loans. A number of variants of the model exist, but the key feature of the model is group-based and graduated financing that substitute collateral as a tool to mitigate default and delinquency risk [11].

Figure 1.1 below describes the structure of group lending scheme of joint liability or solidarity formed by the Grameen Bank of Bangladesh since it is successful foundation in 1976, and today it is adopted by many microfinance institutions and Islamic microfinance institutions across the world.

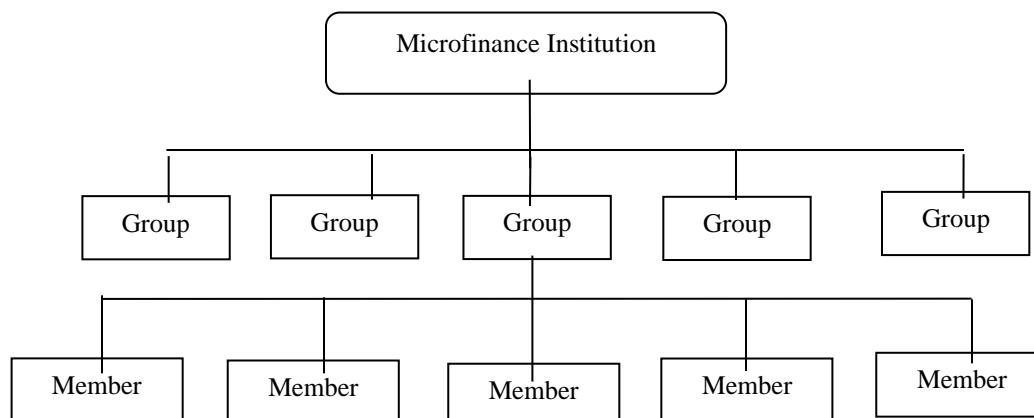


Figure 1. Grameen Bank's Structure of Solidarity Group Lending Scheme
Sources: Habib Ahmed [6], Islamic Approaches for Microfinancing Concepts, 60.

In implementing the above scheme, Mohammed Obaidullah and Thariqullah Khan [18] clarify:

In this concept, individuals come together to form small groups and apply for financing. Members of these small groups are trained regarding the basic elements of the financing and the requirements they will have to fulfill in order to continue to have access to funding. Funds are disbursed to individuals within the group after they are approved by other members in the group. Repayment of the financing is a shared responsibility of all of the group's members. In other words, they share the risk. If one defaults, the entire group's members face set back. This is a basic but effectual credit scoring mechanism that may mean a provisional suspension from the program and therefore no access to financing for the group or other penalties.

Ahmed Khan [3], furthermore, asserts that the above concept of lending scheme solidarity structure formed by Grameen Bank in Bangladesh has widely adopted by many microfinance institutions throughout the world, such as Asia, Africa and Latin America, with several following reasons:

- i. Peer monitoring
The ability of borrowers to monitor the investment behaviour of one another during the course of a loan makes sure that each borrower only undertakes safe investment projects with the borrowed money.
- ii. Social ties
The social cohesion that exists in some communities means that the sanctions that a borrower would receive from the group for defaulting results in each member wanting to repay faithfully.
- iii. Group pressure

The group pressure between borrowers to repay means that group can be expelled as none members if they default, thus, excluding them from continued access to credit.

However, a critique of group lending scheme mentioned above was raised by Rahman [19]. He claims that perhaps it is difficult to promote group lending scheme in regions where social ties are not necessarily high because many entrepreneurs are individualistic. He also doubts that they like working in groups and they may also compete with each other and be unwilling to share confidential information with potential competitors.

Mannan [1] asserts that the Grameen Bank has charged the borrowers a high interest rate of up to 54.95 percent per annum, if the hidden cost for documentation of membership fees and obligatory provision for blocked amounts are taken into consideration. Since non-reducing method of accounting is applied in case of the repayment of loan installments, this raises the interest rate by an additional 31.46 percent, pushing the total interest rate to a whopping 86.41 percent.

Definitely, this is clearly exploitative and cannot be justified by higher monitoring costs and other rational factors. Although Bangladesh is a predominately Muslim country, the Grameen Bank is not a Syari'ah compliant institution as it charges interest (riba) on its loans and pays interest to depositors, such as interest for income generating basic loans is 20 percent, whole housing loans are charged at 8 percent and higher, education loans at 5 percent, implying a degree of cross subsidy, savings rates vary from 8.5 to 12 percent depending on the category and size of deposit [1]

4.2 Foundation of Islamic Microfinance

As mentioned earlier, all Islamic financial systems including Islamic microfinancial system was founded on the religious philosophy, i.e. Achievement of al-falah (success) in the worldly life and more importantly, in the Hereafter. Therefore, Islamic commercial law strongly promotes the principles of cooperation (al-musharakah), justice (al-cadl), magnanimity (al-ihsan) and trust (al-amanah) to ensure the property will not be placed in jeopardy through unfair dealings and totally disallows usury (riba), gambling (maysir), hoarding (ihtikar), ambiguity to one party or both parties (gharar) and other forms of exploitation that will make financial transactions invalid and prohibited.

With respect to the foundation of Islamic microfinance, Rowey, et al [20] clarified that:

Islamic microfinance was founded on principles of the Islamic law of financial transactions (fiqh al-mu'amalat al-maliyyah). The basic sources of these principles are the Qur'an and Sunnah, which are followed by the consensus of the Muslim jurists (Ijma' al-'ulama'). The central characteristic or feature of Islamic microfinance and all Islamic financial systems is the prohibition of the payment and receipt of interest (riba). The strong disapproval of interest by Islam and its vital role in modern financial markets, such as microfinancial institutions and banking system have led Muslim thinkers to explore many ways and means to gain the goal of interest-free bases of economy and financial systems.

Regarding the prohibition of the payment and receipt of interest (riba) as the vital prohibition in Islamic microfinance and all Islamic financial systems, Archer and Ahmed [6] stated:

The Interest (riba) is banned in Islam because a pure return of rent on money is considered to be immoral. To be entitled for a return, a provider of finance must either undertake business risk or provide some other services, such as supplying an asset; otherwise, the financier is, from Syari'ah point of view, not only an economic parasite but a sinner.

In addition, Akhyar Adnan [21] argued that prohibition of interest (riba) is simply, because it unjust (zulm). In the last part of the Qur'an (al-Baqarah: 297), Allah s.w.t says: "Deal not unjustly (by asking more than your capital sums), and (you) shall not be dealt with unjustly (by receiving less than your capital sums)." Likewise, Rosly [22] emphasis added, that riba is condemned in Islam because it constitutes wealth created at the expense of other people's wealth. Doing so is unjust (zulm).

The above arguments would seem to be an adequate overview of Islamic principle in the prohibition of interest (riba). The appearance of this prohibition in the Qur'an is also relatively frequent. There are four verses relating to usury or riba (interest) in the Qur'an. This indicates how important, clear and final prohibition of usury or riba in the Qur'anic view.

Besides prohibition of interest (riba), as mentioned earlier, Islam strongly emphasizes the efficient manner to produce maximum output and to fulfill Allah's plan of establishing prosperity in this world and achieving of al-falah

(success) in the Hereafter. In this aspect, Siddiqi [23], stated that Islamic law of financial transactions (fiqh al-mu'amalat al-maliyyah) emphasizes the Islamic attitude to achieve the objectives of wealth creations and economic activities among Muslims, especially to those who are involved in economic activities. Therefore, the Holy Qur'an and Sunnah have given specific guidelines as follows:

- a. Islam looks first at the wealth as a life sustaining vehicle, to be used efficiently and gained from halal (pure) sources.
- b. Private ownership is affirmed but viewed as a trust (amanah).
- c. Islam encourages enterprises, efforts to create wealth, which have been characterized as Allah s.w.t.'s bounty.
- d. All Muslims are obligated to fulfill contracts and keep their promises.
- e. All exchanges should be with willing consent of the parties concerned.
- f. The use of wealth and exercise of freedom of enterprise are constrained by the Obligation not to harm others.

Based on the previous points of view, it has been shown that Islam consists not only of ritual activities, but containing a comprehensive guide for life. It is a total way of life. It provides all kinds of norms and philosophical spiritual that might be applied by people wishing to achieve al-falah (success), in the world and more importantly in the Hereafter. The concept of secularism and socialism has no place in Islam. That is way, any activities included in the microfinance activities must be founded on divine revelations

4.3 Historical Development of Microfinance and Islamic Microfinance

No one knows for sure when the microfinance concept of business in the world began. However, some economists said that the philosophy or concept of microfinance is not new. Micro savings, credit groups and micro insurance activities have been operating for centuries in several countries under many different terms, such as "Koperasi" in Indonesia, Malaysia and Brunei Darussalam; "Tontines" in the West of Africa and "Pasanaku" in Bolivia as well as numerous micro savings groups, entrepreneurs and burial societies all over the world [1].

According to University of Gadjah Mada [UGM] Research Team [24], the origin and the development of microfinance concept in the world have essentially driven by the issues of poverty based on the capitalistic economic system. The existence of microfinance system in a country is very important tool to break the wall of poverty as a result of the capitalistic economic system. Therefore, the first microfinance organization which was born in England [25] to solve the problem of daily needs of its members by way of togetherness based on the basic principles of justice, trust, unity and responsibility, known as "Rochdale Principles". Within a short time, in France some microfinance institutions have also been established, which engaged in the productions [26].

As we have alluded before that, Indonesia has a long and earlier differentiated microfinance sector among developing countries in Asia. This sector in Indonesia has evolved more than one century ago, such as Schulze-Delitzsch [27], Syirkah al-cInan [28], Volkscredit Wezen [29], Serikat Dagang Islam [30], and Budi Utomo Foundation [31]. Masngudi [32] has discussed broadly the historical origin and development of microfinance sectors in Indonesia. He has found in his study that the movement of microfinance sectors in Indonesia, actually, was born in the late nineteenth century [33]. At that time, Indonesia was under the Dutch colonization. Therefore, the microfinance climate was not favorable for the country and its people. After the Indonesian independence in 1945, Mohammad Hatta, was known as "The pioneer of Indonesian microfinance", put microfinance formula in the Indonesian Law of Constitution or Undang-Undang Dasar (UUD) 1945, Article (33).

Since that time, the growth of microfinance sectors in Indonesia had better growth and rapid development. The emergence of microfinance in Indonesia was became a reflection of a strong desire and commitment of the Indonesian people in promoting financial products and services in the micro scales. Likewise, there was government was committed in establishing and advocating various types of micro finance institutions and disseminating knowledge about it among the people of Indonesia [34].

Subsequently, Ahmad Djazuli [35] said that the other most important development of microfinance sectors in Indonesia that attracts the highest attention was the establishment of the Islamic microfinance in 1990. The development of Islamic microfinance has been paralleled by Islamic banking, known as Bank Mu'amalat Indonesia (BMI). In the same time, Ridho Gusti Cooperative in Bandung (East Java) has the distinction of being the first Islamic microfinance institution in Indonesia, which has launched an Islamic microfinance products and services based on Islamic law of financial transactions (fiqh al-mu'amalat al-maliyyah).

After 1995, when PINBUK has started in promoting a model of Islamic microfinance institutions all over Indonesia under the new name, i.e. Bayt al-Mal wa al-Tamwil (BMT) institution, their number evolved in four stages of growth and development, namely: (1) an initial period of moderate growth up to 1995; (2) the promotion of rapid

growth by PINBUK starting from 1995, with big jumps in numbers during the economic and politic crisis situation in 1997 and 1998; (3) a slowing-down of growth during 2000 and followed by stagnation; (4) then after year 2000, they continued with big jumps and development [36]

See table 1.1 below regarding the evolution of Islamic microfinance such as BMT institutions in Indonesia

Table 1. The Evolution of Islamic Microfinance of BMT Institutions in Indonesia

Phase of Growth & Development	Periods of BMT Institution	Number of BMT Institutions
Initial growth	1990-1995	300
Rapid growth (beginning promoted by PINBUK)	1996	700
	1997	1,501
	1998 (June)	2,470
Slowing down of growth	2000	2,938
Slowing down and stagnation	2001	3,037
	2003	2,856
Rapid growth (promoted by PINBUK, Ministry Cooperative & SMEs)	2010-2024	4,500

Source: Seibel [37], Islamic Microfinance in Indonesia, 93 [38]

Kholis [39] has clarified that Bayt al-Mal wa al-Tamwil (BMT) is an Islamic microfinance institution, established by Muslim society in Indonesia. It takes initiatives to help micro entrepreneurs as a strategy for eradicating rural poverty especially in villages or traditional markets. It is operationally based on Syarī'ah principles and Islamic values. Nowadays, BMT institutions are emerged among the Indonesian society because of some rational reasons, such as: (1) there are more than 43,22 million of micro entrepreneurs in Indonesia; (2) there are just a few Islamic banks having good attention and willingness to provide credit or financing schemes for micro entrepreneurs.

According to Seibel [40], the establishment of PINBUK was encouraged by the harsh reality of the economic positions of Muslims due to the policy of the new era called "Orde Baru (ORBA)" during 32 years of President Suharto regime that was in favor of the conglomerates. PINBUK aims to realize the Islamic microfinance sector as the most fundamental issue for small enterprises to be empowered. Therefore, PINBUK set up as much as possible of BMT institutions in all parts of the country with the expectation to help the entire local communities, especially the Muslim entrepreneurs. The presence of BMT institutions in many villages and towns all over Indonesia has brought better local economic development in the country, such as agriculture, animal husbandry, trade, crafts people and other informal economic growth.

As of the end of 2010, around 4000 BMT institutions were spread in 36 provinces from Sabang (Aceh) to Merauke (Irian Barat) and registered at PINBUK. The achievement of BMT institutions, however, is still considered small in numbers, compared to the capital needs of businesses, markets and other sectors surrounding the 39.5 million of small enterprises across the country. If each BMT institution could finance about 200 small entrepreneurs on average, the number of BMT institutions need to be established for 39.5 million small enterprises is 197, 500 BMT institutions [41].

Thus, the development of BMT institutions can be deemed as an alternative economic system in the country, with the expectation of serious attention from the government and all societies, especially Muslims, in order to encourage faster growth of BMT institutions in the midst of society

4.4 Finding and Recommendation

Finally, after analyzing relevant material discussion conducted for this study leads to the following conclusions:

- a. Islamic microfinance can be defined as a system or concept regarding the islamic modes of financing and services on a small scale such as micro savings, micro equity, micro credit and micro insurance, etc., provided by the islamic microfinance institutions to help the micro entrepreneurs or poor households, especially muslims, so that they can manage and improve their financial resources more effectively. Islamic microfinance is guided by the teachings of the islamic law of financial transactions (fiqh al-mu'amalat al-maliyyah) and islamic ethics (al-akhlaq al-islamiyyah).
- b. There are some important similarities between islamic microfinance institutions and conventional ones, namely: (1) both advocate entrepreneurship, profit and risk sharing; (2) both believe that the poor should take part in such activities, and developmental and social goals; (3) both function as institutions which offer particular services, such as micro credit, micro equity, micro savings, micro transfers, micro insurance and so forth. These similarities, however, are too broad and too superficial to be regarded as an argument to equate both types of microfinance institutions.
- c. Although the basic format of islamic microfinance is similar and related to its conventional microfinance counterpart, but there are certain qualitative differences between them, namely: (1) islamic microfinance system emphasizes ethical or moral, social and religious factors to promote equality and fairness for the welfare of society as a whole; (2) it encourages profits and risk sharing, individual rights and duties, property rights; (3) the syar'i'ah compliance aspect and the sanctity of contracts are part of the islamic code that underlies the islamic financial system.
- d. There are many kinds of prohibited contracts in islam besides riba (usury), and almost all of them involve prohibited sales. The reasons of prohibiting these sales go back to the capacity of the parties, the format of the contract, and some legal description or the subject of the contract. These kinds of contract can be identified in many books of fiqh mu'amalat maliyyah (islamic law on financial transactions). However, the essential elements of syar'i'ah compliance and relevant norms for islamic microfinance in general, namely: the prohibition of usury (riba), uncertainty (gharar), hoarding (ihtikar), gambling (maysir) and other constraining norms in islamic microfinance, such as, unmandated sale (bay'fuduli), fraudulent overbidding (najash), sale of haram (prohibited) articles, alcoholic drinks and unjust brokerage.
- e. This study dictates that the majority of islamic microfinance institutions in indonesia attempt to use the islamic micro financial system and apply islamic corporate culture, morality and faith, and at the same time bring much benefit to their customers and employees. However, the survey found that some products and services are not in line with syar'i'ah principles and values, although the percentages are relatively small. Overall, it can be said that the products and services of islamic micro financial institution are not totally islamic although in a sense that they are so much better if compared to conventional products.
- f. One of the main aspects that differentiate the islamic from the conventional financial institutions is the syar'i'ah supervision (al-raqabah shar'iyyah) aspect. In indonesia, all islamic financial institutions whether banking institutions or non-banking institutions are required to have ssb members in their organizational structures as the extension of the national syar'i'ah board or dewan syari'ah nasional of majelis ulama' indonesia (dsn-mui) to ensure all products and services comply to shari'ah islamiyyah

5. CONCLUSION

Interest (riba) or usury becomes the most important concept in conventional microfinance system is totally avoided by Islamic microfinance besides other prohibited elements. Islamic microfinance institutions adopt the Islamic economic values or ethics. This particular difference has led to many other differences in products and services, organizational structure and management of the microfinance institutions, the customer groups and even to some extent in microfinance theory and practices. In respect to the foundation of Islamic economics and financial theory, it seems that different authors set different formula because this system is strongly based on the basic principles of tawhid (sovereignty), rabbaniyyat al-masdar wa al-hadif (divine source and objective), tazkiyyah (purification), ukhuwwah (brotherhood) and accountability.

However, a strong financial system needs to be supported by a strong regulatory and legal framework that can effectively discourage undue risk-taking behavior, particularly in the Islamic microfinance to prevent it from being harmful or disobeying Syari'ah commercial law. It must also have adequate standards for effective risk management, financial disclosure standards and governance. These are areas for development to bring Islamic microfinance to the

next level of exponential growth. Despite these challenges, the Islamic microfinance industry has grown to become available alternative for many, whether for reasons of personal faith or on economic grounds

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