DINASTI PUBLISHER
DIJDBM: Dinasti International Journal of Digital Business Management
E-ISSN: 2715-4203
P-ISSN: 2715-419X
https://dinastipub.org/DIJDBM dinasti.info@gmail.com +62 811 7404 455
DOI: https://doi.org/10.38035/dijdbm.v6i3

Sharia Bank Sharia Index

Dedy Sukmana[1*]
[1]Universitas Indonesia Maju, Jakarta Selatan, Indonesia, dedysukmana@uia.ac.id

*Corresponding Author: dedysukmana@uia.ac.id[1]

Abstract: This paper discusses the concept of the Shariah Index or Shariah Compliance Index for Islamic banks. The purpose of this index is to evaluate the extent to which these banks comply with the principles and practices of Shariah law, which governs all financial transactions in Islamic banking. This index is essential to ensure that Islamic banks provide financial products and services that are in accordance with the ethical and religious guidelines set by Islam. This paper explores the creation, development, and significance of the Shariah Compliance Index, including its impact on the financial performance, customer trust, and overall credibility of Islamic banking institutions.

Keywords: sharia index, sharia bank, banking, sharia

INTRODUCTION

Islamic banking refers to a banking system that operates in accordance with the principles of Sharia law, which prohibits activities considered haram (prohibited) such as charging or paying interest (riba), making speculative investments (maysir), and investing in businesses related to alcohol, gambling, and other unethical activities. As the Islamic finance industry grows globally, ensuring banks' compliance with Sharia principles is becoming increasingly important (Khan, 2010). One of the tools used to measure and verify this compliance is the Shariah Index or Shariah Compliance Index. This index helps stakeholders, including investors, regulators, and customers, to assess the level of Shariah compliance within a financial institution (Hassan & Sadaqat, 2011).

Shariah compliance in banking is more than simply avoiding interest-based transactions; it involves ensuring that all business practices, from financial products to customer relationships, are in accordance with Islamic ethical principles (Wilson, 2009). Key features of Shariah-compliant Islamic banking include:

1. **Prohibition of Usury (Interest)**
   Islamic banks do not engage in interest-based lending and borrowing activities, which are the core of the conventional banking system.
2. **Prohibition of Gharar (Uncertainty)**
   Transactions must be free from excessive uncertainty or ambiguity.
3. **Prohibition of Maysir (Speculation)**
   Gambling and highly speculative transactions are prohibited in Islamic finance.

4. **Halal Investment**
   Islamic banks are required to invest only in businesses and assets that do not violate Islamic principles, such as businesses that sell alcohol or engage in unethical practices.

The Importance of the Sharia Compliance Index

The development of the Sharia Index is very important for several reasons Islamic Financial Services Board (IFSB, 2020):

1. **Ensuring Integrity and Trust**
   An index provides a benchmark for evaluating the authenticity of a bank's Sharia compliance (Todorof, 2018). This builds customer trust and strengthens the reputation of Islamic banks.
2. **Guide for Investors and Regulators**
   Investors, especially those following ethical investment guidelines, need a reliable way to determine whether a bank operates in accordance with Sharia principles (Ahmed, 2014). Regulators can use this index to monitor compliance with relevant laws and standards.
3. **Driving Industrial Growth**
   The Shariah Compliance Index encourages competition among banks to improve their compliance with Shariah principles, which in turn promotes transparency and efficiency in the Islamic banking sector (Malini, 2020).

Several global initiatives aim to measure and track Sharia compliance in Islamic banks (Jamshed & Uluyol, 2024). Notable examples include:

1. **Dow Jones Islamic Market Index (DJIM)**
   This index evaluates and records companies that comply with Sharia law (Kulmie & Omar 2024). A similar index also exists for Islamic banks, allowing investors to choose Sharia-compliant financial institutions.
2. **FTSE Shariah Global Equity Index Series**
   This index includes Sharia-compliant stocks and funds, helping investors to identify companies and banks that meet Sharia standards (Putra & Nurdiantoro, 2024).

In some countries, such as Malaysia and Bahrain, Islamic banks are required by law to maintain a minimum level of Sharia compliance, with regular audits conducted by an independent body.

METHOD

This study uses a descriptive qualitative approach that aims to develop and formulate a Sharia Compliance Index framework for Islamic banks. Data were obtained through literature studies from academic sources, regulatory reports, and international practices and standards related to Sharia compliance in banking (Kurniawati & Fernando, 2024). The methodological process is carried out in several stages:

1. **Identify Critical Components**
   Fundamental aspects of Islamic banking operations are analyzed, including the Sharia governance structure, product and service compliance, Sharia audit processes, and public information disclosure (Mulazid et al., 2024).
2. **Formulation of Indicators**
   The indicators used in the index include: the existence and effectiveness of the Sharia Supervisory Board (DPS), frequency and results of Sharia audits, product compliance scores, and the level of transparency of reporting to the public (Rehan et al., 2024).
3. **Index Model Construction**

The index is designed as a combination of quantitative and qualitative measures that produce a percentage compliance score. The model also considers ESG (Environmental, Social, Governance) dimensions in the context of Islamic finance (Islam, 2024).

4. **Global Comparative Study**
   Examples of global Shariah compliance indices such as the Dow Jones Islamic Market Index and the FTSE Shariah Index are used as references to develop a locally relevant yet internationally adaptive framework.

To develop the Sharia Index, several factors need to be considered (Alam & Miah, 2024):

1. **Sharia Governance Structure**
   This includes the existence of a Sharia Supervisory Board (SSB) within the bank which ensures that all products and services comply with Islamic law.
2. **Compliance with Sharia Principles in Products and Services**
   Banks need to review their financial products, ensuring that they do not involve interest or unethical business practices.
3. **Sharia Audit**
   Regular audits conducted by independent Sharia scholars to verify compliance and address potential issues.
4. **Transparency and Reporting**
   Banks must disclose information related to their Shariah compliance processes and products to the public, which promotes accountability.

This index may include qualitative and quantitative measures (Minaryanti & Mihajat, 2024), such as:

1. **Compliance Score**
   Percentage score representing the level of compliance with Sharia principles in various areas.
2. **Audit Findings**
   Frequency and results of Sharia audits conducted within the bank.
3. **Involvement of the Sharia Board**
   Assessment of the effectiveness and qualifications of the Sharia Supervisory Board.

RESULTS AND DISCUSSION

The analysis resulted in four main pillars in measuring Sharia compliance:

1. **Sharia Governance**
   The existence of an independent and competent DPS is crucial in assessing the bank's commitment to Sharia principles.
2. **Product Compliance**
   Financial products and services must be free from usury, gharar and maysir elements and must be oriented towards halal activities.
3. **Shariah Audit and Review**
   Internal and external audits conducted periodically by Sharia scholars provide validation of the implementation of Sharia principles.
4. **Transparency and Reporting**
   Banks that provide regular Sharia compliance reports demonstrate a commitment to public accountability.

One of the main challenges in implementing an index is the difference in interpretation between schools of thought and the absence of an agreed global standard. This creates methodological variations that make it difficult to compare banks across countries. The implementation of an index encourages healthy competition among financial institutions to improve integrity and efficiency. Investors can use the index as a reference in choosing banks that meet ethical investment principles, while regulators can use it as a monitoring tool. Technologies such as blockchain can be used to create a transparent and non-manipulated Sharia reporting system. Artificial intelligence can also be applied for automated analysis of bank transactions and policies. The integration of ESG in the index will expand the meaning of Sharia compliance to not only normative but also sustainable.

CONCLUSION

Sharia Index or Shariah Compliance Index plays a very important role in the Islamic banking industry by providing a clear and measurable way to assess compliance with Islamic principles. It serves as a tool to enhance transparency, trust and ethical business practices within the industry. While challenges remain in developing a universal standard for Shariah compliance, continued efforts to refine and implement such an index will help promote growth, trust and sustainability in the global Islamic financial market.

The future of Islamic banking lies in developing transparent and effective mechanisms to ensure Shariah compliance. As demand for ethical and sustainable finance increases, there is potential to expand the Shariah Compliance Index to include a more comprehensive assessment that includes environmental, social and governance (ESG) factors as well. In addition, technological advances, such as blockchain and artificial intelligence, can help streamline the Shariah compliance audit and monitoring process, making it more efficient and reliable.

Despite its importance, there are challenges in creating and implementing the Sharia Index, including:

1. **Differences in Interpretation of Sharia**
   Different schools of Islamic thought can have different interpretations of what constitutes Sharia compliance, leading to inconsistencies in how banks are evaluated.
2. **Lack of Standardization**
   Although several indices exist, there is no universally accepted standard for measuring Shariah compliance across the industry.
3. **Transparency Issues**
   Not all banks disclose their Shariah compliance measures or provide access to the data necessary to assess their compliance with Islamic principles.

REFERENCES

Ahmed, H. (2014). Islamic banking and shari'ah compliance: A product development perspective. Journal of Islamic finance, 3(2), 15-29.

Alam, MK, & Miah, MS (2024). Do Islamic banks use institutional theory in the light of Shariah governance? Empirical evidence from a Muslim dominant country. Heliyon, 10(2).

Hassan, M. K., & Sadaqat, M. (2011). Shariah Compliance in Islamic Banks. Journal of Islamic Economics, Banking, and Finance, 7(3), 5-21.

Islam, MT (2024). The Shari'ah Foundation of Islamic Banking. Dirasah International Journal of Islamic Studies, 2(1), 36-67.

Islamic Financial Services Board (IFSB). (2020). Shariah Governance Framework for Islamic Financial Institutions. Kuala Lumpur: IFSB.

Jamshed, K. M., & Uluyol, B. (2024). What drives to adopt Islamic banking products and services: is it shariah compliance or convenience?. Journal of Islamic Marketing, 15(11), 2891-2915.

Khan, F. (2010). Islamic Banking: What It Is and What It Could Be. International Journal of Middle East Studies, 42(2), 305-320.
Kulmie, D.A., & Omar, M.M. (2024). The impact of participatory Islamic finance on Shari'ah banks' profitability. Asian Economic and Financial Review, 14(7), 482.
Kurniawati, DT, & Fernando, Y. (2024). Financial technology readiness for Shariah-compliant banking services: post-merger perspectives. Journal of Islamic Marketing, 15(6), 1651-1671.
Malini, H. (2020). Determinants of Shariah Banking Performances in Indonesia Through the Perspective of Economic and Social Level. Journal of Business Economics and Entrepreneurship, 9(1), 47-57.
Minaryanti, AA, & Mihajat, MIS (2024). A systematic literature review on the role of sharia governance in improving financial performance in sharia banking. Journal of Islamic Accounting and Business Research, 15(4), 553-568.
Mulazid, AS, Saharuddin, D., Muttaqien, MK, Wicaksono, ATS, Fatmawati, F., & Fauzan, F. (2024). Determinants for acceptance and use of shariah banking digital services in Indonesia: Applying UTAUT 3, trust, and shariah compliance. Journal of King Abdulaziz University: Islamic Economics, 32(1), 55-77.
Putra, DA, & Nurdiantoro, AA (2024). Determinant Profitability of The Islamic Banking Industry in Indonesia: Literature Review. Journal of Accounting, 14(2), 171-180.
Rehan, R., Khan, M.A., Fu, G.H., Sa'ad, A.A., & Irshad, A. (2024). The determinants of Shariah banks' capital structure. International Journal of Economics and Financial Issues, 14(5), 193-202.
Todorof, M. (2018, August). Shariah-compliant FinTech in the banking industry. In Forum Era (Vol. 19, No. 1, pp. 1-17). Berlin/Heidelberg: Springer Berlin Heidelberg.
Wilson, R. (2009). Shariah Compliance in Islamic Banking. Journal of Islamic Finance, 1(1), 13-25.