

**PRODUCT INNOVATION OF ISLAMIC FINANCIAL
INSTITUTIONS IN THE PERSPECTIVE OF SHARIA ECONOMIC
LAW**

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Abstract

Product innovation in Islamic financial institutions has become a must in the face of evolving global market dynamics. This article explores the views of Islamic economic law on product innovation with the aim of revealing the key role of Islamic economic law in designing, implementing, and regulating innovative Islamic financial products. Basic concepts of Islamic economic law, such as the prohibition of usury, the prohibition of maysir and gharar, as well as the principle of zakat, play a central role in shaping the framework of Islamic product innovation. However, the product innovation of Islamic financial institutions is also faced with a number of challenges and controversies, such as legal considerations, supervision, and ethical issues. This article considers these challenges and proposes possible solutions to overcome them. By combining the perspective of Islamic economic law with the innovation of Islamic financial products, this article provides in-depth insight into how these products can develop in accordance with Islamic principles, as well as their impact on the development of the Islamic economy more broadly.

Keywords: *Sharia Economic Law; Product Innovation; Islamic Financial Institutions*

1 Introduction

Innovation plays a crucial role in the development of Islamic financial institutions and the Islamic economy. In the face of evolving market demands, Islamic financial institutions must continue to innovate to meet customer needs and expectations, as well as maintain their competitive advantage (Tatiana et al., 2015).

By innovating, Islamic financial institutions can create products that are more in line with sharia principles, provide more inclusive financial solutions, and increase accessibility for the community. Innovation in Islamic financial institutions encourage the development of more sophisticated and efficient technology.

Innovation enables Islamic financial institutions to develop unique and innovative products and services. By combining Islamic principles with new technologies and business strategies, Islamic financial institutions can create products that are attractive and different from conventional financial institutions. For example, Islamic banking products such as sharia microfinancing, sukuk, and sharia insurance are the result of innovations that bring benefits to the community.

Innovation can help build the trust and reputation of Islamic financial institutions in the eyes of the public. By continuing to innovate, Islamic financial institutions can demonstrate their commitment to providing financial solutions that comply with sharia principles, as well as maintaining integrity and transparency in their operations. This will strengthen public and investor confidence in Islamic financial institutions, as well as encourage overall Islamic economic growth (Aladağ, 2023).

In order to meet market demands and develop the Islamic economy, innovation is an important factor that cannot be ignored by Islamic financial institutions. Through innovation, Islamic financial institutions can present financial solutions that are more inclusive, efficient, and in accordance with sharia principles, thus having a positive impact on the development of the Islamic economy at large.

The development of the Islamic economy globally and regionally has experienced significant growth in recent decades. The global Islamic economic market has experienced rapid growth. Countries with a majority Muslim population such as Indonesia, Malaysia, the United Arab Emirates, and Saudi Arabia are the centers of Islamic economic growth. In addition, non-Muslim countries such as the United Kingdom, Singapore, and Japan have also begun to develop Islamic economic initiatives to attract investment from this market. The Islamic finance industry is one of the main sectors in the global Islamic economy. Islamic banks, sharia insurance companies, and sharia capital markets are growing and offering products and services that are in accordance with sharia principles (Nugroho, 2021).

This growth is driven by the increasing demand of Muslim communities seeking financial solutions that are in accordance with their faith. The development of global Islamic economic infrastructure is an important focus. Islamic financial institutions and the government work together to establish regulations and frameworks that facilitate the development of the Islamic financial industry. In addition, education and training institutions also play an important role in producing a qualified workforce in the field of Islamic economics (Ahmed, 2014).

2 IMPLEMENTATION METHODS

The writing of this article adopts the method of literature research by collecting and analyzing relevant documents such as books, scientific papers and papers and journals related to the Islamic economic system. The steps carried out in this Literature Study method are reproducing data in the form of editing and summarizing in order to obtain the main data about the essence of the article, presenting data, drawing conclusions, verifying and reviewing the data obtained in order to draw the right results (Sugiyono, 2018).

3 RESULTS AND DISCUSSION

3.1 Sharia Economic Law Concept

In sharia economic law, there are concepts that include the introduction of the main principles, namely the prohibition of usury, the prohibition of maysir and gharar, and the concept of zakat. This concept forms the basis in Islamic economics and regulates various aspects of economic life within a framework that is in accordance with Islamic teachings.

Riba is the practice of taking or giving interest or usury in financial transactions. In Islamic economic law, riba is considered unfair and detrimental. Therefore, usury is prohibited in all forms of financial transactions. Instead, the principle of profit sharing (mudharabah) or fixed profit (murabahah) is used in Islamic financial transactions to ensure equality and fairness in profit sharing (Noman, 2001).

Maysir refers to the practice of gambling or speculation that involves unfair uncertainty and risk. Gharar refers to excessive uncertainty or vagueness in financial transactions, such as vagueness regarding the price, quality, or quantity of goods traded. Sharia economic law prohibits maysir and gharar because they are considered detrimental and economically unstable. Transactions involving these elements are considered invalid and not in accordance with sharia principles.

Zakat is an obligation for Muslims to give a portion of their wealth to those entitled to receive it. Zakat is one of the important pillars in the Islamic economy and serves to

redistribute wealth, reduce social inequality, and provide assistance to those in need. Zakat is given on property that reaches nisab (minimum limit) and has been in possession for one year.

These principles provide guidance in Islamic economic law and affect a wide range of sectors, including banking, capital markets, insurance, and investment. These principles aim to create justice, transparency, stability, and prosperity in an economic system based on Islamic values.

In Islamic economic law, there is a strong emphasis on the compatibility of these principles with the innovation of Islamic financial products. These principles form the framework that Islamic financial products must adhere to to ensure conformity with Islamic values. (Izziyana, 2017)

Islamic financial products must comply with the principles of Islamic economic law such as the prohibition of usury, maysir, and gharar. This means that Islamic financial products must be free from elements of interest, excessive speculation, and excessive uncertainty in financial transactions. Islamic financial product innovation must ensure that these principles are not violated.

Although there are limitations in the principles of Islamic economic law, there is room for creativity in the structure of Islamic financial products. Innovation can occur in the development of product structures or mechanisms that enable the fulfillment of economic needs and objectives while adhering to sharia principles. For example, in Islamic banking, products such as mudharabah, musharakah, and murabahah have been innovated to accommodate financing and investment needs in accordance with sharia principles (Laldin & Furqani, 2016).

To ensure the compatibility of Islamic financial products with the principles of Islamic economic law, supervision and certification are required. Islamic financial institutions and sharia authority bodies are tasked with ensuring that sharia financial products meet the stipulated sharia requirements. This supervision and certification process is important to maintain public integrity and trust in Islamic financial products.

Increasing education and awareness about the principles of Islamic economic law and Islamic financial products is very important. People need to understand these principles and how Islamic financial products can provide solutions that are in accordance with their beliefs. With a better understanding, Islamic financial product innovation can be more effective in meeting the needs of the Muslim community.

In order to promote innovation of Islamic financial products in accordance with the principles of Islamic economic law, collaboration between Islamic financial institutions, sharia authorities, scholars, and sharia law experts is essential. The process of developing Islamic financial products should involve consultation with Islamic scholars and legal experts to ensure conformity with sharia principles.

3.2 Product Innovation of Islamic Financial Institutions

The Islamic financial industry has experienced significant development in terms of financial product innovation in accordance with the principles of Islamic economic law. Here are some types of Islamic financial product innovations that have been introduced:

- a. Musharakah: Musharakah is a form of cooperation or partnership between two or more parties to share profits and risks in a business or project. Innovations in musharakah include the use of musharakah contracts in project financing, the inclusion of risk management mechanisms, or the development of more flexible structures to accommodate diverse business needs.

- b. **Mudharabah:** Mudharabah is a form of cooperation between the owner of capital (shahibul maal) and the manager (mudharib) in which profits are shared according to the previous agreement. Innovations in mudharabah include the use of risk management mechanisms, the use of mudharabah in microfinance or special projects, and the development of innovative mudharabah investment products.
- c. **Murabahah:** Murabahah is buying and selling with a profit that has been agreed in advance between the seller and the buyer. Innovations in murabahah include the development of more flexible financing structures, the inclusion of risk management mechanisms, and the use of murabahah in the financing of property, cars, or other goods.
- d. **Wakalah:** A wakalah is a contract in which one party authorizes the other party to act on its behalf in carrying out a particular transaction. Innovations in wakalah include the development of wakalah-based sharia insurance products, where the insurer acts as a representative and pays claims to policyholders.
- e. **Sukuk:** Sukuk is an Islamic financial instrument that represents partial ownership of a particular asset or project. Innovations in sukuk include the development of more complex sukuk structures, such as asset-based sukuk, project-based sukuk, or waqf-based sukuk.
- f. **Takaful:** Takaful is a sharia insurance concept based on the principle of mutual assistance and risk sharing. Innovations in takaful include the development of more innovative sharia insurance products, the inclusion of more effective risk management mechanisms, and the use of digital technology in the provision of takaful services (Alamad et al., 2021).

These are just a few examples of Islamic financial product innovations that have been introduced in the Islamic financial industry. Development continues in line with market needs and emerging challenges. It is important to note that any innovation must still comply with the principles of Islamic economic law and obtain approval from the competent Islamic authorities before being introduced to the market.

3.3 The Role of Sharia Economic Law in Product Innovation

Sharia Economic Law plays an important role in the design, implementation, and regulation of innovative Islamic financial products. Here is an analysis of how Islamic economic law affects these aspects:

- a. **Product Design:**
 - 1) **Compliance with Sharia Principles:** Islamic financial products must be designed with due regard to the principles of Islamic economic law, such as the prohibition of riba (interest), gharar (uncertainty), maysir (speculation), and haram (things prohibited by the Islamic religion). Product design must ensure that these principles are met and that there are no elements that contradict Islamic values.
 - 2) **Fairness and Balance:** Islamic financial products should be designed to achieve fairness and balance between the rights and obligations of the parties involved. Product design must ensure that risks and benefits are shared fairly and in accordance with Shariah principles.
- b. **Product Implementation:**
 - 1) **Transparency and Responsibility:** The implementation of Islamic financial products must be carried out with high transparency, where all relevant information must be available to the parties involved. In addition, Islamic

financial institutions must also be responsible for running products by ensuring compliance with sharia principles and effective risk management.

- 2) Sharia Supervision: Islamic financial products must be managed and supervised by an independent sharia supervisory board. This board is tasked with ensuring that the products and operations of Islamic financial institutions are in accordance with the principles of Islamic economic law. This supervision is important to maintain public integrity and trust in Islamic financial products.
- c. Product Regulation:
- 1) Sharia Authority: Islamic financial products must comply with regulations and guidelines set by the competent sharia authority. This authority is tasked with regulating and supervising the Islamic financial industry, ensuring that the products introduced meet established sharia standards and do not violate the principles of Islamic economic law.
 - 2) Sharia Accounting Standards: Islamic financial product regulations also include Islamic accounting standards that must be followed by Islamic financial institutions. This standard helps ensure that financial statements reflect transactions and operations based on the principles of Islamic economic law.

Sharia economic law has a significant impact on the design, implementation, and regulation of innovative Islamic financial products. Each product must comply with sharia principles, carry out transparent and responsible implementation, and comply with regulations and supervision set by sharia authorities. This is important to maintain public integrity and trust in the Islamic financial industry.

The role of scholars and supervisory institutions is very important in assessing product compliance with sharia principles in the Islamic financial industry. Ulema play a key role in assessing the compliance of Islamic financial products with the principles of Islamic economic law. The role of scholars in establishing fatwas or legal opinions on the validity of a product is very important to ensure conformity with sharia principles. Scholars who have in-depth knowledge of Islamic economic law and its principles will study in depth the products and transactions involved in the Islamic financial industry. They will evaluate whether the product contains elements of usury, gharar, maysir, or contradicts other principles. Fatwas issued by clerics serve as guidelines for Islamic financial institutions and the public in determining halal and compliance with these products (Chiu et al., 2013).

Sharia supervisory institutions are tasked with supervising and assessing the compliance of Islamic financial products with sharia principles. This institution usually consists of an independent sharia supervisory board and consists of scholars and experts in sharia economic law. Sharia supervisory institutions will review and evaluate products offered by Islamic financial institutions, and ensure that these products are in accordance with established sharia principles. They also examine the implementation process and risk management carried out by Islamic financial institutions. This institution has the authority to provide sharia certification or labels to products that meet sharia standards and principles.

The roles of scholars and sharia supervisory institutions complement and influence each other. These two parties work together to ensure that Islamic financial products comply with sharia principles and maintain the integrity of the Islamic financial industry as a whole. The involvement of scholars and sharia supervisory institutions provides confidence and confidence to the public that Islamic financial products are in accordance with Islamic values.

However, keep in mind that the assessment of a product's compliance with sharia principles can be subjective and require proper interpretation. Therefore, it is important for Islamic scholars and supervisory institutions to continuously update their knowledge and

collaborate with other experts to face new challenges and innovations in the Islamic financial industry.

3.4 Challenges and controversies

In an effort to integrate the principles of Islamic economic law in the innovation of Islamic financial products, there are several challenges and controversies that may arise. Here are some of them:

- a. **Interpretation of Sharia Principles:** The interpretation of the principles of sharia economic law may vary between scholars and sharia supervisory institutions. There is controversy in terms of interpretation of sharia principles that can affect the design and structure of Islamic financial products. These differences of opinion can create uncertainty and complicate consistency in product development.
- b. **Product Structure Complexity:** Islamic financial products often have a more complex structure than conventional products. This is due to the need to ensure compliance with sharia principles. The complexity of this structure can make it difficult to understand and evaluate products by consumers and regulators. In addition, this complexity can also increase operational and compliance risks for Islamic financial institutions.
- c. **Innovative Product Development:** The development of innovative Islamic financial products often faces challenges in terms of compliance with established Islamic principles. In the face of growing market demand, Islamic financial institutions need to ensure that the innovative products offered remain in accordance with the underlying Islamic principles. Controversy can arise when there are differences of opinion about whether the product actually adheres to those principles.
- d. **Supervision and Regulation:** Adequate supervision and regulation is an important challenge in integrating the principles of Islamic economic law in Islamic financial products. A competent and independent sharia supervisory institution is needed to ensure product compliance with sharia principles. However, effective and consistent supervision is often difficult due to differences in approach and interpretation between sharia supervisory agencies in different countries.
- e. **Education and Awareness:** Another challenge is the lack of understanding and awareness about Islamic financial products among the general public. Adequate education is needed to increase understanding of sharia principles and the benefits of Islamic financial products. This lack of awareness can be an obstacle in the acceptance and adoption of Islamic financial products.

Tackling these challenges and controversies requires cooperation between Islamic financial institutions, clerics, sharia supervisory institutions, and regulators. The role of independent Islamic scholars and supervisory institutions is important in ensuring product compliance with sharia principles, while adequate regulation and education will help overcome challenges in integrating Islamic economic law principles in Islamic financial product innovation (Poon et al., 2020).

To overcome the obstacles that arise in integrating the principles of Islamic economic law in the innovation of Islamic financial products, some possible solutions can be considered as follows (Al-Salem, 2009):

- a. **Harmonization and Standardization:** Efforts are needed to harmonize and produce clearer standards in terms of interpretation of sharia principles. Holding

dialogue and consultation between clerics, sharia supervisory institutions, and Islamic financial institutions can help reach agreement on principles that can be applied consistently. Standardization can also help create legal certainty and facilitate the understanding of Islamic financial products.

- b. **Qualification and Capacity Building:** Increasing qualifications and capacity for scholars, Islamic supervisory institutions, and Islamic finance professionals is essential. With adequate training and education, they can understand and apply the principles of sharia better. This will help ensure that innovative Islamic financial products remain compliant with the underlying Islamic principles.
- c. **Research and Innovation Development:** In-depth research on sharia principles and the development of Islamic financial product innovation need to be encouraged. Islamic educational institutions and financial institutions can work together to generate new knowledge that is useful in facing existing challenges and controversies. Research and innovation can also help create Islamic financial products that are more effective and in accordance with sharia principles.
- d. **Strengthening Supervision and Regulation:** Strengthening sharia supervisory institutions and adequate regulation is essential. Independent and competent sharia supervisory institutions must be supported by adequate resources to conduct effective supervision of sharia financial institutions. Clear and consistent regulations are also needed to provide legal certainty for Islamic financial institutions and consumers.
- e. **Public Education and Awareness:** Broader education efforts are needed to increase public understanding and awareness of Islamic financial products. Targeted information and education campaigns can help eliminate ignorance and increase acceptance of Islamic financial products. Education on the principles of sharia can also be provided in formal and non-formal educational institutions.

By implementing these solutions, it is hoped that obstacles in integrating the principles of Islamic economic law in Islamic financial product innovation can be better overcome. This will enable the development of Islamic financial products that are more innovative, in accordance with sharia principles, and can provide greater benefits to society and the environment (Rammal, 2006).

4 Conclusion

Product innovation in Islamic financial institutions is an important step in meeting the needs of the growing market and expanding access to Islamic finance. However, this innovation must pay attention to the underlying principles of Islamic economic law. Sharia economic law principles, such as the prohibition of *riba* (interest), *gharar* (uncertainty), *maysir* (gambling), as well as economic justice and sustainability, should be the main foothold in developing innovative Islamic financial products. Obstacles and challenges that may arise in integrating the principles of Islamic economic law in the innovation of Islamic financial products include differences in interpretation of sharia principles, complexity of product structure, innovative product development, supervision and regulation, and lack of public understanding and awareness. To overcome these obstacles, solutions that can be considered include harmonization and standardization of interpretation of sharia principles, improvement of qualifications and capacity of Islamic scholars and supervisory institutions, development of research and innovation, strengthening supervision and regulation, as well as education and

raising public awareness. The importance of paying attention to the principles of sharia economic law in the innovation of sharia financial products to maintain compliance with the underlying sharia principles. The main challenges in integrating the principles of sharia economic law in the innovation of sharia financial products include different interpretations of sharia principles, complexity of product structure, innovative product development, supervision and regulation, and lack of public understanding and awareness. By implementing the principles of sharia economic law in product innovation of sharia financial institutions, it is expected to create a conducive environment for the development of innovative sharia financial products, in accordance with sharia principles, and provide greater benefits to the community.

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