EPBI
Journal of Economic Perspectives and Business Innovation
ISSN 3109-2667

SHARIA MUTUAL FUNDS

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Articel Information	Abstract
Keywords: Sharia mutual funds, investment, screening, cleansing Vol. 3, No. 3, 2026 xxxxxxxxxx/IPES Submitted: Sept. 11th, 2025 Accepted: Dec. 12st, 2026	Investment activities in Sharia mutual funds are permissible because they do not contradict Islamic principles. In principle, mutual funds not only provide investment opportunities but also offer various types of investment instruments that can be developed. Mutual funds serve as an alternative investment for the public and provide opportunities to obtain better investment returns over a certain period. Sharia mutual funds do not invest in shares or bonds issued by companies whose business activities, management practices, or products are contrary to Islamic principles, such as manufacturers of alcoholic food and beverages, pork products, cigarettes and tobacco, conventional financial services, defense and weapons industries, and entertainment businesses associated with immoral activities. The fundamental difference between conventional mutual funds and Sharia mutual funds lies in the implementation of screening and cleansing processes.

INTRODUCTION

Mutual funds began to gain recognition in the nineteenth century. The origins of the mutual fund industry can be traced back to 1870, when Robert Fleming, a Scottish textile mill accountant, was sent to the United States to manage his employer's investments. During his time there, he observed new investment opportunities emerging following the end of the American Civil War. Upon returning to Scotland, he shared his findings with several of his friends. He intended to take advantage of these opportunities but did not have sufficient capital. This situation encouraged him to raise funds from his friends and subsequently establish The Scottish American Investment Trust in 1873, which was one of the earliest investment management companies in the United Kingdom.

The company was similar to what is now known as a closed-end fund. In Indonesia, mutual fund instruments began to be recognized in 1995 with the launch of PT BDNI Reksa Dana. Based on its characteristics, BDNI Reksa Dana was a closed-end mutual fund. Following the enactment of Capital Market Law No. 8 of 1995, mutual funds began to develop actively in Indonesia. Mutual funds that experienced rapid growth and development were predominantly open-end funds.

The growth of Islamic Financial Institutions (LKS) generated optimism and increased public interest in Sharia-based investment. Consequently, in 1997, a Sharia mutual fund was introduced under the name Danareksa Syariah. Subsequently, in 2000, another product was introduced under the name Danareksa Syariah Berimbang (Sudarsono, 2003, p. 202).

General Overview of Mutual Funds

Mutual funds are internationally known as unit trusts or mutual funds. They first emerged in Brussels, Belgium. At that time, King William I of the Netherlands established a fund participation scheme that enabled small-scale investors to obtain loans from foreign governments. In 1860, England and Scotland followed this initiative by providing their citizens with opportunities to obtain loans through foreign governments. In 1863, England established its first unit trust under the name The London Financial Association and The International Financial Society.

Subsequently, in 1868, the Foreign and Colonial Government Trust of London was established (Pangmanan, 1997, p. 47). The emergence of mutual funds was a response to various questions surrounding investment and provided an appropriate solution for novice investors seeking to invest their funds. With relatively limited capital and knowledge, investors can reduce investment risks through diversification and collective fund management conducted by institutions with professional expertise in investment.

Most mutual funds are structured as Collective Investment Contracts (Kontrak Investasi Kolektif/KIK), which collect funds by issuing investment units. An investment unit is a measurement that represents each unit holder's interest in a collective investment portfolio. Therefore, an investment unit serves as evidence of ownership by the unit holder in a mutual fund.

Under BAPEPAM Regulation No. IV.B.1, as stipulated in the Appendix to the Decree of the Chairman of BAPEPAM No. Kep-03/PM/2004 dated February 9, 2004, mutual funds established in the form of Collective Investment Contracts (KIK) may only purchase and sell the following instruments (BNI Dana Syariah and BNI Danaplus Syariah Mutual Fund Prospectus Update, 2006, p. 2):

1. Securities that have been offered to the public and/or listed on stock exchanges, both domestically and internationally.
2. Domestic money market instruments with maturities of less than one year, including Bank Indonesia Certificates, money market securities, promissory notes, certificates of deposit denominated in rupiah or foreign currencies, and bonds issued by the Government of the Republic of Indonesia.
3. Domestic commercial paper with a maturity of less than three years that has been rated by a securities rating agency.

Definition of Mutual Funds

From an etymological perspective, the Indonesian term *reksa dana* consists of two words: *reksa*, meaning to guard or maintain, and *dana*, meaning a collection of money or funds. Thus, *reksa dana* can be understood as a pool of funds that is collectively managed and maintained for a particular purpose (Muhammad, 2002, p. 118).

According to Article 1 Paragraph 27 of Capital Market Law No. 8 of 1995, a mutual fund is a vehicle used to collect funds from investing members of the public, which are subsequently invested in a securities portfolio by an investment manager licensed by BAPEPAM. A securities portfolio refers to a collection or combination of securities, financial instruments, or other investment instruments that are managed as a portfolio (Soemitra, 2009, p. 166).

Meanwhile, a Sharia mutual fund refers to a mutual fund whose management and investment policies are based on Islamic principles (*Sharia*). Sharia mutual funds, for example, do not invest in shares or bonds issued by companies whose business activities, management practices, or products are contrary to Islamic principles. These include companies engaged in the production of food or beverages containing alcohol, pork products, cigarettes and tobacco, conventional financial services, defense and weapons, and entertainment businesses associated with immoral activities (Soemitra, 2009, p. 212).

Characteristics of Mutual Funds

Mutual funds have several characteristics that distinguish their forms and operations. These characteristics include the following (Soemitra, 2009, p. 214):

1. Closed-End Fund

   A closed-end fund is a mutual fund that does not continuously repurchase its shares from investors. In other words, shareholders cannot sell their shares directly back to the investment manager. If a shareholder wishes to sell the shares, the transaction must be conducted through the stock exchange where the mutual fund's shares are listed.

2. Open-End Fund

   An open-end fund is a mutual fund that offers and repurchases its shares or investment units from investors up to the amount of capital that has been issued. Investors in this type of mutual fund may sell their shares or investment units back at any time, subject to the applicable provisions. The investment manager, through the custodian bank, is required to repurchase the units based on the Net Asset Value (NAV) per share or investment unit at the relevant time.

Characteristics of Sharia Mutual Funds

The fundamental principles underlying the characteristics of Sharia mutual funds are as follows:

1. Business activities must not contradict Islamic principles.

   The business activities of companies included in the investment portfolio must comply with

Islamic principles. Prohibited activities include gambling, conventional interest-based financial institutions (*riba*), businesses that produce, distribute, or trade in unlawful food and beverages, and businesses that produce goods or services that damage morality or cause harm.

2. Transactions must not contain prohibited elements.
   Transactions must be free from practices prohibited under Islamic law, such as *najasy* (artificially influencing prices), *ba'i al-ma'dum* (selling something that does not exist or is not owned), and *insider trading*. Investments should also avoid companies whose level of debt is excessively dominant compared with their equity.
3. Investment activities must comply with Sharia principles.
   Investments may only be made in securities issued by companies whose principal business activities and primary sources of income comply with Islamic principles and relevant Sharia investment guidelines.
4. Implementation of Screening and Cleansing.
   Sharia mutual funds apply a screening process to identify investments that comply with Islamic principles and a cleansing process to remove or purify any income that does not meet Sharia requirements (Soemitra, 2009, pp. 171–173).

Forms of Mutual Funds

Based on Article 18, Paragraph (1) of Capital Market Law No. 8 of 1995, there are two legal forms of mutual funds in Indonesia: mutual funds established as a Limited Liability Company (Perseroan Terbatas/PT) and mutual funds established in the form of a Collective Investment Contract (Kontrak Investasi Kolektif/KIK).

1. Mutual Funds in the Form of a Limited Liability Company (Corporate Type)
A mutual fund in the form of a Limited Liability Company is a company whose legal structure is generally no different from that of other limited liability companies. The distinction lies in its business activities, which focus on managing investment portfolios. Under this structure, the mutual fund company raises funds by issuing and selling shares. The proceeds from the sale are subsequently invested in various types of securities traded in the capital and money markets (Sudarsono, 2008, p. 214).

The characteristics of this type of mutual fund are as follows:

a. Its legal form is a Limited Liability Company (PT).
b. The management of the mutual fund's assets is based on a contract between the company's board of directors and the appointed investment manager.
c. The safekeeping of the mutual fund's assets is based on a contract between the investment manager and the custodian bank.

Collective Investment Contract (KIK)

A Collective Investment Contract (KIK) is a contract entered into between an investment manager and a custodian bank that also binds the holders of investment units as investors. Under this contract, the investment manager is authorized to manage the securities portfolio, while the custodian bank is authorized to provide custody and investment administration services.

In this type of mutual fund, the investment manager and the custodian bank enter into an agreement that, under the Capital Market Law, is referred to as a Collective Investment Contract (KIK). Through this agreement, both parties commit themselves to serving the interests of investors by establishing a vehicle through which the public can invest their funds in mutual funds and obtain investment units.

Therefore, an important aspect of mutual funds is the contract (*akad*). Although investors do not directly sign the KIK, they are required to read the prospectus and sign an application form to participate in the mutual fund before making an investment. Consequently, investors may be considered legally bound by the terms and conditions of the contract.

The investment manager is one of the key parties in the mutual fund system. However, similar to Islamic financial institutions, Sharia mutual funds involve another important party that functions as a supervisory body, namely the Sharia Supervisory Board (Dewan Pengawas Syariah/DPS). The Sharia Supervisory Board consists of Islamic scholars and experts who understand Islamic economic law (*Sharia*), particularly the application of Islamic values and ethics to economic principles based on the Qur'an and Sunnah (Muhammad, 2002, p. 191).

Types of Mutual Funds Based on Portfolio Composition

Based on their portfolio composition, mutual funds can be classified into several types as follows (Sudarsono, 2008, p. 204):

1. Money Market Fund
   A money market fund is a mutual fund that invests exclusively in debt securities with maturities of less than one year. Its primary objective is to maintain liquidity and preserve capital.
2. Fixed Income Fund
   A fixed income fund is a mutual fund that invests at least 80% of its assets in debt securities. The primary objective of this type of mutual fund is to generate a relatively stable rate of return.
3. Equity Fund
   An equity fund is a mutual fund that invests at least 80% of its assets in equity securities, particularly stocks. This type of mutual fund generally carries a higher level of risk than the two previously mentioned types, but it also offers the potential for higher returns.
4. Balanced Fund
   A balanced fund is a mutual fund that invests in a combination of equity securities and debt securities. This type of fund seeks to balance potential returns and investment risks through portfolio diversification.

Issuance Process of Open-End Mutual Funds

The issuance process of an open-end mutual fund begins with the establishment of a contract between the Investment Management Company (Perusahaan Manajer Investasi/PMI) and the Custodian Bank. Under this contract, the investment management company is responsible for managing the mutual fund's assets, including cash and investment portfolios. Meanwhile, the custodian bank is responsible for the administration and safekeeping of the mutual fund's assets.

A legal consultant subsequently provides a legal opinion regarding the investment management company, the custodian bank, the contract signed by both parties, and other relevant documents.

The mutual fund must then obtain an effective statement from BAPEPAM before conducting a public offering. This effective statement specifies, among other matters, the number of Investment Units (Unit Penyertaan) that may be issued. The investment units are subsequently offered to the public through a process known as a launching or public offering.

Following the launch, the mutual fund continues to offer and sell investment units to the public as long as there are investors willing to purchase them (Sudarsono, 2008, p. 217).

Net Asset Value (NAV)

Net Asset Value (NAV), or Nilai Aktiva Bersih (NAB) in Indonesian, is one of the measures used to assess the performance of a mutual fund. The NAV is derived from the value of the mutual fund's investment portfolio. The assets of a mutual fund may include cash, deposits, money market securities, Bank Indonesia Certificates (SBI), commercial paper, stocks, bonds, rights, and other securities.

The Net Asset Value (NAV) represents the total value of assets after deducting all existing liabilities. The NAV per Investment Unit is calculated by dividing the total NAV by the number of outstanding Investment Units held by investors at a particular point in time.

The NAV per share or investment unit is calculated daily by the Custodian Bank based on the valuation of the mutual fund's assets. The NAV is subject to daily fluctuations depending on changes in the value of securities within the investment portfolio. An increase in NAV indicates an increase in the investment value of shareholders or investment unit holders. Conversely, a decrease in NAV indicates a decline in the value of the investor's investment (Sudarsono, 2008, p. 218).

Benefits and Advantages of Mutual Funds

Mutual funds offer several benefits that make them an attractive alternative investment instrument, including the following (Sudarsono, 2008, p. 178):

Professional Management, The management of a mutual fund portfolio is carried out by an Investment Manager who specializes in fund management. The role of the Investment Manager is important because individual investors generally have limited time and resources to conduct research, analyze securities prices, and access information from the capital market.

Investment Diversification, Diversification or the distribution of investments within a portfolio can reduce investment risk, although it cannot eliminate risk entirely. Mutual fund assets are invested in various types of securities, thereby spreading the investment risk. In other words, the risk is generally lower than that associated with an individual investor purchasing only one or two types of stocks or securities.

Information Transparency, Mutual funds are required to provide continuous information regarding the development of their portfolios and associated costs. This enables investment unit holders to monitor their returns, costs, and risks. Mutual fund managers are also required to publish the Net Asset Value (NAV) regularly and provide periodic financial reports and prospectuses, allowing investors to monitor the development of their investments.

High Liquidity, For an investment to be effective, the investment instrument should have an adequate level of liquidity. Investors can redeem their Investment Units at any time in accordance with the provisions established by each mutual fund. This provides investors with greater flexibility in managing their funds. Open-end mutual funds are generally highly liquid because they are required to repurchase Investment Units in accordance with applicable regulations.

Lower Costs, Because mutual funds pool funds from many investors and manage them professionally, they can achieve greater efficiency in investment transactions. Consequently, transaction costs may be lower than those incurred when individual investors conduct transactions independently in the capital market.

Services for Investors, Mutual funds generally provide various services and facilities to attract and serve investors. For example, some mutual funds may offer automatic reinvestment of dividends and capital gains that would otherwise be distributed to investors.

Investment Risks of Mutual Funds

Before investing in mutual funds, investors need to understand the types of risks that may arise from purchasing mutual fund units. These risks include the following (Sudarsono, 2008, p. 180):

Risk of Declining Investment Unit Value, This risk is influenced by a decline in the prices of securities, such as stocks, bonds, and other securities, included in the mutual fund's portfolio. Such declines may be caused by various factors, including poor stock market performance, declining issuer performance, uncertain political and economic conditions, and other fundamental factors.

Liquidity Risk, Liquidity risk concerns the difficulties that an Investment Manager may face when a large number of investment unit holders simultaneously redeem their units. Under such circumstances, the Investment Manager may experience difficulties in providing sufficient cash to meet redemption requests.

This risk may occur when investors in a particular mutual fund withdraw substantial amounts of funds at the same time. This situation is commonly referred to as a rush, meaning a large-scale withdrawal of investment units. Such a situation may be triggered by extraordinary negative factors that encourage investors to redeem their mutual fund units. These factors may include deteriorating political and economic conditions, the closure or bankruptcy of public companies whose stocks or bonds are included in the mutual fund's portfolio, or the liquidation of the Investment Manager responsible for managing the mutual fund.

Political and Economic Risk, Political and economic risk arises from changes in economic or political policies that may simultaneously affect the performance of financial markets and companies. Consequently, changes in the prices of securities may affect the value and performance of the mutual fund's investment portfolio.

Market Risk, Market risk arises because the value of securities traded in financial markets fluctuates according to general economic conditions. Fluctuations in the securities market directly affect the net value of an investment portfolio, particularly when market corrections or negative movements occur.

Market risk occurs when the prices of investment instruments decline due to a significant deterioration in the performance of stock or bond markets. This condition is commonly associated with a bearish market, in which stock prices or other investment instruments experience substantial declines.

Market risk may indirectly cause the Net Asset Value (NAV) of mutual fund investment units to decrease. Therefore, before investing in a particular type of mutual fund, investors should consider market trends affecting the instruments included in the mutual fund's portfolio.

Inflation Risk, Inflation risk occurs when inflation causes a decline in the real return on an investment. The income generated from a mutual fund investment may be insufficient to compensate for the decline in purchasing power, resulting in a loss of purchasing power.

Foreign Exchange Risk, Foreign exchange risk may arise when foreign securities are included in a mutual fund's investment portfolio. Changes in exchange rates can affect the value of foreign investments after they are converted into the domestic currency.

Specific Risk, Specific risk refers to the risk associated with each individual security held in a mutual fund portfolio. Although general market conditions influence securities, each security also carries its own specific risks.

The value of a particular security may decline when the performance of the issuing company deteriorates or when the company faces the possibility of default, meaning an inability to fulfill its financial obligations.

Operating Mechanism of Mutual Funds

The operating mechanism of mutual funds involves not only the Investment Manager, Custodian Bank, and investors, but also intermediaries in the capital market, such as brokers and underwriters, as well as financial institutions in the money market, such as banks. The activities are also subject to supervision by BAPEPAM in accordance with the applicable regulations.

The mutual fund operating mechanism can be explained through the following stages:

1. Application for the Purchase or Redemption of Investment Units Investors submit an application to purchase investment units or redeem previously held units.
2. Payment for Investment Units or Redemption Proceeds Investors transfer the required funds for the purchase of investment units, or the proceeds from the redemption of units are paid to investors.
3. Investment Transaction Order The Investment Manager issues instructions to conduct investment transactions based on the mutual fund's investment objectives and portfolio strategy.
4. Execution of Investment Transactions The investment transaction orders are executed through the relevant capital market or money market intermediaries.
5. Transaction Confirmation Confirmation of the executed investment transactions is provided to the relevant parties.
6. Transaction Settlement Instruction Instructions are issued for the settlement of investment transactions that have been executed.
7. Transaction Settlement and Safekeeping of Assets The transactions are settled, while the mutual fund's assets are held and safeguarded by the Custodian Bank.
8. Daily Net Asset Value per Investment Unit Information Information regarding the Net Asset Value (NAV) per Investment Unit is calculated and published daily through mass media or other authorized information channels.
9. Daily and Monthly Valuation Reports The Investment Manager and relevant parties prepare daily and monthly valuation reports concerning the mutual fund's portfolio and assets.
10. Monthly Report to BAPEPAM Periodic reports concerning the mutual fund's activities and financial condition are submitted to BAPEPAM in accordance with applicable regulations.

Procedures for Investing in Sharia Mutual Funds

Investing in mutual funds is relatively straightforward. Investors only need to contact the Investment Manager of the selected mutual fund. The investor then completes the capital participation or Investment Unit purchase form and transfers the required funds to the Custodian Bank. Afterward, the investor submits proof of payment and the completed form to the Investment Manager. The investor will subsequently receive evidence of participation or ownership of Investment Units in the mutual fund, which is delivered directly to the investor's registered address.

The minimum investment amount is determined by the Investment Manager and is officially stated in the mutual fund's prospectus. A prospectus is a document containing comprehensive information about a mutual fund and serves as a reference for investors when evaluating and selecting a mutual fund as an investment vehicle. Investors can obtain the prospectus from the relevant Investment Manager (Soemitra, 2009, p. 192).

Sharia mutual funds operate based on Islamic principles and involve two primary legal agreements (*akad*), namely (Anshori, 2008, p. 67):

1. Wakalah Agreement between the Investor and the Investment Manager

   The relationship between the investor and the Investment Manager is established through a wakalah arrangement. Under this agreement, the investor authorizes the Investment Manager to manage the funds entrusted to it, with the expectation that the invested funds will generate returns.

   In this arrangement, the investor acts as the shahib al-mal (capital provider), while the Investment Manager acts as the party entrusted with managing the investment funds.

2. Mudharabah Agreement between the Investment Manager and the Investment User

   The agreement between the Investment Manager and the investment user is based on

   a. mudharabah arrangement. This agreement has several characteristics (Anshori, 2008, p. 68):
   b. Profit sharing between the capital provider and the investment user is based on a predetermined proportion agreed upon by both parties.
   c. The investor's risk is limited to the amount of capital that has been provided.
   d. The Investment Manager, acting as a representative, is not responsible for investment losses as long as such losses are not caused by negligence or misconduct on the part of the Investment Manager.

Proof of Ownership and Case Study in Mutual Funds

Unlike placing funds in a bank deposit, investing in a mutual fund involves purchasing shares or Investment Units issued by the mutual fund. Investment Units can be compared to shares in a company. For example, if a company's shares are valued at IDR 1,500 per share and there are 100,000,000 shares outstanding, the market value of the company would be:

IDR 1,500 × 100,000,000 = IDR 150,000,000,000.

Similarly, if a mutual fund's Investment Unit is valued at IDR 2,000 per unit, with a total of 10,000,000 Investment Units outstanding, the mutual fund's Net Asset Value (NAV) would be:

IDR 2,000 × 10,000,000 = IDR 20,000,000,000.

The price per Investment Unit, referred to as the Net Asset Value (NAV) per Investment Unit, is calculated by the Custodian Bank on a daily basis and published through various newspapers and other authorized information channels.

As another example, suppose an investor invests in a mutual fund by purchasing Investment Units at the price determined on the transaction date. For instance, on June 1, 2000, an investor invests IDR 3,000,000 by purchasing a mutual fund at a price of IDR 1,500 per Investment Unit. Assuming there is no purchase fee, the number of Investment Units received would be:

IDR 3,000,000 ÷ IDR 1,500 = 2,000 Investment Units.

As proof of ownership of the Investment Units, the Custodian Bank will send the investor a Confirmation Letter of Investment Unit Ownership. Some mutual funds may not send a separate confirmation letter but instead issue a monthly statement that also serves as proof of ownership of the

Investment Units (Pratomo & Nugraha, 2002, p. 49).

If the investor purchases 2,000 Investment Units at IDR 1,500 per unit and subsequently sells them at IDR 2,000 per unit, the investment gain, assuming there is no redemption fee, would be:

IDR 2,000 − IDR 1,500 = IDR 500 per unit

Therefore, the total investment gain would be:

IDR 500 × 2,000 Investment Units = IDR 1,000,000.

Thus, the investor would obtain a capital gain of IDR 1,000,000 from the investment.

Determination and Distribution of Investment Returns in Sharia Mutual Funds

According to DSN-MUI Fatwa No. 20/DSN-MUI/IV/2001 on Guidelines for the Implementation of Sharia Mutual Fund Investments, particularly Chapter V, Article 11 concerning the determination and distribution of investment returns, the following provisions apply:

1. Investment returns received as part of the collective assets owned by investors in a Sharia mutual fund shall be distributed proportionally among the investors.
2. The investment returns distributed to investors must be free from non-halal elements. Therefore, the Investment Manager is required to separate any portion of income containing non-halal elements from income considered halal. This process is known as *tafriq al-halal min al-haram*, or the separation of halal income from non-halal income.
3. Investment income that may be received by Sharia mutual funds includes:
   a. From Sharia-compliant shares: dividends, rights, and capital gains.
   b. From Sharia-compliant bonds or sukuk: periodic profit-sharing returns received from the issuer's profits.
   c. From Sharia-compliant money market securities: profit-sharing returns received from the issuer.
   d. From deposits: profit-sharing returns received from Sharia-compliant banks.
4. The calculation of investment returns that may be received by the Sharia mutual fund, as well as the investment income that must be separated due to non-halal elements, is conducted by the Custodian Bank. The results must be reported to the Investment Manager at least once every three months and subsequently communicated to investors and the National Sharia Board (Dewan Syariah Nasional/DSN).
5. Investment income that must be separated because it originates from non-halal sources shall be allocated for the benefit of the public (*maslahah al-ummah*). Its utilization shall be determined by the National Sharia Board and reported transparently.

Sharia Perspective on Mutual Fund Investment Practices

The Sharia perspective on Sharia mutual fund investment practices was discussed in the workshop of Islamic scholars on Sharia mutual funds, organized by the Indonesian Ulema Council (MUI) in cooperation with Bank Muamalat Indonesia (BMI) on 24–25 Rabi' al-Awwal 1417 H, corresponding to

July 29–30, 1997, in Jakarta.

In principle, transactions in *muamalah* are permissible as long as they do not contradict Islamic principles. This view follows the legal maxim held by the Hanbali school and other Islamic jurists: the basic principle governing transactions and their associated conditions is permissibility unless prohibited by Sharia or contrary to an established Sharia text (*nash*) (Huda & Edwin, 2008, p. 119).

Mutual funds have generally been regarded as an institution and an investment mechanism. From an Islamic perspective, mutual funds fall within the framework of Islamic muamalah. Accordingly, the permissibility of mutual funds can be understood through various Islamic legal principles derived from the Qur'an, Hadith, and the opinions of the majority of Islamic scholars.

In other words, Sharia principles may accommodate investment activities such as mutual funds as long as their operations do not contradict Islamic principles. As stated by Wahbah al-Zuhayli, any condition that does not conflict with the fundamental principles of Sharia and whose legal basis can be established through analogy (*qiyas*) may be considered a valid condition (Muhammad, 2002, p. 120).

Allah SWT commands believers to fulfill the contracts and agreements they have made. This principle is stated in Surah Al-Ma'idah, verse 1.

يَٰٓأَيُّهَا ٱلَّذِينَ ءَامَنُوٓاْ أَوۡفُواْ بِٱلۡعُقُودِۚ أُحِلَّتۡ لَكُم بَهِيمَةُ ٱلۡأَنۡعَٰمِ إِلَّا مَا يُتۡلَىٰ عَلَيۡكُمۡ غَيۡرَ مُحِلِّي ٱلصَّيۡدِ وَأَنتُمۡ حُرُمٌۗ إِنَّ ٱللَّهَ يَحۡكُمُ مَا يُرِيدُ ١

“O you who believe, fulfill the contracts. Lawful to you are grazing livestock, except for what is recited to you, without permitting hunting while you are in a state of pilgrimage. Indeed, Allah decrees what He wills.”

The conditions applicable to a contract (akad) are conditions established by Muslims themselves, provided that they do not violate Islamic teachings. The Prophet Muhammad (peace be upon him) provided the following limitation in a hadith:

“Reconciliation is permissible among Muslims, except for reconciliation that makes unlawful what is lawful or makes lawful what is unlawful. Muslims are bound by the conditions they have agreed upon, except for a condition that makes unlawful what is lawful or makes lawful what is unlawful.” (Huda & Nasution, 2008, p. 121)

Conventional mutual funds involve *muamalah* contracts that are generally permissible in Islam, such as sale and purchase transactions and profit-sharing arrangements (*mudharabah* and *musyarakah*). Therefore, conventional mutual funds may provide various benefits, such as contributing to economic development, generating mutual benefits among the parties involved, and minimizing risks in the capital market. However, conventional mutual funds may also contain elements that are contrary to Sharia principles in terms of their contracts, operations, investments, transactions, and profit distribution (Muhammad, 2002, p. 121).

The operational relationship between investors and the Investment Manager in Sharia mutual funds is based on the wakalah system. Under a *wakalah* agreement, investors authorize the Investment Manager to carry out investments on their behalf and for their benefit, in accordance with the provisions stated in the mutual fund's prospectus.

Investments are made exclusively in financial instruments that comply with Islamic principles. These instruments include Sharia-compliant stocks, deposits placed with Sharia-compliant commercial banks, and short- and long-term debt securities that comply with Sharia principles.

To ensure that Sharia mutual funds operate in accordance with Sharia requirements as stipulated in the DSN fatwas, a Sharia mutual fund is required to have a Sharia Supervisory Board (Dewan Pengawas Syariah/DPS).

The primary function of the Sharia Supervisory Board is to advise the Investment Manager on matters related to Sharia aspects and to serve as a mediator between the mutual fund and the National Sharia Board (Dewan Syariah Nasional/DSN).

Sharia mutual funds differ from conventional mutual funds in terms of their operational practices. One of the most significant differences is the screening process used in constructing the investment portfolio. Screening based on Sharia principles excludes stocks associated with prohibited activities, such as riba (interest/usury), alcoholic beverages, gambling, pork products, and tobacco or cigarettes (Huda & Nasution, 2008, p. 122).

Conclusion

Based on the discussion presented above, the following conclusions can be drawn:

1. In principle, all activities in *muamalah* are permissible as long as they do not contradict Islamic Sharia principles.
2. Investment activities in Sharia mutual funds are permissible because they do not contradict Sharia principles.
3. In principle, mutual funds not only provide investment opportunities but also offer various types of investment instruments that can be developed.
4. Mutual funds serve as an alternative investment for the public and provide opportunities to obtain investment returns over a certain period.
5. Mutual funds are managed by two main parties, namely the Investment Manager and the Custodian Bank.
6. Sharia mutual funds do not invest in shares or bonds issued by companies whose business activities, management practices, or products contradict Islamic principles, such as companies producing alcoholic food or beverages, pork products, cigarettes or tobacco, conventional financial services, defense and weapons, and entertainment businesses associated with immoral activities.
7. The fundamental difference between conventional mutual funds and Sharia mutual funds lies in the implementation of the screening and cleansing processes.

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