

Report and Findings of the 1st International Conference on Islamic Business^{*} (ICIB - 2011)

Islamic Business and Finance: The Present State and the Way Forward (7, 8-9 February), 2011

ICIB-2011 was organized by the Riphah Center of Islamic Business (RCIB) of the Riphah International University (RIU), Islamabad with Support from:

- i) Islamic Development Bank (IDB) through Islamic Research & Training Institute (IRTI), Jeddah
- ii) State Bank of Pakistan (through its) Islamic Banking Department (IBD) & National Institute of Banking and Finance (NIBAF)

The Conference, originally envisaged as a national summit, turned out to be a unique international event by dint of scholarly contributions by top level economists and practitioners involved in evolution of Islamic finance industry. This was the first international conference held in Pakistan on the subject. Spreading over 8 working sessions during two days, the conference discussed the present state of Islamic business and finance and how and in what way the economic problems of the Muslim and other countries could be resolved efficiently. Twenty six presentations / papers were presented in addition to eight presentations made in pre-Conference Workshops on Islamic banking and *takāful* on February 7, 2011.

The keynote speakers included Dr. Abbas Mirakhor (INCIEF, Malaysia), Dr. Hussain Hamid Hassan (Sharī'ah Advisor of many institutions and member OIC Fiqh Council), Dr. Monzer Kahf (Professor of Islamic Finance, QFIS, Qatar Foundation, Doha), Dr. Muhammad Umer Chapra, Advisor IRTI, Jeddah, Prof. Khurshid Ahmad (Chairman IPS Islamabad), Dr. Akram Laldin (ISRA, Malaysia), Dr. Munawar Iqbal (Former Chief, IRTI / IDB), Dr. Zubair Hasan (Professor at INCEIF, Malaysia), Dr. Muhammad Qaseem, Sharī'ah Advisor, DIB, Pakistan; Dr. Muhammad Tahir Mansuri (IIUI and Sharī'ah Advisor, Askari Islamic Bank), Mr. Omar Mustafa Ansari (Ernst & Young Ford Rhodes Sidat

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Hyder, Karachi), Dr. Zeeshan Ahmed (LUMS), Mufti Najeeb Khan (Sharī'ah Advisor, Habib Bank A. G. Zurich), Mr. Rustam M. Idrees (Bank Negara Malaysia), Mr. Riaz Riazuddin (State Bank of Pakistan) and Mr. Saleemullah (State Bank of Pakistan). Federal Minister for Finance & Economic Affairs, Mr. Abdul Hafiz Sheikh was the Chief Guest while Mr. Yaseen Anwar, the then acting Governor of State Bank of Pakistan was the Guest of Honor in the inauguration ceremony.

The Conference was attended by economists, research scholars, policy makers in the state institutions, educationists, judiciary people and legal practitioners, trainers and heads of human resource departments, Islamic business and finance executives, CEOs from the business, industry and corporate sectors, officials of the securities & exchange commission, journalists, Islamic banking, regulators, *sharī'ah* scholars, students of universities and business schools and the managers of companies.

Inauguration by the Federal Finance Minister

The Conference was inaugurated by the Federal Minister for Finance & Economic Affairs, Mr. Abdul Hafiz Sheikh. He appreciated the joint effort of RIU, IDB and its research and training arm IRTI, State Bank of Pakistan and its training arm NIBAF for organizing the international conference and providing a platform for discussing the vital issue of development of Islamic business and finance and creating awareness about the emerging issues.

The Minister observed that despite severe global financial crisis, Islamic principles of finance have proven their viability worldwide and Islamic financial institutions are in the field to exploit the potential benefits. Creating financial assets out of nothing and putting others in undefined risks is not acceptable in *sharī'ah* based financial system. Piling up of fictitious assets without any real economic activity and unjustly transferring risks to others are the major problems of the current financial system. The number of reserve currencies in the global payments system has to be increased for the purpose of diversification. He contended that international financial institutions may facilitate development of multi reserve currencies if the objective to avoid the possible turmoil in the global finance and to develop the world economy at sound footings is to be achieved.

Fortunately, a number of economists and financial experts have been talking for some time of green finance and ethical investments. "The strategy has to be framed to enhance the demand of asset based finances in all parts of the world. Islamic finance is well-placed to serve this purpose

because transparency, justice and fulfillment of social responsibilities are among its core values. It has the potential to become an alternative model for global system beneficial to all societies and for close interaction between the Muslim and the non-Muslim societies". The Minister emphasized. He urged the economists to devise such strategies that increase in monetary assets is matched by the real assets in an economy with a possible allowance for realizing the growth potential of respective assets, businesses and economies during the related plan period.

Mr. Abdul Hafiz Sheikh briefly mentioned the Islamic banking model introduced in Pakistan and expressed concern that transformation of government debt to *sharī'ah*-complaint instruments was much more challenging than the transformation of the conventional banking instruments. He observed that although Islamic banking is more suitable by nature for agriculture, but the Islamic banking institutions (IBIs) have negligible presence (of less than 1%) in agribusiness compared to 6.1% of the banking system as a whole. The main potential areas like Agriculture, Housing, SME and Micro finance may be marketed either directly or through special purpose sector-wise subsidiaries, House Building Finance Institutions, NGOs and Micro Finance Institutions.

Prior to that, Dr. Anis Ahmed, Vice Chancellor of the RIU made a Welcome Address. He thanked the keynote speakers and the participants for their contributions and making the conference a success.

The Chairman Riphah Center of Islamic Business (RCIB) Mr. Khurram Khan introduced the RCIB to the participants and appreciated launching two publications of RCIB in a short span of time since its establishment in 2009.

Dr. Hussain Hamid Hassan delivered a keynote address on Islamic Financial Industry: Its Present Status and its Future. He observed that Islamic finance is being recognized internationally not only for Muslims, but also for the others. Everyone believes, while keeping in view the recent financial crisis, that the only viable financial system for the humanity is the Islamic financial system. The scholars, teachers and practitioners, anchors and legal experts express their respective views on the cause of failure of the conventional system. According to some, it is due to interest itself, some say that it was due to structured products like futures, options and swaps. Some others say it was due to the regulators' or the practitioners' negligence, while according to some others, it is because of the rating agencies; and so on and so forth. It gives a good

lesson for the Islamic financial industry for which interest and *gharar* are prohibited.

Shari'ah puts the *gharar* in three categories, first is the uncertainty like salt in food, which refers to business risk and is necessity. If you want to take the profit, you must expose yourself to some kind of business risk. There is another kind of risk which renders the contract or agreement null or void. We call it excessive uncertainty or *gharar-e-kathir*. It is some kind of speculation, which is not allowed. As we see, the structured or derivative products of about 600 trillion Dollars like options, futures and swaps are the main cause of the recent crisis while the real global economy is of about six trillion Dollars only. The huge amount held as derivatives had no investment, no development and no real economic activity. We believe that Islamic finance is a blessing for the humanity. The solution for the humanity lies only in Islamic finance. The experience has shown that the conventional banks when converted to Islamic principles, they gave better performance. For example, Sharjah Bank's share was of 3 dirham on the closing of 30 June, 2002 and when the bank opened on 1st July, 2002 after conversion to Islamic finance, its share price went up to 7 dirham; and the Bank used to give 1.2% rate of interest to the depositors while after six months it distributed 3.5% profit for the depositors. The same is the case of all Middle East based banks and financial markets.

We need new innovations and products for the emerging Islamic finance industry. While the conventional banks have only one product - loan with interest, a large number of products have been introduced for Islamic finance by the scholars and jurists. While avoiding *riba* and *gharar*, Islamic finance experts may innovate and develop more and more products. Dr Hassan clarified that if a product or a contract is *shari'ah* compliant, it is Islamic and no distinction may be made between the two. He added that decisions of the *shari'ah* boards may be made binding only if *shari'ah* boards take responsibility of the consequences of implementing their binding decisions.

Papers & Presentations

The Conference aimed at discussing the present state of Islamic business and finance and how and in what way the same can contribute to the stability to the national and global economies. In particular, it discussed the following:

- i) International Financial Architecture & Islamic Finance - How and in what way Islamic finance can address the vulnerabilities of current international financial paradigm?
- ii) Concept, Practice & Experiences of Islamic Banking and Finance - likelihood of convergence of current Islamic banking and finance practices with that of the conventional system;
- iii) Monetary and fiscal management in the light of Islamic economic principles; solutions that Islamic finance offers for public debt management;
- iv) Tools for socio-economic development, other than *zakāh* like microfinance, *takāful* and *waqf* that can help achieve the objective of socio-economic development in an economy;
- v) The challenges and opportunities, in the current environment, in practicing business in Islamic way.

Specific areas that created enthusiasm leading to detailed discussions pertained to:

- i) The continuing global crisis and the solution that Islamic finance offers;
- ii) Evolution of Islamic Finance, realizing the objectives and possibility of its convergence with conventional finance;
- iii) *Sharī'ah* and Legal issues in floatation of *ṣukūk* in various jurisdictions;
- iv) Issues in financing the Government / public sector needs;
- v) The process and implication of structured Islamic financial products like *tawarruq* / Commodity Murabaha;
- vi) The challenges and prospects for managing businesses in *sharī'ah* compliant way

A brief of discussions held on the above areas is given in the following pages:

A. Global financial crises and possible solutions:

Dr. M. Umer Chapra and Dr. Monzer Kahf presented papers on the subject.

Dr. Kahf discussed the financial crises and their solutions and remedies. He called for a return to the fundamentals of finance and

suggested reform steps to be taken in the short run like taming speculation and eliminating virtual assets and zero sum transactions from the financial markets. For the long run, he called for a four-pillar reforms by eliminating speculation and all speculative contracts, providing finance on the basis of contracts and methodologies rooted in real ownership of sale on credit, leasing and sharing, creating a financial ombudsman and setting ethics based standards for financial institutions.

The short and the long run strategy suggested by Dr Kahf can be summarized as below:

- i) All zero sum contracts like index trading, CFD (Contract for the Difference), currency price betting, internet currency trading, and their likes should be withdrawn from the finance market and the licensing of their trade forums/platforms should be cancelled.
- ii) Commodity and currency futures should be gradually restricted. This is possible by restricting trading commodities and currencies in organized regulated markets only to real units that deal with these commodities and currencies as real suppliers and demanders. Hedging through futures or options can still be available but only to those who have outstanding positions of future assets or liabilities. There are plenty of these genuine players in the market to the extent that will create real exchange relationships and eliminate the claimed need for risk bearing speculators.
- iii) Imposing restrictions on day trading and de-listing the market makers;
- iv) Short sale can be discouraged by increasing the margin to a high limit that may reach 100%, disallowing lending of shares for trading and depriving short sale from benefiting of any financial facilities including margins.
- v) Debts securitisation should be restricted to interlinked institutions within same holding company in order to force a financial institution that accepts a debt to bear all the consequences of its debt itself alone or with its sister companies within the same holding company.
- vi) Financial market accessibility should be reduced from present 24 hours 7 days a week across the globe to an extent that is barely sufficient to provide needed liquidity in the market only for transacting real exchange and supporting real production.

For the long run, he has suggested four pillars of reform:

- i) Genuinizing organized markets by revising regulations and trading requirements in the equity markets and stock exchanges with the aim of making speculation on shares difficult; many folds multiplication of transactions will not be permitted; option trading should be eliminated so that options can be issued but only exercised or let die, they should not be traded.
- ii) Channeling all finance activities through the venues of sale, lease and venture capital (sharing) - removal of loans from the finance sector and the de-legalization of interest. This creates a one to one correspondence between the financial sector and the real market.
- iii) Strengthen the stake-holders protection institution(s) to become a real financial Ombudsman by giving them the authority to protect the public interests in the process of financial engineering and requiring all new products to pass through a financial ombudsman.
- iv) Creation of stand-by finance provider(s) to remove the harmful effects on the real productive units/corporations of repetitive mishandlings by financial big players – financial giants must not be allowed to halt the functioning of institutions that work, in the real market, on creating goods and services and on producing income and employment.

Dr Umer Chapra argued that the primary cause of the subprime mortgage crisis in the United States was the absence of adequate market discipline in the financial system, which leads to excessive lending, high leverage, speculation, and unsustainable rise in asset prices. Unwinding later on gave rise to a vicious cycle of selling that lead to a steep decline in asset prices followed by financial crisis and economic slowdown. The spread of derivatives like credit default swaps (CDSs) corrupted the markets; the buyer of the swap (creditor) paid a premium to the seller (a hedge fund) for the compensation he will receive in case the debtor defaults. It may not have caused much harm if the hedge funds had also performed some scrutiny and sold the swaps to just the actual lending banks. They, however, sold them also to a large number of other institutions and individuals who were willing to bet on the default of the debtor. These swap holders, in turn, resold the swaps to others and the whole process continued several times. Large imbalances in the U.S. Economy further exacerbated the situation. The continuing huge deficits had already raised the gross public debt of U.S. It had an adverse impact

on the strength of the US Dollar in the international foreign exchange markets.

Islam has, however, laid down a number of conditions to ensure that credit expands in step with the growth of the real sector. Some of these conditions are:

- i) The asset which is being sold or leased must be real, and not imaginary or notional;
- ii) The seller must own and possess the goods being sold or leased;
- iii) The transaction must be a genuine trade transaction with the full intention of giving and taking delivery; and
- iv) The debt cannot be sold and thus the risk of default associated with it must be borne by the lender himself.

Islamic financial system, if implemented earnestly, has the potential of minimizing the severity and frequency of financial crises by getting rid of the major weaknesses of the conventional system. It introduces greater discipline into the financial system by requiring the financier to share in the risk. It links credit expansion to the growth of the real economy and minimizes speculation and gambling by allowing credit primarily for the purchase of real goods and services which the seller owns and possesses and the buyer wishes to take delivery. It also requires the creditor to bear the risk of default by prohibiting the sale of debt, thereby ensuring that he evaluates the risk more carefully.

According to Dr Chapra, following steps would be needed for ensuring the health and stability of the global financial system:

- i) Leverage needs to be controlled to ensure that credit does not exceed the ability of the borrowers to repay.
- ii) Credit needs to be confined primarily to transactions that are related to the real sector.
- iii) The banks may hold the debt on their books until maturity. This would ensure careful underwriting. In case some relaxations are genuinely required, all securitizers should be required to retain a meaningful part of the securities they issue along with the right of recourse for the ultimate purchaser ensuring that every debt is paid.
- iv) It needs to be ensured that Credit default swaps, if needed to provide protection to actual lenders, do not become instruments

for wagering. Their hedging role should be confined to the actual lenders.

- v) The derivatives market needs to be properly regulated to remove the element of gambling that has unnecessarily inflated the outstanding amount of derivatives.
- vi) All financial institutions, and not just the commercial banks, need to be properly regulated and supervised so that they remain healthy and do not become a source of systemic risk.
- vii) Some arrangement needs to be made to make credit available to subprime borrowers at affordable terms to enable them to buy a home, pursue higher education or vocational training, and establish their own small and micro enterprises.

B. Evolution of Islamic finance, realizing the objectives and possibility of its convergence with conventional finance

Dr. Abbas Mirakhor spoke on the overall evolution of Islamic finance and on the “*Development of Structured Islamic Finance Products: Likelihood of Convergence with Conventional Finance*”. According to him, there has been a dissonance between the pioneer scholars’ vision and practitioners’ view of Islamic banking and finance. The former envisioned a financial system firmly rooted in the Qur’an (fundamentally, Verse 275 of Surah 2) in which risk-reward sharing was the driver of system in allocating financial resources in the absence of a fixed, predetermined interest rate mechanism and interest rate-based debt instruments. Their research had shown the stability, growth and development, and poverty reduction characteristics of such a system. What has developed, and rightly referred to as the “Islamic finance industry”, while mostly meeting the non-riba requirement, does not meet the most important condition of Islamic finance: risk sharing. It therefore appears that it does not have the potential to achieve the objectives of stability, poverty reduction, growth and economic development, social progress and social solidarity expected from an Islamic financial system where risk sharing constitutes the financial resource allocation function.

“Practitioners rightly refer to their present operational model as ‘Islamic finance industry’ and an industry cannot be asked to achieve the objectives of Islam. As some practitioners forthrightly assert, an industry is a profit making preposition and as such it cannot be asked to reduce poverty, to achieve stability, growth and development and other economic goals.” Most industry practitioners migrated from and had a strong

background in and affinity with the conventional system of finance. It is perhaps understandable that they developed the “industry” employing a process of replicating, reverse engineering, retrofitting and borrowing directly financial instruments that already existed or were being developed in the conventional finance system. They were not only most familiar with the working of the conventional system but also recognized that an organic relationship with the accepted global operating system was necessary if non-interest based finance was to have a chance for global recognition. He observed that others, especially Professor Kahf, have written in detail about the evolution of the present configuration of industry.

In his view, Islamic finance developed in response to what could be called a market failure in the conventional system in that there was demand for non-interest based financing that was not being met. “As such, it had to retool to meet the non-riba requirement to meet this demand. In the event, many of the available instruments were modified, with the approval of *sharī'ah* scholars, to achieve this objective through means familiar and acceptable to the conventional financial system. In this processes, however, what seems to have been neglected is the most important characteristic of the vision of a truly Islamic finance: risk sharing.”

Achieving the original vision is not possible without an active role of Muslim governments. However, it has been somewhat of a surprise that this issue has not received the attention it deserves. There are very few, if any, conferences devoted to this issue. The absence of discussion on this issue in the many conferences, held globally and often, as well as non-participation of governments in these conferences and their active role in leading, developing and directing Islamic finance industry toward objectives enshrined in the Quran and Sunnah is quite palpable. This is surprising since one of the strongest contributions of Islamic finance is its stability, resilience to shocks and much reduced vulnerability to destabilizing phenomena such as sudden stops.

Muslim governments, however, do not seem aware of the benefits of adopting such a system. He indicated that application of macroeconomic, and monetary and fiscal policies in the framework of Islamic system were not only possible but also practical. A number of research papers have already demonstrated the viability of such framework. A project was being undertaken with the leading role by ISRA-INCEIF of Malaysia to develop a practical model along these lines. “Muslim governments need to be involved in the progress of Islamic finance. At least they can reduce

vulnerabilities of their economies to variety of shocks.” He added that: “it is unfortunate that governments in Muslim countries continue the use of debt instruments to finance their own expenditure while, at the same time, expressing support for development of Islamic banking and finance. Use of external debt instruments exposed their economies to external shocks, despite the fact revealed since 1997 that relying on these instruments can have devastating consequences for the economy”. He added that “unfortunately many Muslim governments, except those in South East Asia, have not yet learnt lessons from the 1997 Asian Crisis much less from the most recent global one that all financial crises of the past many decades have been fundamentally debt crises.” The recent crisis proved that interest based finance structure cannot lead to sustainable growth and stable equilibria.

Referring to Pakistan’s economy, he observed that the country had huge potential that needed to be realized. Sizable amounts of pension funds of various institutions, for example, could be used to finance development expenditure of the government on risk-sharing basis. The Government can develop equity-based instruments to finance the general budget and the development budget. In that case, one important benefit would be improved governance as people would be more conscious about their money - where it might be going and how it would be invested. This way, a wider participation by citizens in the framework of budget making would become a reality.

As regards the development of structured Islamic finance products and likelihood of convergence of Islamic finance with conventional finance, he was of the view that Islamic finance industry was product of the conventional finance in response to what may be called a market failure to meet a pent up demand for non-riba financial instruments. Looked at this way, the question of convergence may mean that all the products of conventional finance will be replicated into the Islamic finance by way of reverse engineering and the productive imagination of *sharī’ah* scholars. However, there is another sense in which convergence can be achieved. An epistemological view of the conventional finance reveals its evolution as a product of advances in extending the neoclassical economics into the field of finance. The roots of neoclassical theory, as the name implies, harken back to classical economic thinking particularly those of Adam Smith. Recent scholarship has demonstrated the close connection of Smith’s vision of the economy in the *Wealth of Nation* with the ethical framework embodied in his book: *The Theory of Moral Sentiments*, written ten years before the *Wealth of Nation*. A convergence of the

systems is possible provided that conventional finance returns to its classical roots. The post-Arrow-Debreu development of theory of finance, however, created a progressively strong deviation from the classical roots. Ideas such as the neutrality of debt and equity in firm's capital structure, capital asset pricing model, the efficient market hypothesis which developed in the 1960-2000 periods led to a metamorphosis of idea of risk sharing into models of risk transfer and, mostly, risk shifting instruments. Whereas in Arrow-Debreu theory, all financial instruments envisioned are "contingent" instruments, meaning that payoffs were possible only after outcomes are known, the later developments in financial theory focused on interest-based debt instruments. Practical convergence of the two systems results as the use of these instruments are de-emphasized and equity, rather than interest-based debt, financing comes to dominate the conventional financial system.

Islam is said to be the "*Deen of Sumha*", easy way of life, and Islamic *sharī'ah* is developed to make things easy within the *sharī'ah*-advised boundaries. One way that Islam eases life for humans is through its emphasis on the need for humans to share the risk of their lives on earth. It also needs to be kept in view that human beings are product of society and its culture. At the present, as long as a culture of greed and 'looking out for number one,' prevails in the society instead of moral and empathic treatment of other humans and nature, as prescribed by the Qur'an and Sunnah, the same motivation prevails in the market. The necessity of a fundamental change in the cultural environment cannot be overemphasized. This can only be done in Muslim societies via compliance with the rules of behavior prescribed in the Qur'an and operationalized by the Sunnah.

Risk management in Islamic and conventional finance may be one aspect of difference between them. The former promotes risk sharing while the latter transfers or shifts risk. Uncertainty and risk are facts of life. The Qur'an emphasizes that human beings are tested from time to time, and it is impossible to think about testing without risk and uncertainty. Dr. Mirakhor quoted a statement of Hanna Arendt that "humanity is surrounded in an ocean of uncertainty" and suggested that whenever uncertainty and risk are reduced for individual humans their lives are improved.

In Islam the emphasis is on sharing the risk because "an important corollary of the first axiom of Islam, *tawheed*, is that creation is one, reflecting the Oneness of the Creator. Therefore, the unity of humanity is an important desideratum of Islam. Risk sharing, as envisioned in the

Qur'an and Sunnah, is one of the most important means of achieving the unity of mankind. Through sharing uncertainty and risk of life together, the people become familiar with one another and familiarity promotes solidarity. It is not very difficult to find parallel sentiments in the writings of classical economists, particularly in Smith's *Moral Sentiments*. Importantly, the most famous neoclassical work that aimed to demonstrate analytically the validity of the classical ideas, i.e. the 'Arrow-Debreu' Model, says that in a market system risk is allocated optimally among participants according to their individual ability to bear it. Similarly, in Islam those who have the ability can share their risk through the market. Risk of those unable to participate in the market has to be shared by those more economically able through transfer instruments and redistributive mechanisms such as *zakāh*, *sadaqat*, *qard al-ḥasan*, *auqaf*, and the Islamic laws of inheritance. Therefore, on the theoretical ground, the two systems converge.

One important problem of communicating the idea that Islamic finance is, first and foremost, about risk sharing to the practitioners is that there appears to be confusion in the minds of the latter between risk taking and risk sharing. Practitioners understand that their job is to reduce risk for their clients. Their response, almost always to the scholar's assertion that unless risk sharing is an integral element of financial transactions, the objectives of a truly Islamic finance are not achieved is that "our clients want low risk investments." It is apparently not realized that risk sharing reduces risk for individual investors. Risk taking is a real phenomenon. This means that when an entrepreneur decides to undertake a project in the real sector, the risk is taken. When that project enters the financing phase, the risk of the project can be shared, transferred, or shifted. Of the three modes of financing, only risk sharing reduces the risk for individual investors participating in the financing process. Analysis of the rapidly expanding structured products in the industry suggests that they replicate the complexity and non-transparency of conventional products. Often, large teams of lawyers, financial engineers and *sharī'ah* scholars join to creatively render a conventional finance packaging "*sharī'ah*-compliant." While creativity, borrowing, and engineering are often useful and commendable, much has been written about the dubious nature of these products in terms of contribution to achieving objectives envisioned for Islamic finance.

If there is any validity to the assertion that many of the structured products being developed in the in the industry have the same risk characteristics as of their counterparts in the conventional finance system

plus the added legal risk and “*sharī’ah* risk”, then, emergence of crises cannot be ruled out. As is often the case, the risks and costs of such crises are shifted ultimately to the taxpayers. It is argued by practitioners that Islamic finance is an industry and its objective is to earn profit. Other objectives, no matter how important from a societal point of view, cannot be imposed on the industry from outside. A strong incentive structure must be put in place to demonstrate that pursuing objectives important to the society such as risk sharing enhances ‘the bottom line’ for the industry. And, that kind of incentive structure cannot be put in place without the leadership role of government. Muslim governments can play this role as the *wakeel* and ultimate risk manager of their societies. Moreover, economic theory has long ago showed that where there is a market failure, government’s role becomes crucial. Demonstrably, there is a market failure in Islamic finance at the present since there is a dearth of risk-sharing instruments in the industry. In finding ways and means of non-interest rate based financing of their expenditures, Muslim governments can simultaneously create the needed incentive structure as the risk-sharing instruments they develop for this purpose could well be of the type what Robert Shiller has called “macro-market instruments.” These instruments would be low risk with, possibly, better payoffs than traditional interest rates. At a minimum, development of such instruments would eliminate an important and long-standing challenge facing the industry: a non-interest rate based benchmark.

There are many conferences on Islamic financial system, but there are no scholarly discussions on Islamic finance and its relation with the government policies. We generally talk about *maqāṣid-al-sharī’ah* ... but not about how one can derive practical policy recommendations from the literature on this topic that would be so radically different from the objectives already espoused by governments in one form or another. Moreover, those who advocate, in abstract, the idea of *maqāṣid* either do not realize or at least do not acknowledge that this literature developed as an expression of response of scholars of the Middle Ages of Muslim societies to the challenging problems of their societies at the time. Not much thought is devoted to the relevance, applicability or usefulness of these ideas. At worst, advocating the ideas of *maqāṣid* developed by scholars centuries ago is an unfortunate signal of the paucity of Muslim intellectual endeavor to apply the universal and immutable instructions of the Qur’an and Sunnah to the challenging problems of contemporary societies. “Our scholars need to work on actual policy framework applicable to our societies based on the Quran and Sunnah of Prophet

Muhammad (pbuh) just as people like Ghazali and Shatibi did for their time and their societies.”

A careful study of the Sunnah of the Blessed Prophet as the temporal head of the State in Madinah suggests an Islamic government to be, above all, the risk manager of the society. Its main function is to ensure stability, safety and prosperity for the society through rule compliance. It can be demonstrated that the institutions (or “rules of the game” using a new institutionalists’ terminology) prescribed in the Qur’an and operationalized by the Blessed Prophet guarantee economic stability, growth and development as declared in the Qur’an (see Verse 96, Chapter 7).

Considering the model that Prophet Muhammad (pbuh) established in Madinah, a compelling argument can be made that in a Muslim society, the government’s most important responsibility is indeed one of assuring rule compliance via supervision and regulation. One of the earliest acts of the Blessed Prophet was to establish *ḥisbah* agency responsible for market supervision. In contemporary societies, this agency’s principle function of supervision and regulation is assigned to a large and complex network of agencies, ministries, central banks, security commissions, legal institutions, legislatures, law enforcement agencies and so on. There is no primary role of government in production. The most important task of government in contemporary Muslim society is to establish a governance structure according to rules prescribed in the Qur’an and in Sunnah by which the trust of the society is restored, all the property rights principles as given by Islam are implemented, the rule of law prevails, contracts are enforced, and that everyone has equal access to the resources in the society and is treated commensurate with the dignity which Allah SWT has bestowed on all humans. Such a state would not have to be overly concerned with financial resources as the credibility that it would build in the market would be strong enough to attract the needed resources. Even at the present, it is estimated that in the Middle East alone the high net worth individuals hold about 1.8 trillion Dollars ready to be invested. Compare this with the most optimistic estimate for the Islamic finance of about one trillion dollars. If these investors are offered the opportunity to invest in a sovereign instrument on a risk-sharing basis with expected payoffs in order of 5-7 percent on average or in an interest-based instrument with significantly lower payoff, the choice would be rather clear. Therefore, it is imperative that research be undertaken to develop robust and practical macroeconomic policy to demonstrate the efficacy and benefits of implementation of Islamic finance.

Dr. Shahid Hasan Siddiqi of Research Institute of Islamic Banking and Finance Karachi, spoke on the topic, “**Achieving Socio Economic Objectives in Islamic Banking Framework**”. He emphasized that Islam pleads an economic system that aims to secure extensive socio-economic justice. Therefore, Islamic banking system, if any, must contribute to the achievement of that objective. But, it is not being achieved by Islamic banks operating worldwide. “IBIs may be judged not merely by rise in the quantum of assets but also by the contribution they can make in achieving the socio-economic objectives in respective countries”. He reiterated. The main reason he identified for the failure was working of Islamic banking institutions (IBIs) in parallel with the conventional *riba* and *gharar* based system.

For all practical purposes, IBIs are following the bench-marks of conventional banks by use of *hibah* and some other tactics. “This violates the very spirit of *shari’ah* and is a violation of the agreement with the depositors, as all remunerative deposits are accepted on profit and loss sharing (PLS) basis; in most cases, paying negative real rates of return to depositors, even more negative than conventional banks at least in Pakistan”. More severe injustice is that they are paying higher rates of return to “priority” depositors as compared to depositors of small amounts in the same tenure category. He quoted from the SBP’s Financial Stability Review FY-2009 depicting: “The very fact that SBP was able to implement a fixed rate of return on all savings deposits including PLS deposits is a clear indication of their non-*shari’ah* compliant status.” Quoting from SBP Annual Report 2009-10, he indicated that the spread of IBIs at 8.90% was larger than that of Pakistan banking industry as a whole (7.60%). IBIs’ non-performing financings (NPFs) are much lower than NPLs of conventional banks, which according to Dr. Siddiqi was because they were relatively new in the field. He also gave some sector-wise and mode-wise data of financing by IBIs in Pakistan.

Advances Deposits Ratio of No. of A/cs of banking sector as a whole (at 15.1%) is better than that of the IBIs (9.36 %); net result in financing operations in IBIs and conventional banks is practically the same. He drew the following conclusions regarding Islamic banking operations in Pakistan:

- i) IBIs discouraged savings and encouraged consumption;
- ii) Banking facilities in rural areas not provided;
- iii) IBIs exploited the depositors;

- iv) IBIs did not share the losses sustained by the entrepreneurs which is the essence of Islamic banking as bulk of financings have been on fixed return basis.
- v) It enlarged the gulf between the rich and the poor;

Following are his main recommendations:

- i) Steps needed for transformation of the whole economy for success of Islamic banking in a country, include re-shaping the society, re-structuring the economic system and re-framing the laws according to the dictates of Islam.
- ii) IBIs should equitably share their profits with the depositors under strict supervision of the central banks (it is ironical to note that presently some IBIs, while giving deposits targets to their branch managers, advise that (80) % of the deposits be in Current Accounts so that higher business profits might go to the Shareholders, instead of the depositors);
- iii) *Sharī'ah* scholars should announce in clear terms that the existing parallel system of banking is un-Islamic and a time-frame of say two years be given for complete switch over to Islamic banking system in Muslim countries, in a phased manner with quarterly targets.
- iv) *Sharī'ah* scholars must impress upon the banks to enhance the share of *musharaka* financing in real sense - ensure that at least 50 percent of the new financing is made on the basis of *musharaka* starting from July 1, 2011;
- v) IBIs' financing under consumer finance schemes should be discouraged and special focus should be on micro-finance including financing to small and landless farmers.
- vi) The *sharī'ah* advisors should be bankers of at least five years standing in officers' capacity who should be provided special training in *sharī'ah* matters before, appointing *sharī'ah* advisors.
- vii) IBIs should be directed by Central Banks to restrict banking spread to 3.5 percent, as far as possible.

C. Money creation and control from Islamic perspective

IDB laureate, **Prof. Dr. Zubair Hasan** of INCEIF, Malaysia presented a paper on “**Money creation and control from Islamic perspective**” According to Dr. Zubair, there is actually no difference between the legal

tender money and bank credit: they work in tandem to the same ends in an economy, conventional or Islamic. Also, it does not matter what serves as money – solid gold or flimsy paper – for keeping its value stable. Money is just an instrument: it was never nor can ever be classified into Islamic and non-Islamic. What it does – good or bad – depends on how we create and use it. Money does not generate crises; its creation and mismanagement does - it is the human factor that has been the source of good or evil for mankind including money matters. And true religion can alone improve the quality of human factor. Money evolved as a social convention to overcome the difficulties of barter system. Stability in the value of money is important, not what is used. All reforms will fail to deliver unless human beings are reformed.

Dr Zubair briefly discussed the evolution of money and the central banking. Paper money grew gradually out of gold coinage. The era of 100% reserve for notes issue was very short. For a long time, gold controlled the volume of money in circulation through keeping a minimum gold reserve. He resisted the call by some economists to restore the Gold standard, which, according to him was evolved by the erstwhile imperial powers to exploit colonies for obtaining raw material and other inputs for their growing industries and open their vast markets for selling their products. The autonomy of central banks is illusory. Governments have always been the prime movers in the matter of money supply. Fiscal policies have frequently been the undoing of monetary policies initiated by the central banks.

Credit creation in the conventional system is meant to keep the growth of base money smooth over time. This has remained untouched even in the emerging Islamic banking system - it chose to follow in the footsteps of the same system that it rose to replace. Islamic banks have little option in the matter of credit creation: their methods and precautions could of course be different. The real problem in fact is on the control side: what would or could replace the bank rate as control weapon in the hands of the central banks. The rising leverage ratios and commissions have to be curbed. Perhaps, there exists a case for taxation of leverage gains with steep progression.

D. Issues in financing the Government / public sector needs

The paper captioned, “*Challenges of Transforming riba-based Government Debt to Sharī'ah-Compliant Instruments in Pakistan*” was presented by Mr. Riaz Riazuddin, Chief Economic Adviser, State Bank of Pakistan. He briefly discussed the efforts made for Islamic banking in

Pakistan where the policy of transformation of the whole economy to *sharī'ah* compliant basis was changed in 2002 to Islamic banking working parallel with the conventional banking. Substantial progress has been made in that regard. The parallel approach adopted in Pakistan has the potential to achieve the objective of transformation of the economy, if and only if, concerted efforts from key national institutions continue to move forward. Progress has been much slower in respect of Islamisation of government debt obligations compared with Islamic banking as a whole. He identified the challenges and emphasized the need to overcome them for the benefits from macroeconomic management point of view. The main challenges identified by him include:

- i) eliminating the domestic public debt held by the SBP (the central bank);
- ii) acquirement of *sharī'ah* compliant debt obligations by SBP to face monetary policy challenge;
- iii) speeding up the issuance of sovereign *ṣukūk* that have the potential to replace permanent (long term) portion of domestic debt;
- iv) gradually transform the mindset of investors towards active acceptability of *sharī'ah*-compliant products through publicity campaigns; and
- v) the long-term challenge of creating appropriate non-interest-based benchmarks for linking *sharī'ah*-compliant returns to investors.

He also gave some suggestions to speed up the process of transformation of public sector financing towards *sharī'ah* compliance by way of *ṣukūk* issuance. He added that “the main challenge for the government is to identify the assets, with full documentation and valuation, which can be used to structure the required *ijara ṣukūk*. Meeting this challenge would result in a benefit of financial prudence because the amount of resources raised would be limited by the value of identified assets”. But for this, the government should be firmly committed to transform the existing debt towards *sharī'ah*-compliant asset-backed instruments. Mr. Riazuddin also observed that if the government limits its borrowing to the extent of value of its assets, it will pave the way for the private sector to raise more resources to undertake productive economic activities that promote investment and growth.

Accumulation of the debt held by SBP (27.1% of total GoP domestic debt) has been by way of a very simple book entry - SBP crediting the amount required by the government and booking a liability there against

as an asset (called Market Related Treasury Bill) in its books of accounts. It conceals one of the greatest financial evils invented by financial wizards - purchasing power created and transferred to the government comes out automatically, without any real productive business activity taking place neither in present nor in future. "This is a unique kind of loan, where the principal created also seems to be very similar to *riba*, not to mention the interest received by the SBP, leading to creation of excessive or hyper inflation". ... "Currency is debased even further when SBP transfers its "profits" to government and if it spends this on any activity other than retirement of existing debt". He asserted.

He quoted Al-Ghazali saying, "To put a bad money into currency is an injustice for the reason that the person who makes a transaction with that money is harmed.' "Circulation of one bad dirham is worse than theft of a hundred dirhams, as theft is one sin and it is finished once for all; while spending bad money is an act of evil which affects all those who use it". He posed a question to *sharī'ah* Scholars, "shouldn't this transaction between SBP and government be prohibited completely?"

According to Mr. Riazuddin, a significant portion of SBP debt can be reduced by gradually withdrawing from surplus cash balances of government and public sector enterprises lying unutilized in several commercial banks that amounted to Rs 913 billion (63.7 percent of debt take from SBP) as in December 2010.

As regards the central bank's monetary policy in Islamic framework, he observed while citing the view point of Ibn Khaldun, Al-Ghazali, Ibn Taimiyah and Al-Maqrizi that inflation control with the objective of 'price stability' should be the main goal for a central bank. Solution lies in removing the monetary overhang from the system meaning that "if the government actions have created excess currency in circulation, it has to be drained back from the system to bring inflation down". For this, the central bank may be allowed to issue *sharī'ah*-compliant instruments against its assets. While it may seem at present that SBP will be constrained severely by its inability to issue its own *sharī'ah*-compliant instrument in large sizes, this will actually be the greatest advantage in controlling its balance sheet because of the benefit embedded in the self limiting character of Islamic finance. The purpose can also be achieved by using the GoP *sharī'ah*-compliant instruments held by SBP to manage liquidity through their outright sales and outright purchases from the financial institutions.

With regard to developing the *sharī'ah* compliant benchmark for pricing the finance and investment products, Mr. Riazuddin suggested that usufruct derived from a real estate could be valued at the potential rent it might earn when rented out. Annual rate of rental would be the annual rent amount expressed as percent of the value of real estate. Surveys in major cities can be conducted to establish an “Office Price Index” and an “Office Rent Index”. Annual rental rate can be easily derived from these indices. Further, instead of constructing office price and rent indices, median (or any other appropriate non-parametric central tendency measures) rental yield can be selected as the benchmark yield and tracked periodically. The variation in annual rental value, which is a ratio of market value of rent to the value of property, will depend on the difference between growth rate of numerator and the growth rate of denominator. An alternative approach, based on sample surveys of knowledgeable real-estate agents, can also be considered.

Regarding changing the mindset of educated Muslim elite, he observed that “a carefully launched publicity/education campaign to remove the cynical perceptions of a large number of Muslims in Pakistan will go a long way in converting the faith-based latent demand to an effective demand for Islamic financial products”.

E. NPL and controlling defaults in repayments of loans

Prof Iqbal Hashmi, Legal advisor at Askari Bank, FFBL, Red Crescent, NLC and former Special Prosecutor & Legal Consultant, NAB presented a paper on “*NPL: Loopholes in the Procedures of Banking Institutions- At Cross road to Article 2 of the Constitution of Pakistan and the Tenets of Islam*”. His paper was divided into following parts.

- i) Banking Courts and select legal provisions.
- ii) Unsound Collaterals.
- iii) Top 50 Nonperforming loans (NPL)
- iv) Seeking Legal Advice a formality – lacking the will.
- v) A Cry from a Contentious Banker.
- vi) Saying and practice of Prophet Muhammad in respect of loan defaulter
- vii) Few Recommendations for way out.

According to findings of Mr. Hashmi, the most of the NPL is due to some very big names in the country, but they were not doing their duty

toward the nation as also God mainly due to white collar crimes by way of maneuvering between the banks' corrupt officials and greedy rich. He lamented that practically, banks' officers do not provide documentary evidence, ocular evidence does not depose incriminating material, legal wizard pays empty handed courtesy calls; call it temporary duty, persuasion, liaison, efficiency or give it any name, but banks interest remains empty and so is the national interest. Things are put under the carpet and no one knows. Thus white collar crime is executed and also abated in financial matters. There should be no room for a once upon a time LLB non practicing officer, with connections to head or manage the legal affairs of any bank. He suggested the following measures:

- i) Meaningful prosecution within the time provided in the Law and care in Adjournments;
- ii) Amendment in banking laws
- iii) Awareness campaign, essential provisions of banking laws should be made known and understood to the concerned citizen by way of organizing seminars, talk shows, short courses.
- iv) Award by the bank for success of case by lawyers of integrity.
- v) No hefty fee to be paid to any lawyer what so ever by any bank, financial institution.
- vi) The unreasonable fee is for unreasonable purpose. Fee should commensurate at juxtaposition in moral and Islamic value.
- vii) The tenure of the Bank's legal Advisor should be 3 to 5 Years, extendable beyond 5 years on the basis of tangible success - could be implemented by way of promulgation of enactment. He should be made responsible for losses for legal negligence, to the extent of his share pro-rata.

F. *Sharī'ah* and Legal issues in floatation of *ṣukūk* in Various Jurisdictions

Dr. Mohamad Akram Laldin, Executive Director, ISRA, Malaysia discussed various unresolved legal and *sharī'ah* issues surrounding *ṣukūk* that, if not correctly responded to, may cause trouble to Islamic finance industry in the future. The Paper regarding issues in *ṣukūk* is backed by Empirical Findings from two ISRA Research Projects:

- i) A Synthesis of *Sharī'ah* Issues and Market Challenges in the Application of *w`ad* (undertaking) in Equity-based *ṣukūk*

ii) A Diagnosis of Tranching in the Light of *Sharī'ah* Principles

Among the significant issues discussed in the paper included issues of ownership of underlying assets, tranching, re-purchase undertaking by the originators and thus guaranteeing the fixed return to holders, *ṣukūk* trading, credit enhancement facilities, legal documentation and other related aspects. Dr Laldin observed that the most of the *ṣukūk* issued are **asset based** where no true sale occurs and the asset is seen as a facility to enable the *ṣukūk* issuance; the asset remains in the issuer or the originator's book and is not transferred to the *ṣukūk* holders. The only recourse the certificate holders have in the event of default is to exercise the purchase undertaking made by the issuer. *Sukūk* should be rather **asset-backed** in which case true sale is a requirement and thus, the ownership of the asset transfers to the certificate holders; in the event of default, they can dispose it to third party in order to obtain remedy for their losses. Purchase undertaking by the originator at the pre-agreed price also creates serious *sharī'ah* related issues. It becomes somewhat like a guarantee of the capital and this is not possible where *ṣukūk* is an investment instrument. However, if undertaking is made to purchase the *ṣukūk* certificate at market value, *sharī'ah* has no objection. It is further argued that the most of the *ṣukūk* structures are far away from the objectives of *sharī'ah* which include promoting justice and removing harm.

This is why that since start of issuance in 2001, *ṣukūk* have been accused to be identical to conventional bonds. This is because they possess some similar features and provide similar economic effects. There had been a call for reexamination of their structure particularly after the well-known remarks made by the Chairman of AAOIFI's *sharī'ah* Board that 85% of the *ṣukūk* were non-*sharī'ah* compliant. Further, the 2009 defaults in several *ṣukūk* issues have also triggered the need to re-examine their *ṣukūk* structures and the industry as a whole.

The recent default in respect of some *ṣukūk* has caused disputes between parties and some cases were brought to courts. Legal examination found that there might be some flaws with *ṣukūk* and various *sharī'ah* and legal issues were raised. It is feared that courts are not familiar with *sharī'ah* transactions and might wrongly interpret the contract as the legal documentation would be the main reference in relation to the transaction.

Strict *sharī'ah* and legal scrutiny from times to times need to be carried out so that all the unsettled issues in relation to *ṣukūk* deals are unveiled and corrected. There is also concern that legal documents do not match the *sharī'ah* requirements thus allowing chances for the transaction to be declared as null and void. *Sharī'ah* scholars should have the capability and ample time to scrutinize the legal documents as it shall evidence the true right and obligation of the parties as well as whether justice and *sharī'ah* guidelines are followed. Dr. Akram Laldin suggested following solutions which may have the potential of lasting effect:

- i) Legal Practice Reform
- ii) Cautious management of documentation risk. Parties must understand all the terms in the document and ensure they conform to *sharī'ah*
- iii) Lawyers need to understand *sharī'ah* requirements; or else there could be conflict of terms that cause conflict in *sharī'ah* requirements
- iv) To include a clause for resolution through Alternative Dispute Resolution (ADR) in case of disputes and making ADR as the first choice in case of dispute
- v) To have specialized expert in courts or special courts to resolve the issues
- vi) Amendment to related statute to make it binding upon courts to refer to *sharī'ah* Advisory Council in *sharī'ah* related aspect.

G. *Sharī'ah* Governance Framework for IFIs and the Role of *Sharī'ah* Boards

Mr. Rustam Idrees of Islamic Banking & *Takāful* Department, Bank Negara Malaysia and Dr. Muhammad Qaseem of Dubai Islamic Bank Pakistan made presentations on the subject. Mr. Rustam discussed various *sharī'ah* governance models instituted by the IFIs in selected jurisdictions and the issues surrounding such models. He also discussed the recent issuance of the IFSB *Sharī'ah* Governance Standard and its implication on the Islamic financial industry. He explained the parameters suggested in the Standard and discussed implications for development of Islamic finance industry. He also shared the experience of development of the *sharī'ah* governance framework in Malaysia. He underlined that the principles of Islamic finance place great emphasis

on strong corporate governance values & structure, transparency, disclosure of information & strict adherence to *sharī'ah* principles. In this regard he briefly discussed the role of AAOIFI, IFSB and OIC Islamic Fiqh Academy and indicated competencies for *Sharī'ah* Governance on the basis of Malaysian experience.

According to the Central Bank of Malaysia Act 2009, Rulings made by the Sharī'ah Advisory Council (SAC) are binding on IFIs, courts and the arbitrators. The *Sharī'ah* Governance framework provides comprehensive guidance to the board, *sharī'ah* committee and management of an IFI in discharging its duties in matters relating to *sharī'ah*. The framework provides solid rules for the following:

- i) Oversight, Accountability & Responsibility - of the board of directors, *sharī'ah* committee and management of the Islamic financial institutions
- ii) Independence - ensuring sound *sharī'ah* decision-making, and emphasis on the role of the board of directors in recognizing the independence of the *sharī'ah* committee
- iii) Deciding competencies to ensure that key functionaries are capable of implementing *sharī'ah* governance
- iv) Observing and preserving confidentiality and improving the level of consistency in decision making by the *sharī'ah* committee / board

Mr. Rustam indicated the following challenges with regard to *sharī'ah* governance:

- i) Ensuring competency of *sharī'ah* scholars to understand the complexity of Islamic financial instruments
- ii) Demand for talented *sharī'ah* experts outstrips its supply
- iii) Whether a robust *sharī'ah* governance framework is essential for each institution regardless of their structural differences?
- iv) Absence of *sharī'ah* audit framework

Dr. Muhammad Qaseem presented Paper on “Role of *Sharī'ah* Boards in Product Development and Ensuring *Sharī'ah* Compliance in IFIs”.

He dilated upon the meaning of *sharī'ah* compliance, its importance in the Islamic banking industry and how non-compliance can

jeopardize the integrity of the system. He also suggested a mechanism that could help *sharī'ah* boards in playing their role effectively to overcome the challenges. He discarded the difference between “*sharī'ah*-based” and the “*sharī'ah*-compliant” contracts as mistakenly understood by some of the experts / economists and observed that any contract which is *sharī'ah* compliant is also *sharī'ah* based, meaning that the *sharī'ah* has not disallowed it and that the same is valid provided it leads to a *sharī'ah*-compliant outcome as well. “The *sharī'ah* disallows an apparently *sharī'ah*-compliant contract if it is evident that it is being used as a legal device to work around a prohibited contract. *Bai' al 'ina* and organized *tawarruq* are examples of such transactions, and hence have been prohibited by the *fuqaha*”. It, however, is baseless to argue that “Islamic banking will not be *sharī'ah*-compliant unless it serves certain financial visions and objectives”. He further observed, “While there is no dispute that all IFIs should observe *sharī'ah* principles in all areas, also including dress code or *hijab*, however, non-compliance in such areas would not render their financial transactions *sharī'ah* repugnant provided the contracts fulfill the *sharī'ah* requirements”. “If the *sharī'ah*-compliance objective is achieved through a *sharī'ah*-compliant contract, rather than through a loan with interest, with similar economic consequences (as in the case of a conventional product), the similarity in result should not render the *sharī'ah*-compliant contract, repugnant.

Dr Qaseem observed that a *sharī'ah*-compliant contract must not contain any condition which runs against its nature. Further, “if there is a consensus of jurist scholars on the prohibition of a contract, it will remain so, and no new *ijtihad* is allowed in this regard. However, if there is a difference of opinion regarding the permissibility of a specific contract, IFIs may follow the opinion of that *fiqhi* school which has the predominant number of followers in the area of its operation. If a case is made for standardization and global acceptability of Islamic banking products, IFIs would be better off selecting, through collective deliberation and discussion amongst *sharī'ah* scholars, such opinions that serve the *sharī'ah* objectives in a better way and are supported by stronger evidence. In this regard, IFIs should avoid basing their products on opinions regarded as weak, or on opinions cherry picked from different schools of *fiqh* in a manner that the composite structure would not be acceptable to any one school”.

With regard to effectiveness of *sharī'ah* supervisory function in an IFI, Dr Qaseem observed that the *sharī'ah* board must not be made subservient

to the Board of Directors of the IFI. As a single *sharī'ah* advisor might not be able to carry out the duties in a befitting manner, the regulatory authorities should make it obligatory on the IFIs to constitute full-fledged *sharī'ah* boards for fatwa and supervision of their activities from *sharī'ah* perspective. They should also ensure that IFIs are bound by the *sharī'ah* pronouncements, opinions and guidance given by their respective *sharī'ah* boards and the national *sharī'ah* board, if any. Through reviews and inspection from time to time, the regulators should also penalize the erring IFIs to ensure that *sharī'ah*-compliance stays at the top of their priorities.

As regards the competency, the *sharī'ah* board members should have the required technical knowhow on banking operations and commercial practices enabling them to properly understand the issues and queries and suggest / approve *sharī'ah* compliant solutions. There should also be a full-fledged *sharī'ah* department, manned by the persons having adequate knowledge of *sharī'ah* as well as banking, in an IFI that should have at least the following units: i) Product development, structuring and documentation; ii) *sharī'ah* audit and compliance; and *sharī'ah* related training. Training for staff of this Department should be planned in a way that a person with *sharī'ah* background should be given specialized training in banking while the person with banking and financial knowhow should undergo specialized *sharī'ah* training.

He also suggested the steps and measures that have to be taken by the management to ensure that the *sharī'ah* board plays its role in an effective manner. A *sharī'ah* compliance manual should be developed that determines the duties and functions of the *sharī'ah* board and the responsibilities of the management vis-à-vis the board.

Sharī'ah board must be properly involved in product development, audit and training and supervise the process of product development taking into account the *maqāṣid al-sharī'ah*, avoiding dubious products and mimicking the conventional structures and aiming to take Islamic banking to the next level. "The tasks of product development, structuring of new transactions and documentation cannot be left to the management alone". "Similarly, the *sharī'ah* board should be directly involved in *sharī'ah* audit and training of the staff on the products and services provided by the IFI". Dr Qaseem concluded.

H. The process and implication of structured - Islamic financial products like Commodity Murabaha /Tawarruq

On this subject two papers were presented followed by intensive discussion by some delegates and particularly by Dr. Monzer Kahf. Dr

M. Tahir Mansoori presented a paper on the use of *ḥiyal* in Islamic finance and their *sharī'ah* legitimacy with special reference to the current practice of commodity *murabaha*. With reference to a number of references as reported in classical *fiqh* literature, he discussed some instances of use of *ḥiyal* in current Islamic finance practices like *bai' al-'inah*, *tawarruq* and commodity *murabaha*. He referred to the Fatwa issues by the Fiqh Academy of Muslim World League that allowed *tawarruq* with certain conditions in its 15th session but reviewed its fatwa in its 17th session declaring current *tawarruq* practices by the Islamic banks invalid. He concluded that current *tawarruq* practice by Islamic banks was only a legal device (*ḥilah*) to circumvent the obstacle posed by the prohibition of *riba*. Even more serious is the fact that Islamic banks that are using commodity *murabaha* / *tawarruq* are financing the interest based conventional banks. "The commodity does not come into the possession or risk and liability of bank that buys it. It is only a *ḥilah* to get a certain fixed increase on the amount lent to the financial institution". He also discussed the Sale and Lease-back *ṣukūk* that also contain some invalid legal devices. He quoted the following observation by Mufti Muhammad Taqi Usmani regarding *ṣukūk*:

"If we consider the matter from the perspectives of the higher objectives of Islamic Law or the objectives of Islamic economics, then ṣukūk in which are to be found nearby all of the characteristics of conventional bounds are inimical in every way to these purposes and objectives. The mechanism used in ṣukūk today, however, strike at the foundations of these objectives and render the ṣukūk exactly the same as conventional bounds in terms of their economic results".

The other presentation was made by **Mufti Muhammad Najeed Khan** on the subject of "*Sharī'ah Compliance issues in Commodity Murabaha as being Practiced*". He discussed the juristic features of *tawarruq* and the current practice of Commodity Murabaha (CM) by involvement of one, two or even three brokers. To him, extreme care needs to be taken while practicing such product and following points need to be ensured:

- i) Is CM free from organized and pre-agreed return of goods/commodities to first seller?
- ii) Is to ensure *sharī'ah* compliance of the third sale responsibility of Islamic bank?

- iii) Is the sale a genuine transaction or a mere documents movement?
- iv) Does the broker/vendor from whom the commodity in the first sale have ownership of goods?
- v) Are goods available for sale owned by those who are presented as owner?
- vi) Is there a mechanism to ensure ownership of goods and physical availability?

He tended to approve the need for (liquidity management by IFIs) and the current practice of Commodity Murabaha in Pakistan provided the Basic principles of sale are followed by the banks strictly. Some of the delegates retaliated to this stance and were of the view that fulfilling the requisite conditions is virtually impossible for the banks who undertake the transaction just for placement of their liquidity and it generally takes a few minutes to complete the process by two or three sales by the brokers on behalf of the two banks.

Dr Monzer Kahf was of the view that there should be no need of invalid products like Commodity Murabaha or *tawarruq*, because alternative tools or methodologies are available in Islamic finance that can accommodate the liquidity management and genuine financing needs. He urged the *sharī'ah* scholars to keep in view the objectives of *sharī'ah* for any prohibitions like that of *riba* and *gharar*/gambling. Sale is an alternative to *riba* based transactions, but it should be a real sale – not collusion of the parties to circumvent the prohibition. Putting a transaction into three separate documents by way of collusion will not make it permissible if it is invalid *per se* as a whole. He referred to the principle advised by the cautious *sharī'ah* experts that whenever there is collusion, whether explicit or implicit, usual and customary, in one document or in three documents, or even in three separate contracts, it will be *'inah* and prohibited as collusion is a fake arrangement, not acceptable in Islamic finance. To him, *tawarruq* is a conventional banking product and is being used by those 'Islamic' bankers who themselves talk of Islamic banking converging into the conventional banking. Almost all delegates of the Conference appreciated the view point of Dr. Kahf.

I. Tools for socio-economic development –*Waqf*, Microfinance, and *Takāful* that can help achieve the objective of socio-economic development in an economy:

Presentations on the subject areas were made by Dr. Zeeshan Ahmed of LUMS, Mr. Salman Ahmed Shaikh of Halal Tamweel – A Subsidiary of BMC Pakistan and Mr. P. Ahmed CEO of Pak Qatar Family *Takāful*.

Dr Zeeshan spoke on the topic of “Potential of *Waqf* for Socio-economic Development and Poverty Alleviation”. He explained the differences and similarities between *waqf* and the contemporary ‘Trust’ and discussed the role that *waqf* can play to achieve the *maqasid al-sharī’ah* necessarily including socio-economic development of a society. Exploring the Islamic history Dr. Zeeshan indicated that *waqf* played a crucial role before going to decline.

The institution of *waqf* declined because of the following:

- i) The decline of awareness among Muslims about the virtues and reward
- ii) The states taking on the responsibility for providing for the well-being of the society
- iii) Benefits flowing to the favorite rather than deserving
- iv) Lack of accountability on part of the government; *waqf* encumbered by debt
- v) *Mutawallis* were granted rights to determine who would benefit from the revenues
- vi) Right to benefit from *waqf* was being transferred, inherited, and sold
- vii) Population increased at a faster rate compared to real assets, so the overall donations to this institution have fallen drastically
- viii) The weak judiciary and legal system

He also discussed the “cash *waqf*” that although critiqued by some jurists, yet validated by Ulema based on *zarorat* and *maslaha*. He suggested a Cash *Waqf* Model for Pakistan. He recommended the following steps for revival of the highly useful institution of *waqf*:

- i) People should be told of the virtues of donation, especially *waqf*, in Friday sermons, Islamic conferences and other religious sermons.
- ii) Students should be taught *waqf* in schools and universities as part of their curriculum.
- iii) Wide-scale awareness campaign
- iv) Perpetuity Issue: The *waqf* can support the victims of the similar calamity like flood in some other area, or the victims of another flood, or the victims of some other natural disaster. Careful Statement by Waaqif rather than a rigid one!
- v) Prudent Governance mechanism. Selection of *mutawalli*, *waqf* board, monitoring on specific criteria
- vi) As for the administrators of the *waqf* itself, the State should ensure that *mutawalli* is honest, pious, and skilled with good interpersonal skills.

Mr. Salman Ahmed Shaikh presented his Paper captioned, “Microcredit using Equity Financing: an Alternate Approach to Micro Financing in an Interest Free Economy”. He discussed whether the equity modes of financing are usable in an Islamic economy and what institutional arrangements could be needed to use them in Pakistan; given the fact that the currently practiced Islamic finance mostly uses methods which tie cash flows with an interest based benchmark. He suggested a new thought to solve the principal agent problem and the problems of moral hazard and adverse selection in micro-equity. According to Shaikh, ‘making *rabb-ul-maal* completely responsible for sharing all losses is unjustified, and the clause of willful negligence is insufficient to protect the financers / banks’ depositors from losses strictly due to business cycle fluctuations’. He proposed a change that “*mudarib* can be asked to contribute some capital” and that “*mudarib* can be asked to share in loss to some extent”. However, he took a totally different and irrational stance with respect to the loss sharing in *Shirkah* in general and in *mudaraba* in particular, view point that is against the *ijma*’ of all traditional and contemporary jurists – the loss has to be shared strictly according to the ratio of capital or investment made. It has no rationale as well. He mistakenly categorized all deposits of Islamic banks as “Liability Side”, which is case only to small proportion of non-remunerative current deposits.

It can be provided in the policy that instead of capital provision by the financial institutions only (case of *mudaraba*), entrepreneurs may

also be required to contribute some capital so that the problems of adverse selection, moral hazard and principal-agent conflicts could be minimized. But the loss sharing principle would remain the same - the loss in a joint has to be shared strictly according to the ratio of capital provided by the partners of the business.

Mr. Salman suggested that Microfinance needs can be met through two separate institutions: i) Micro Venture Capital (VC) funds who could invest in micro enterprises for group based financing; and ii) Micro VC funds that could provide standalone financing (non-group) through *qard al-ḥasan* and through issuing Profit Participation Certificates (PPC).

He also discussed the use of *zakāh* and *'ushr* as poverty alleviation tools and keeping in view the two *'ushr* rates (10% for produce of rain fed land and 5 % in case of irrigated land), he suggested imposition of *zakāh* on industries employing both labor and capital @ 5% and from industries employing only labor or only capital @ 10% of their produce. Similarly, he suggested imposition of *'ushr* on profits / dividends from stocks, mutual funds, rental incomes, etc. This has to be paid to the government that has no right to impose any other tax. As all these concepts are against the fundamental principles accepted by the jurists as consensus, the Conference delegates severely criticized and some senior level scholars advised the author to reconsider his view point.

J. Some specific Islamic finance aspects

Prof. Dr Zubair Hasan, Mr. Muhammad Aman Ullah, and Mr. Muhammad Javaid Ismail made presentations on some specific aspects of Islamic banking and finance. **Dr Zubair Hasan** presented a comprehensive paper on “Islamic house financing: current models and a proposal from social perspective”. Availability of shelter for the people is an Islamic imperative. Islamic banks have entered the field with varying schemes for house financing guided by profit motive. But, at present they are playing no mentionable role in the sector, the author observed. Giving example from Malaysia and Bahrain, the two leading Islamic finance hubs, he indicated that the share of construction in total finance is just 5.7%. Even there the expenditure on residential housing is very low. The situation is no different in Indonesia, Pakistan, Bangladesh or Egypt, the most populous of countries in the Muslim world.

Further, a social dimension has to surface in course of time. The models banks currently use for house financing remain under the juridical gaze, more so as the practice is not always found transparent. The difficulty with Muslim countries, according to the author, is that “they have not yet been able to free themselves fully of the Western thought process, value system and culture ethos they perforce acquired during the long colonial occupation of their lands. Islamic economics and finance took off well but now charter the un-chosen course. Islamic institutions cannot find roots and deliver in a set-up dominated with alien ways and ends. Islamic finance is not showing concern for housing because the Islamic insistence on the fulfillment of basic needs does not form the core of planning in Muslim countries”.

The author has evaluated the efficacy of current financing structures, with special reference to Malaysia, and suggested a new approach. The current models that he discussed include i) BBA - sale with price deferment with and without buy-back (*inah*) provision; banks insist that whatever be the time point of default, the remaining debt has to be cleared in full; and ii) Diminishing *musharaka* Model which, according to the author, is little different from the operational mechanism of the conventional model (as practiced in Malaysia). Rather, the conventional banks terms were more specific and straight forward. He proposed the diminishing balance model which tends to meet the norms of equity, fair play and openness and does not presumably violate any other Islamic norm. [It may be observed here that the Diminishing Musharaka procedure followed presently in Pakistan is almost the same as diminishing balance model suggested by the author. An added feature of Pakistan’s DM procedure is that rental is calculated keeping in view the (decreasing) number of units in the bank’s ownership.] He has also suggested some policy shifts to integrate Islamic house financing with broader social goals of an Islamic economy.

The suggestions that he made for improving the contribution of Islamic finance in the housing sector, inter alia, included:

- i) Establish National Housing Foundations in all countries with regional offices in different areas; provide seed money and encourage people to register and make deposits to own a home in the future. People should know and feel, through effective media campaign, that something is really being done for providing a roof over their heads;

- ii) Issue housing *shukūk* to mobilize funds, open even to international subscriptions;
- iii) Persuade and if need be instruct banks to support the housing sector. “They may find it beneficial to combine in bigger units to meet the challenges (Nannana U. J, 2010)”.
- iv) Establish an apex body for integrating various countries programs and support research in designing and construction of cheap yet comfortable homes.
- v) Effort at the national and regional levels for creating the environment in which Islamic banks could perform and deliver.

Mr. Aman Ullah, Dr. Nasim Shah Shirazi and Mr. Muhammad Akhtar of Riphah International University contributed a paper on “A Framework for Sharing Business Profit for IFIs under *Musharaka* and *Mudaraba* Contracts” They argued that the most of the IFIs could not successfully operationalize *musharaka* and *mudaraba*. They examined the feasibility of implementing these modes in the wake of contemporary financial reporting on the basis of which profit is to be distributed and which has failed to deliver even in a secular framework leave alone an Islamic framework. According to the authors, the process of Islamisation is focusing on one half of the issue and a very important second half, the process of determining profit by the business organizations under the so called “Generally Accepted Accounting Principles” is being completely ignored. “The basic mistake in the whole process of Islamisation of banking and economics has been to accept the existing market structure, banking system and financial reporting framework as given, legitimate and inevitable”. They argued that with present financial reporting framework *musharaka* and *mudaraba* might not be feasible.

About the contemporary financial reporting they observed, “It was after the 1929 NYSE crash that the debate of harmonization of accounting practices by removing rampant diversity started. They indicated that for the first 15 years IASC did not have any written conceptual framework and the focus remained on haggling with practical issues rather than developing the conceptual basis for the solutions. Mechanics preceded the philosophy and even the logic. The term “Generally Accepted Accounting Principles” was used by the Secretary of NYSE and is used since then with really no specific definition”. “In fact, the IASC had approved 26 International Accounting Standards (IASs) before it began work on conceptual

framework at the end of 1986". "Ambiguous terms like fair value, reserves, substance over form make financial reporting incomprehensible not only for non-finance people but also for qualified accountants"; they added.

They quoted Paul Rosenfield saying, "Financial reporting apparently is the only activity in which the providers of products or services look to the needs and desires of the providers rather than the needs and desires of the consumers to determine how to design the products or services" The result is in the form of ENRON, Xerox and many more. Recognition of the revenue is a complex issue which needed to be taken care of properly.

In addition to the fact that accounting profit is not an absolute figure having absolute meaning, there are some specific problems from *musharaka* perspective:

- i) The accounting profit does not include changes in the values of assets during the period for which profit/loss is calculated. Revaluation, if any, directly goes to revaluation surplus in the equity section of the balance sheet. Should we ignore it in a *musharaka* contract?
- ii) With regard to the impairment of assets, it is the prerogative of the management to decide as to when and what assets are to be declared as impaired. IAS/IFRS provide guidelines but it's a matter of judgment. The impairment of assets passes through income statement as an expense. Writing off impaired assets in a particular year, to be decided by the management, remains in conformity with GAAP and does not violate the norm of consistency as stipulated in the *musharaka* contract designed by the State Bank of Pakistan.
- iii) Research and Development remains a sore point in contemporary financial reporting. It creates inter temporal problems of distribution of profit. The cost of research, even if it is capitalized in case of development, is born by one set of shareholders and benefits enjoyed by another set. How should it be dealt in *musharaka*, particularly if it is short term?

The authors observed that the fundamentals of the prevalent system need to be revisited so that real profit could be shared among the partners. Practicing *musharaka* and *mudaraba* may not be feasible with present financial reporting framework. They also argued that until

an appropriate framework is prepared, no progress towards achievement of the objective would be possible.

Mr. Muhammad Javaid Ismail of the State Bank of Pakistan made presentation on “Restructuring Islamic Finance Facilities”. Non-payment of the payables / debts by the banks’ clients is a serious issue in global finance, but it is more serious issue for IFIs. Mr. Ismail shared relevant data with regard to some Islamic countries including Pakistan, Kuwait, UAE, Turkey and Saudi Arabia and referred to AAI OFI *sharī’ah* Standard No.3 on default in payment by a debtor and IFSB-1-Guiding Principles of Risk Management for IFIs. A number of *sharī’ah* and legal issues in *ṣukūk* led to loss of confidence of the investors. The knock on effect of global financial crisis led to: i) deterioration in financial performance of financial institutions; ii) high non-performing portfolio on the books of the banks; sharp decline in the Corporate *ṣukūk* volumes; iii) default on some *ṣukūk*; iii) rating downgrade; and iv) Increased restructuring and rescheduling activities by the banks. With the decline in asset prices, credit risk increased due to erosion in the value of collateral, especially in high leveraged countries like UAE and Qatar, where large share of financing was channeled to the once booming real estate market. Some IBs suffered large losses due to credit concentration. Global Finance House (a wholesale IB) lost \$730 million due in part to taking \$311 million in provisions for real estate project in Dubai. Bahrain Islamic Bank exposure to Saudi groups Saad and Algozaibi contributed to the \$51 million losses in 2009. Mr. Javaid recommended the following for the future:

- i) Introducing regulatory limits on sector specific concentration;
- ii) Appropriate risk resolution framework addressing Islamic finance specific issues;
- iii) Developing effective dispute resolution framework for early settlement of Islamic finance facilities;
- iv) Amending legal framework for swift court proceedings;
- v) Developing a body of literature on recent approaches to restructuring Islamic finance facilities; and
- vi) Building capacity of legal community in the area of Islamic finance

K. The challenges and prospects for managing businesses in *sharī'ah* compliant way

With regard to doing business in the *sharī'ah* compliant way, presentations were made by Sheikh Hashim Ahmed, Sheikh M. Naem, Mr. Arshad Iqbal Malik, Mr. Suhail Nadeem and Mr. Khalid Waheed.

Sheikh Hashim Ahmed of Al-Khair Karachi, made presentation on “Islamic Business: Philosophy and Practice with Case Study”. According to him, conducting Islamic business means obedience to the tenets of *sharī'ah* and a fine balance between the worldly life and the Hereafter. Al-khair’s vision is to transform perceptions, objectives and practices of business from material base to *‘ubudiyyah* base, while its mission is to i) establish and sustain a business organization based on Islamic and professional excellence; and ii) provide humanity with beneficial products aligned with a healthy and meaningful lifestyle. Core values of a business must comprise Islamic excellence, professional excellence and benevolence. Islamic excellence means *eman / yaqeen, ikhlas / naseehah*, *sharī'ah* Compliance with spirit of Sunnah and character / morals while professional excellence refer to personal management and discipline, initiative, creativity / innovation and teamwork. Islam also requires care and development of all associates in the organization, suppliers/service providers, customers, community, industry, country and the humanity at large. As a whole, business as per *sharī'ah* injunction would mean:

- i) Vision / Mission oriented life
- ii) Honesty/ Integrity
- iii) Continuous quest for knowledge
- iv) Continuous quest for excellence
- v) Dedication / Commitment (*‘azm*)
- vi) Consistency (*istaqamah*)
- vii) Cleanliness

He indicated that Al-Khair is working for the development of all associates in five areas, namely spiritual, intellectual, emotional, physical and adaptation of a visionary life in the light of Islamic principles. With regard to HR, it is trying to follow the best Islamic and professional practices such as: recruitment / orientation, defined JDs, attendance, monitoring, maintenance of personnel files and evaluations. Its procure department is striving to acquire the most suitable materials to optimize

the benefit of AK's products, for both the consumer and the company. Production department is working in line with the best of Islamic and professional excellence which includes optimum quality, time frames, cost and overall efficiency.

Marketing and sales department is trying to contribute to the betterment of lives of people by facilitating them to use Al-Khair's beneficial products. Its core functions include:

- i) To identify 'real needs' of the people which are aligned with AK's Mission statement and generating functional appeal
- ii) Marketing mediums to be *sharī'ah* compliant and with the spirit of Sunnah
- iii) Promoting the culture of mutual benefit (abundance of resources) as against scarcity of resources (cut throat competition)
- iv) Providing timely financial information to facilitate better informed business decisions
- v) Accurate assessment of business performance to help facilitate higher levels of professional excellence
- vi) Developing, implementing and monitoring AK Policies and Procedures, leading towards Islamic and Professional Excellence

Referring to one product of Al-Khair – Miswak, he indicated that starting from 1997 with 2000 Miswaks, it marketed 5 million Miswaks in 2009 and, in addition to local supply, exported to more than 35 countries. Target for 2010 – 11 has been set at 10,000,000 *miswaks*.

Sheikh M. Naeem of Shafi Group of Companies presented Case Study on practicing Islamic values in business and highlighted the developments of their journey of success - 1925 to 2010- from a small cart on foot path in Calcutta to 5 companies now. He indicated that business is conducted by the Group to seek the pleasure of Allah SWT, earn RIZQ e HALAL, fulfill family commitments, support economic activities of the country and to feel sense of accountability before Allah SWT. Personnel recruitment is made keeping in view the competence, character, family background and Islamic knowledge & supplication. Arrangements are made for moral training. Banking and finance needs are met in the best possible *sharī'ah* compliant way. Financing is not taken from any bank while *zakāh* is paid regularly. Staff welfare scheme comprises of the following:

- i) Subsidized Food
- ii) Hajj Policy
- iii) Home Shelter
- iv) *Riba* Free Loan
- v) Transport Facility
- vi) Medical Facility
- vii) EOBI Scheme
- viii) Social Security Contributions
- ix) Children Education Allowance

Rate of staff retention is very high and shifting is only for better opportunity. Salaries are fair & equitable / market Competitive, paid on time without delay; minimum salary is according to Govt. policy and performance based rewards and incentives system is implemented. *Nizam-e-Salah* has been implemented: 70% presence attendance in *salah*; top management offers *salah* in the Mosque and motivational & educational methods are applied to get maximum attendance in the purpose-built spacious mosque. Commitments to buyers, suppliers/vendors, staff, regulatory bodies, affiliated bodies and other stakeholders are fulfilled. Keeping in view the nature of production process, maximum safety measures are taken in factory and offices; for example, chemical treatment...environment friendly, health standard, personal protective equipments, fire hydrant system and extinguishers. Marketing and promotion on electronic & print media is in accordance with Holy Qur'an & Sunnah and things are presented as they are with transparency. Following activities are undertaken as part of social responsibility: Establishment of IQRA School for under privileged area, High School, Technical College, Girls college, and employment (preferably) from the vicinity.

Mr. Arshad Iqbal Malik of **Iqbal & Company** discussed challenges in Practicing Business in Islamic Way and emphasized that given the will, commitment and effort, conducting business by observing the rules of *sharī'ah* is possible even in the scenario wherein corruption and allied maladies are rampant. Every business must have a clear vision that gives direction, motivation, helps in decision making and reduces the risks of failure. For undertaking a business, one must have knowledge of Islamic value system and the business around. "It is not MUST for every Muslim to do business but if one opts to do business then it is MUST for him/her

to follow the *sharī'ah*". The difference between Islamic and conventional way of business lies in respective ethics of doing business. Ethics in Islam predominantly shape the complete life of a Muslim and emerge from the Qur'an, the Sunnah and the secondary sources like *ijma'*, *qiyas* and *ijtihad*. It needs to be taken seriously that while over 95% of people are Muslims in Pakistan, over 95% of businesses in Pakistan are run without following the *sharī'ah*. One must evaluate the business in order to ascertain its legitimacy. The Dos and Don'ts of HALAL BUSINESS include:

- i) *Niyyah* & '*azm* [determination] to earn *halal*;
- ii) Shun *riba* in every form;
- iii) Trade with mutual consent;
- iv) Truthfulness in all transactions;
- v) Trustworthiness in transactions
- vi) Generosity & leniency in transactions
- vii) Honoring & fulfilling business obligations
- viii) Fair treatment of workers
- ix) Avoid dealing in prohibited [*haram*] items
- x) Avoid sale of *al-gharar* [uncertainty & speculation]
- xi) Avoid the arbitrary fixation of prices
- xii) Avoid hoarding of Food Stuff [*ihhtikar*]
- xiii) Avoid exploitation of one's ignorance of market conditions
- xiv) Avoidance of *Al-Najsh* [trickery]
- xv) Avoid cheating and fraud in business transactions
- xvi) Avoid swearing in business
- xvii) Avoid giving short measures
- xviii) Avoid dealing in stolen goods and
- xix) Balancing the role in the business, family and society - success in one area of life should not be at the cost of another area of one's life (The strength of a chain is the strength of its weakest link).

Mr. Arshad Malik also provided a *sharī'ah* Check List to be observed by all businesses. There should be no bribes for gas/electricity connections

or payment / clearance of bills. All taxes and duties must be paid and all transactions documented with one book of accounts. Duties prescribed by the regulators must be performed, e.g. Pharmacist Instead of a Pharmacist Degree. Finance needs must be fulfilled in *shari'ah* compliant way. Marketing is one of the most critical areas; one must not portray any product through exaggeration or misleading advertisements, false promises, subliminal messages, using women/men to sell products. Similarly, one must not pay for personal chores of decision makers [doctors/nurses/technicians/clerks] or send them on FOC trips overseas in lieu of business attainment.

Mr. Malik also presented case study of his firm, "Iqbal & Company" and shared with the audience how they met the challenge of doing business observing the Islamic injunctions in a hostile environment. According to the vision, "**IQBAL & COMPANY**" is a leading importer and supplier of medical devices. It prides itself in adhering to Islamic principles irrespective of the obstacles being faced in the current market. Honesty, sincerity and truthfulness are the traits by which we wish to be judged. We value the association of our employees, our vendors and our customers; together we are striving to work for a better tomorrow in this world and for a better *aakhirah* in the next. May Allah guide us to the right path and assist us in obtaining *rizq-e-halal, Aameen*". **Strengths** of the company include:

- i) Established: Over 25 years in the areas of specialization (no start up costs/risks)
- ii) Large installation base of equipment
- iii) Business in all sectors; Government, private, defense, equipment, disposables, maintenance
- iv) Skilled personnel
- v) Right products at the right time
- vi) Ahead of competition
- vii) Large, inventory of equipment, spares and disposables.
- viii) No borrowing from bank
- ix) Trained staff including foreign trainings
- x) Full access to communication channels computer, emails, fax, telephones and new software under development
- xi) Dedicated/devoted/satisfied staff

- xii) Belief that ultimate help comes from Allah and we get what we are destined to, by His Will (SATISFACTION)
- xiii) Specialized / Focused approach
- xiv) Market leader in several products.
- xv) Trend setters.
- xvi) Free from corrupt practices.
- xvii) Excellent after sales & service support.

Weaknesses of the Company, as listed by Mr. Malik, include:

- i) Marketing information
- ii) Marketing not skilled enough
- iii) Relaxed attitude - Relying on a few customers and on a few products
- iv) Too much reliance on tenders
- v) Require improvement in contact with end users
- vi) Ineffective follow-up
- vii) Visit of old customers not frequent enough
- viii) Do not visit or occasionally visit customers of competitors
- ix) Large Accounts Receivables, Earnest Moneys, Securities (High costs)
- x) Limited product range
- xi) Inflexible when it comes to demands of customers
- xii) Some products not suited to market - High prices and High end specs
- xiii) No plan to expand the business.
