

Islamic Banking

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Basic Principles in Islamic Banking

- Compliance with Shari'a
- In term of Islamic banking:
 - no riba
 - no prohibited items
 - no prohibited dealings (gharar, unjust enrichment, etc)
 - no prohibited purpose (5 maqasid shari'a)
 - risk as an important factor to justify the profit

Basic Principles in Islamic Banking

- Riba can be of these three types:
 - Riba Fadl;
 - Riba Nasi'ah; and
 - Riba Jahiliya

Basic Principles in Islamic Banking

- Riba Fadl – also known as Riba Buyu', i.e, the exchange of good of the same kinds but of different quantity or quality or in term of delivery
- Riba Nasi'ah – also known as Riba Duyun, i.e, the usury that arises when lending or borrowing does not meet the criteria of alghunmu bil ghurmi (profit goes along with risk) and al kharaj bi dhaman (income goes along expense)
- Riba Jahiliyah is a debt to be paid in excess of its principal due to the borrower's inability to pay the loan at an agreed time.

Basic Principles in Islamic Banking

- Riba Fadl – example: non-cash sale and purchase transactions of foreign currencies
- Riba Nasi'ah – example: payment of interests on credits as well as on savings/deposit accounts
- Riba Jahiliyah – example: the imposition of interests on credit card charges that are not fully paid.

- Source: Adimarwan A. Karim at pp 34-8.

Basic Principles in Islamic Banking

- No prohibited items (the subject matter)
- It can be prohibited by itself, eg, transactions relating to port, alcoholic drinks, etc.
- It can be prohibited, not due to itself, but as such subject cannot be made the subject for certain transactions, eg, gold and silver as the subject for financing facility.

Basic Principles in Islamic Banking

- No prohibited dealings
- This will include elements prohibited by Shari'a.
- No transaction = upon property of minor without the authorization of the legal guardian
- No transaction = based on gharar
- No transaction = upon something one do not have (except in case of salam or istisna)

Basic Principles in Islamic Banking

- No prohibited purpose (maqasid Shari'a)
- This will include all transactions the result of which will go against the maqasid Shari'a.
- No transaction = to construct temples
- No transaction = to build a premise to be used for gambling, prostitution, restaurant serving alcoholic drinks, etc
- No transaction = to supply weapons to non-muslim countries that have declared war against a muslim country

Basic Principles in Islamic Banking

- Risk – to justify profit
- This element is the underlining concept that justifies the validity of many Islamic banking products

Banker >< Customer relationship

- Conventional banks: debtor >< creditor
- In Islamic banks: depends on the kind of relationship between the party; however, it would not be a debtor and creditor relationship (due to the prohibition of taking benefit in loan transaction)