# Anatomy of Islamic Finance

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## 1-INTRODUCTION

Islamic finance is a faith based scheme of socio-economic system. Guidelines for modern Islamic financial system are inferred from Islamic jurisprudence (based on Qura'n and Sunnah). Under Islamic law there is a set criterion for issuing a juristic opinion. Accordingly, the foremost important source of law is Qura'n followed by Sunnah, Ijma'a and finally Ijtihad. There are many socio-economic issues directly addressed in The Qura'n and verdict from Qura'n is final. If an issue is not discussed in Qura'n or needs further explanation, then Sunnah is consulted to seek guidance. Anything found in Sunnah relating to a prevailing socio-economic issue is accepted as final verdict (if it is not in contradiction with Qura'n). When an issue is neither discussed in Qura'n, nor guidance is available in Sunnah--and there are many issues of modern life which are not directly discussed in these two primary sources of Islamic law--then Ijtihad is applied in the light of core principles laid down by Qura'n and Sunnah. Throughout the Muslim history, Muslim Clerics have worked on an important aspect of Islamic religion--objectives of Shari'a. This concept is about extracting/inferring goal seeking of religion; as what Islam wants to develop in a human-community. It includes following objectives of Shari'a (Siddiqi, 2010):

*Hifz ul Emaan***:** Within the society religious freedom should be ensured, and particularly for Muslims a conducive environment must be developed to practice their faith. Necessary steps must be taken by collective power (government) of people to ensure freedom of Islamic way of living.

*Hifz ul Jaan:* Second objective of Shari'a is identified by experts in Islamic law is security of life of every individual member within the jurisdiction, irrespective of religious beliefs. Peace and security within the community must be ensured by the government/members.

*Hifz ul Maal:* Safety and security of wealth of all members of the community is a collective responsibility of members/government. Again establishment of just society is required to achieve this objective. Rule of law and order is required by Islamic law in the society. Islamic finance is required to ensure compliance and help the society in achieving this objective of Shari'a.

*Hifz ul Nasal:* Protection of Lineage (Nasal) of members of community must be ensured by collective power (government) of the society

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*Hifz ul Aqal:* Security to intellect is required by religion of Islam. One should have independence to think and apply the brain in decision making. Rationality should prevail in the society.

Taking into account objectives of Shari'a, various efforts for reforming Muslim communities around the world were made by Clerics in 20th century after getting liberation from colonial powers and development of modern Islamic finance is one of those efforts.

**2-Historic Developments**

Modern Islamic Finance is a recent development as a reaction to the prevailing financial system (primarily based upon interest as a charge). According to Abrahamic religions (Judaism, Christianity and Islam) charging of Riba (literally means increase and includes interest and usury) is prohibited (Psalm 15:1,2, 5; Proverbs 28:8; Nehemiah 5:7; Deuteronomy 23:19; Ezekiel 18:8.9 As quoted by Usmani, 1999 and Qura'n 30:39[1], 4:161, 3:130, 2:275-81). After liberation from colonial powers in mid of twentieth centuries, Muslims started looking around at socio-political system through Islamic lenses and tested the systems on religious criteria. In economics prevailing dominant system (capitalism) was challenged by Muslim scholars and offered alternatives (Modoodi, 1962; Ibrahim, 2000; Siddiqi, 2010; Usmani, 2002; Qaradawi, 1960; Modoodi, 1962; Rehman & Tug, Siddiqi, 2010; Zaman, 2010; Ayub, 2007). Major motivational factor in building of modern Islamic financial institutions was elimination of interest, although current operations of the industry covering many other ethical aspects (including *Halal* businesses, discouraging *Gharar* and *Myser*, promoting profit and loss sharing and asset based financing) beyond interest charge. A very brief time line of events in the history of Islamic finance is presented here.

1936-Modoodi, (1962), was the first scholar in subcontinent who criticized the existing practice of interest-based-banking and interest income on deposits with conventional banks declared *Haram*[page 228].

1949- Objective resolution was passed by National Assembly of Pakistan, declaring Islam as state religion.

1960s-Malaysia started program of Hajj financing (Tabong Haji) in sixties, which was converted to full fledge Islamic banking operations, at later stage.

[1] Surah and Verse

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1963-First ever practical experience of interest-free-banking was done in Mitghamar, a town of Egypt, which could not last longer. During same period a bank was offering Islamic finance services in Karachi, but author could not find a written source[2].

1973-Mile stone in the history of Islamic banking was the conference of finance ministers of Organization of Islamic Cooperation (OIC) in 1973, where establishment of Islamic Development Bank was agreed.

1973-In Pakistan it is recognized constitutionally that interest free banking would be the banking of the economy (CoP, Articles 2, 31, 37, 227),

1975-Islamic development bank established and also Dubai Islamic bank started operation.

1979-After revolution, Iran started shifting whole of its economy on interest free operations and major steps taken in 1980s.

1980-However first ever genuine effort was made by Council of Islamic Ideology (CII)-Pakistan in 1980, in the form of a report on "elimination of interest from the economy" and suggested transition and implementation of Islamic banking at operational level.

1984-Interest free banking in Sudan-1984

1985-Pakistan started efforts initially by converting specialized financial institutions (e.g. HBFC, ICP) from conventional to Islamic and transformed total banking system on interest-free-system in 1985 (The Presidential Order # 14). However this optimism failed very badly, primarily, due to non-conduciveness of socio-economic and political environment including lack of human resources, expert in Islamic banking (Khan & Bhatti, 2006) and operations of banking industry continued on conventional system, under the umbrella of profit and loss sharing.

1991-This hypocrisy was not acceptable to practicing Muslims of Pakistan and they took the matter to federal Shari'a court. Apex court issued order, declaring the existing practice (of banking) *Haram* (prohibited), and ordered the government to take drastic measures for implementation of interest free banking as agreed in constitution of Pakistan (FSC-1991).

1991- AAOIFI was established in to issue guidelines for Islamic financial institutions (IFIs) in the area of business, accounting, auditing and corporate governance. (By Nov 2016, 54 Shari'a standards 27 accounting standards, 7 governance standards and 2 codes of ethics were issued for the guidance of Islamic finance industry).

[2] Mr. Alvi A Rahim, Ex chairman CBR, told the author personally.

1999-After receiving the order of the Federal Shari'a court, government of Pakistan analyzed its strengths and weaknesses and once again lack of trained human resources hindered the state from converting conventional system into Islamic. Government of Pakistan responded through two pronged strategies. First; a commission was set up under the able chairmanship of Raja Zafar-ul-Haq to analyze whether interest free system is workable (in fact to re-invent the wheel, as same job had been done by CII in 1980). Second; government went into appeal against the federal Shari'a court decision in Shari'a appellate bench of supreme court of Pakistan (perhaps to get some time in implementation of decision). It is interesting to note there were above 60 appeals, against the decision of federal Shari'a court, in Supreme Court of Pakistan, which were heard by honorable court as a single case[3]. Government failed on both fronts. Commission recommended the applicability of interest free system, and in 1999, Supreme Court issued a detailed decision favoring application of interest free economy (SCP-1999).

2000-By early 2000, state bank of Pakistan (SBP) adopted a different strategy, for promotion of Islamic banking, as parallel to conventional banking. Islamic banking department (IBD) was set up in SBP to guide, facilitate and regulate Islamic banking stream.

2002-Given the binding to execute order of Higher courts, and failure of successive governments in development of Shari'a compliant economic system, in 2002, government of Pakistan filed a review petition in the Supreme Court and case was remanded to Federal Shari'a court to revisit, which is pending to-date.

2002-International Islamic Financial Market-IIFM was established in Bahrain (By Nov 2016, IIFM has issued 9 standards)

2002-International Financial Services Board-IFSB was established in Malaysia (By Nov 2016, 18 standards)

**3-Principles of Islamic Finance**

Islamic finance is based on *Shari'a* (Islamic law). Ulema (Clerics in Islamic law) have identified objectives of Shari'a including safety of faith, Life, property, next generation and intellect (Hifz ul Eemaan, Jan, Maal, Nasal and Aqal) [Siddiqi, 2010]. Every design of community institutions should at least ensure conformity with objectives of Shari'a, if not enhance performance on these

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[3] [This shows the deep roots and resistance level displayed by promoters of conventional financing in Pakistan]

fronts. Based on these objectives of Shari'a following principles of Islamic finance have been documented.

*a. Prohibition of Riba*

First is prohibition of interest and usury in financial dealings. In Qura'n four sets of verses have been identified dealing with the charging of Riba (Al-Qura'n, 30:39, 4:161, 3:130, & 2:275-281). Several *Hadiths* (traditions of Prophet Muhammad PBUH) clearing the meanings of Riba in various transactions have been reported (English translation by Khan, 1989). Furthermore resolutions of council of Islamic Fiqh Academy, Jeddah, are very much qualifying the status of *Ijma'a* (consensus) on the issue of Riba. Also there are several *Ulema* (clerics) who declared both usury and commercial interest Haram (Unlawful) (e.g. see SCP-1999; Usmani, 2002; Qaradawi, 1960; Modoodi, 1962; Rehman & Tug, Siddiqi, 2010; Zaman, 2010; Ayub, 2007). Implication of this principle of Islamic finance is discouraging time value of money in its conventional banking sense. Under Islamic financial system money is mere a medium of exchange and not a factor of production independently. Human labor is required in addition to money to earn a return, hence there is no fixed return for capital, however capitalist can participate in business under profit and loss sharing with or without participation in management of an entity (Shari'a standard # 12).

*b. Avoidance of Gharar*

Second principle of Islamic finance is avoidance of Gharar (absolute uncertainty) in a business transaction (Ayub, 2007, p 57; Mansoori, 2007, p 179; Ghazi, 2010, p 237). Ayub, (2007) defines "Gharar refers to entering into a contract in absolute risk or uncertainty about the ultimate result of the contract and the nature and/or quality and specifications of the subject matter or the rights and obligations of the parties [p 75]. Mansoori, (2007), documented that Gharar contains [certain] characteristics such as risk, hazard, speculation, uncertain outcome, and unknown future benefits.

*c. Prohibition of Myser & Qimar*

Third principle of Islamic finance is avoidance of Myser (speculation) or any game of chance (Ghazi, 2010). Ayub, (2007), documented that Maisir refers to easily available wealth or acquisition of wealth by chance, whether or not it deprives the other's right. Qimar (similar to Myser) means the game of chance; one gains at the cost of other(s) right [p 62]. Myser is prohibited by Holy Qura'n [ 2: 219 and 5: 90] as well as in Hdiths (Khan 1989, p 92)

*d. Promotion of Musharaka*

Fourth principle is profit and loss sharing. As per this principle capitalist demanding profit on capital should also participate in loss as well (Usmani, 2002, p 87; Ghazi, 2010, p 386; Khan, 2007, p 307 & Shari'a standard # 12). According to a famous Hadith (saying of the Holy Prophet Muhammad PBUH) *"sale transaction of something which is not in your possession is not lawful, nor is the profit arising from something which does not involve liability"* (English translation by Khan, 1989). According to this principle an investor can earn return on his investment subject to risk of loss, hence concept of risk free return is disappeared under Islamic financial system.

*e. Mudaraba*

Mudaraba is partnership between capital and skill. Under this concept entrepreneur and capitalist join hands where by one party (Mudarib) provides skills to develop business and other party (Rab ul Maal) provides required money and both share profit of the business. In case of loss, monetary loss is borne by capitalist while manager loose reward for his skill.

*f. Halal Operations*

Fifth principle of Islamic finance is financing for only *Halal* (permitted) businesses. According to Qaradawi, (1960) "Nothing is Haram except what is prohibited by a sound and explicit Nas [Verse of Qura'n and/or an authentic Sunnah] from the law-Giver Allah SWT". Ulema (Clerics) have made the list of prohibited businesses in which investment for Muslims (including Islamic financial institutions) is prohibited. Activities such as liquor, pork, pornography, adultery, dance clubs, conventional banking, insurance etc. are unlawful, hence earning return through investment in any of these activities is not allowed under Islamic financial system (KMI-30).

To conclude Islamic financial system ensures justice between savers and investors. By demolishing risk free return and promotion of profit and loss sharing, justice is ensured for both parties i.e. capital supplier as well as capital user. As a model of modern commercial banking, initially capital is supplied by depositors and later on by bank to business community. Under Islamic financial system bank can invest in businesses to earn variable return based on actual results of activities and share profit earned with depositors based on agreed sharing formula. Hence it is ensured to distribute the actual outcome and none is to bear risk alone and none is to earn with zero risk.

## 4-Operational Modes

Although any of the existing/new operational modes under Islamic finance can be developed and practiced, however Shari'a compliance in the light of Islamic finance principles is required. Following modes are being suggested/practiced by Islamic Finance Industry. These operational modes of Islamic finance are classified objectively into six groups:

- Selling Modes (Bai Murabaha & Muajal, Bai Salam, Bai Istisna'a)
- Rental Modes (Ijarah)
- Profit & Loss Sharing Modes (Musharak & Mudaraba)
- Capital Market Operations (Equities & Sukuk)
- Islamic Insurance (Takaful)
- Cash Financing (Credit cards, Qard e Hasan and Time Multiple Counter Loan)

*a. Selling Modes*

Islamic financing is different from conventional banking as its design is not meant for providing commercial loans (personal as well as business). To meet this requirement of modern banking supply of assets to customers by following trading rules of Shari'a is being used by Islamic finance industry. Under these modes of operations, Islamic banks are more of trading houses/supplier of goods than financial institutions. Under these modes of operations, Islamic financial institutions purchase goods from manufacturers/suppliers by making cash payment and then deliver to customers on credit. Differences in prices of goods purchased and sold make their profits.

Bai Murabaha is a form of sales made on the basis of cost plus profit. Cost of purchase as well as profit charged by the bank is required to be disclosed to the customer. Under this mode of financing a customer request an Islamic financial institution to provide a specific asset on credit. Bank purchases required asset from supplier for spot payment and sell to customer on credit. Prices is payable either in installments or lump sum as agreed between the parties. This mode of financing is very popular in Islamic banking industry given the more of similarities than differences with conventional loans. The major difference with conventional loans is Asset based nature of the transaction. Bai Muajal differs from Murabaha only in disclosure of cost to customer.

Bai Salam is a sales transaction whereby a specified asset is purchased by making spot payment of the price with delivery asset at a foreseeable future date. This mode of financing is designed for agricultural financing, where by farmers get cash in advance for delivery of goods at the time of harvesting. Banks dispose of salam goods in the market after receipt from farmers. Differences in prices of sale and purchase make their profits.

Bai Istisna'a is a concept of sales under Islamic financial system, which is being used for manufacturing goods. Accordingly a customer places an order for manufacturing of a specific product to a manufacturer/supplier and delivery date is fixed. Price can be paid in advance, in installments or at the time of delivery as agreed between parties. Islamic banks use this mode of financing for extending credits to manufacturing sector by providing cash in advance for exchange of goods at a foreseeable future date. After receipt of goods from supplier, Islamic banks dispose in the market and differences in purchase and sales prices make their profits.

There is no restriction from Shari'a point of view in getting help from customers by banks in execution of any of sales transactions mentioned above subject to bearing ownership risk and reward. (e.g. a customer can be asked to select a commodity and supplier under Murabaha; a customer can be requested to find purchaser of goods under Salam and Istisna'a on behalf of the bank).

*b. Rental Mode (Ijarah)*

Ijarah is a rental contract whereby IFI leases an asset for a specific rent and period to the client. Ownership risks of the asset are born by IFI while expenses relating to use the asset are the responsibility of client. The difference between Ijarah and sale is that ownership in Ijarah remains with lesser while in case of sales it is transferred to purchaser. Ending Ijarah in sale of asset is allowed by IFA through a separate contract at completion of term of lease. Contract can be executed prior to purchase and possession of asset. Consumables cannot be leased out. Right of lessee to use the asset is restricted to lease agreement or/and as per normal course of business. Lessee is liable for any harm to the asset caused by any misuse or negligence on his part. Rentals of joint property are shared according to equity. A joint owner can rent his share only to the co partner. Inter Bank Rate can be used as a benchmark for amount of rentals. At the completion of Ijarah term either asset is returned to IFI or purchased by client (Shari'a standard 9). Ijarah has replaced successfully the facility of leasing under conventional financial system.

*c. Profit & Loss Sharing Modes (Musharak & Mudaraba)*

Musharaka means partnership in capital. According to Hadith Qudasi (revelation reported by Prophet Muhammad PBUH) "Indeed, Allah the Exalted says: I am the third of the two partners so long as the one does not cheat the other, and when he cheats, I withdraw myself" (Khan, 1989). Literal meaning of Musharaka is sharing. Its root in Arabic language "Shirka" means being a partner. Musharaka means a joint enterprise formed conducting some business in which all partners share the profit according to pre agreed ratio while loss is shared according to the ratio of contribution (Meezan bank guide 2002). For a valid Musharaka fulfillment of certain conditions required. First is there must be an agreement written (verbal) among the partners stating clearly the terms and conditions including management, capital contributions, profit and loss sharing among the partners. Second capital can be contributed in cash as well as in assets. However once an asset is contributed as capital that belongs to firm and contributing partner is relieved from the bar of risks and returns attached with ownership. Third profit is distributed according to agreement of partnership however sleeping partner cannot claim share in profit more than his proportionate share in equity. None of the partner can guarantee the capital or profit share to any other partner (Shari'a standard 12). Under Musharaka IFIs are receiving deposits and finances business requirements for profit and loss sharing.

Mudaraba is a type of partnership whereby skill and money brought together to conduct business. Profit is shared according to agreement while loss is born by capital provider only. Under this scheme of financing IFIs provide capital to financially weak but skilful people to do the business and share outcome with IFIs. This scheme is also used in deposit collection. Mudaraba contract can be restricted or unrestricted. No one can claim a lump sum amount of profit it must be based on actual outcome (Shari'a standard 13).

*d. Capital Market Operations (Equities & Sukuk)*

There are many liquidity instruments available for conventional financial industry (including government securities, corporate bonds etc.), however Islamic banks are restricted to get benefit due to interest based operations. Investment in equities through stock exchange is the only avenue of investment left with Islamic banks as for liquidity management is concerned, however, as we know Islamic financial institutions are required to ensure Shari'a compliance in all of their operations, hence, IFIs are not free to invest in any security issued on profit and loss sharing basis. Shari'a compliance of the company issuing securities with variable returns is required.

Ideally a security should have two features at least to be called as Shari'a compliant, including Halal business (business of the company should not consist of an activity which is prohibited by Islamic law e.g. liquor, pornography, pork, speculation, hoarding etc.etc.) and free from interest in its operations.(e.g interest received on bank deposits, interest paid on overdrafts and loans, discounting of bills of exchange, interest paid on bonds and even dividend on preferred stocks are all interest based transactions and contradict with Shari'a compliant financial system). If we filter the investment opportunities available at hand with these two criteria, we will find none or a very minor number of companies meeting both criteria. Even if we found a small number of companies meeting both criteria, the issue of listing with stock exchange (which is vital for ready market to convert into cash) and low financial performance of these companies might hinder investment by IFIs.

This led the Shari'a experts and finance professionals to pay due consideration to underlying problem of liquidity management by IFIs and come up with solutions. Any of the solution to the problem through financial engineering is deemed fit if it is not violating basic principles of Islamic financing. Investment in marketable equity securities of public companies is permitted in Shari'a being providing variable returns. However, adherence of underlying company to Shari'a principles of trade and commerce is required in order to make its equity security Shari'a compliant. There are dozens Islamic indexes operating globally with set criteria for a company to be qualified as Shari'a compliant. Filtering criteria of FTSE NASDAQ Dubai Shariah Index is reported as under (There are differences in filtering criteria of different Islamic indexes, see for detail Derigs & Marzban, 2008).

1. Companies involved in the following activities will be considered to be non-permitted business sectors:

a) Conventional Finance (non-Islamic Banking, Finance and Insurance, etc.)

b) Alcohol

c) Pork related products and non-halal food production, packaging and processing or any other activity related to pork and non-halal food

d) Entertainment (Casinos, Gambling, Cinema, Music, Pornography and Hotels)

e) Tobacco

f) Weapons, arms and defence manufacturing

This list is not exhaustive and is provided as a basic guidance to the broad principles involved.

2. After companies have been screened by their business sector activity, the remaining companies are further examined on their finances to ensure that those companies are Shariah compliant. Only those companies that pass the following financial ratios will be considered Shariah compliant:

a) Debt is less than 33.333% of total assets

b) Cash and Interest bearing items are less than 33.333% of total assets

c) Accounts receivable and cash are less than 50% of total assets

d) Total interest and non compliant activities income should not exceed 5% of total revenue

Companies that change financial compliance between two successive quarters will be monitored to check if their debt, and/or cash/interest bearing ratios fall within 33.333% +/- 5% (i.e. below 31.667% and 35% or above). If during the monitoring period any company remains above or below 33.333% +/- 5% for two consecutive quarters, the compliance of that company will change accordingly.

Appropriate purification of dividends at 5%. This ratio calculates the recommended purification amount to be paid by the investor.

Sukuk is a creation of IFIs to meet their liquidity requirements. Sukuk provide an opportunity to distribute the value of an asset/enterprise/project/usufruct into smaller amount certificates of equal value to create an opportunity for small investors to share the benefits of investment which is otherwise impossible keeping in view the larger amounts required to acquire or build an asset or enterprise/project. According to Shari'a standard # 17 investment Sukuk are certificates of equal value representing undivided shares in ownership of tangible assets, usufruct and services or (in the ownership of) the assets of particular projects or special investment activity, however, this is true after receipt of the value of the Sukuk, the closing of subscription and the employment of funds received for the purpose for which the Sukuk were issued. All Sukuk are tradable in secondary market.

There is empirical evidence to suggest that Sukuk structures were used within Muslim societies as early as the Middle Ages, where papers representing financial obligations originating from trade and other commercial activities were issued. The word, "Sukuk", can also be traced back to classical commercial Islamic literature, used in reference to certificates for goods or groceries ("sakk al-bada'i") as the method of paying the salaries of government officers, who would later redeem such certificates in line with their day-to-day consumption of such goods or groceries.

However, the Sukuk, as understood in its contemporary form, lies in a decision of the Islamic Jurisprudence Council (the "IJC") dated 6-11 February 1988 which provided that, *"any combination of assets (or the usufruct of such assets) can be represented in the form of written financial instruments which can be sold at a market price provided that the composition of the group of assets represented by the Sukuk consist of a majority of tangible assets*." [DIFC Sukuk Guide]

*e. Islamic insurance (Takaful)*

Insurance is a business activity engaged in diversification (spread) of risks of a person among all participants. Traditionally insurance companies are providing indemnity against a certain type(s) of risks for a premium. Businesses are subject to many risks including fire, theft and accidents etc and insurance companies are sources of risk mitigation. Concept behind the organization and management of insurance business is working on the principle of cooperation. In its simplest form it is a fund created by a number (e.g. 100) of persons having same type of asset (e.g. cars) to compensate the one(s) who suffered loss due to destruction or theft of said asset (car). Everyone is contributing in the fund a specific amount known as premium (e.g. 5000) to be indemnified by an amount equal to loss of asset subject to a maximum limit (e.g. 150,000). Insurance business is also covering disability and or death of participants, known as life insurance. Practically this concept of insurance is changed to commercialization in the modern framework of business, where a company guarantees the making loss of policy holders good, by charging a premium, based upon length of period, probability of occurring loss and amount of compensation to be paid. Furthermore, there are re-insurance companies providing an opportunity to the insurance company to share the risk; as well as loss/compensation by sharing the amount of premium. From Islamic finance perspective sharing of risk among the participants is permitted, however, the present practices of insurance sector are not matching with the spirit of cooperation, encouraged by Islam.

According to AAOIFI, SS # 26, Islamic insurance is a process of agreement among a group of persons to handle the injuries resulting from specific risks to which all of them are vulnerable. A process thus initiated involves payment of contributions as donations, and leads to the establishment of an insurance fund that enjoys the status of a legal entity and has independent financial liability. The resources of this fund are used to indemnify any participant who encounters injury, subject to a specific set of rules and a given process of documentation. The

fund is managed by either a selected group of policy holders, or a joint stock company that manages the insurance operations and invests the assets of the fund, against a specific fee.

*f. Cash Financing*

There are certain customer needs including payment of operating expenses, an urgent payment to a vendor, long distance travels and tours, children education, marriage expenses, health expenses and credit card facility etc. which cannot be fulfilled through any of above listed modes of financing, hence require cash loans. However, in present practice of Islamic banks one cannot get loan in cash except Qarz e Hasan (charity loan). Qarz e Hasna is not a business model in itself. Islamic banks are not charitable institutions rather commercial houses. In fact, Islamic banks or any other business can survive only through earning profit which does not exists in transaction of Qarz e Hasna. It is appreciable that Islamic banks must reserve a certain amount for Qarz e Hasna; however, that can only be done in a prosperous Islamic bank.

Time Multiple Counter Loan (TMCL) is a concept suggested by Council of Islamic Ideology (CII), Pakistan in its first report on "elimination of Riba from the economy" in 1980. As per this concept a needy customer can get cash loan without paying any interest from bank, however a small amount of counter loan/deposit (free of charge) for a longer period is to be provided to bank. Under this mode of financing a larger amount of cash loan with shorter maturity issued by bank is compensated through a smaller amount of loan/deposit for a larger period by customer. Bank can earn higher rate of profit by investing this shorter amount of cash in a long term project.

Some Islamic banks have introduced credit cards whereby a fee is charged to customer instead of charging interest for amount due, which needs to be further refined in the light of Shari'a principles.

## 5-Conclusion

To conclude there are major principle-differences in conventional and Islamic finance which needs to be appreciated in practice. Islamic finance is clearly different in business models from conventional finance. Over the years Islamic finance industry has succeeded in development of new products and services, although, further financial engineering is required to match the ever growing needs of business communities. Islamic finance has expanded in the area of banking, insurance and capital market operations. Islamic finance has promoted commonalities and unity among Muslim countries in the form of global institutions including AAOIFI, IIFM and IFSB

etc. Islamic finance industry faces certain challenges including benchmark profit rate, cash financing and legal framework.

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