

Unresolved Issues In Islamic Banking and Finance: Deposit Mobilization

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Introduction

Islamic banking effectively started in the 1970s with personal initiative of the concerned Muslims to address the problem of *ribā*. There was no initial working model to act upon, except the belief that interest-based banking might be replaced by banking on the basis of profit-and-loss sharing. This effort took place when the financial system at large, as also the regulatory environment, was *ribā*-based.

As against the above, the current position is that Islamic banking and financing has won recognition by international financial institutions, professional bankers and the academia. There are more than 200 Islamic financial institutions all over the world with investment funds in excess of \$250 billion. The annual growth rate of Islamic banking industry worldwide is 16%+. In some Muslim countries, total or partial transformation has taken place in favour of Islamic banking.

With the completion of the phase of creating a niche for itself, Islamic banking is now set to reach new horizons. A lot of work has been done in giving Islamic banking an international standard. AAOIFI has done commendable unification effort. IFSB (International Financial Services Board), established by central banks of several Muslim countries, is expected to take this effort further.

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Main work so far has been done in the area of Islamic financing. The deposit mobilization side has been taken for granted. It is, therefore, not surprising that a closer look reveals little difference between workings of interest-based banks and Islamic banks on the deposits side. Is the difference between Islamic banking and interest-based banking really thin on the deposit mobilization side? Or, is there some thing that is being missed? This paper addresses these questions.

This paper proposes a systematic study of (1) the issues in deposit mobilization, (2) their Shari‘ah-compliant solutions and (3) implications for Islamic banking. It takes note of players on the deposits plane, their legitimate goals/concerns, Shari‘ah -compliant financial products for doing the needful and the Shari‘ah issues in funds management. The argument runs as follows.

In section 2, the issues on the deposit side are outlined. In section 3, the conventional deposits scene is described. In section 4, potential options in the Islamic setup are outlined. In section 5, some practical issues in management of deposits according to the Shari‘ah are addressed.

2. Deposits Side of Banking - The Issues

Other than the banks, players on the deposit scene pursue a variety of goals ranging from mere safekeeping of the funds to seeking stable income flows. There are also those who have other considerations that, in turn, necessitate keeping of funds with the banks. Table 1 gives a catalogue of these players and their concerns keeping in view the existing realities.

Every **instrument** serves a unique purpose for the **Savers**—owners of funds:

1. On one extreme, the owners of funds seek just safekeeping of the funds, presumably for payment purposes, with the help of banks. The instrument for this purpose is “**Demand Deposits**”.
2. At the other extreme, the savers are interested in investment of their funds for a fixed period with one-time settlement at the end. The relevant instrument is a term or fixed deposit, labelled in Table 1 as “**Investment Deposits**”.
3. In between the above extremes, depositors pursue a combination of the aforesaid goals. The banks offer **General Savings Deposits** for this purpose.

4. In a variant of the second case, depositors want an ongoing investment relationship with the banks for stable income flows. Such depositors include pensioners, widows and other vulnerable members of society who want fixed income over a stretch of period. These deposits fall under fixed income schemes offered by interest-based banks, and they usually carry some brand name.

Table 1: Bank Deposits Scene – Instruments, Players and Their Concerns

INSTRUMENTS	PLAYERS BY TYPES OF DEPOSITS	
	SAVERS (OWNERS OF FUNDS)	BANKS*
1. DEMAND DEPOSITS	Safe-keeping of funds with maximum flexibility in their withdrawal, but without seeking a return	Flexibility for gainful use of funds
2. INVESTMENT DEPOSITS (Term Deposits)	Investment for a prescribed time	
3. GENERAL SAVINGS DEPOSITS (Saving-cum-Investment Deposits)	Safekeeping of funds with flexibility in the withdrawal along with some return	
4. INVESTMENT DEPOSITS WITH STABLE INCOME FLOWS	Relatively safe Investment for a prescribed time**	
5. OTHERS	Management of payments and receipts	

* Banks are mainly interested in working with funds without intervention by the owners of the funds.

** These are risk-averse depositors who are willing to trade-off some return for safety of their money.

Last but not least, the clients may engage banks in order to look after their payments and receipts matters. In the process, they hold deposits with the banks.

Banks, on their part, want maximum flexibility in the use of the funds at their disposal with no or minimal interference by the depositors. They are commercial concerns interested in their return.

The issues of interest for us are as follows. What are possible contractual arrangements to regulate the bank-depositor relationship? What are their implications for management of funds at the banks' end? Answers to these questions are explored hereunder. We start with a recounting of the factual position in the existing interest-based framework.

3. The Conventional (Interest-based) Deposits Scene

In first four of the aforementioned cases, the **contractual relationship** between owners of funds and banks is a **lender-borrower relationship**. In the **1st case**, namely Demand Deposits, the depositors are not interested in any return. The **2nd, 3rd and 4th options** are made attractive for depositors with provisions of interest payments. The return is predictable for the depositors in the case of ordinary Investment Deposits (the **2nd case**) as well as other Investment Deposits offering Stable Income Flows (the **4th case**). However, rate of return on General Savings Deposits (the **3rd case**) is at the discretion of the banks who employ a complex formula to determine the various depositors' entitlements to interest.

In the **5th case**, banks render a service, and receive funds for discharging it. But they also invest any idle balances in their own interest. Technically speaking, this implies that the ownership of funds is treated as if vested with the banks until a payment claim against the client arises. In this sense, there is again a lender-borrower relationship between the clients and the banks in respect of the unutilized funds.¹

Funds in all of the above deposits are shown on the liabilities side of the banks. This is again an acknowledgement of the deposits being "debt" against the banks.

In the management of these deposits, banks follow an aggregative approach (see Figure 1). All funds, regardless of the category of the deposits or depositors, are put together in one financing pool. Banks make all advances from this pool. There is a financial year for accounting purposes. At the end of the year, banks do their financial closures. Income and expense are

taken into account, and profit and loss statements are prepared. Interest paid to the depositors during the course of the financial year is treated as expense for the banks.

4. The Islamic Deposits Scene

Our concern here is to identify the Islamic options. Direct comments on the existing practices are avoided in view of the sensitivities involved.

The Shari‘ah options for deposit mobilization can be worked out by respecting two principles:

1. The aim of the exchange at hand must be recognized in the Shari‘ah.
2. The modalities to achieve the said aim must be Shari‘ah-compliant.

It is notable that the aims being pursued by depositors as well as the banks, as listed in section I, are not in conflict with the Shari‘ah. We, therefore, proceed to the practical possibilities.

4.1 Demand Deposits

In this case, the depositors’ concern is safe-keeping of funds with maximum flexibility in their withdrawal—without seeking any return. Banks, on the other hand, want to utilize the available funds at their discretion. Both these considerations can be accommodated by treating the deposits as (interest-free) “loans” from depositors to banks. A recourse to *amānah* (امانة) or *wadi‘ah* (وديعة) is inadvisable for the following reasons:

- i) In the case of *amānah*, banks will not have the authorization to draw benefits from the funds while they are with them.
- ii) The Shari‘ah has provided the *wadi‘ah* for situations where usufruct of an asset is separable from the main body of an asset.² This is not true about money.

Compliance with the Shari‘ah requirement of being explicit on the duration of loan can be addressed as follows. The tenure of the deposited sum can be set anywhere between 1-hour and 1-day after which the depositors may claim their money on demand.

It is worth mentioning that banks may offer overdraft facilities (counter-loans) on an interest-free basis to the depositors. This would be akin to giving a counter-loan in a Shari‘ah-compliant way. However, the banks ought to respect the Shari‘ah constraint of not offering any perquisites to the depositors. This is because, according to the *Hadīth* of Anas B. Malik, the

Prophet SAAWS has prohibited the creditors from drawing even trivial benefits from those indebted to them.³

4.2 Investment Deposits

Investment deposits represent the case when owners of funds seek a return on their funds, and are willing to spare these funds for an agreed period. Three arrangements can apply here: *muḍārabah*, *mushārah* and *ijārah*. We explain them one by one.

Muḍārabah Deposits

A *muḍārabah* transaction requires that the contract be explicit on the following matters: goal or purpose of the *muḍārabah*, its tenure, role function of the concerned parties, profit-sharing ratio, principle for sharing losses, the extent to which indebtedness can be created in the name of the *muḍārabah* and the principle for final settlement.⁴ It also requires that unless some payments to third parties become necessary for the discharge of role function of the working partner (*muḍārib*), personal expenses be borne by him and not charged to the *muḍārabah*. Against this backdrop, the following arrangements are conceivable.⁵

There can be more than one line of *muḍārabah* deposits in order to address diverse goals and concerns of the depositors. Each such line of deposits can be for a distinct purpose, and has separate starting and maturity dates.

A separate *muḍārabah* form may be prescribed for every *muḍārabah*. Whereas formula for distribution of the depositors' share in the profits among them may be a part of the general terms, the overall profit-sharing ratio in favor of the depositors must be separately stated for every line of *muḍārabah* deposits. However, if a *muḍārabah* involves rollover, such ratios may be announced periodically, say, at the beginning of every quarter, six months or year.

For illustrative purposes, one may consider a hypothetical example of a 4-month *muḍārabah* for financing, say, export trade:

- i) On some date, say, in the second half of a month, a bank may invite deposits for a 4-month export trade *muḍārabah* that would start operations on the 1st of the next month. The formula for distribution of the expected profits should be announced at the same time.

- ii) Deposits may be accepted one day before the start of the *muḍārabah* operations, and the *muḍārabah* would be truncated at the end of the fourth month. In order to avoid any accounting complications, the *muḍārabah* may be restricted only to those depositors who are ready to keep their funds with the bank for full 4 months.
- iii) Accounts for the *muḍārabah* are to be maintained separately from other accounts of the bank. At the end of the *muḍārabah* period, the bank can calculate the profits, keep its share and distribute the depositors' share among them on a proportional basis along with reimbursement of their respective deposit. This last point presumes that the share of each depositor in total profits would equal the fraction of his deposit in the total *muḍārabah* funds multiplied by the overall profit-sharing ratio in favour of the depositors.

The following points would also be relevant for the *muḍārabah*.

- i) The profit-sharing ratios might be set such that while the bank's concerns are addressed, depositors can also look forward to getting a reasonable rate of return that is consistent with market trends.
- ii) The bank may utilize the *muḍārabah* funds for export financing through both trading and partnership modes. In case the bank operates through a trading mode and some goods remain un-exported, the same can be valued at actual cost basis and treated as property of the bank for the settlement of accounts. If the bank employs money through a partnership mode, the same formula may be used with either the bank or the other partner(s) claiming the output and settling the accounts.

As mentioned above, there can as well be separate *muḍārabahs* for different lines of business. Their starting dates and maturity periods may be the same or different. This will enable banks to accommodate the depositors according to the ability to spare funds as well as their risk-return preferences.

***Mushārah* Deposits**

On the above pattern of *muḍārabahs*, banks may also invite **deposits on *mushārah* basis**. The wisdom behind such an arrangement is simple: if a bank also commits a part of its equity, this will serve as signal of the bank's seriousness about profitable application of the funds for risk-averse depositors.

In general, the Shari'ah requirements for a *mushārah* are the same as those noted above for a *muḍārabah*. However, it should be noted that the

mushārahah option can be construed as sharing in both capital and effort. There is no hard or fast Sharī‘ah rule for the quantum of effort to be put in by any partner. Therefore, banks may restrict the active involvement of depositors to just receiving the financial reports and reviewing them.

Investment Deposits under Bank Management - The *Ijārah* Option

This interesting possibility is employed in the Iranian banking system.⁶ It can work like the foregoing example of *muḍārahah*, but with following differences.

According to this option, ownership of funds always remains with the depositors, and is at no stage shared with the banks (as opposed to the case of *muḍārahah* or *mushārahah*) or transferred to them (as in the case of a loan). The banks come in the picture as manager (or, *ajeer* (أجير)) of depositors to administer the funds.⁷ Under these circumstances, owner of the funds and, hence, all profits belong to the depositors. The banks would be entitled to a fee.

The bank fee needs to be fixed in advance. It can be a lump sum amount or some percentage of the funds involved, to be debited to the various depositors according to some prescribed formula. In any case, this fee cannot be supplemented by a share in the profits. That would tantamount to clubbing an *ijārah* (employer-employee) contract with a partnership agreement. This is not permissible in the Sharī‘ah due to the potential of conflict of interest at the bank’s end.

It is worth mentioning that there is no Sharī‘ah bar on the banks claiming their fee in advance. However, prudent banking practices would require it—or, a larger part of it—to be payable at the end of the deposit period.

4.3 General Savings (or, Saving-cum-Investment) Deposits

These are hybrid of Demand Deposits and Investment Deposits. The depositors are interested in the safekeeping of their money with flexible withdrawal terms and some return. Two possibilities exist here:

- i) The deposits can be replaced by units of a growth fund—or, a mutual fund—that are encashable at any time. Of course, it would be essential that the growth fund, in turn, represents a Sharī‘ah permissible investment portfolio that is also relatively risk-free. In this case, the depositors would be buying (selling) the units in order to become part of (come out of) the growth fund. However, they may have to forsake the flexibility of withdrawing funds in small

amounts, as at present in the framework of interest-based savings deposits.

- ii) Fresh accounting conventions can be developed that are compatible with the Shari'ah and allow for daily calculation of profits and losses.⁸ Technically speaking, this will enable the conversion of the *muḍārabahs* and the *mushārahahs* into **revolving or perpetual muḍārabahs and mushārahahs**, respectively. This, in turn, would help the depositors get into and, more importantly, come out of the *muḍārabah* or *mushārahah* accounts at their convenience. Along with this arrangement, banks may also offer composite accounts in which one of the two accounts is essentially an interest-free account, technically a loan to the bank, that might be drawn upon to meet the depositors' emergent cash needs.

4.4 Investment Deposits with Stable Income Flows

The goals at the depositors' end in this case are two fold: security of their capital, and stable—rather, fixed—income flows. These twin goals may be achieved as follows:

1. The deposits can be invested in Shari'ah-compliant fixed income securities, such as those based on leasing. Alternatively, funds can be utilized in relatively low-risk Shari'ah-compliant investments. There may also be the possibility of having a diversified investment portfolio to minimize risk.
2. The contract between a bank and a depositor may stipulate withholding and reinvestment (by the bank) of any excess profits due in favour of the depositor. And, the contract may have provisions for temporary loan from the bank to the depositor to cover any shortfall when the profits earned fall short of the prescribed amount. Such a loan can be adjusted against the profits realized in subsequent periods.

Both the design and practice of an instrument along the above lines, offer a great challenge for Islamic bankers.

4.5 Special Accounts

Notwithstanding their role as financial intermediaries, banks have now become the mainstay of the modern payments system. Governments, public sector organizations, companies and businesses of all sizes depend on the banking system in order to pay to their staff and suppliers. Except in cases of

transfer of funds against cash payments, the clients maintain balances with banks for payment purposes. In this regard, the thinking needs to be clear on four issues:

- i) the legal relationship between the banks and their clients;
- ii) the type of account that would serve the clients' needs and suit the banks as well;
- iii) the banks' stake in the arrangement, whether in lump sum or on a transaction-by-transaction basis; and
- iv) the banks prescribing minimum balance requirements for their clients and charging penalties in the event of a default.

Let us consider the case of the government using the medium of banks for making and receiving payments. In principle, the government can have its own disbursement officer in order to give salaries and to make other payments. Quite obviously, efficiency and safety considerations necessitate recourse to the banking system. This perspective immediately draws attention to two points:

- a) The banks role in doing the needful would be similar to that of an employee of the government. The employee-employer relation between a bank and the government can be accommodated in the framework of the *ijārah* contract.
- b) The banks may claim compensation that can be a lump sum wage, a fraction of the sum involved, a per person fee in the case of disbursement of salaries or a per cheque fees in the case of payments to third parties.

The funds to be kept with the banks ought to be handled as interest-free loan for two reasons:

1. The *amānah* contract will not be feasible and the *wadī'ah* contract not admissible for reasons noted earlier.
2. An *ijārah* contract can be supplemented by a loan contract, though not vice versa. This will also give the banks the flexibility of using any idle funds held with them as loans till such time as they are needed to make the necessary payments.

Keeping in view these factors, payments services can be sought from the banks through supplementing the existing current account medium to an *ijārah* contract, not the other way round, between an interested party and a bank.

As for banks prescribing minimum balance requirements for the said accounts, the idea is admissible for the following reason. The basic framework for the above arrangement is an employer-employee relationship. And, provision of sufficient funds is the client's responsibility. If, therefore, the client defaults, this entitles the other party to abrogate the existing contract and seek a fresh contract. The financial penalty by bank would serve the purpose of compensating the bank for entering into a fresh contract.⁹

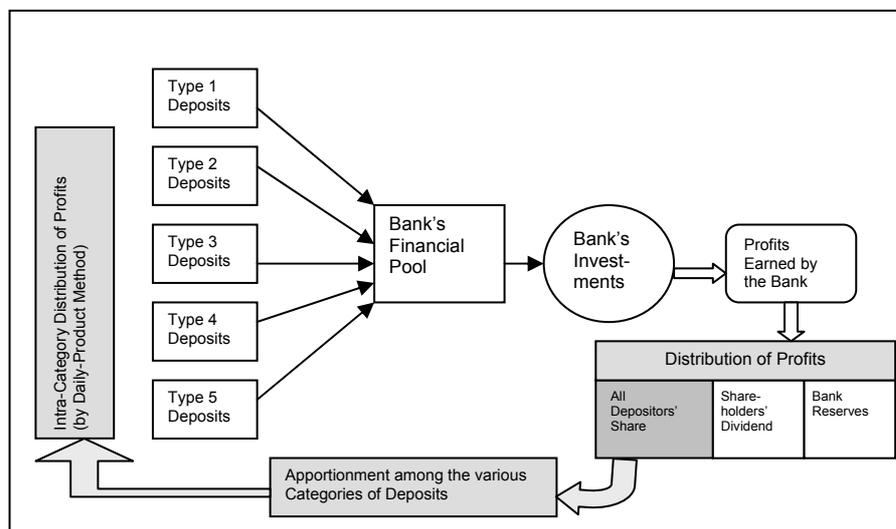


Figure 1: Deposits and Their Management by Conventional Banks
 (Type 1, Type 2, Type 3, Type 4 and Type 5 Deposits correspond to the five categories in Table 1.)

5. Practical Issues in the Management of the Deposits

In the existing interest-based system, banks' obligations to depositors consist of paying back the principal along with pre-agreed interest, depending on the case at hand, in the framework of lender-borrower relationship. The nature of contractual relationship and obligations thus has the following implications, partially noted in section II:

1. The banks follow an aggregative approach to the management and financing of deposits (*Figure 1*).
2. All deposits appear as liability on balance sheets of the banks.
3. Interest payments to depositors are treated as bank expenses.

Two more points are also noteworthy:

1. In general, initial instalments paid by the borrowers are counted toward recovery of interest, and treated as bank income.
2. Banks can also meet their operating expenses out of funds in the deposits.

Prudential regulations are prescribed by the central bank in order to ensure solvency of the banks. The Shari‘ah, however, gives rise to issues of a different sort for Islamic banking. These are discussed below under three headings: management of accounts, admissible operating costs for partnership-based deposits and reporting matters.

5.1 Management of Funds in Various Categories of Deposits

Islamic banks at present follow the aforementioned aggregative approach used by interest-based banks (*Figure 1*) for the management of funds.¹⁰ This practice needs review, especially for investment deposits. Some of the reasons are noted hereunder.

Ahkām of the Shari‘ah are given at the micro level. The Islamic position on ownership implies that if someone does business with his money, then the goods purchased, proceeds from their sale and the profits (= sale proceeds minus costs) also belong to him. Others would require his express willing consent (*An-Nisaa’* 4: 29) before they can exercise any claim on these profits. This principle carries over to two-person *muḍārabah* as follows.

As noted in section III.2, *muḍārabah* is a limited purpose arrangement for a specified period. The provider of capital shares its ownership with the *muḍārib*. This enables the *muḍārib* to exercise his discretion on the funds—of course, according to the stipulated purpose of the *muḍārabah*. And, there is no need for fresh approval of the ultimate owner of funds for every action taken by the *muḍārib*. This joint ownership means that profits, if any, belong to both the parties.¹¹ Accordingly, the *muḍārabah* is consummated with division of the profits between the partners as per the agreed formula, of course, along with the owner of capital getting back his funds.

Ahkām for *muḍārabah* or *mushārahah* between bank and its depositors are logical extension of the above principle. Consider first the simple case of there being only one line of *muḍārabah* deposits **Muḍārabah 1** offered by an Islamic bank. The working of this *muḍārabah* is shown under **Muḍārabah 1** in *Figure 2*.

The bank comes in the picture with its effort to invest the Investment Pool-1. Proceeds from the *muḍārabah* operations consist of capital of the *muḍārabah* (contributed by the depositors) and profits. The capital and agreed share of the depositors goes to them, and the bank gets its share of the profits. Ultimately, every depositor gets back his actual deposit and proportionate share in the total profits going to the depositors. Bank's share of profits forms part of its income.

Next, let us bring into picture another line of investment deposits: ***Muḍārabah 2***. The foregoing argument applies separately to this category of deposits. The reason is that depositors in this category are different from those in ***Muḍārabah 1***. With the matters handled in this way, interests of the two groups of depositors do not mix up. And, the bank also achieves its goal of earning income through providing investment services to the respective owners of funds.

The foregoing argument applies to any number of *muḍārabahs* or *mushārahahs* that a bank may enter into with depositors. As against this, the aggregative approach frees the banks from the need for maintaining separate accounts for investments made on behalf of different categories of investment deposits. A redress for the above issues is sought through use of the daily-product method for distribution of profits.¹² However, conflict with the Shari'ah is not resolved for the following reasons:

1. There always remains the possibility of profits actually belonging to one group of depositors being passed on to another, and losses of one category of deposits shifted to another.

This issue cannot be ignored as either trivial or irrelevant on grounds of no objection from the depositors. The Shari'ah is a Divinely-ordained code of acceptable conduct. Where the lines are clearly drawn by Allah SWT and His Prophet SAAWS, there is little room for human discretion (*al-Hujuraat* 49: 1).

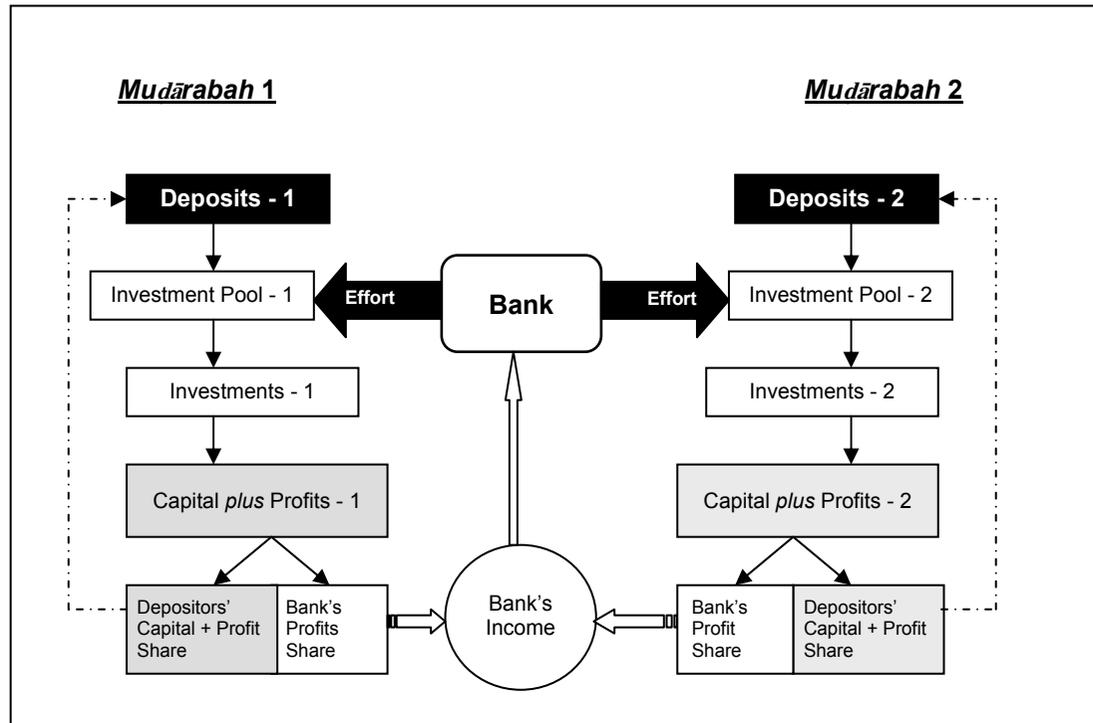


Figure 2: Management of Partnership-based Deposits

2. Application of the daily-product method along with reduction in the period in the calculation of profits and losses may lessen the above problem. But reliance on the daily-product method needs review for the following reasons:
 - i) It is well-known that *ijtebād* in the sense of taking a new position is admissible when the Shari‘ah is silent on a matter. Thus, one could make recourse to daily-product method if the Shari‘ah were silent on principles for settlement of accounts. But, as noted above, this is not the case here.
 - ii) The daily product formula applies *ex post facto*. Thus, a depositor cannot form an opinion about his actual share, in percentage terms, at the time of entering into the contract. In this sense, the daily-product arrangement has *gharar*.
 - iii) The principle of willing consent (*An-Nisaa’* 4: 29) of the actual owners—depositors in the present case—needs to be respected in both letter and spirit in the design of any settlement arrangement. This, in turn, requires that there should be some arrangements for bringing into the picture the depositors’ point of view after profits actually arise, not before. The daily-product method misses this point.

The above problems are avoided if investment of the deposits in different categories and their accounts are separately maintained.

In passing, it may be mentioned that the *fiqhī* principle of *الخراج بالضمن* warrants that the banks also shoulder the obligations for Shari‘ah-compliance, as proposed above, in order to justify their entitlement to profits allowed to them by virtue of economies of scale.

Notwithstanding the above, however, a disaggregated approach to management of funds has its own advantages. For example, separate handling of deposits in different categories and the maintenance of separate accounts for them will reduce the chances of bank failures, and improve banking stability. It is noteworthy that this may be achieved without limiting the range of financial products for the depositors. For example, there would be relatively low risk deposit schemes like multipurpose *muḍārabahs*, *mushārahahs* with banks committing their own funds and mutual funds type arrangements. Similarly, investment deposits with different maturity periods, ranging from short to long, and mutual funds type financial products may serve needs of short-term as well as long-term investors.

5.2 Admissible Operating Costs for Partnership-based Deposits

Banks are legal entities. It is noteworthy that a bank's legal person includes its buildings, furniture & fixtures and permanent staff. Banks perform their promised functions for partnership-based on the strength of these elements. If one takes out these things, a "bank" would lose meanings for the depositors. The following point need to be appreciated against this backdrop.

In principle, in a *mudārabah* personal expenses of the *mudārib*—the working partner—are his personal responsibility. And, only those expenses are admissible as costs of the *mudārabah* that are payable to third parties in lieu of *mudārabah* operations. This principle also applies to working partners in the framework of *mushārahah*.

A corollary of the above principle is that banks should not claim their overhead expenses as costs in the management of *mudārabah* - or *mushārahah*-based deposits. Of course, they can address their concerns in this regard through claim a higher percentage of profits for themselves. Moreover, if need be, they can seek interest-free loans from the *mudārabah* or *mushārahah* pools in order to meet contingencies, and adjust these loans against their share of profits.¹³

5.3 Reporting Matters

At present, Islamic banks report all deposits as their liabilities, and all their advances (bank "investments") as assets in their balance sheets. This principle may be adopted for deposits acquired on a loan basis, such as demand deposits, but not for investment deposits mobilized on partnership basis. The reason is that ownership of funds under *mudārabah* or *mushārahah* rests with the depositors. The banks "share" this ownership just for operational reasons. Since their ownership is not transferred to the banks, such deposits are not "liability" of banks in the traditional sense. By the same token, any investments made from such deposits are assets of the banks alone.

The above considerations require that investment deposits and financing from them should be off-balance sheet items for Islamic banks, and only their share of profits should appear in their income statements.

6. Concluding Remarks

Islamic banking started with preoccupation with the problem of *ribā* in bank financing. For some reason, the case of deposits did not come up for scrutiny. However, it may not be too long before the depositors start to ask: what is the material difference, from the Shari'ah point of view, between Islamic banks and interest-based banks? This, in turn, requires that some steps be taken sooner than later so that depositors do not lose trust in Islamic banking. It is hoped that the leads provided in this paper will be pursued further in order to establish models of Islamic banking above reproach.

One may claim that treating each *muḍārabah* and *mushārah* separately for accounting of revenues, costs and distribution of profits may reduce the asset diversification benefits, through an Islamic bank, for the depositors. This need not be so for the following reasons. Firstly, banks may introduce multipurpose *muḍārabahs*. Extension in the scope of *muḍārabah* will have the same risk-reduction implications as are associated with a diversified investment portfolio. Secondly, as noted earlier, *mushārah* deposits are effectively a signal to depositors about safety of their deposits. Prudential regulations for investments and maintenance of separate bank accounts for the various lines of deposits can further strengthen this purpose. Thirdly, mutual funds type arrangements may come into existence to attract such depositors. Last but not least, competition among Islamic banks will ensure availability of a wide range of financial products for all kinds of depositors.

Notes

¹ Absence of this thing would call into question legal justification for the banks investing the funds and keeping the profits unto themselves.

² *Amānah*, *wadī'ah*, *bay'ah* (trading), *ijarah* (leasing), *shirkah* (partnership) and *qard* (loan) represent Shari'ah arrangements to address particular situations. For example, a person might want someone to temporarily look after his thing without transferring the ownership or allowing the latter use it. *Wadī'ah* becomes relevant when the thing at hand also needs to be tended to and it yields some benefits as well. For example, a farmer, proceeding to Hajj, may leave his cow with his neighbour for safekeeping. Neither the owner wants to sell, nor the neighbour wishes to buy the cow. The cow needs to be fed, and also gives milk. Simple *amānah* cannot help here. Thus, *wadī'ah* comes in the picture.

It is noteworthy that in the example of cow, the asset and its usufruct are separable. "Money" does not have this attribute. It is fungible: it exhausts itself in the process of use. It can as well be left idle. In view of these factors, money is not fit to

be the subject of a *wadī'ah*. If, however, a bank indeed wants to utilize the depositors' money, it can make invoke the Sharī'ah option of getting it either as a loan or on a partnership basis.

³ See *Ibne Majah* (Sakhar, 1995), Ḥadīth No. 2423.

⁴ See IIIE (1999), pp. 54-7, for these and other practical matters related to modarabah and *mushārahah*.

⁵ Details of these and other partnership-based arrangements for deposits mobilization are available in IIIE (1999), pp. 60-1.

⁶ See Mahdavi (1995).

⁷ Of course, when the bank will be acting on behalf of the depositors while managing their funds. In this sense, it would be their attorney or *wakeel*. Notwithstanding this, the legal relationship between the depositors and the bank would be that of *ajir* and *ajeer*, i.e., employer and employees, respectively.

⁸ In principle, such a step is also necessary for Sharī'ah-compliant mutual funds.

⁹ It should be clear that this logic cannot be extended to ordinary demand deposits because the primary relationship between depositor and bank is a lender-borrower relationship. It also does not apply to partnership-based deposits, because the choice for a bank is between offering or not offering such deposits, and issue of minimum balance does not arise in "loans".

¹⁰ See, for example, Bank Islam Malaysia Berhad, p. 47 and Chapter IV (Accounting Procedures).

¹¹ The incidence of monetary loss on the owner of capital is for the very reason that funds belong to him. Of course, the *mudārib* too suffers losses in the form of his effort going unrewarded.

¹² See CII (1991) pages 48-51.

¹³ See IIIE (1999), p. 55.

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