

Diploma in Islamic Banking (DIB), Part-I

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Chapter:
8,9 & 10

Session-IV

(Risk management; regulation, supervision and Governance of the alternative financial system; opportunities, issues and challenges)

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**Islami Bank Training & Research
Academy (IBTRA), Dhaka**

Presenter

Muhammad Habibur Rahman
VP & Head of Shari'ah Audit
Shari'ah Secretariat, IBBPLC, HO

Session overview

The following important topics will be covered as per [chapter 8](#) (risk management), [chapter 9](#) (regulation, supervision and governance of the alternative financial system) and [chapter 10](#) (opportunities, issues and challenges) of Paper-101 of DIB Part-I:



Concept of Risk, Risks faced by financial institutions, Unique Risks faced by IFIs, Risks in Islamic contracts, Risk management & its Shari`ah basis, Risk management Process etc.



Corporate Governance (CG), Islamic CG, Shari`ah governance, Importance of CG for IFIs



Challenges faced by IFI



Short Notes

1. Risk



Definition: Risk is the possibility that something **bad** or **unexpected** might happen. It involves **uncertainty** about the future, which could result in either a **gain** or a **loss**.

Example: Imagine walking on a wet street. There's a risk you could slip and fall due to the slippery surface. While you might cross safely, there's also a chance of falling—that's the risk.

Risk in Financial Institutions: Though all businesses face uncertainty, financial institutions are exposed to special kinds of risks due to the nature of their operations. These risks could impact their financial health and ability to meet objectives.

N.B: 'Risk concept in Shari'ah' has been discussed in session-III

1.1 Risks faced by financial institutions

Financial institutions can face different types of risks. **Financial risk** is the **umbrella term** used for multiple types of risks associated with financing and related transactions. Some major risks are:

- 1. Credit risk:** This is the risk that arises due to debtor's non-performance. It is the potential that a **counterparty will fail** to meet its obligations in accordance with agreed terms
- 2. Liquidity risk:** This is the potential of loss to a financial institution arising from their **inability** to either **meet their obligations** or inability to easily exit a position without incurring unacceptable costs or losses.
- 3. Market risk:** Also known as **Systematic risk**. This is the risk of losses in on- and off-balance sheet positions arising from **movements in market prices** i.e. fluctuations in values in tradable, marketable or leasable assets, F. Currency fluctuation, political instability.



1.1 Risks faced by financial institutions (Contd.)

4. **Operational risk:** This risk is defined as the risk of loss resulting from **inadequate or failed processes, people, systems or from external events**. One of the operational risks which is only relevant to IFIs is **Shari'ah non-compliance risk**.
5. **Rate of return risk:** This risk refers to the risk that the **return on assets** (investments) will be lower than the **expected returns** for fund providers (depositors), creating a **mismatch**. This mismatch can lead to **displaced commercial risk**.
6. **Displaced commercial risk:** **Displaced commercial risk** in Islamic finance occurs when an Islamic financial institution (IFI), such as an Islamic bank, feels pressure to pay **higher returns** to depositors or investors than what it actually earned from its investments. This happens when the return on the bank's investments is lower than what competitors (such as conventional banks) are offering. To stay competitive, the Islamic bank may use its own funds to **make up the difference**, even though it's not obligated to do so under Islamic finance principles.

1.2 Unique Risks faced by IFIs

Besides the above common risks, the IFIs may face the following unique risks:

- 1.2.1 Shari`ah non compliance risk :** The Shari`ah **non Compliance** Risk refers to the risk that arises from the bank's failure to comply with the Shari`ah rules and principles determined by the relevant Shari`ah regulatory councils. (Ref, *The Risk Management Guidelines (December 2014) of IFSB*)
- 1.2.2 Inventory risk :** Inventory risk, in the context of Islamic Finance Institutions (IFIs), refers to the potential financial exposure or uncertainty associated with holding physical commodities or goods as part of their business operations. Inventory risk can arise due to factors such as price fluctuations, damage, spoilage, theft, or changes in market demand.
- 1.2.3 Equity investment risk :** Equity investment risk as the risk arising from entering into a partnership for the purpose of undertaking or participating in a particular financing or general business activity as described in the contract and in which the provider of finance shares in the business risk. (Ref. <http://www.ifsb.org/standard/ifsb1.pdf>)
- 1.2.4 IT adaptation risk :** Risk associated with the implementation and integration of Information Technology (IT) systems and solutions within the framework of Islamic finance. It pertains to the challenges and uncertainties that arise when adopting and using IT infrastructure and software while ensuring compliance with Islamic principles and Shari'ah guidelines.

1.2 Unique Risks faced by IFIs (Contd.)

- 1.2.5 Efficiency risk** : It refers to the risk associated with the potential inefficiency or suboptimal utilization of resources, leading to decreased operational effectiveness and financial performance. This risk is particularly relevant to IFIs as they strive to operate in a manner that is both financially sound and compliant with Islamic principles.
- 1.2.6 Customer acceptance risk** : Customer acceptance risk in Islamic Finance Institutions (IFIs) refers to the potential risk that arises when IFIs onboard new customers or clients who may not fully understand or accept the Islamic finance principles, products, or services offered by the institution.
- 1.2.7 Differentiation of opinion (of SSC) risk**: the potential risk that arises when the Shari'ah supervisory committees of various IFIs hold differing opinions or interpretations regarding the permissibility (or non-permissibility) of certain financial products, transactions, or practices within the context of Islamic finance.
- 1.2.8 Communication risk**: potential risk associated with the way IFIs communicate with their stakeholders, including customers, investors, regulators, and the general public, regarding their Shari'ah-compliant financial products, services, and operations.

13 Risk management

Risk management is a process of identifying potential risks before they occur, assessing the possible impact of the risks when they materialize and setting procedures and taking action to avoid the risk entirely or minimize its potential impact.



1.3.1 Shari`ah Basis of Risk management

Islam encourages manage/mitigate the risk resulting from uncertain events to avoid loss. Because, without risk management it is nothing but driving into darkness with the headlights turned off.

Allah SWT says in the Holy Quran:

"And he said, O my sons, do not enter from one gate but enter from different gates; and I cannot avail you against [the decree of] Allah at all. The decision is only for Allah ; upon Him I have relied, and upon Him let those who would rely [indeed] rely". (Sura Yusuf: Verse 67)

We should not leave everything for Allah SWT to manage. We must try to manage things to our best. It is mentioned in the Holy Quran,

“That is because Allah would not change a favor which He had bestowed upon a people until they change what is within themselves. And indeed, Allah is Hearing and Knowing.”

(Al Anfal: 53)

1.3.1 Shari`ah Basis of Risk management (Contd.)

Prophet (pbuh) once asked a Bedouin (a nomadic Arab) who had left his camel untied, “Why do you not tie your camel?” The Bedouin answered, “I put my trust in Allah”. Prophet (pbuh) then said, “tie up your camel first then put your trust in Allah”.

The history of the Prophet (pbuh) peace be upon him is also full of lessons, how Muslims should manage the risks.

For instance, the Prophet (pbuh) initiated his sacred mission right from home and then moved to the people closely associated with him. This is to reduce the risk of rejection.

At the time of Prophet (pbuh)'s migration to Madinah, he (pbuh) reduced the risk of getting killed by asking Ali (R) to sleep in his bed during the night of emigration. The assassins posted by Quraish around the Prophet (pbuh)'s house were waiting to kill him at the moment he left his house early in the morning, peeping now and then through a hole in the door to make sure that he was still lying in his bed.

He (pbuh) also reduced the risk of being attacked with enemies through setting out on foot for the southward Yemen leaving the busy northward path to Madina.

1.3.2 Risk management Process

Islamic financial Institution can protect the interest of depositors and investment accountholders through following proper Risk Management Processes:



1.3.3 Risk management Process in IFIs: IFSB Requirement

The general requirements prescribed by IFSB relating to the risk management process are as follows:

- IFIs shall have in place a **sound process** for executing all elements of risk management, including risk **identification, measurement, mitigation, monitoring, reporting and control**.
- This process requires the implementation of **appropriate policies, limits, procedures and effective management information systems** for internal risk and reporting and decision making that are commensurate with the scope, complexity and nature of the IFIs' activities.
- IFIs shall ensure an **adequate system of controls** with appropriate checks and balances is in place. The controls shall:
 - ❖ Comply with **Shari'ah** rules and principles;
 - ❖ Comply with applicable **regulatory and internal policies and procedures**;
 - ❖ Take into account the **integrity of risk management processes**.

1.3.3 Risk management Process in IFIs: IFSB Requirement (Contd.)

- IFIs shall ensure the **quality and timeliness of risk reporting** available to regulatory authorities. IFIs must be prepared to provide **additional and voluntary information** needed to identify emerging problems possibly giving rise to systematic risk issues. When appropriate, the information contained in the report shall remain **confidential** and shall not be used for public disclosure.
- IFIs shall make appropriate and **timely disclosures of information to investment account holders** so that the investors are able to assess the potential risks and rewards of their investments and to protect their own interests in their decision making process. Applicable international financial reporting and auditing standards shall be used for this purpose.

2. Corporate Governance (CG)

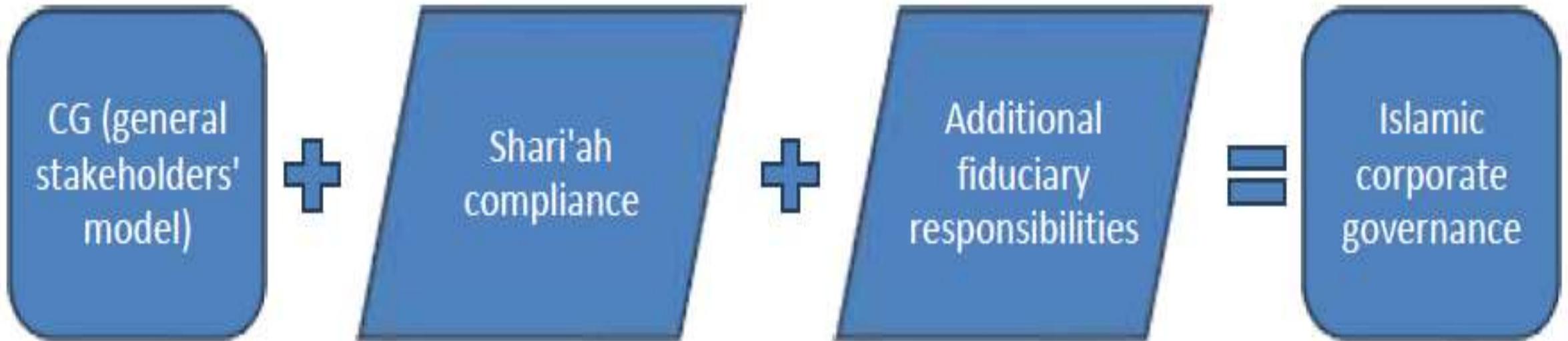
Corporate Governance, in brief **CG** refers to the way a company is managed, directed, and controlled to ensure that it works effectively, fairly, and responsibly. It involves a set of rules and practices that guide how decisions are made to achieve the company's long-term goals which satisfy shareholders, creditors, employees, customers and other stakeholders.

The **International Chamber of Commerce (ICC)** defines:

“Corporate governance is the **relationship** between **corporate managers, directors and the providers of equity**, people and institutions who save and invest their capital to earn a return. It ensures that the board of directors is accountable for the pursuit of corporate objectives and that the corporation itself conforms to the law and regulations.”

Although the scope of CG in IFIs is **larger** than in conventional FIs, the overall concept of CG is the same.

2.1 Islamic Corporate Governance



Components of Islamic CG

2.2 Importance of Corporate Governance for IFIs

AAOIFI has laid down various underlying reasons for pursuing effective CG in its [Governance Standard No. 6](#) 'Statement on Governance Principles for IFIs'. Such as,

i) Enhancing confidence : The financial services industry (whether conventional or Islamic) is one in which ['trust' is vital](#). Sound governance practices serve to enhance public confidence. (para. 16)

Confidence in an IFI cannot be developed without several important measures, one of which is a transparent governance structure. (para. 19)

The Board of Directors, Shari'ah Supervisory Board, management, employees and other parties dealing with or working for an IFI must strive to enhance confidence and trust which are vital to the [survival and growth](#) of its business. (para. 20)

ii) Shari'ah compliance : Governance in the context of an [IFI goes well beyond the boundaries of 'CG' in the conventional](#) context since it also has religious connotations attached to it.

Typically, a stakeholder associates himself with an IFI for [two reasons](#); its [efficiency](#) or competence, and its [Shari'ah compliance](#). It is therefore important to have a governance mechanism in place to ensure the latter. (para. 21)

2.2 Importance of Corporate Governance for IFIs (Contd.)

iii) Business model

The business model of an IFI is characterized by **contracts that are designed to be compliant with Shari'ah**. The risks associated with such contracts are **unique and unlike** a typical conventional lending contract. It is important that both the IFI and its clients recognize the distinguishing features. (para. 23)

iv) Stakeholders' interests

It is important for those charged with governance to **understand who their key stakeholders are**. This understanding allows for the establishment of a governance structure which is characterized by high levels of accountability. (para. 25)

An IFI's interaction with stakeholders has much to do with **dissemination of timely and sufficient financial and non-financial information** regarding its operations and performance. (para. 27)

2.2 Importance of Corporate Governance for IFIs (Contd.)

iv) Social responsibility

The principles of Shari'ah strike a balance between the **interests of the individual and those of the society to which he or she belongs**. Thus, the governance structure of an IFI should align, to the extent possible, the interests of the stakeholders, of those charged with governance and of the society. IFIs are established to assist in using wealth and financial resources in a manner beneficial to investors as well as to the community at large.

vi) Business ethics and culture

Codes of ethics in an **IFI comprise values that are derived from Shari'ah**. Such values underpin the behaviour of all persons employed by or associated with the IFI in carrying out or undertaking their respective duties or obligations to the institution. (part 32)

2.3 Shari`ah governance

A proper Shari`ah governance framework would ensure strict Shari`ah compliance in all practices of the industry. This would give credibility to the industry and instill public confidence. It would also promote operational and financial stability, since it would ensure that the value propositions of Islamic finance are implemented in practice.



2.3.1 Shari`ah governance in IFIs

Definition

As per IFSB-AAOIFI Revised Shari`ah Governance Framework 2022: “*Shari'ah Governance Framework which encompasses a set of institutional and/or system-wide arrangements for the **effective and independent oversight of Shari'ah compliance** of its products/services, processes and business operations.*”.

Elements of Shari`ah governance



2.3.2 Shari`ah Supervisory Board/Committee in IFIs

Definition

- AAOIFI defined “A Shari`a supervisory Board (SSB) is an independent body of specialised jurists in Fiqh Al-Mua`malat (Islamic commercial jurisprudence).” (AAOIFI GS-1, Sec. 2)
- As per IFSB-AAOIFI Revised Shari`ah Governance Framework 2022: “An independent body of specialized Shari`ah scholars (and experts, as the case may be) set up by an IIFS to provide oversight on the Shari`ah compliance of the IIFS”.

2.3.2 Shari`ah Supervisory Board/Committee in IFIs (Contd.)

Role & Responsibilities

- The SSB is entrusted with the duty of **directing**, **reviewing** and **supervising** the activities of the Islamic financial institution in order to ensure that they are in compliance with Shari`ah rules and principles. The fatwas, and rulings of the Shari`ah supervisory board shall be binding on the Islamic financial institution. (AAOIFI GS-1, Sec. 2)
- The SSB must be vested with appropriate **power** and authority as may be necessary to perform its duties and responsibilities effectively
- The **report** of the Shari`a supervisory board shall be published in the annual report of the Islamic financial institution

2.3.2 Shari`ah Supervisory Board/Committee in IFIs (Contd.)

As per IFSB-AAOIFI Revised Shari`ah Governance Framework 2022, The SSB must supervise the IIFS's operations, transactions and processes to ensure compliance with Shari`ah principles and rules. Accordingly, the following shall apply:

- All relevant documentation for products and services, including contracts, agreements, operational documentation used in the IIFS's business transactions, must be approved by the SSB.
- All policies and procedures relating to the IIFS must be reviewed and approved by the SSB, with regard to any Shari`ah compliance consideration.
- The SSB must oversee and approve the profit/loss calculation and distribution to the IAHs.
- The SSB must review and approve the accounting treatment of products and services with regards to Shari`ah.
- The SSB must review and approve the IIFS's annual zakāh calculations on behalf of the shareholders.
- The SSB must review the reports internal Shari`ah audit function and provide advice on such reports.
- The SSB must provide their input to the annual plans of internal Shari`ah audit..
- The SSB must specify the means of disposal of earnings that have been realised from sources or by means prohibited by Shari`ah principles and rules.

3. Challenges faced by IFIs

3.1 So Many compliance Issues

As a Shari`ah based financial institution IFIs have to abide by so many compliance issues. It is the biggest challenge of IFIs for all times. Such

- Shari`ah compliance issues
- Money Laundering and terrorist finance issues
- Ethical Issues
- Compliance of Central Bank policies/circulars/guidelines.
- Compliance of govt. laws/policies/guidelines
- Combating cyber issues.

3.2 Default Culture & Investment Reschedule

One of the foremost challenges confronting the banking sector in Bangladesh is the pervasive culture of willful default among many clients. This issue particularly impacts Islamic banks more severely compared to conventional banks. Unlike conventional banks, Islamic Financial Institutions (IFIs) cannot consider late payment charges, compensation, and penalties as regular income, which compounds the losses they incur due to defaults.



3.3 Limitation of Islamic Money Market & Capital Market Instruments

IFIs have not yet been successful in devising an interest-free mechanism to place their funds on a short-term basis.

In the **Capital market** of Bangladesh, there are limited tradable Financial Instruments. For that reason, the Islamic bank can't deploy their excess liquidity. That's why they are being deprived of the benefit from the income. Islamic banks can't invest in the traditional Instruments as those are interest based. Therefore:

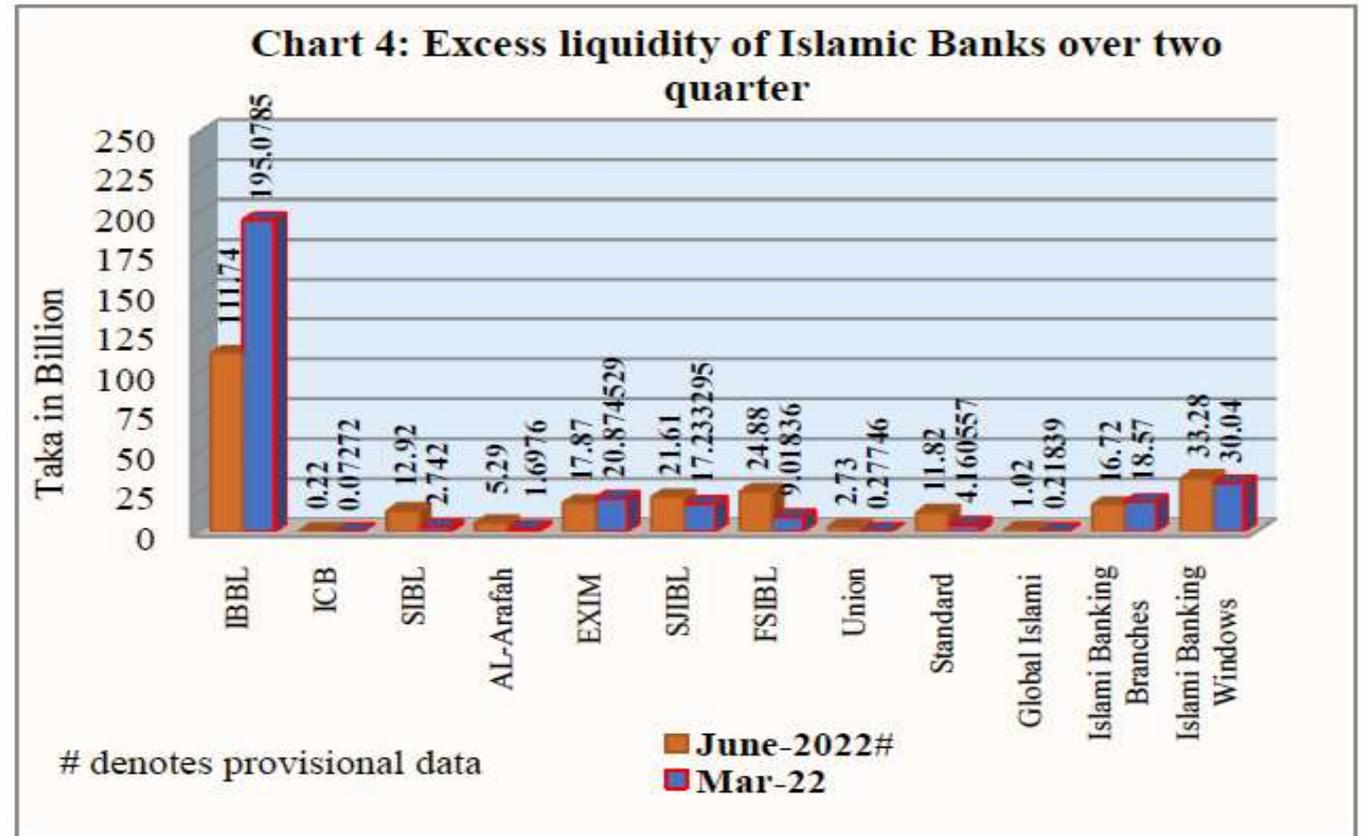
- Bank's excess liquidity remains idle.
- CRR and SLR reserve can't be deployed due to unavailability of interest free instrument.



3.4 Limitation of Islamic Money Market & Capital Market Instruments (Contd.)

Excess liquidity (June'22)

10 Islamic banks	= 210.09 billion
Is. banking branches	=16.72 billion
Is. banking windows	= 33.28 billion
Total Excess Liquidity	=160.09 billion



(Ref. Developments of Islamic Banking Segment in Bangladesh (April-June 2022), available at https://www.bb.org.bd/pub/quaterly/islamic_banking/islamic_apr-jun2022.pdf)

3.5 Leakage of income

Being interest free, Islamic bank can't take part in the field where there is a sing of interest. Bank can't include their income from reschedule investment as compensation charge to income account as this income is treated as 'Haram' in the eye of Shariah principles. As a result, depression of profit incurs here. Such as

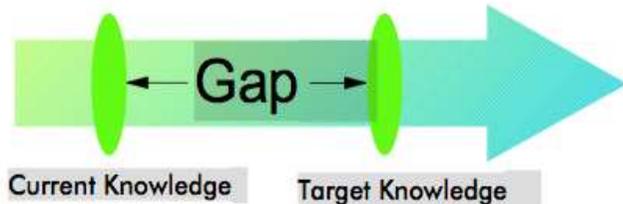
- Income from **Foreign currency clearing A/C** is treated as interest.
- Income from **'Nostro Account'** is treated as interest.
- Shariah non-compliant income derived from inspection by *Muraqib* is treated as **doubtful** and is kept aside to 'Charity Fund'.
- Incomes from defalcated investment as **compensation/penalties** are not included to banks profit.

3.6 Shortage of trained and efficient manpower committed to Islamic Banking

There is a shortage of Islamic Finance and Shariah knowledge based manpower to appraise, monitor, evaluate and audit the projects they are required to finance who can answer the query of the clients with full satisfaction.



3.7 Knowledge gap among the mass people



Though Bangladesh is a Muslim majority country, but still is gap of knowledge regarding Islamic banking system among the people of different levels. They find hardly difference between two systems without name.

3.8 Mismatching between business needs and existing investment products of IFIs

Most of the cases IFIs practice the products copying the conventional system after necessary modifications. Often the business needs of the clients can not be met by the existing product line of IFIs. Such as

- The **cash requirement** of the client can not be met in some cases.
- **Forward Booking** in case foreign exchange business
- Financing in case of **Bidding the tender**.
- Financing in the **service sectors**
- Financing Mobile Financial Services (MFS) like **Mcash, bKash** etc.

3.9 Moral Hazards in practicing PLS Mode of Finance

A **moral hazard** is an economic term that describes a scenario in a transaction in which one party can indulge in risky behavior because they know that the terms of the agreement will require the other party to assume any negative consequences.

The moral Hazards risk involved in **profit-sharing mode** of finance seems to be so high that most of the banks have resorted to those techniques of financing which bring them a fixed assured return. As a result, there is a lot of criticism that the IFIs have not abolished interest but have in fact only changed the nomenclature of their transactions.



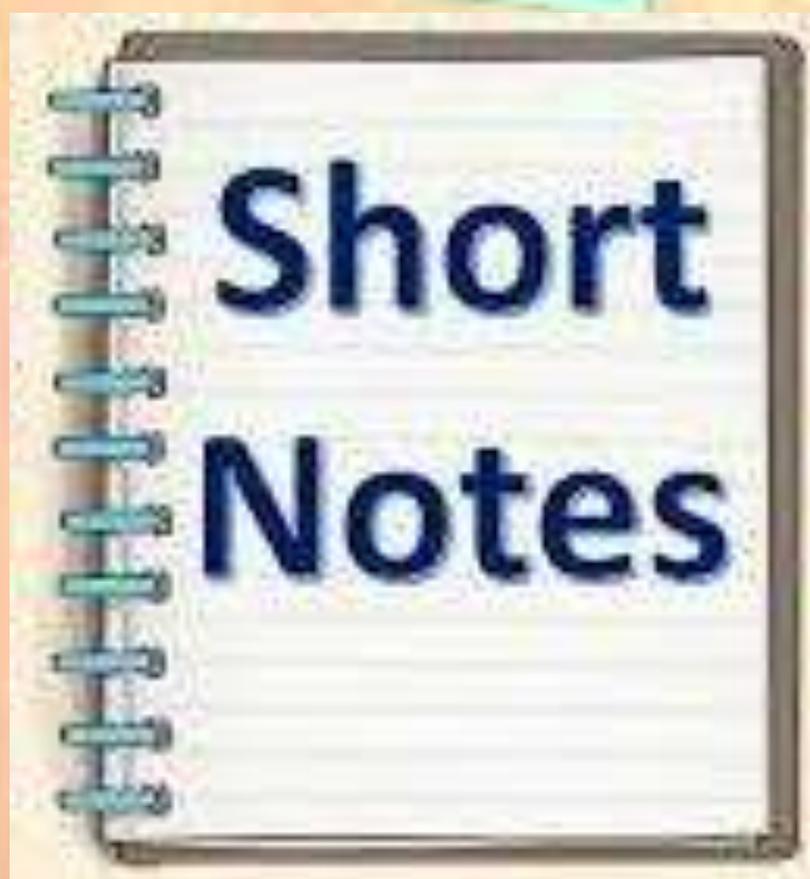
3.10 Accounting system challenge



Islamic Banks have to apply the interest based Accounting system that as there is **no separate** Islamic accounting system.

In most of the cases title of accounts treatment of income differs among conventional, local and international standard.

5.



4.1 Weightage and ISR for Mudaraba Profit Distribution

Weightage: The weightage system is a concept of profit distribution in Mudaraba. Here are some salient features of the weightage system in mudaraba profit distribution:

The weightage system assigns different weightages or multipliers to the capital contributed by the investor (rab al-maal). These weightages are used to calculate the share of profits for each party. In this system, the depositors (mudarib) are given provisional profit which is adjusted after accounts finalization. It is called double tier profit Calculation System.

The weightage system can be customized to suit the specific needs and preferences of the parties involved in the mudaraba arrangement. The profit-sharing ratio and weightages can be adjusted through mutual agreement. This system is mostly practiced by Full Fledged Islamic banks of Bangladesh

ISR/IISR: Income Sharing Ratio (ISR) is another concept in the profit distribution mechanism of Mudaraba contracts in Islamic banking. The profits generated from the venture are shared between the two parties based on the agreed-upon Income Sharing Ratio. In this system, no provisional profit is declared. It is called Single tier profit Calculation System.

4.2 Al Wadeeah and Amanah

Deposits in current accounts with Islamic banks are regarded as Al Wadeeah and Amanah. If the bank obtains authority to use the funds in the current accounts to invest in its business, *Amanah* transforms into a loan from the depositor to the bank and the bank is liable to repay the full amount in the current account, irrespective of profit or loss made by the bank.

Base for Difference	Al Wadeeah	Amanah
Meaning	Custody, safekeeping	Trust, reliability, trustworthiness, loyalty, honesty
Definition	safe-keeping of a sum of money with permission to use and refund on demand	refers to deposits in trust. Holding property in trust for another,
Liability	keeper and trustee of funds becomes wholly responsible and liable for its safekeeping.	entails the absence of any liability for loss, except for breach of duty.
Reward	The bank may offer reward the customer with a payment in the form of Hibah as appreciation for keeping the funds with the bank	No relevancy with this

4.3 CRR & SLR

Cash reserve requirement (CRR)

CRR or cash reserve ratio is the minimum proportion / percentage of a bank's deposits to be held in the form of cash. Banks have kept these as cash with Central Bank.

All banks (conventional & Islamic) have to keep CRR of 4.00% of their deposits as per regulations.

When a bank's deposits increase by tk.100 crore, and considering the present cash reserve ratio of 4%, bank will have to hold additional tk 4 crore with central Bank and will be able to use only tk. 96 crore for investments and lending. Therefore, higher the CRR, lower the amount that banks can lend. Thus Central Bank can control the Liquidity by changing the CRR i.e. increase CRR to reduce the lendable amount and vice-versa.

Statutory Liquidity Ratio (SLR)

SLR is the reserve requirement that banks are required to maintain in the form of cash, gold reserves and central bank-approved securities before disbursing loans to the customers.

Islamic banks have to keep SLR of 5.5 per cent of their deposits, whereas for conventional banks it is at least 13 per cent as per regulations.

4.4 Bangladesh Government Islamic Investment Bond (BGIIB)

Conventional banks have been maintaining their excess liquidity through Government Treasury Bills and Bonds while the Islamic banks cannot invest their surplus liquidity in these monetary instruments due to interest bearing nature of these instruments. However, considering the excess liquidity problems of Islamic banks government of Bangladesh introduced Bangladesh Government Islamic Investment Bond (BGIIB) in 2004 with the objective to develop a sound foundation for the Islamic bond market and also to convert excess liquidity into investment through Islamic bonds.

Features of Government Islamic Investment Bond GIIB

- a. Can be purchased by any individual, private or public companies, IFIs for a minimum investment of Taka 100,000.
- b. Can be used as collateral for a loan or investment from any financial institution.
- c. Considered as qualified securities for the purpose SLR of the Bank

4.5 Islamic Trust Receipt

- A trust receipt is a notice of the release of merchandise to a buyer from a bank but these goods remain hypothecated to the bank. The buyer is allowed to hold the merchandise in trust for the bank, for manufacturing or sales purposes.
- This arrangement often falls under a letter of credit financing. The trust receipt serves as a promissory note to the bank that the loan amount will be repaid upon sale of the goods.
- An Islamic trust receipt is a financial instrument used in Islamic finance that facilitates trade transactions while adhering to Islamic principles. In an Islamic trust receipt arrangement, a bank or financial institution purchases goods on request of a customer, after acquiring ownership and possession over the goods the bank sells the goods to the customer at an agreed-upon price, which includes a profit margin. The customer takes possession of the goods but bank's control remains over the goods until they have fully paid the price of the goods to the bank. The customer may use the goods for their business purposes while making installment payments to the bank.
- This type of transaction helps to reduce the costs and risks associated with storage of the goods and products for Islamic banks

4.6 Murabaha to the Purchase Orderer (MTPO)

A Murabaha transaction may be concluded without a prior promise to buy, in which case it is called an ordinary Murabaha. If it is concluded with a prior promise to buy, submitted by a person interested in acquiring goods through the IFI, it is called a "banking Murabaha" or "Murabaha to the purchase orderer". AAOIFI defines Murabaha to the purchase orderer as:

"... the sale of an item by the institution to a customer (the purchase orderer) for a pre-agreed selling price which includes a pre-agreed profit mark-up over its cost price, this having been specified in the customer's promise to purchase. Normally, a Murabaha to the purchase orderer transaction involves the institution granting the customer a Murabaha credit facility."

The practical application of Murabaha to the purchase orderer (MTPO) transaction involves a prior promise to buy or a request made by the customer interested in acquiring goods on deferred payment terms. Murabaha is the most common contract used by Islamic banks globally. On the asset side, its practical applications include working capital finance, auto finance, housing finance and other fixed assets finance. It is also used in trade finance.

4.7 Wakalah

- Wakalah is a contract in Islamic finance where one party acts as an **agent** (the wakil) on behalf of another party (the **principal**) to perform specific tasks or transactions. Wakala in Islamic banking refers to a contractual arrangement where one party acts as an agent (the wakil) on behalf of another party (the principal) in conducting specific financial transactions or managing assets. The agent may or may not receive a **fee** or commission for their services.
- Wakala contracts provide a mechanism for Islamic banks to offer a range of financial services while complying Shari'ah principles including investment management and agency services.
- Overall, wakala contracts play a vital role in the functioning of Islamic banks, enabling them to provide diverse financial solutions to their clients in a manner that is consistent with Shariah principles and values.

4.8 Mudaraba Liquidity Support (MLS)

The "Mudaraba Liquidity Support (MLS)", introduced by Bangladesh Bank through "[DMD Circular 2/2023](#)", is a Shari'ah-compliant liquidity management facility designed for Islamic banks in Bangladesh. It operates under a "Mudaraba" contract, where Bangladesh Bank serves as the "Rabb-ul-Mal" (capital provider), and the Islamic bank receiving the funds acts as the "Mudarib" (investment manager).

The MLS provides short-term liquidity for "[7, 14, or 28 days](#)", with the profit rate tied to the bank's "three-month Mudaraba Term Deposit Receipt (MTDR)" rate. Banks can apply for a minimum of "[Taka 10 crores](#)" or multiples thereof. Eligible securities for collateral include "claims against remittance incentives" and "financial stimulus claims". The "Actual/Actual" day count convention is used for profit calculation.

MLS ensures that Islamic banks can manage liquidity efficiently without compromising Shari'ah principles, promoting the stability and flexibility of the Islamic banking system.

ALLAH HAFEEZ

THE END