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**SUBJCT# ISLAMIC BANKING**

**DEGREE# BBA**

**MODULE# 8th Semester**

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**Q1. How can modern banks use Salam to offer products to a wide range of customers in different fields? Briefly explain and give examples of actual banks and their products in Pakistan who are offering Salam based financing.**

**Answer:** Salam is allowed in Islam, it is basically the mode of financing for the small traders and customers. This mode of financing can be used by the modern banks and institution to offer a product to a wide range of customers in different fields such as Farmers etc. The bank will advance the cash to their customers and their conclusion of the contract of delivery of goods in during the period (which is during the future culture).it is a structured financing that can help customers to move away informal financing means such as money lender, whereby they are charged with a heavy interest on a compounding basis.as pointed out earlier, the prince in Salam may be fixed at a lower rate than the price of those commodities delivered at the spot. In this way, the difference between the two prices may be valid profit for the banks or financial institution.

Following are the points shows how banks uses Salam to offer a product to ide customers,

Step 1: Submission of application form with necessary documents i.e.s identification credential land ownership, other source of income and past production volume to the bank for credit screening.

Step 2: the bank will offer a purchase price to the customers based on the credit worthiness evolution, crop quality delivery date, etc.

Step 3: The client accepts the offer and sign a Bai Salam contract stating the predefined products,

Delivery date, product quality between the customers and the banks.

Step 4: the bank plays the settlement price on the spot as defined in the contract.

Step 5: The client delivers the product to the bank on the agreed specification and pre-defined delivery date and venue.

Step 6: The bank sells the products matter in the market at the selling price.

Note: the selling price will be higher than the purchase price in which the difference will be the banks.

In the original mode of Salam financing, the bank will receive commodity from the client and not money. being conversant with dealing in money only, it seems to be cumbersome for them to receive different commodities from different client to sell them in the market. they cannot sell those commodities before they are actually delivered to them, because it is prohibited in Shariah. Besides the bank will also facing a problem of storage and maintaining the commodity.

**Actual banks and their products in Pakistan who are offering Salam based financing:**

Salam is the contract in which seller and buyer agree to the future contract in which buyer pay the advanced payment on the spot and seller and seller supply the product in future date. Salam is a sale where by the seller under take to supply some specific goods to the buyer at a future date of exchange of an advanced price fully paid at spot. The contract of Salam creates a moral obligation on the Salam seller to deliver the goods. The best examples of banks and product that are using Salam based financing HBL BANKS FBL BANKS MEAZAN BANKS and the product that are used for Salam based financing are

**Q2. What is the basic logic behind the Mudarabah mode of financing? Briefly explain. Also explain the scope and potential of Mudarabah for Islamic banks in Pakistan.**

**Ans: Basic Logic behind the Mudarabah mode of financing:**

*Mudaraba* is [venture capital](https://en.wikipedia.org/wiki/Venture_capital) funding of an entrepreneur who provides labor while financing is provided by the bank so that both profit and risk are shared. As a mode of financing Mudarabah is a sort of partnership.

Both parties participate in the profit that is going to be generated by the financed activity. The parties are free to agree on the ratio of profit distribution (70% - 30% or 50% - 50% or any other).

Furthermore, it is a Shari’ah requirement in mudarabah that all of the capital has to be paid at the signing of the contract. It is not allowed to pay it later or on installments basis.

Once operation starts, the financier has no right to interfere in the day to day business. If agent fails to follow the instructions and satisfy the conditions, then he is liable for loss of capital. The mudarib don’t guarantee capital nor profit to the financier. Rather he or promises good conducted honesty. This is the source of moral hazard and adverse selection in mudarabah.

**Scope and potential of Mudarabah for Islamic banks in Pakistan**

* Islamic banking in Pakistan the Mudaraba has been suggested a technique which shall provide the basis for the Islamic re-organization of commercial banking sector.
* In actual practice of Islamic banking, Mudaraba has not made much progress on the asset side of the balance sheet, although on the liability side the Islamic banks on Mudaraba accept the funds in investment accounts
* The Islamic bank becomes interested to receive the amounts from investment account holders and to share the profit generating from them based on a pre-agreed ratio, while the losses, if any, will be borne by the funds provider, except the case of a verified misconduct, negligence or violation of the conditions by the Islamic bank.
* The Islamic banks have a healthy domestic funding base. Close to 85.3 percent of the assets are funded by customer deposits, and about 63 percent are PLS deposits accounts based on Mudarabah contracts while current accounts are mostly based on Qard. Funds due to OFIs account for a very small share.
* Short/medium/long - term financing, Project financing, Small & medium enterprises setup financing, Large enterprise financing
* Project financing, Small & medium enterprises setup financing.

**Q3. (a) Do all of the conditions of a normal sale transaction as defined in Islamic Shariah apply to Istisna? Why and why not? Elaborate your answer by comparing and contrasting conditions of a valid sale with the conditions of Istisna**

**b) Briefly explain parallel Istisna with an example.**

**Answer:**

* **Under Reasonable condition:**

 It is necessary for Salam that the price is paid in full in advance, while it is not necessary in istisna

* **Delivery or possession:**

The time of delivery is an essential part of the sale in Salam while it is not necessary in istisna that the time of delivery is fixed.

* **Price:**

The time of delivery is an essential part of the sale in Salam while it is not necessary in istisna that the time of delivery is fixed.

* **Exist able:**

The subject of istisna is always a thing which needs manufacturing. The Subject matter of Sale must exist at the time of Sale

* **Termination of Contract**

In Sale Contract cannot be cancelled immediately while the contract of Istisna’ creates a moral obligation on the manufacturer to manufacture the goods, but before he starts the work, any one of the parties may cancel the contract after giving a notice to the other. However, after the manufacturer has started the work, the contract cannot be cancelled.

**(B) Briefly explain parallel Istisna with an example.**

The parallel istisna' involves: the customer (the buyer); the Islamic bank (the seller); and the manufacturer (in some cases it can also involve sub-contractors), where the buyer can obtain financing from the Islamic bank. The bank opts to use two mutually independent istisna contracts called parallel istisna.

**For example**, fictional customer Acme, Inc., approaches the World’s Best Islamic Bank to manufacture a housing scheme with specifications for $1 million. Then the bank enters an agreement with A Construction Company to build the houses with the same specifications for $800,000.

When the construction project is complete, A Construction Company hands over the project to the bank, which verifies the specifications and delivers the product to Acme, Inc., on the payment basis agreed to in that part of the istisna.

The bank goes for a parallel contract in this scenario because it can’t produce the assets and doesn’t want to hold the produced assets after their completion. In a parallel contract, the bank has both a buyer for its products and a manufacturer.

**Q4. (a) Briefly explain the basic rules of Musharakah.**

**Answer: Musharakah:**

*Musharakah* is a term frequently referred to in the context of Islamic modes of financing. The connotation of this term is a little limited than the term “shirkah” more commonly used in the Islamic jurisprudence.

**The Basic Rules of Musharakah**

* Musharakah or Shirkat-ul-amwal is a relationship established by the parties through a mutual contract
1. The parties should be capable of entering into a contract;
2. The contract must take place with free consent of the parties without any pressure, fraud or misrepresentation, etc.
3. the contracting parties must be sane and mature

**Distribution of Profit**

The percentage of profit to be distributed between the partners must be agreed upon at the time of effecting the contract.

**Ratio of Profit**

* Is it necessary that the ratio of profit of each partner conforms to the ratio of capital invested by him?

**View of Imam Malik and Imam Shafi’i**

it is necessary for the validity of musharakah that each partner gets the profit exactly in the proportion of his investment. Therefore, if A has invested 40% of the total capital, he must get 40% of the profit. Any agreement to the contrary which makes him entitled to get more or less than 40% will render the musharakah invalid in Shari ‘ah.

**the view of Imam Ahmad**

 is that the ratio of profit may differ from the ratio of investment if it is agreed between the partners with their free consent. Therefore, it is permissible that a partner with 40% of investment gets 60% or 70% of the profit, while the other partner with 60% of investment gets only 40% or 30%.

**The third view is presented by Imam Abu Hanifah**

which can be taken as a via media between the two opinions mentioned above. He says that the ratio of profit may differ from the ratio of investment in normal conditions. However, if a partner has put an express condition in the agreement that he will never work for the musharakah and will remain a sleeping partner throughout the term of musharakah, then his share of profit cannot be more than the ratio of his investment.

**Sharing of Loss**

But in the case of loss, all the Muslim jurists are unanimous on the point that each partner shall suffer the loss exactly according to the ratio of his investment.

**The Nature of the Capital** Most of the Muslim jurists are of the opinion that the capital invested by each partner must be in liquid form. It means that the contract of musharakah can be based only on money, and not on commodities.

* However, there are different views in this respect.
1. **Imam Malik** is of the view that the liquidity of capital is not a condition for the validity of musharakah, therefore, it is permissible that a partner contributes to the musharakah in kind, but his share shall be determined on the basis of evaluation according to the market price prevalent at the date of the contract. This view is also adopted by some Hanbali jurists.
2. **Imam Abu Hanifah and Imam Ahmad** are of the view that no contribution in kind is acceptable in a musharakah. Their standpoint is based on two reasons:

**However, there are some specific conditions for the validity of *musharakah* contract.**

**Some important conditions are outlined in the following:**

1. The ratio of the profit-sharing between the partners must be determined at conclusion of the contract. The profit for each partner should be in the percentage of actual profit. This is not permissible to determine a profit in lump sum amount of money or in the form a percentage of the capital. For example, if they agree that “A” will get 5% of his capital, then the contract would not be valid.

2. It’s allowed for working partner to set his profit more than his share of capital with mutual consent of the parties. However, if a partner explicitly mentions in *musharakah* contract that he will take part in management of the business and will remain as sleeping partner, then his ratio of profit would be more than his share of capital. For example, if he invested 50% capital in *musharakah* venture, then he is entitled to stipulate his profit share within 50% percent, not more than that.

3. If loss occurs in *musharakah* venture, every partner will suffer the loss according to his ratio of investment. This principle is agreed by all jurists and scholars across the different schools of Islamic law. For example, if a partner has invested 30% of the capital, he shall suffer exactly 30% of loss. Therefore, it’s not allowed to put any condition contrary to this principle. Otherwise, the contract become invalid.

4. In principle, the capital in *musharakah* contract should be contributed in the form of monetary assets. However, many contemporary scholars are of the view that capital may be contributed in the form tangible assets if all partners are agreed. In this case, it’s necessary to determine the monetary value of these assets in currency. So, the share of each partner is known clearly.

5. In general, every partner shall have a right to participate in the management of *musharakah* and work for it. However, it’s permissible that the partners may agree that only one of them work for the *musharakah* and other remain as sleeping partners. If all the partners agree to work for *musharakah* venture, each one of them shall be treated as the agent of the other in all the business matters of the business.

**(b) List the elements of a valid sale.**

**Answer: Essentials elements of a Contract of Sale**

The following six features are essential elements of any contract of sale of goods.

* Goods
* Price
* Two parties
* Transfer of ownership
* All Essentials of a Valid Contract of Sale
* Includes both a ‘*sale* ‘and ‘*an agreement to sell* ‘