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1. Introduction

Islamic banking has a fairly brief history – first Islamic banks opened their doors merely 50 years ago when the 1970's saw a specific set of circumstances that allowed for this development. They sought to provide an alternative to conventional banking and offer products that would be in accordance with basic rules of Islamic law – namely the abolishing of interest and instead using a partnership based on profit and loss sharing.[1] Islamic banking can be understood as a banking activity that is compliant with the principles of sharia and their practical manifestation through Islamic economics. During the past five decades, Islamic banking faced various challenges and had gone through major changes. Their development took different paths in different countries and regions and Islamic banking can hardly be seen as a perfectly monolithic and uniformly regulated sector.

Despite several slowdowns that the development of Islamic banking was facing in the past, it now presents a considerable and growing part of the global financial system. According to Ernst&Young, "Islamic banking assets grew at an annual rate of 17.6% between 2009 and 2013, and will grow by an average of 19.7% a year to 2018".[2] While usually associated with countries with a Muslim majority, such as Iran, Malaysia or Saudi Arabia, Islamic law compliant products have been offered by conventional banks as well and the year 2014 saw a major advance for Islamic finance when Britain became the first western country to issue a sovereign sukuk (Islamic alternative to bonds) which £200m sale attracted orders of £2.3 billion[3]. Private sector is following the lead with Société Générale, Bank of Tokyo-Mitsubishi UFJ and Goldman Sachs reportedly preparing issues of *sukuk* to raise money.

Given these recent developments, it seems more then timely to examine Islamic banking and put it in context with the reality of European Union. While it may seem that Islamic banking is a distant feature that has little influence on our domestic banking sector, its growing size demands our attention and our ability to understand it. Even more than before, current European banking sector is largely interconnected and developments in the Western Europe affecting financial services providers can be of great influence on their Czech subsidiaries.

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[1] WARDE, I., *Islamic finance in the global economy*, p. 2.
[2] Big interest, no interest: The market for Islamic financial products is growing fast.
[3] Big interest, no interest: The market for Islamic financial products is growing fast.

This thesis will be based on analysing selected banking products being offered by Islamic banks and comparing them with their conventional counterparts. Additionally, I will present both international regulatory bodies issuing standards applicable to Islamic banking and some specific aspects of internal regulatory rules of Islamic banking institutions. Brief description of Pakistani banking system will illustrate some of the theoretical points. In a 1999 landmark case its Supreme Court has ruled that Pakistani banks cannot as of 2002 base their transaction on interest, while this decision was reversed in 2002, Pakistan can still be given as an example of an Islamic banking system since it government has decided to gradually steer the country towards interest-free banking. Furthermore, I will offer a short description of the recent developments in Germany where a first Islamic bank in Europe is set to open on 1 July 2015.

The main goal of my work is to present banking products of Islamic banks in order to give a good overview of main aspects of Islamic banking and possible issues arising from their distinctive nature. Consequently, I want to answer a question of possible competitiveness between the two systems and regulatory challenges that are facing Islamic banking in current interconnected banking world. In this area, I will put a special emphasis on international regulatory bodies and standards that affect Islamic banks and on internal supervisory mechanisms whose role is to ensure that all activities are compliant with Islamic law. I will complement this part of my thesis by comparison between the two banking systems which will argue that they can exist side to side in the current banking world and possibly even benefit from each other, especially in the area of reducing risks and increasing responsibility.

Given the nature of this topic, the approach to my research will be highly interdisciplinary. Knowledge of the financial system and the banking sector must be combined with a legal analysis of relevant legislation and good understanding of Islamic law. To allow the reader to get acquainted with various aspects influencing the nature of Islamic banking, individual chapters will be devoted to each topic. The first chapter should be understood as a pivotal part of this thesis since it will introduce the main characteristics of Islamic law. The following chapters will deal with characterization of selected Islamic products – *mudaraba, murabaḥah, musharaka* and *ijara,* and with their comparison to relevant conventional products. Next, I will introduce regulatory aspects of Islamic banking and finance focusing especially on international regulatory bodies and the question of compliance with *sharia*. I will follow up with two brief case studies and, finally, I will present a conclusion where I will draw on findings of this thesis.

My research is based mainly on the available primary sources including state legislation of relevant countries, bank regulations and internal documents of Islamic banks. These will be complemented by secondary literature which has recently multiplied in numbers. However, the main works have been largely descriptive and dealing solely with Islamic banking itself. Very few works have dealt with Islamic banking in comparative perspectives with particular examples. The most notable secondary sources that I cannot omit are undoubtedly *Islamic finance: Law and Practice* by Craig R. Nethercott and David M Eisenberg[4] and *Islamic Law and Finance: Religion, Risk, and Return* by Frank E. Vogel a Samuel L. Hayes [5]. Recently, other important books have been published. I will try to use as many of them as possible given their relevance to my topic and their availability.

Special remark needs to be made regarding the transcription of Arabic terminology. I will be using the most common ways the relevant vocabulary is being transcribed into English. While at times, it may be not consistent with the strictly academic transcription, I believe it will enable the reader to make easier connections when looking for further information.

2. Sources of Islamic Law

The main source for Islamic law (or Sharia, used interchangeably in this thesis), and therefore Islamic finance, is the Qur'an which is believed by Muslims to be a revelation from God. It is the central religious text governing in a complex way the entire life of an individual as well as society. It is complemented by the teachings of Muhammad, called Sunna. It contains Muhammad's acts, words, acknowledgements and even tacit consents and serves as a supplement to Qur'an. These two are considered as primary sources and are treated as such by most of Islamic jurist and legal schools. Secondary sources include consensus (*ijma*) and legal reasoning by strict analogy (*qiyas*).[6] While secondary sources are considered only when Qur'an or Sunna are in any way ambiguous, in fact they are the prominent aspect forming the nature of Islamic law. The simple reason for their importance lies in a rather vague language of the primary sources – often the wording does not provide for a clear norm. Also, a certain matter

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[4] NETHERCOTT, Craig R.; EISENBERG, David M. *Islamic finance: law and practice*.
[5] VOGEL, Frank E.; HAYES, Samuel L. Islamic law and finance: religion, risk, and return.
[6] HALLAQ, W. B., An introduction to Islamic law, p. 21-27.

can be discussed at more than one place in the source which can lead to uncertainness and even contradictions.

The authority of consensus stems from the belief that when all legal experts cannot find an answer from the primary source and use their reason to reach the same conclusion, such an opinion is valid and right. After all, Mohamed himself said that "*my followers will never agree upon an error or what is wrong*" and that "*God's hand is with the entire community*". However, Muslims do not agree on a single definition of consensus. For some schools, only opinion of jurists is relevant when forming a consensus, others believe that an agreement of the whole community is needed. In the modern times, doctrine of consensus was used as an instrument of reform by number of Islamic scholars reinterpreting such matters of Islamic law as polygamy.

Legal reasoning aims to present an answer to a legal problem by drawing analogies to a previously accepted decisions. Sound analogy derives its arguments form logic used in Qur'an and Sunna. Yet again, views on admissibility and position of legal reasoning differs among the scholars. The majority of Muslim scholars believed that the doors of legal reasoning have closed after the 10th century when the major legal schools have already been established and majority of jurists was not using this method independently. This position was reversed only during the 20th century, when part of Muslim legal community opened the symbolic door and allowed for independent legal reasoning again.

Other sources of Islamic law include public interest (*maslaha*), overriding necessity (*darura*) or local customs (*urf*). They can be used as supporting arguments based on the logic of primary sources. Despite their relatively less significant nature, they have served to develop new ideas or adopt concepts formerly excluded from Islamic law. The degree to which they are used and permitted varies among the scholars and legal schools allowing for maximum flexibility and pragmatism as desired.

Secondary sources are used by Islamic jurists to arrive to the right interpretation of the primary sources and to understanding what is the law. Here, it must be mentioned that contrary to both continental and common law systems, the prominent role in Islamic law belongs to a jurist, not to a judge. Judge is considered merely a technocratic figure, strictly applying the law but not engaging in legal interpretation. That is left to lawyers and jurists and every jurist is entitled to his own legal reasoning and thus interpretation of the primary sources. Whether such interpretation will be taken into consideration by the judge and by other jurists depends on the

accomplishments of this jurist. The most accomplished jurists were able to found entire legal schools and attract large number of followers, therefore creating particular legal doctrines. Four legal schools of Sunni Islam gained prevalence during the 8th and 9th century. They were named after their founders – Hanafi, Maliki, Shafi'I, and Hanbali. Each of these schools, or *madhhab* in Arabic, had a distinct set of views on various issues and interpretative method and became prevalent in different regions of Muslim world. However, today, number of scholars have become a founders of their own legal doctrines and digressed from the original four schools.

The corpus of Islamic jurisprudence is called *fiqh* and can be described as the human understanding of Islamic law. Or in other words, it can be said that *fiqh* is the interpretation of Islamic law (*sharia*)[7] in the context of legislative needs of a Muslim society (*umma*). In English, or indeed in other languages as well, the term Islamic law can mean both sharia and *fiqh* causing at times misunderstandings. Sharia is only one, perfect and all-encompassing while *fiqh* being a human comprehension can be faulty, multiple, uncertain and changing.[8]

The whole life of a devout Muslim is described by Islamic legal system. Matters that are between man and God (*ibadat*) are distinguished from matters among the community (*muamalat*) and this distinction influences also the methodology of interpretation used. While *ibadat*, which include e.g. praying or fasting, does not permit for excessive interpretation, *muamalat*, e.g. all matters of finance and trade, is open to change and development, thus allowing for facilitation of human interactions within the limits of other Islamic principles. All human actions, as well as actions of the whole community, are divided into five categories (1) obligatory, (2) meritorious, (3) morally neutral, (4) reprehensible, and (5) forbidden. All of these mode naturally contain certain exceptions that allow a simple Muslim to live a normal life (e.g. the sick or children are not supposed to fast during Ramadan which is otherwise obligatory). Only modes obligatory and forbidden are enforceable and punishable by in this world. In between modes are given all legal validity and permissibility. They are given a moral consequence that can entail punishment or commendation but that can happen only in the Hereafter and by the God. Given all above mentioned principles, it should be clear at this point that Islamic law is far from the rigid, immutable legal system that is quite often presented. On

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[7] Sharia is in its meaning much wider than just Islamic law. It covers both profane and sacred spheres of human conduct and is believed to be unlimited, given by God and consisting of even those rules that are yet to be revealed. In the Qur'an, it is used in the meaning of divinely appointed path. As a concept it is therefore wider than how we usually understand common law or civil law.

[8] VOGEL, F. E.; HAYES, S. L., Islamic law and finance: religion, risk, and return, p.32.

the contrary, especially in its *muamalat* dimension, Islamic law can be accommodated to developments in the society, for innovations and exceptions and for previously unknown scenarios.

There is no central authority in Islam that could pronounce one legal opinion to be the right one – that can be done only by the God. Therefore, the nature of Islamic law is highly pluralistic allowing itself to be flexible and adaptable to various societies as well as to development over time.[9] I would like to stress this particular dimension of Islamic law as it is often one aspect that quite often seems to be misunderstood. Not only there is no single religious authority in the majoritarian Sunna branch of Islam, but even more surprisingly to many western lawyers, there is no single secular authority either. Islamic law is not a national law the way Czech or French law is[10] and neither is it purely a set of religious dogmas and rules.

Throughout the history of Islam, there have been attempts to classify and interpret sources of law and to describe modes of behaviour using different methodology. Consequently, there has never been a time when all Muslims agreed on one single way to interpret and use Islamic law. Today, there is a wide range of countries with majority of Muslim population that have decided to incorporate Islamic law into their legal orders to various degrees. On one side, there are countries like Turkey, which based its legal codifications mainly on European models, and on the other side we have Saudi Arabia which is trying to include *fiqh* in most of its legal order. However, no country has managed, or even can possibly manage, to incorporate the whole *fiqh* in its complexity. Taking Pakistan as an example we can see that although proclaimed as an Islamic state, large parts of its laws are remnants of its history as part of the British Empire complemented by modern legislature based on different models of European and American laws.

Without going too deep into this issue, a special point needs to be made regarding possible changes in Islamic law over time. While Qur'an and Sunna remain an unchanging, rigid sources, legal reasoning, consensus and other additional sources allow for certain changes. Given the above mentioned characteristics of Islamic law, it is only natural that there is large number of different opinions not only on the exact norms of Islamic law but on the permissibility of specific interpretation methods as well. The spectrum of juristic opinions

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[9] HALLAQ, W. B., An introduction to Islamic law, p. 27.
[10] As a consequence, a party to a contract cannot choose Islamic law as a binding law of the contract.

ranges from absolute rigidness that allows only very strict adherence to Quranic text to liberal approach taking into consideration notions of public benefit, local customs and others. Even the concept of consensus varies among legal schools – some view it as a consensus of Islamic jurists, other as consensus among the whole community, and yet other say that only the Companions of the Prophet could agree on a binding consensus. In the following chapters, I will come back to the notion that certain term or concept has various meanings and is interpreted in various ways. The above mentioned explanation serves to show that such variability is not inconsistent but in fact the very nature of Islamic law.

It is useful to keep mind this very specific aspect of Islamic law when discussing Islamic finance. It will be easier to understand the fact that we can hardly talk about one single banking system. Rather, each country, and even each bank, can be governed according to slightly different rules. There is simply no "*fixed, unchanging framework for Islamic finance, applicable everywhere, that has been established once and for all by religious scholars*."[11] However, as this is not an attribute favoured by clients of any financial institutions, number of regulatory bodies has been set up over the last several years and decades.

3. History of Islamic Finance

The recent resurrection of Islamic banking in the 1970's may seem as a new idea whose sudden emergence was boosted by the rise of Islamism and of Islamic states. However, principles of Islamic finances have been set up by the ancient Qur'an and by the teachings of Muhammad. The prohibition of interest and speculative practices were integral part of pre-Modern Muslim states and were abandoned only when European influence, and later European dominance, in the region introduced Western banking systems, later adopted by virtually all Muslim countries.[12] The period of following the World War II has seen an emergence of the modern Middle East and independent Muslim countries. The period has been marked by Islamic revivalism[13] which can be explained as a return to the fundamental principles of Islam as defined by Qur'an and Sunna. The reasons for this movement were numerous and had their base both in the historical development of the region and in the natural cycle of growth and

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[11] NETHERCOTT, Craig R.; EISENBERG, David M. *Islamic finance: law and practice*, p. 1.
[12] VOGEL, F. E.; HAYES, S. L., Islamic law and finance: religion, risk, and return, p.6.
[13] SAEED, A., Islamic banking and interest: a study of the prohibition of riba and its contemporary interpretation, p. 5.

decline. Revivalism had various branches that argued often conflicting ideas and its origin was laid already in the 18th century.

First Islamic financial institutions appeared in Egypt in the 1960's and 1970's – the Mit Ghamr project of 1963 and Nasser Social Bank in 1971. Soon after that followed the important year of 1973 that marked the establishment of multinational Islamic Development Bank under the Organization of the Islamic Conference. Number of other Islamic financial institutions has been established in the following years – private as well as public and state-controlled.[14] The most important factors that lead to this development were the rising wealth of conservative Gulf states, the revivalist movements outlined above and the readiness of (authoritarian regimes) Muslim countries to adopt the traditional interpretation at policy-making level.[15]

Ever since the 1970's the environment has been favourable to further development of Islamic banking. Even though it saw its highs and downs, the number of Islamic banks increased significantly over time – by 1980, there were already nine Islamic banks functioning in the Muslim countries. During the next five years, twenty-four more financial institutions have been established. Recently, we could witness Islamic banks being opened also in non-Muslim countries as well as conventional banks opening special branches dealing with Islamic finances. Pakistan (announced Islamicization of its banking system 1979 which however failed and had to be abandon only to be re-launched partly in 2001), Iran and Sudan (both in 1983) should also be mentioned as examples of states running their economies entirely on Islamic basis.[16] Malaysia, now the leader in Islamic finance and banking, introduced an Islamic banking legislation in 1983. At the same year, the state Bank Islam Malaysia Berhad was created. Malaysia did not intend to Islamicize its banking sector entirely like above mentioned countries, rather it wanted to encourage a dual banking structure where both systems co-exist and complement each other.[17]

It needs to be mentioned that the creation of first Islamic banks did not bring an instant success. Far from that, the first models proved to be unworkable and were hit hard by global recession and decline in oil prices in the 1980's accompanied by several financial scandals and

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[14] VOGEL, F. E.; HAYES, S. L., Islamic law and finance: religion, risk, and return, p. 4.
[15] SAEED, A., Islamic banking and interest: a study of the prohibition of riba and its contemporary interpretation, p. 8.
16 SAEED, A., Islamic banking and interest: a study of the prohibition of riba and its contemporary interpretation, p. 15.
[17] NETHERCOTT, Craig R.; EISENBERG, David M. *Islamic finance: law and practice*, p. 4.

collapses.[18] Later evolution and necessary changes were influenced as much by inner development in the Muslim world as by the changing world order and revolution in international finance. Islamic finance were given a second chance and moved towards more viable way of replicating conventional finance through *sharia* compliant products and within limits set by *sharia* advisers. Islamic banks no longer desired to create a completely new financial system. Instead, they wanted to achieve the same goals as conventional banks while making sure that they fulfill their Islamic obligations. A new *ijtihad* (independent reasoning according to *qiyas*) developed in order to accommodate the ongoing changes of the position of Islamic finance in the world of globalization and deregulated finance.

Nethercott and Eisenberg identified two main models of Islamic finance – one associated with the Gulf countries and the other with Malaysia. Whereas the outset of Islamic banking system in the Gulf countries was driven mainly by its economic success and the surpluses generated by oil exports, Malaysia created the Islamic part of its dual banking system as an answer for the need to develop and push its economy.[19]

4. Basic principles of Islamic Finance

Generally, Qur'an encourages trade by mutual consent even favouring it over other legal means of gain such as gift and inheritance. The two key elements are mutual consent and gainful exchange. It is said in the Sunna that being asked: "*What form of gain is best? The Prophet said, 'A man's work with his hands, and every legitimate sale*."[20] Islam places an emphasis on consent and intention, clearly favouring matter over form and encouraging a rightful gains and striving for prosperity and better life. Similarly, Islam does not disapprove of incurring debt, provided that the debt is set in writing and is not for something that is unlawful. Qur'an and Sunna also encourages leniency to debtors calling onto the creditor to grant a deferral or even a remission as a form of desirable charity.

Wealth in Islam is considered a positive good, property is respected and profit making work is encouraged but portion of this wealth is owed to the community and those less fortunate. Earliest Arabs were skilled merchants that created number of practices used even today for the

[18] NETHERCOTT, Craig R.; EISENBERG, David M. *Islamic finance: law and practice*, p. 4.
[19] Ibid., p. 11.
[20] VOGEL, F. E.; HAYES, S. L., Islamic law and finance: religion, risk, and return, p. 60.

purposes of business and commerce – such a practice was e.g. *hawala*, a letter of credit, or *sakk,* a modern day checque. While capitalist at heart, the early Arab society had a different position on money than their modern followers. Money is according to sharia scholar a mean to achieve an objective, in itself, it has no intrinsic value and cannot be traded.

The twelfth-century Islamic theologian and jurist Abu Hamid Muhammad ibn Muhammad Ghazali stated that money was created "*so that it may be circulated between hands and act as a fair judge between different commodities and work as a medium to acquire other things*." He added that "*whoever effects the transactions of money is, in fact, discarding the blessings of Allah, and is committing injustice, because money is created for some other things, not for itself. So the one who has started trading in money itself has made it an objective, contrary to the original wisdom behind its creation, because it is an injustice to use money other than what it was created for*."[21] Given this rationale, one cannot create money out of money and, therefore, cannot lend money at interest. This injunction is the most well-known principle of Islamic finance, although in itself it is not sufficient in creating an appropriate picture of the nature of Islamic finance. The following rules of Islamic finance should be viewed as an extension of the general, underlying values of Islamic law briefly outlined in these paragraphs.

4.1. Interest - *Riba*

One of the most common perceptions about Islamic finance is that it bans interest. However, this is a gross simplification. The original term *riba* can be translated both as interest and as usury. The ambiguity concerning translation of *riba* stems from the various interpretations of Qur'an where the word was originally used in the meaning of growth or increase. Here, I will first discuss the relevant sources and interpretation regarding the nature of interest and its understanding in Islamic finances. It is essential in order to understand any further discussions regarding Islamic banking. The term used in Arabic to denote interest is *riba*. It appears in Qur'an in this exact form eight times and the root r-b-w appears twenty times with the meaning of growing, increasing, etc. and the term *riba* is used in the sense of an increase.[22] The first instance where *riba* appears in Qur'an is in verse:

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[21] IRFAN, Harris. The Nature of Money: Islamic Banking and Conscious Capitalism.
[22] SAEED, A., Islamic banking and interest: a study of the prohibition of riba and its contemporary interpretation, p. 20.

"*And whatever you may give out in riba so that it may increase through other people's wealth, it does not increase in the sight of God; but whatever you give by way of charity seeking God's pleasure, will manifold increase*."(Qur'an 30:39)

It is followed and preceded by verses commanding Muslims, especially the wealthy ones, to provide financial support to those in need, orphans, widows, etc. It corresponds with general theme present in Qur'an that one should not hoard his wealth but should share it with the less fortunate ones and encourages Muslims to be socially responsible. Spending which aims to relieve the suffering of the poor and needy is found right and just. In this context, the verse first mentioning *riba* can be understood as an antithesis of charity. Later, *riba* was prohibited even more clearly in the following verse: "*Do not consume riba, doubled or redoubled.*" (Qur'an 3:130)

This verse was uttered in the sense of prohibiting the increase of amount payable by a debtor when the debtor desires to defer the repayment. According to the concurrent sources, *riba* was imposed at maturity as a means of extending the debt's due date.[23] Muhammad commands Muslims to demand only the original amount indebted without the additional *riba* as means to be just and charitable. The exact definition of what is *riba* and which transactions should be regarded as such has been matter of discussion since the Quranic times. The key factor for our understanding is the rationale for its prohibition which is not clear from the Quranic verses.

While the prohibition of *riba* in Qur'an could be easily understood as more lenient interpretation, *riba* was also subject of Sunna literature which deals with its definition in a more specific way. According to one concept, *riba* arises only when dealing in six particular commodities (gold, silver, barley, dates, salt, and wheat).[24] These need to be exchanged only kind for kind and without any increase in value. Other principles talks about the exchange being made on site – hand to hand, or about only exchanging articles of equal measure and of a similar type.[25]

During the 20th century, modern Muslim scholars focused on the definition of *riba* in the context of modern banking system. To some of them, e.g. Muhamad Abduh, Rashid Rida, Abd al-

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[23] SAEED, A., Islamic banking and interest: a study of the prohibition of riba and its contemporary interpretation, pp.22-23.
[24] Ibid, pp. 31-32
[25] NETHERCOTT, Craig R.; EISENBERG, David M. *Islamic finance: law and practice*, p. 43.

Razzak or Maaruf al-Dawalibi, interest, unlike usury, was permissible. In their works, they tried to widen the prohibition of usury also on compound interest based on the original assumption that Qur'an aims at protection of the weak from the exploitation of the strong. However, such interpretation is not universally accepted and The Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI), for example, prohibits the use of credit cards that involve interest. [26]

Some modern scholars of Islamic law, including A. Saeed, suggest that the Qur'anic prohibition of riba was driven by moral and humanitarian considerations. The practice prohibited in the Qur'an was aimed at protecting a person in financial difficulties from exploitation rather than at avoiding any increase in the amount paid back to the creditor as such. Sunna composed during the later years focused on certain contracts for sale, not necessarily on further development of the prohibition on riba. The jurists have later concentrated mainly on provisions of Sunna, paying little attention to the original Qur'anic wording. As a result, the juristic discussions have become more and more legalistic and semantic and left behind the original need to answer the need for borrowing and lending. As a result, people had to resolve to various stratagems in order to lend and borrow. Fazlur Rahman, a prominent modern jurist, emphasized the original Qur'anic rationale behind prohibition or *riba* – injustice. However, such an opinion is not prevalent among current conservative scholars that are saying the main word in influential Gulf States as well as other countries with Muslim majority. A rethinking of the current concept of *riba* is to be expected in the following years in order to resolve some of the problems facing Islamic finance.[27]

Modern interpretations already suggested a different approach to issue of *riba* and interest/usury. Syrian scholar Marouf al-Daoualibi in the 1930s suggested that the Qur'an bans *riba* on consumption loans, not on investment loans and ten years later Egyptian scholar al-Sanhuri wrote that the goal of Qur'anic prohibition was to ban interest on interest. Another Egyptian scholar, Shaikh Muhammad Sayyid Tantawi declared in 1989 that interest on some of interest-based government investments was not forbidden.[28] And yet another prominent Egyptian figure, Mahmud Shaltut, who became the Grand Imam of Al-Azhar University in the

[26] Ibid, p. 45.
[27] SAEED, A., Islamic banking and interest: a study of the prohibition of riba and its contemporary interpretation, p. 143.
[28] VOGEL, F. E.; HAYES, S. L., Islamic law and finance: religion, risk, and return, p. 46.

1950s and 1960s, a leading school of Islamic law by some Muslims considered to be the highest authority in Sunni Islamic thought and Islamic jurisprudence, issued a fatwa permitting to accept one's share of the profits from a savings fund. [29] He based his justification on the fact that the client has deposited his funds voluntarily and with the goal of retaining the value of his property and allowing the financial institution to invest it and therefore increasing its profits which it can use to hire more people, stimulate the economy and bring prosperity. The Qur'an says: "*And Allah knows him who means mischief from him who means good*".[30] The investor in a saving fund should be viewed as that who means good.[31] Needless to say, the views of Mahmud Shaltut were not widely accepted in Egypt and later scholars defaulted again to the blank prohibition of interest on all banking products.

4.2. Speculation - *Gharar*

Gharar can be understood as "*a notion encompassing excessive or avoidable risk, deceptive ambiguity, and risk shifting*"[32] which gained the overall meaning of speculation. While the AAOIFI deems *gharar* relevant only in bilateral contracts, for the majority of Muslim legal schools *gharar* can impair all types of contract. The definition of *gharar* is not based primarily on Qur'an, but on Sunna where it is specifically said that "*Allah's Messenger forbade transaction determined by throwing stones, and the type that involves some uncertainty*." [33] In other parts of Sunna, it is also forbidden to sell "*the bird in the air, a fish in the water, an escaped animal or slave, or anything else that the vendor might be unable to deliver owing to lack of possession*."[34] Essentially, *gharar* involves a contractual risk that can result in the loss of property.

The exact scope of gharar has been a subject of discussion among Islamic scholars. The State Bank of Pakistan defines gharar as "*excessive level of uncertainty or ambiguity created due to the lack of information or control in a contract*".[35] AAOIFI classifies *gharar* into categories

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[29] SKOVGAARD-PETERSEN, Jakob. Defining Islam for the Egyptian state: muftis and fatwas of the Dār al-Iftā, p. 299.
[30] Qur'an 2:220
[31] KROPÁČEK, Luboš. *Duchovní cesty islámu*, p. 137.
[32] NETHERCOTT, Craig R.; EISENBERG, David M. *Islamic finance: law and practice*, p. 4.
[33] Ibid, p. 46.
[34] Ibid.
[35] AHMAD, Imran a Ghulam SHABBIR. STATE BANK OF PAKISTAN. *Frequently Asked Questions On Islamic Banking*.

based on its extent, whether it is excessive, medium or, minor.[36] Only excessive *gharar* renders the contract null and void.

4.3. Gambling – *Maysir* and Legal stratagems – *Hiyal*

Gambling is an exception to the general approval of trade by mutual consent. It is called a "*game of chance*" [37] and is put on a same level as intoxicants and worship of idols. Gambling and intoxicants are according to Qur'an Satan's acts through which he want to sow enmity and hatred among people.[38]

Legal stratagems or artifices serve as a way to use law in a formalistic way to achieve one's goal. The concern for an external form of transactions wins over parties' substantive intentions and is used to cover the real aim of concluded agreement. Scholars have found only those *hiyal* unacceptable that clearly go beyond the scope of legitimate goals and break the law's basic rules and principles. Hiyal are used by modern banks to overcome some prohibitions inflicted on them by Islamic law. As an example can serve Pakistan, where banks commonly use a transaction used for inventory financing when a firm sells its inventory to the bank for cash and simultaneously repurchases it for credit. Such inventory is usually never properly identified. [39]

4.4. Forbidden - *Haram*

All modes of human behaviour can be subsumed under five categories ranging from forbidden (*haram*) to mandatory. Only matters forbidden would be punished by a religious court, other modes are generally falling under the divine jurisdiction. While above mentioned principles determine how, or rather how not, can a capital be used, haram concerns the goods that are subject of a commercial or financial activity. Certain set of activities and articles are considered forbidden based on primary sources of Islamic law and their interpretation. Probably the best known part of human life where haram comes into mind is food. Muslims are forbidden from drinking intoxicating drinks and eating particular food. Consequently, it is not allowed to trade

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[36] NETHERCOTT, Craig R.; EISENBERG, David M. *Islamic finance: law and practice*, p. 47.

[37] AHMAD, Imran a Ghulam SHABBIR. STATE BANK OF PAKISTAN. *Frequently Asked Questions On Islamic Banking*.

[38] Qur'an 5:90-91, "*O you who believe! Intoxicants (all kinds of alcoholic drinks), gambling, Al-Ansab, and Al-Azlam (arrows for seeking luck or decision) are an abomination of Satan's handiwork. So avoid (strictly all) that (abomination) in order that you may be successful. Satan wants only to excite enmity and hatred between you with intoxicants (alcoholic drinks) and gambling, and hinder you from the remembrance of Allah and from As-Salat (the prayer). So, will you not then abstain?*"

[39] VOGEL, F. E.; HAYES, S. L., Islamic law and finance: religion, risk, and return, p. 39.

in these goods or otherwise engage in their distribution. Moreover, Muslims cannot trade in pornography, drugs, armaments or gambling. However, haram in fact includes all activities described in the previous paragraphs – such as *riba* or *gharar*, which are also forbidden.

The above mentioned principles serve well to illustrate the model theory or the ideal form of Islamic finance. The reality, however, needs to be understood in the context of the evolving industry and the interactions and connections between Islamic and conventional finance.

5. Islamic banking products

Islamic banking products offer clients the possibility of using financial services compliant with Islamic law as illustrated in the above mentioned principles. If we summarize them in a very superficial way, we can simplify their main goal to prevent exploitation of the weak, prohibiting interest, avoiding excessive risk and speculation and not dealing in forbidden goods. Overall, this system is often characterized as profit sharing or risk participation. Money is in Islamic finance simply a medium of exchange and should not be used to increase one's wealth. Increasing wealth and achieving prosperity is highly desirable but should be done through work and trade only. Reward is intended for those that are willing to take risk and understand that their project can result in both profit and loss. Sharing of profit and loss is the key principle underlining all of the products described in the following paragraphs. While not directly related to financial regulation, understanding their difference from conventional banking products is key for discussing challenges of banking regulation in countries with Islamic banking.

Two basic principles serving as a base for Islamic financing are that return on capital must be a proportion of profits, not a pre-set fixed amount. Second, capital is liable to the financial risks of a venture, labour can only yield loss in itself and in time. Another view is that Islamic finance is due to its transaction risk sharing equity based rather than debt based. This concept features prominently especially in two of the oldest forms of Islamic financing – joint venture contracts of *musharaka* and *mudaraba*.

5.1. Musharaka

The term *musharaka* comes from Arabic word for partnership or involvement in someone else's affairs. While none of the Qur'anic verses uses this exact term in the meaning of business partnership, jurists were able to justify its validity based on verses 4:12 or 30:28. Verse 4:12 deals with inheritance and states that in certain circumstances "*if [the deceased had] more than*

two [brothers and sisters], they share in a third"[40] of the inheritance. Verse 30:28 goes as follows: "*He sets forth for you a parable from your ownselves, - Do you have partners among those whom your right hands possess (i.e your slaves) to share as equals in the wealth We have bestowed on you?"*[41] In these and other verses, Qur'an established a lawfulness of partnership of the property. The notion of business partnership was further elaborated in Sunna, although it did not set any specific conditions. The terms and details of valid musharaka were product of legal reasoning of Islamic jurists during the following centuries.[42]

It is an act of "*joining together in an affair of common interest to two or more parties*".[43] Partnership, or *musharaka*, can be categorized by its subject matter into (1) contractual partnership and (2) property partnership; by its origin into (1) involuntary partnership arising by operation of law (such can be the case when two or more persons inherit share in a property) and (2) voluntary partnership where two or more persons voluntary agree on a common interest in a particular asset.

Classical Islam recognizes a number of contractual partnerships of which mutual partnership (*sharikat inan*) is the simplest and most widespread.[44] In this partnership, "*each partner contributes a specific amount of property on the basis that each partner may deal in the property of the partnership*"[45]. Each partner acts as a principal and as an agent at the same time – as a principal to his own contribution to the partnership and as an agent to his partner's share provided that actions undertaken as an agent are approved by the other partner. In accordance with the profit and loss sharing principle, the contract must involve a just distribution of both profits and losses according to each partner's contribution to the common capital. Consequently, a partner cannot be required to guarantee the obligations of other partners or to be liable to them, unless acting outside stipulated and approved agency capacity. This construct allows for considerable flexibility. All partners can decide to participate in the management of their joint venture or they can appoint a person, either one of the partners or a third party agent, to manage the venture. The manager can be reimbursed for his role.

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[40] Qur'an, verse 4:12.
[41] Qur'an, verse 30:28.
[42] SAEED, A., Islamic banking and interest: a study of the prohibition of riba and its contemporary interpretation, p. 59.
[43] NETHERCOTT, Craig R.; EISENBERG, David M. *Islamic finance: law and practice*, p. 176.
[44] Ibid.
[45] Ibid.

Musharaka is such a universal cooperative principle that it can take on number of different shapes. Two persons can decide to cooperate and own together number of shares in a company with each person investing particular equity and receiving a corresponding number of shares. Or it can be used to form a company with the articles of association constituting the *musharaka* agreement between the parties and similarly it can be used to create a partnership. Each partner is required to bring into the partnership assets of identifiable value invested in return for an ideal and undifferentiated share of the venture's profit. It is possible to agree in the contract on specific division of profit, although generally it is divided equally. And the same holds true for losses – for example, in case of dissolution of a company after paying its creditors, each partner would receive an equal part of his investment (if the company lost half of its equity, each partner would receive only half of his investment).

In Saudi Arabia, the concept of *musharaka* is used for creation of limited liability companies that provide limited liability protection to their shareholders where shareholders are considered as partners, whereas shareholder in a joint stock company is referred to as an equity participant.[46] Classical Islam does not require *musharaka* to be registered in order to be enforceable among the parties. Whether to incorporate or not incorporate a newly founded partnership depends on the parties but also on the statutory requirements of their jurisdictions. Naturally, not having an incorporated joint venture can lead to certain disadvantages and limitations.

Musharaka can be used not only for a simple equity relationship, a profitable joint venture as described above but it can also serve as a financing tool. The so-called diminishing *musharaka* involves participation of a financing party and a project sponsor on an identified project.[47] The scheme is similar to that of a simple *musharaka* with the difference that at the beginning, the financing party provides for up to 99% of the contributions and correspondingly receives the appropriate share of voting rights. Over time, the project sponsor purchases from the financing party its shares in the joint venture for a fair market price according to an initial agreement setting up the *musharaka*. The financing party therefore gradually withdraws from the partnership with each purchase of its contributions. These purchases can be linked in the agreement to distribution of any profits gained during the existence of the partnership.

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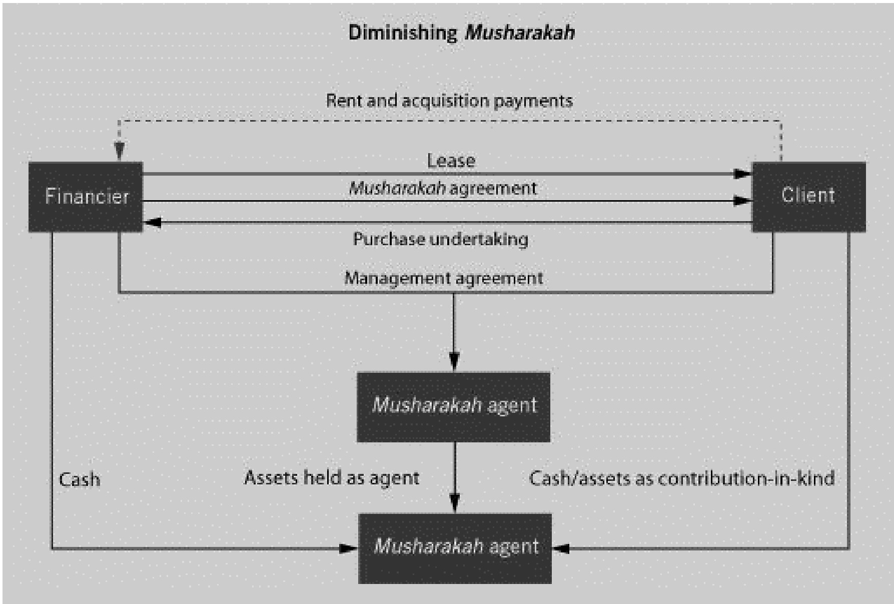
[46] NETHERCOTT, Craig R.; EISENBERG, David M. *Islamic finance: law and practice*, p. 178.
[47] Ibid, p. 179.

Eventually, the financing party's interest in the joint venture diminishes at the same time as its share to profits reduces whereas the project sponsor's interest and share of the profit increases.

Even if this scheme is based on a profit and loss sharing principle which aims at limiting the risk with which parties are entering into contracts, the financing party brings to diminishing *musharaka* financial resources whereas the other party invests at the beginning "only" his entrepreneurship. Consequently, the parties may wish to reduce the profit risk by entering into agreement which create two possible instruments, both compatible with Islamic law. First, the financing party may lease part or all of his share to the other party in return for specific amount and term. Second, a reserve account may be created where a percentage of profit from successful years is reserved to cover years during which there is no profit made.

However, these instruments do not provide any insurance to the financing party that the project sponsor will in fact conclude all purchases as was agreed. As a result, the financier might require the project sponsor to purchase all of the share left in the event of default on payment. Neither do they prevent the project sponsor, who is usually responsible for management of the project, from particularly bad management that can lead to reduction in market value of each share which usually determines the price of the share at the time of its purchase by the project sponsor. If this is the case, the financier might be able to recover his loss suffered by a lower purchase price than what was expected through a broadly drafted indemnity. While this is an understandable step by any financial institution, it can easily be interpreted as avoidance of risk sharing and thus not compliant with Islamic law.



Source: Islamic finance: key principles and recent developments.

5.2. Mudaraba

The meaning of the root *d-r-b* is to strike or to travel in the sense of travelling or striking to reach one's fortune. Mudaraba can be than translated as "striking out together on a financial venture".[48] The concept goes back into times of Prophet Mohammed whose wife reportedly used to entrust him with her money to be used on trading during his travels.[49] However, there is no mention of mudaraba in the sense outlined above either in Qur'an or in Sunna. Its lawfulness was argued by Islamic scholars in 11th century based on the need of people for such a contract (e.g. jurist Sarkhasi) as well as on the prolonged use by the Muslim community.

Whereas in mushraka both parties' contribution to their joint venture is equity based, mudaraba brings together a partner with sufficient funding and a partner with necessary know-how, skills and time. Essentially, where one side is investing capital, the other is investing labour and time – he manages the joint venture. This is also the official definition used by AAOIFI in its Sharia Standards. Capital in this case must be in the form of cash or other tangible asset. It is not possible for the investor to set up the capital as a debt owed to the manager. This concept was considered unlawful because it could easily allow the debtor/investor to use the common project as a way to recover from a debt and even possibly benefit from it which is seen as *riba*.[50]

The manager provides his time and labour to the venture and is provided with necessary freedom to in the management and decision making related to the project within the limits set by the agreement. The exact scope of this freedom differs according the overall liberality of a legal school ranging from almost absolute freedom to purchase goods, hire people and generally act as any merchant would to possibility of buying or hiring only when stipulated in the agreement.[51]

Profit distribution depends on an agreement between the parties and can be amended according to circumstances. The distribution should be set as a ratio, not as a fixed amount. The investor is liable only for the capital that he invested in the venture and the manager should not, therefore, enter into any arrangements that would require higher capital than that, otherwise he

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[48] NETHERCOTT, Craig R.; EISENBERG, David M. *Islamic finance: law and practice*, p. 184.
[49] Ibid, p. 184; SAEED, A., Islamic banking and interest: a study of the prohibition of riba and its contemporary interpretation, p. 51.
[50] SAEED, A., Islamic banking and interest: a study of the prohibition of riba and its contemporary interpretation, p. 53.
[51] Ibid, p. 54.

himself is liable. Losses are born by the financing party only, the second party, entrepreneur who actively manages the project, suffers loss in terms of losing his time and efforts. However, if the agent engages in any undertaking that breaches the limitations set in the agreement, he will be held liable for any loss or expense resulting from his actions. The element of financier placing his property in the hands of the entrepreneur can be referred to as a trust arrangement where the entrepreneur acts as a trustee and is treated as such in some jurisdictions, others consider the asset to be held in beneficial ownership (Saudi Arabia, United Arab Emirates).[52]

Mudaraba is in principle agreed for an open-time term although the parties can agree on a fixed term. This stipulation would be considered rather unusual as the contract can be easily terminated by the financier through withdrawing of the funds or by dismissing the agent. However, current banks often include a clause on duration in mudaraba agreements as the banks are interested in liquidating mudaraba and returning of the capital. The financing party may also choose to place restriction on the use of the capital and the agent is generally liable for breach of such restrictions. However, the financier cannot require the manager to provide a guarantee for return of the capital or for profit. That would infringe the nature of the relationship between the investor and the agent which is strictly fiduciary and based on trust. The flexible structure of mudaraba as described above provides for a wide range of applications including investment accounts, bilateral finance facility or investment agency agreement.

In the Middle East, *mudaraba* is often used for a short-term commercial purpose in the following scheme. A client enters into an agreement with an Islamic bank. The client receives financial support from the bank (these would be usually funds from investors, not bank's own funds), purchases goods from a seller and sells them at higher price with a profit. The bank will ask its client to provide information on the nature of goods in question, possible sources from which they can be purchased, and on all costs associated with the purchase and re-sell. The client will also provide details on the expected sale price, cash flow, and profit margin to let the bank make an informed decision. If the bank is satisfied with the information provided by the client and with the profit margin presented, it will grant the financial support. The bank opens a special account for the management of *mudaraba* from which it pays directly the original

[52] NETHERCOTT, Craig R.; EISENBERG, David M. *Islamic finance: law and practice*, p. 185.

seller after being identified by the client. The agent (client) manages the purchase, storage and re-selling of the goods, is responsible for any mistake and is required to insure the goods.

Mudaraba does not require that a company, incorporated or not, is formally created. Bank can make an investment in an already existing enterprise on the condition that all profits arising from bank's investment can be determined separately from the general profits. Even if the original nature of *mudaraba* put all risk of loss of capital on the investor, Islamic banks, in reality, try to avoid such risk. As illustrated above, the outcome of the transaction is almost certain and the bank insures itself against any risk by limiting the conduct of the agent to maximum. As a result, a loss of the bank's capital is unlikely to occur very frequently which makes *mudaraba* similar to any other low risk investment operation.

5.3. Murabaha

Given its simplicity and flexibility, *murabaha* is one of the most common Islamic products of modern Islamic banking. It can be defined as "a fiduciary credit sale with a fixed and disclosed profit margin over the cost of the subject matter of the sale"[53] or more simply a sale with markup.[54] It is used not only for acquisition of assets, commodities and goods, but also as a corporate finance tool for working capital and liquidity management. *Murabaha* is based on a sale whose requirements must be satisfied. In its simplest form, the seller buys goods at the request of a customer – purchaser. During the process, the seller takes title to such goods, although physical possession is not necessary, and only after that enters into contract to sell these goods to the purchaser at an agreed profit in addition to the purchase price. In exchange, the title to the goods is transferred to the purchaser. The second transaction between a bank and its client is usually arranged on credit although both sales can be on credit in theory. Islamic banks make profit from *murabaha* both through the markup based on the services provided during the sale and especially through extension of credit in the second sale.

It is necessary for *murabaha* to be valid that the purchase price and the profit over the purchase is agreed on and disclosed before parties enter into the agreement. Such an agreed price cannot be changed later unless the original seller gives the intermediary seller a better price than was agreed on, then the purchaser is entitled to appropriate reduction in the purchase price as well.

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[53] NETHERCOTT, Craig R.; EISENBERG, David M. *Islamic finance: law and practice*, p. 193.
[54] VOGEL, Frank E.; HAYES, Samuel L. Islamic law and finance: religion, risk, and return, p. 140.

Most legal schools agree that the seller can also add to the purchase price expenses spent over the transportation, insurance or packaging. AAOIFI is of a same opinion on the condition that the institution (the seller) must disclose such expenses before concluding the contract of sale. The agreed price can be paid at any time either in instalments or in lump sum. The payment can also happen at any time but must be agreed, similarly to price, before the sale transaction is commenced. Any goods can be the subject matter of *murabaha*, unless they are haram, cash or commodities considered to be cash equivalent, such as silver or gold.

The following are the uses of *murabaha* (1) purchase of raw material, goods and merchandise of all kinds and description, (2) purchase of equipment, (3) import of goods and merchandise, (4) export financing (pre-shipment), (5) other financing of working capital nature. Islamic banks are trying to narrow down any risks by employing various legal stratagems that are bordering on lawfulness. In practice, it is not unusual to see deals where the second transaction, between the bank and its client, takes place immediately after the first one, or even at the same moment as the bank takes title to the goods. Thereby the bank virtually eliminates all risks associated with storage of the goods. Financial institutions also usually allocate the risk of defects in the goods or breach of warranty to the purchaser. Banks can, and often do, appoint the client as an agent for the purpose of purchasing of the goods from the original seller, therefore reducing any risks associated with any possibility of error and eliminating the burden and costs with buying and delivering the goods.

Presently, the majority, 80% according to Vogel and Hayes[55], of financing extended by Islamic banks is based upon murabaha which is causing concern to Islamic banks that are reducing this dependency on one particular product that is economically very close to standard interest-lending.[56] The Islamic Fiqh Academy, which was created at the decision of the second summit of the Organisation of the Islamic Conference (OIC) 1974 and inaugurated in February 1981, even warned about the overuse of *murahaba* and urged Islamic banks to minimize number of *murabahas* and to replace them by profit and loss sharing investments.[57]

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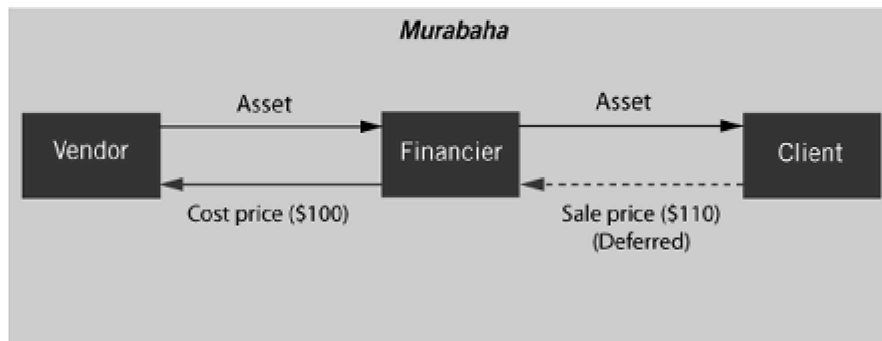
[55] Ibid, p. 136.
[56] AHMAD, Imran a Ghulam SHABBIR. STATE BANK OF PAKISTAN. *Frequently asked questions on islamic banking*.
[57] Decision 3,2, fifth session (1988), Fiqh Academy Journal 2:1599.



Source: Islamic finance: key principles and recent developments.

5.4.Lease - *Ijara*

Lease can be understood as transferring the use of an asset, or the sale of usufruct. Therefore, its rules follow the rules for an ordinary sale.[58] Islamic banks offer leasing, or *ijara*, is used mainly as an alternative to instalment sale for financing purchases of equipment. However, in the case of *ijara*, the lessor, in this case a bank, retains legal title to the property. Among the main advantages of *ijara*, we can name its flexibility in payment terms, negotiability, transferability and, in some jurisdictions, tax savings when compared with sale. Lease has an advantage, comparing to other modes of finance, of not requiring the same intensity of investigation and audit of the lessee's affairs that would be the case if a bank would be to make an outright investment in the lessee's enterprise.[59]

To conclude an *ijara*, the customer approaches a bank and expresses his desire for a particular asset/property. The bank acquires that asset as per undertaking of the customer and leases (transfers the use of the asset) it to the customer for an agreed period of time and against an agreed amount of rentals. An *ijara* agreement, signed between the bank and the customer, stipulates all the relevant conditions with regard to the transaction. During the *ijara* period, the corpus of the leased property remains in the ownership of the bank and only its usufruct is transferred to the lessee.[60]

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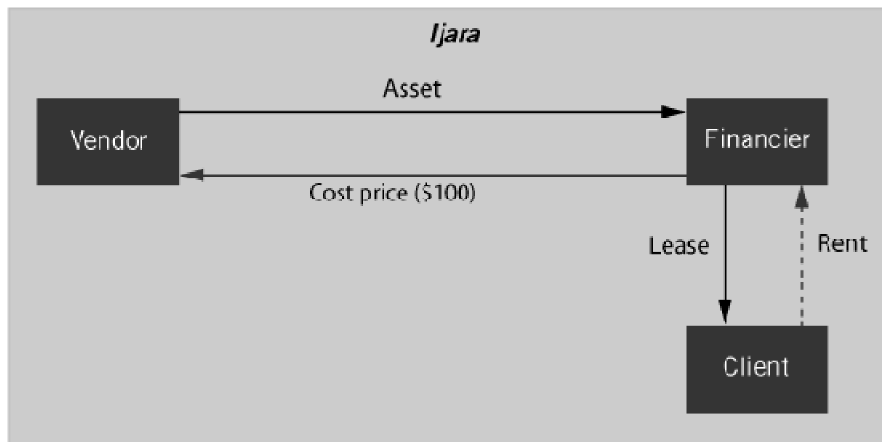
[58] VOGEL, Frank E.; HAYES, Samuel L. Islamic law and finance: religion, risk, and return, p. 144.
[59] VOGEL, Frank E.; HAYES, Samuel L. Islamic law and finance: religion, risk, and return, p. 190.
[60] AHMAD, Imran a Ghulam SHABBIR. STATE BANK OF PAKISTAN. *Frequently asked questions on islamic banking.*



Source: Islamic finance: key principles and recent developments.

6. Islamic financial institutions and their regulation

Islamic financial institutions are established under Islamic law which is based on the notion that money does not have a time-value separate from the value of goods exchanged through the use of money. They follow the principle of sharing profit and loss and reject interest. Within these limits, they offer wide range of services including Islamic commercial banking using products mentioned in the previous chapter. Islamic financial institutions arrange clients' money, provides loans, manages corporate and project finance structures and offers other banking services such as money transfer services.[61] Naturally, Islamic financial institutions (IFI) offer wealth and asset management, insurance and social services similarly to conventional financial institutions. However, this thesis focuses specifically on the banking aspect of IFI.

Islamic financial institutions can exist in two basic modes. Either (1) the whole institution is set up under Islamic law and as a whole provides complex set of services compliant with Islamic law. Other option (2) is a branch or subdivision of a conventional financial institution that is dedicated to catering to clients interested in products and services compliant with Islamic law. In both cases, it is necessary for the institution to appoint a Sharia Supervisory Board that is required in order to ensure the institution's compliance with Islamic law. In Europe, Islamic financial institutions exist mainly in the United Kingdom, Switzerland, or Germany.

National regulation models of Islamic finance are closely tied with governments' approaches to its existence and development. Bellow, I will briefly illustrated that given London's desire

[61] NETHERCOTT, Craig R.; EISENBERG, David M. *Islamic finance: law and practice*, p. 55.

to become a Western hub for Islamic finance, it is paying much closer attention to its regulation as well. The same can be said about countries with majority of Muslim population. Vogel and Hayes divided some of the Muslim countries into the following categories[62]:

(1) Countries that have transformed their internal financial systems to an Islamic form – Iran, Pakistan (which is in the process of transformation and could be placed under number (2) for more accurate description of the current situation) and Sudan;
(2) Countries that embrace Islamic banking as a national policy while supporting dual banking tracks – Bahrain, Brunei, Kuwait, Malaysia, Turkey, United Arab Emirates;
(3) Countries that neither support no oppose Islamic banking within their jurisdiction – Egypt, Yemen, Singapore, and possibly Indonesia; and
(4) Countries that actively discourage a separate Islamic banking presence – Saudi Arabia, Oman.

European countries could be included in number (3) since they generally allow for various degrees of Islamic banking within their jurisdictions. Just over a fifth of Malaysia's banking system, by assets, is *sharia*-compliant. The average for Muslim countries is usually around 12%, and often a lot less.[63] In 2012, Iran accounted for 43% of the world's Islamic banking assets, with Saudi Arabia (12%) and Malaysia (10%) ranking second and third.[64] While the reasons for various approaches to Islamic banking outlined above are largely political (especially in the case of Saudi Arabia which is trying to avoid a creation of separate Islamic banking system as a political weapon of Islamic extremists), the consequences are present also in the field of financial regulation.

There are two dimensions to regulation of Islamic financial institutions. First, we can talk about the internal versus external aspect. Islamic financial institutions, contrary to conventional financial institutions, have a very strong focus on internal self-regulation. That is based on the need to assess whether certain product or activity complies with Islamic law. This assessment is carried out by the Sharia Supervisory Board appointed by each Islamic financial institution. I will address the issue of Sharia Supervisory Boards in the following chapters. External regulation comes both in a sense of secular regulation and in some cases Sharia Boards

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[62] VOGEL, Frank E.; HAYES, Samuel L. Islamic law and finance: religion, risk, and return, p. 11.
[63] Banking on the ummah.
[64] Big interest, no interest: The market for Islamic financial products is growing fast.

appointed by state regulatory authorities. Secondly, we can distinguish between regulation executed by national authorities and by multilateral organisations. While national regulation is dependent on every country, international standards and frameworks are necessary in order to overcome national differences and allow Islamic finances to become a global system.[65] International institutions that would ensure religious standards for all groups of Muslim investors regardless of their nationality and religious affiliation would also allow for a creation of a much needed secondary market for Islamic securities.

Especially in the United Kingdom, Islamic financial institutions were giver particular attention and London is striving to be the capital of Islamic finance in West. In 2007, the UK Financial Services Authority, then a general regulator which was transformed to current Financial Conduct Authority following the financial crisis[66], published a discussion paper *Islamic Finance in the UK: Regulation and Challenges* which highlighted main aspects of regulation of IFI in the UK.[67] Western regulators are facing a challenge posed by the combination of religious and temporal matters. In Malaysia, the relevant regulatory authority appoints its own Sharia scholars which allows it to oversee the Islamic nature of products and services offered by Malaysian IFI in a substantive matter, whereas the British regulator considers himself a secular, not a religious regulator and follows a formal model of regulation.[68]

An important regulatory issue that governments are facing related to Islamic banking is the relationship between "bank liquidity needs, profitability, and the appropriate composition of the capital structure".[69] Concerns about the liquidity have caused Islamic banks to be cautious about in their investment policies harming their profitability in return. In Turkey, reserve requirements for Islamic investment deposits are set at 1%, in contrast to 10% reserve required for conventional bank deposits. In some countries with Islamic banking, governments have established informal means in order to assist Islamic institutions in case of a liquidity crisis.[70]

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[65] Claire Jones, Regulating Islamic finance: a primer.
[66] History of the FCA.
[67] NETHERCOTT, Craig R.; EISENBERG, David M. *Islamic finance: law and practice*, p. 56
[68] Ibid.
[69] VOGEL, Frank E.; HAYES, Samuel L. Islamic law and finance: religion, risk, and return, p. 12.
[70] Ibid.

6.1. International regulatory bodies

Islamic financial institutions fall primarily under the regulations and standards of national regulatory authority. However, in addition to national bodies, number of international regulatory bodies have been established in order to develop and set regulatory and *Sharia* standards for Islamic financial institutions. At the moment, the two most important international bodies are the Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI) and the Islamic Financial Serviced Board (IFSB). Their significance can be attested by several national regulators relying on standards issued by these two bodies.

AAOIFI, based in Bahrain and operating since 1991, is "*an Islamic international autonomous non-for-profit corporate body that prepares accounting, auditing, governance, ethics and Shari'a standards for Islamic financial institutions and the industry*".[71] AAOIFI is supported by 200 institutional members from 40 countries including central banks, Islamic financial institutions, and other participants from the international Islamic banking and finance industry. AAOIFI standards were adopted in number of countries including Bahrain, Jordan, Lebanon, Qatar, Sudan and Syria. National authorities in other countries issued guidelines that are based on AAOIFI's standards. These countries include Indonesia, Malaysia, Pakistan, Saudi Arabia but also Australia. At the moment AAOIFI issued 88 standards, more than half of them being on Sharia, about quarter on accounting and the rest on auditing, governance and code of ethics.

IFSB, established in Kuala Lumpur in 2002, is "*an international standard-setting organisation that promotes and enhances the soundness and stability of the Islamic financial services industry by issuing global prudential standards and guiding principles for the industry, broadly defined to include banking, capital markets and insurance sectors*".[72] The IFSB's work complements that of the Basel Committee on Banking Supervision, International Organisation of Securities Commissions and the International Association of Insurance Supervisors and up to date issued 22 standards, guiding principles and technical notes.

While other international institutions have been established, these two remain the most significant with the highest impact. Standards set down by AAOIFI and IFSB do not have a direct effect on any particular Islamic financial institution similarly to Basel Committee's

[71] About AAOIFI.
[72] About IFSB.

recommendation. Their standards however can be adopted, and in fact are being adopted, by a national regulatory authorities or serve as an inspiration for its work. And even in absence of binding rules, the standards are used as a guidance pointing to best practises and example of regulatory rules.

6.2. Compliance with Basel III

An appropriate regulatory framework is just as necessary in an Islamic banking framework as it is in a conventional banking system. In response to the deficiencies in banking regulation worldwide which were revealed in the context of the global financial crisis, third installment of international regulatory framework for banks – the Basel Accords (Basel III)[73], was adopted in 2011. It focuses, among other issues, on the question of liquidity and capital requirements. Basel III is the latest configuration of an evolving set of internationally agreed standards developed by supervisors and central banks. While not all Islamic banks were established in the member countries of the Basel Committee, there is number of countries adhering to its regulatory frameworks with more or less developed Islamic banking sector. In the European Union, the Basel III Accords were largely adopted through the Capital requirements regulation and directive (CRR/CRD IV)[74] and are therefore affecting all European banks, including e.g. the newly established fully *sharia*-compliant KT Bank AG (see Chapter 6.2) We can therefore raise a question of the compatibility of Basel Accords with Islamic banking system given the fact that this framework was primarily designed for the conventional banking system.

In the future, we can expect greater collaboration between the Basel Committee and Islamic regulatory bodies that could lead to possible consideration of Islamic banking processes and standards. Even today, the central banks of several countries with prominent Islamic banking are members of the Basel Committee itself or the Basel Consultative Group, including the Islamic Financial Services Board, Central Bank of Malaysia or Qatar Financial Centre Regulatory Authority. More emphasis on the challenges faced by Islamic banks might be in the future brought forward also by European countries where Islamic banking is gaining more exposure and attracting first clients.

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[73] International regulatory framework for banks (Basel III).
[74] Capital requirements regulation and directive – CRR/CRD IV.

In fact, IFSB reacted to the newly adopted Basel III with its own guidelines that adapted principles of Basel III to the uniqueness of Islamic banks' products and operations. In December 2013, IFSB released IFSB-15 standards on capital adequacy with the purpose of introducing a framework for capital adequacy and liquidity requirements to suit the uniqueness of Islamic financial institutions.[75] The IFSB-15 calls back to Basel III repeatedly and the relationship between these two standards can be described as follows: "*the Standard [IFSB-15] also provides guidance on the application of new features introduced by the BCBS in its Basel III documents, with necessary adaptations for IIFS [Institutions Offering Islamic Financial Services] – namely, the capital conservation buffer, the countercyclical buffer and the leverage (or common equity to total exposures) ratio*."[76]

To illustrate the complementing nature of Basel III and IFSB, we can take a look at Middle Eastern countries. For example, Qatar Central Bank has decided to apply Basel III standards to both conventional and Islamic banks in addition to implementing IFSB-15 standards by their Islamic banks. Other Gulf countries – the United Arab Emirates and Saudi Arabia are implementing both standards separately, giving their banks more time to deal with each of the documents.

If the Islamic finance industry is ever to become truly global, it will also need to be regulated in line with international standards such as Basel III, though there are many that warn against too much reliance on such standards given the uniqueness of Islamic finance. This obstacle can be easily overcome by including central banks and Islamic regulatory institutions in the Basel Committee, as is already happening, and seeking further collaboration between BIS and IFSB.

Number of studies and articles[77] have been published dealing with the impact of Basel III on Islamic finance. Most of the authors pointed out that Basel III, given its focus on conventional banks, can be viewed as a double-edged sword when applied to Islamic banks since it points out both advantages and disadvantages of Islamic banks over their conventional counterparts.

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[75] HIDAYAT, Sutan Emir. The important role of sukuk in the Basel III era.

[76] IFSB-15. Revised capital adequacy standard for institutions offering Islamic financial services [excluding Islamic insurance (takāful) institutions and Islamic collective investment schemes].

[77] See for example KARA, Hafsa. MOHIELDIN, Mahmoud. Realizing the Potential of Islamic Finance; HERSH, Emily Sarah. Islamic Finance and International Financial Regulation; or HARZI, Adel. The Impact of Basel III on Islamic Banks: A Theoretical Study and Comparison with Conventional Banks.

Basel III has decided to increase the ratio, and the importance, of the Tier 1 Capital, which is mainly composed of equity capital. Given the structure of Islamic banking, most of the Islamic banks' capital is is essentially compounded of Tier 1 Capital (bank's own capital) – with some stating that as much as average 80% of Islamic banks' capital is Tier 1.[78] Required changes in the composition of banks' capital did not, therefore, impact Islamic banks. Islamic banks, due to the nature of their products, already maintain capital levels well above the regulatory minimum. According to Adel Harzi this fact can even lead to "*a positive impact in terms of competitiveness for the Islamic banks, as the conventional banks will see their capital decreased by a larger share than the Islamic banks, hence the former will then experience higher costs of compliance than the latter.*"[79]

On the other hand, Basel III's focus on liquidity will pose special difficulties for Islamic banks that have been dealing with the lack of cross-border liquidity since it started developing. Claire Jones wrote about the compliance of Islamic financial system with Basel III the following: "Owing to the internal nature of approval of Islamic finance products, there is a natural barrier against producing standardised products for which a deep and liquid global market can be created. This, along with the fact that there are few highly-rated sukuk (bonds), means there is also a lack of an Islamic interbank market."[80]

Overall, comparatively with conventional banks, Islamic banking industry seems to be less impacted by Basel III as their business model is generally more conservative and derivatives and short selling is forbidden. In many aspects, Islamic financial institutions have already exceeded requirements set by Basel III.[81] Islamic banks' limited use of derivatives and securitised structures will benefit the levels of capital adequacy. In addition, they will remain immune from the costs needed to address the inherent risks in such products. Finally, the lack of leverage in most Islamic banks means they will not be impacted by the leverage ratio of Basel III.

The fact that Islamic banks worldwide are following the Basel Accords, either implemented through the standards of IFSB or directly, shows the much needed demand for their

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[78] KARA, Hafsa. Islamic banks hold Basel III advantage.
[79] HARZI, Adel. The impact of Basel III on Islamic banks: A theoretical study and comparison with conventional banks
[80] CLAIRE Jones. Regulating Islamic finance: a primer, p.3.
[81] KARA, Hafsa. Islamic banks hold Basel III advantage.

transparency and accountability. The raising importance of Islamic banking industry both in Europe and globally can lead to inclusion of specific Islamic banking-oriented provisions and criteria in the future work of the Basel Committee. Basel III is unlikely to fundamentally change the way Islamic banks operate. But for some Islamic banks, the regulatory framework will offer an opportunity to prosper and strengthen their positions.[82]

6.3. The Sharia Supervisory Boards

The key role of the Sharia Supervisory Board is to ensure that all Islamic financial institution's products and services are compliant with Islamic law, examining every new product or transaction and issuing an approval prior to its launch. However, the Sharia Supervisory Boards can play not only an advisory role but also an executive one. In their advisory capacity, they provide their religious legal opinions through the institute of *fatwas*. In order to understand the position of Islamic legal scholars, I will briefly explain the concept of fatwa before moving forward.

Fatwa is essentially a legal opinion issued by a scholar of Islamic law. It is based on a personal religious affiliation, personal understanding of law, but also on utilitarian choice and temporary and changeable necessity. It is no surprise that can exist tens and possibly even hundreds different fatwas on a single legal question. Fatwas do not have built-in any kind of enforceability mechanism and it is entirely up to the addressee of the legal opinion whether or not he will comply with its content.

Originally, scholars appointed to Sharia Supervisory Boards did not have much experience with financial concepts. Their main expertize was classical Islamic law and their opinions were cautious and based on the form rather than the content of a proposed service or product. A new banking industry was searching for its possible shape and the initial shyness of Sharia Supervisory Boards can only attest that. It is on no wonder that two of the most significant international institutions of current Islamic finance, AAOIFI and IFSB were established only in the 90's and in the new millennia. Over the years, experts appointed to Sharia Boards were gaining knowledge and practical experience with international finance and its requirements. Their decisions became more intent oriented than form oriented and reflected the enhanced

[82] KARA, Hafsa. Islamic banks hold Basel III advantage

understanding of financial markets of their authors.[83] While sharia boards have been lenient in past with some of the possible financing structures, they have always stressed the importance of the financing that can benefit the real economy according to the principles of Islamic law. Their role of "guardians" of Islamic principles and law has lead, according Ibrahim Warde, a professor of international business at Tufts University, to situations where: "*Sharia boards acted as a safeguard against the excess of conventional finance.*"[84]

If presented with the same case problem, no two Sharia Supervisory Boards will automatically arrive to an identical answer. That is due to the fact that scholars present in the Sharia Board can come from different legal schools and backgrounds. And even within one legal school, views on certain matter can differ significantly. Sharia Boards can, and sometimes do, change their minds and alter their views. While this can easily sound to a civil law educated lawyer as a unsuitable and incomprehensible uncertainty, it falls perfectly with the notion of plurality of Islamic law and illustrates nicely a point made in the first chapter of this thesis about the danger of perception of Islamic law as one monolithic system.

The Sharia Supervisory Board can be composed of one or more scholars. For example, the Jordan Islamic Bank appoints only one religious advisor whereas the boards of The Faisal Islamic Bank of Egypt consists of five scholars.[85] The advisory body is given a broad authority to examine contracts, methods or activities carried out by the financial institution. In their work, they have instruments available at their disposal similar to those of an auditor in order to in depth inspect the proceedings of their financial institution. Often, they publish an annual report to certify that all activities are compliant with Islamic law. The management of the financial institution consults the Board with any new product or development, essentially asking the question whether a particular case is lawful or unlawful according to Islamic law. The Board in exchange endorses the case or expresses any objections and possibly suggests necessary modifications.

During the examination of validity of certain activity, the Sharia Supervisory Board first consults the primary sources – Qur'an and Sunna. If there is a text that is directly relevant to the issue at stake, the Board consults solely with these sources. In case, there is a diversity of

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[83] NETHERCOTT, Craig R.; EISENBERG, David M. *Islamic finance: law and practice*, p. 10.
[84] SERGIE, Mohammed Aly. The Rise of Islamic Finance. Council of Foreign Relations.
[85] SAEED, A., Islamic banking and interest: a study of the prohibition of riba and its contemporary interpretation, p. 108.

legal opinions, the Board follows any agreement or view that it considers right. For example, the Sharia Supervisory Board of the Kuwait Finance House stated that: "*As for the views on which there are differences of opinion among the scholars, I take the opinion which is lenient and easy for the people as long as the opinion is not a deviation or an isolated one*."[86]

The Boards are to a large extent dependent on the shape of Islamic law as developed in during the first centuries of Islam, or in other words as developed until the doors of legal reasoning have closed. In many cases, modern scholars were not able to provide current legal reasoning with sufficient credibility for the Boards to take it into account even if the scholars of the Board agree with the opening of the door in the 20th century. Consequently, the Board tends to look for the first answer it can find even if it does not correspond to our modern reality. In their justification, the Board scholars do not always provide a thorough consideration to the historical context which prompted the relevant provisions from Qur'an, Sunna or secondary legal sources. Such an example can be found in the case of gold and silver. In Sunna, Prophet Muhammad prohibited selling gold and except on hand-to-hand basis and of equal quantities. This was explained by the nature of gold and silver which was used at that time as a currency. Therefore, similar rules applied to gold and silver as to money, including prohibition of speculating on money to avoid assigning the money a time-value separated from the value of goods exchanged. However, gold and silver no longer play the rule of money in our society and since the collapse of the Bretton Woods system, gold is no longer used to determine the value of currency and the international monetary system is based on pure fiat money. Despite this development, Sharia Advisory Boards have largely ignored current status of gold and silver as a pure commodity and apply similar rules as were commonly used hundreds years ago. The specifics differ according to legal affiliation of particular Board members to various legal schools.[87]

7. Case studies

7.1. Pakistan

After several attempts of transforming the banking system in Pakistan to sharia-compliant, Pakistan has re-launched Islamic banking in 2001 by choosing a mixed system where Islamic

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[86] Ibid, p. 110.
[87] SAEED, A., Islamic banking and interest: a study of the prohibition of riba and its contemporary interpretation, pp. 110-118.

and conventional banking exist side-to-side. Among other challenges that are facing Pakistani banks and regulatory authorities, they have to adhere to a constitutional obligation of ensuring a *riba* free economic system. The Article 38(f) of the Constitution of the Islamic Republic of Pakistan provides: "*The State shall ….eliminate Riba as early as possible*." Following, the government has decided that there would be no specific timeline for conversion rather it would be left to the market forces to decide and any disruption whatsoever in the current system will not be allowed till the market is ready for the new system evolving after thorough trial and testing.[88]

In 2001, Government of Pakistan decided to make shift to interest free economy in a gradual manner without causing any disruptions and allowing for further existence of conventional banks. The following year, the first Islamic Banking License was granted to a domestic bank - the Meezan Bank Limited. Since then, the State Bank of Pakistan has established its Islamic Banking Department and set out its goal to promote and regulate Islamic banking in the country. Currently, six banks operate in a full Islamic mode while other banks are offering an Islamic window – set of services and products compliant with *sharia*.

Pakistan has been an active member of the Islamic Financial Services Board (IFSB), the Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI) and the International Islamic Financial Market (IIFM). In 2013, the Governor of the State Bank of Pakistan, Yaseen Anwar, stated that Islamic banking constitutes over 10% of the country's banking system with a network of over 1,100 branches and estimated that by 2020 the market share will double.[89]

The current legal framework in Pakistan does not distinguish between conventional banking and Islamic banking and Banking Companies Ordinance (BCO) 1962 is equally applicable to both conventional and Islamic banks in Pakistan. For the standardization and harmonization of *sharia* practices in Islamic banking industry of Pakistan, SBP had earlier issued essentials of permissible modes of Islamic banking and finance in Pakistan. Moreover, SBP has also allowed the use of AAOIFI Sharia Standards wherever SBP essentials are not available. SBP as IFSB's founding member is already playing an active role in the development of IFSB's standards. The standards issued by IFSB for Islamic banking industry will be reviewed by the State Bank in

[88] STATE BANK OF PAKISTAN. *Strategy Paper,* p. 4.
[89] ANWAR, Yaseen. Developments of Islamic banking in Pakistan.

the light of local legal and regulatory framework and will be adopted with appropriate amendments according to their issuance. [90]

7.1.1. The State Bank of Pakistan

The key regulatory body in Pakistan is the State Bank of Pakistan (SBP) which has "implemented key regulatory reforms and prudential measures to ensure financial stability and to meet the evolving needs of the industry."[91] To strengthen the sharia compliance environment in Islamic banks, the State Bank has developed a Sharia Governance Framework, which defines the sharia related roles and responsibilities of all key organs of Islamic banking institutions including Board of Directors, the executive management and Shariah Boards.

To promote the Islamic banking sector, the State Bank realised that two key elements must be at the centre of its focus. First, a sound regulatory framework that is flexible, market driven and in line with international best practices. Secondly, a sound Shariah compliance mechanism which is comprehensive, flexible, multi layered and acceptable locally and internationally.[92]

Sharia Supervisory Board of the State Bank was formed in order to guide the State Bank and the whole Islamic banking industry on matters relating to Islamic law. The Sharia Board has a minimum of five members and comprises of at least two *sharia* scholars, one chartered accountant, one lawyer and one member representing the banking sector.[93] This composition ensures that opinions given by the Board are relevant and sound both from *sharia* point of view and from finance and accounting perspective. The State Bank explained its choice by stating that "*the rulings given by the Board are not only sharia compliant but are also workable as they take into consideration the legal and financial infrastructure of the country and the business needs*." Its responsibility is not only to review and approve products and instruments in a similar way as is usual for their private sector counterparts described earlier, but also to advise the State Bank on decision in cases of a conflict arising from *sharia* audits in the private sectors or from conflicting *sharia* opinions.

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[90] STATE BANK OF PAKISTAN. Strategic Plan Islamic Banking Industry of Pakistan 2014 – 2018, p. 3.
[91] ANWAR, Yaseen. Islamic banking potential of Pakistan.
[92] STATE BANK OF PAKISTAN. *Strategy Paper.*
[93] STATE BANK OF PAKISTAN. *Strategy Paper,* Appendix C: Sharia compliance.

7.1.2. Sharia boards of commercial banks in Pakistan

Al Baraka Bank (Al Baraka Pakistan Limited) was established following a first merger in the Islamic banking sector in Pakistan in 2010 and is listed on the stock exchanges in Pakistan. Its predecessor, Al Baraka Islamic Bank Bahrain, has been operating in the country since 1991 and is considered to be the pioneer of Islamic banking in Pakistan.[94] Ever since the merger, the bank is experiencing a progressive growth. Its Sharia Supervisory Board is composed of three members – the Chairman of the Board, Member and Resident Member.[95] As a Chairman of the Sharia Board was appointed Justice Khalil-ur-Rehman Khan, a former Chairman on the Shariah Appellate Bench of the Supreme Court of Pakistan and the Rector of the International Islamic University, Islamabad. He also served as a Chief Justice of the Lahore High Court (an appellate court). He was personally present in the Supreme Court of Pakistan during the time when Pakistan became a truly Islamic economy. Shaikh Esam Mohammad Ishaq Abdul Rahman Ishaq, Member of the Sharia Board, is holding number of positions on Sharia Boards in Pakistan and Bahrain and is associated with several other financial institutions in Bahrain.

The Meezan Bank, a publicly listed company, was incorporated in 1997. In 2002, in an historic initiative, Meezan Bank was granted the country's first full-fledged commercial banking license as a dedicated Islamic Bank by the State Bank of Pakistan.[96] Its Sharia Board is composed of four members – chairman, two members and an advisor. The Chairman, Justice Muhammad Taqi Usmani, has served as a Judge in the Shariat Appellate Bench, Supreme Court of Pakistan and currently holds positions on several Sharia Boards in Pakistan, Bahrain, U.A.E., Dubai, but also in Switzerland and the USA. Other Board members are also linked to institutions in Bahrain, Saudi Arabia, the USA and Switzerland.

7.2. The case of Kuveyt Turk Bank in Germany

This year, on 1 July 2015, we will see a first Islamic bank open for business in the European Union. Turkish Kuveyt Turk Bank has established its first branch in Frankfurt under the name KT Bank AG[97] operating fully in compliance with *sharia*.[98] Kuveyt Turk Bank has already been

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[94] Al-Baraka converted into local bank.
[95] Shariah Board.
[96] Meezan Bank's Corporate Profile.
[97] More information can be found in German on http://www.kt-bank.de.
[98] KT Bank AG, Kuveyt Turk's German subsdiary is granted for the licence to launch its operations; First Islamic bank in Germany to open in July.

operating another of its branches in Mannheim which is, however, not fully functional under *sharia*.[99] Establishing an Islamic bank has happened in Germany 6 years after the BaFin (Federal Financial Supervisory Authority) first proclaimed its readiness for Sharia-compliant financial products. During its conference on Islamic finance, it stated that: "*there were no obstacles under supervisory law preventing the establishment and licensing of an Islamic bank*."[100] It further elaborated on the fact that number of Islamic financial instruments can be identified as alternatives to their conventional counterparts and are therefore subject to the same authorization procedures according to the German Banking Act (Kreditwesengesetz – KWG). *Mudaraba* transaction have been mentioned as slightly problematic as they do not automatically provide for an unconditional repayment claim and cannot be readily assumed to be subject to authorization. They must be, according to BaFin, decided based on the terms of individual case. KT Bank AG performed, according to Kuveyt Turk's press release, "*all the regulatory requirements by obtaining the full-scale banking license in Germany*"[101] and so confirmed the words of BaFin.

8. Conclusion

Many scholars, including Ivana Hrdličková, have drawn parallels between Islamic law, especially in its financial aspects, and common law. Such a comparison is usually based on the role of jurist and the use of analogy, precedent and legal reasoning not in some aspects unlike the common law. In the area of finances, Islamic concept of *waqf*, a religious endowment of property or cash for charitable purposes, carries similarities to common law trust.

One specific consideration that Islamic financial institutions have to make is that all of its products and services are 'Islamic' enough for their clients, while making sure that they yield enough profit in order to satisfy its shareholders. As a result, the Islamic banks have resorted to limited definitions of *musharaka* and *mudaraba* that will allow almost risk-free short term ventures with more or less predetermined return.[102] While conventional banks obviously do not have to consider their religious standing, they are nevertheless more and more pushed by their clients to adhere to some moral or ethical standards. Most of the products and services described

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[99] MATSANGOU, Elizabeth. Germany's first Islamic bank opens for business.
[100] BaFin ready for Sharia-compliant financial products.
[101] KT Bank AG, Kuveyt Turk's German subsdiary is granted for the licence to launch its operations.
[102] SAEED, A., Islamic banking and interest: a study of the prohibition of riba and its contemporary interpretation, p.143.s

in this thesis are products of *fiqh* – Islamic jurisprudence and do not stem directly from primary sources of Islam. Therefore, they are open to interpretation of Islamic scholars and can be altered over time depending on the needs of the society and argumentation of Islamic jurists.

The banks follow the same goals as conventional which often leads to similar products only marketed differently. One can go even further and say that given the fact that Islamic banking has evolved in a reaction to conventional banking, it is pressured to mimic its interest-taking predecessor in order to survive. Banks feel obliged to provide stable, secure, and competitive returns to its clients while facing the fear that losses would cause a run on the banks' deposit funds which would likely lead to a collapse of the bank and discredit Islamic banking as a whole. Islamic banks are more liable to such development since they have fewer resources to avoid a lack of liquidity – they often cannot rely on the support of central bank and cannot borrow at interest.[103] While facing a completely different set of challenges, Islamic banks are being forced to compete with conventional banks which lead to turning away from *mudaraba*, the preferred way of Islamic financing, to *murabaha*, essentially a markup transaction, to offset the need to develop assets and liabilities similarly to conventional banks. *Mudaraba* transactions form today a mere 5% while *murabaha* transactions constitute about 80% of banks' investments.[104] This development is in sharp contrast with the theoretical path envisioned for Islamic banks by scholars and bankers alike.

Islamic banks generally avoid long-term investments for reasons outlined in the description of their products and services. However, short-term investments, while almost risk-free, are also much less profitable then long-term investments which leaves Islamic bank with a modest profit margin. Islamic banks can face a potentially dangerous mismatch between their assets and liabilities. Their clients expect the same liquidity and yields from Islamic banks as they do from conventional banks despite the impossibility of such expectations. The short-term investment strategy of Islamic banks might not prove viable during the upcoming years. Profit margins in Islamic contracts are too low to support the overhead costs and satisfy the needs of bank owners as well as its clients. Islamic banks are particularly careful given the early stormy history of

[103] VOGEL, Frank E.; HAYES, Samuel L. Islamic law and finance: religion, risk, and return, p. 134.
[104] Ibid, p. 135.

Islamic banks during which number of the first institutions collapsed and produced considerable financial scandals.[105]

The fact that the Islamic banking is at the moment costlier than conventional banking is acknowledged by the State Bank of Pakistan as well.[106] It is explained by the ability of conventional bank to achieve economies of scale. Islamic banking is according to the State Bank still at its early stages and does not therefore administer as much clients and businesses as conventional banks. The State Bank of Pakistan adds that higher costs are to be expected since there is bigger amount of documentation needed for the workings of Islamic bank. It concludes by stating that "*while Islamic banking may appear to be marginally costlier at this stage, the incremental cost is not prohibitive in relation to the benefits*".[107] The benefits mentioned here are clearly not of an economic kind but of a religious and ethical one. At the end, it is up to the owner and the client to decide whether that holds true or not and whether he is wishing to forgo part of his profit in exchange for religious and ethical conscience.

Perhaps the Islamic banking model need not be at an economic disadvantage to the conventional model, provided that a critical mass of depositors and business enterprises participate. This is exactly what the Egyptian, Malaysian, and Pakistani experiments of the last few decades have tried to achieve with varying degrees of success. Their challenge was to deliver lasting value within the framework of the fractional reserve banking system—one that stands at odds with the concept of Islamic banking itself.[108]

Vogel and Hayes are of an opinion that Islamic finance is now on the verge of either major transformation, or a period of frustration and probable decline.[109] Similar opinions were expressed by several other authors non-affiliated with Islamic institutions. While it seems that Islamic finance is rapidly succeeding and finding its place in non-Muslim countries, economists and lawyers argue that lack of sufficient regulatory infrastructure and major flaws in the composition of their investments are holding it back and even possibly contributing to its fall.

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[105] NETHERCOTT, Craig R.; EISENBERG, David M. *Islamic finance: law and practice*, p. 8-9.
[106] AHMAD, Imran a Ghulam SHABBIR. STATE BANK OF PAKISTAN. *Frequently asked questions on islamic banking*.
[107] Ibid.
[108] IRFAN, Harris. The Nature of Money: Islamic Banking and Conscious Capitalism.
[109] VOGEL, Frank E.; HAYES, Samuel L. Islamic law and finance: religion, risk, and return, p. 292.

Islamic finance industry has shown that it desires to reform itself in order to overcome the above mentioned obstacles in its development. This can be best seen through its willingness to become a part of the existing regulatory structures of conventional finance, such as the Basel III accords mentioned in Chapter 5.2. The publication of IFSB-15, which is based on Basel III, demonstrates this commitment of the Islamic finance industry to adapt to the new financial regulatory landscape post the global financial crisis.[110] Islamic banking is, however, facing another challenge, one that it needs to resolve internally without the help of global financial system. Different interpretations of sharia across countries pose problems to standardizing the industry and are hard to overcome in the fragmented world of Islamic jurisprudence.[111]

We must keep in mind that Islamic banking is a new system, merely a half century old, still developing, finding its path and trying to understand how to become a sustainable and profitable. While it may seem strange or foreign to us, the underlining theory behind Islamic banking and finance in general is based on promotion of ethical and social oriented practices which are manifested in a religious norms. In the coming years, a crucial test will be awaiting Islamic finance as it spreads to countries where Muslims do not form the majority of population and it will be part of their task to find out whether they have something to offer to non-Muslim costumers as well. Consequently, the conversation about social responsibility, risk and regulation in finance and banking might be affected by a new player in the field – the Islamic banking system.

[110] Basel III: shariah finance's next evolution.
[111] SERGIE, Mohammed Aly. The Rise of Islamic Finance.

9. List of abbreviations

AAOIFI	The Accounting and Auditing Organization for Islamic Financial Institutions
BCO	Banking Companies Ordinance 1962, Pakistan
IAS	International Accounting Standards
IFI	Islamic financial institutions
IFSB	Islamic Financial Serviced Board
IIFM	International Islamic Financial Market
NSAC	National Sharia Advisory Council
OIC	Organisation of the Islamic Conference
SBP	State Bank of Pakistan

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Appendices

1. Main differences between conventional banking and Islamic banking

	CONVENTIONAL BANKING	ISLAMIC BANKING
1	Money is a commodity besides medium of exchange and store of value. Therefore, it can be sold at a price higher than its face value and it can also be rented out.	Money is not a commodity though it is used as a medium of exchange and store of value. Therefore, it cannot be sold at a price higher than its face value or rented out.
2	Time value is the basis for charging interest on capital.	Profit on trade of goods or charging on providing service is the basis for earning profit.
3	Interest is charged even in case the organization suffers losses by using bank's funds. Therefore, it is not based on profit and loss sharing.	Islamic bank operates on the basis of profit and loss sharing. In case, the businessman has suffered losses, the bank will share these losses based on the mode of finance used (*Mudaraba*, Musharakah).
4	While disbursing cash finance, running finance or working capital	The execution of agreements for the exchange of goods & services is a must,

	finance, no agreement for exchange of goods & services is made.	while disbursing funds under *Murabaha*, Salam & Istisna contracts.
5	Conventional banks use money as a commodity which leads to inflation.	Islamic banking tends to create link with the real sectors of the economic system by using trade related activities. Since, the money is linked with the real assets therefore therefore it contributes directly in the economic development.

Source: AHMAD, Imran a Ghulam SHABBIR. STATE BANK OF PAKISTAN. Frequently asked questions on islamic banking. 2008. [cit. 2015-05-30]. Dostupný z WWW: <http://www.sbp.org.pk/departments/ibd/FAQs.pdf>

2. Islamic banking in selected countries

Country	**Regulatory Authority**	**Islamic Banking Law**	**Shariah Committee**		**Shariah Standards**	**Accounting Standard**
			At Central Bank	At Bank Level		
Malaysia	Bank Negara Malaysia	Islamic Banking Act 1983	National Shariah Advisory Council (NSAC)	Shariah Committee	All Products approved by NSAC of BNM	Accounting Standards developed by MASB
Bahrain	Central Bank of Bahrain	NIL	Shariah Supervisory Committee	Shariah Supervisory Board	AAOIFI	AAOIFI

Indonesia	Bank Indonesia	Introduced in 1992 & Amended in 1999	National Shariah Board (NSB)	Shariah Supervisory Board	Fatwa on products issued by NSB	AAOIFI
Iran	Central Bank of Islamic Republic of Iran	Usury free Banking Act 1983	Council of Guardian	N.A	Guidelines provided by Council of Guardians	IAS being adopted
Brunei	Ministry of Finance	Islamic Banking Act Cap.168	Shariah Financial Supervisory Board (SFSB)	Shariah Advisory Board	SFSB Approves Islamic products of Financial Institutions	IAS
Pakistan	State Bank of Pakistan	BCO,62 amended to support Islamic banking	Shariah Board	Shariah Advisor	Essentials for Islamic modes	AAOIFI standards are being adapted by committee of ICAP
Gambia	Central Bank of Gambia	Islamic banking law exists	NA	Shariah Board	NA	IAS

Jordan	Central Bank of Jordan	Provisions for IB included in Banking Law of 2000	NA	Shariah Board	AAOIFI	IAS
Kuwait	Central Bank of Kuwait	Provisions for IB included in Banking Law	NA	Shariah Board	NA	IAS
Sudan	The Bank of Sudan	Islamic banking law exists	Higher Shariah Supervisory Board	Shariah Board	AAOIFI	AAOIFI
Turkey	Central Bank of Turkey (TCMB)	Law about Special Finance Houses covers IBs	NA	NA	NA	IAS
UAE	Central Bank of UAE	Islamic banking law exists	NA	Shariah Board	AAOIFI	IAS

Saudi Arabia	SAMA	NIL	NA	NA	AAOIFI	AAOIFI
Syria	Central Bank of Syria	IB law exists (Legislative Decree No.35)	NA	Shariah Board	AAOIFI Standards	AAOIFI Standards
Yemen	Central Bank of Yemen (CBY)	Islamic banking law exists	NA	Shariah Board	NA	IAS

Source: STATE BANK OF PAKISTAN. Strategy Paper. 2008., Appendix B, Islamic Banking in Some Selected Countries

3. Comparison of banking frameworks

Characteristics	**Paradigm Version of Islamic Banking**	**Conventional Banking**
Nominal value guarantee of: Demand deposits Investment deposits	 Yes No	 Yes Yes
Equity-based system where capital is at risk	Yes	No
Rate of return on deposits	Uncertain, not guaranteed	Certain and guaranteed

Mechanism to regulate final return on deposits.	Depending on banks' performance /profits from investment	No
PLS principle is applied	Yes	Irrespective of banks' performance /profits from investment
Use of Islamic modes of financing PLS and non-PLS	Yes	NA
Use of discretion by banks with regard to collateral	Possible for reducing moral hazard in PLS modes	Yes always
Banks' pooling of deposits funds to provide with professional investment management	Yes	No

Source: ERRICO Luca and FARAHBAKSH Mitra. Islamic Banking: Issues in Prudential Regulation and Supervision., IMF working Paper. 1998.

Teze práce v českém jazyce

Islámské bankovnictví je velmi mladým odvětvím dějin bankovnictví a finančnictví. V moderní době se začalo rozvíjet před pouhými 50 lety. Shoda okolností umožnila v 70. letech otevření prvních islámských bank, které měly za cíl nabídnout alternativu produktům konvenčního bankovnictví, které by byly v souladu se zásadami a pravidly islámského práva. Islámské bankovnictví může být chápáno jako bankovní činnost, která je v souladu se šaríou, islámským právem. Během posledních desetiletí vývoje islámského bankovnictví došlo ke značným změnám v jeho pojetí, které vedly k vytvoření mnoha národních variant tohoto odvětví. Nemůžeme tak hovořit o sjednoceném, jednotně regulovaném sektoru, ale spíše o souhrnu pravidel, která se v jednotlivých zemích různě manifestují.

I přes značné překážky, kterým islámské bankovnictví v minulosti čelilo, zaujímá nyní podstatnou a stále rostoucí část světového finančního systému. Podle společnosti Ernst&Young vzrostly bankovní vklady ročně o 17,6 % a dále budou růst o přibližně 20 % ročně. Přestože je islámské bankovnictví obvykle spojováno se zeměmi s většinou muslimského obyvatelstva, jako je Malajsie, Írán nebo Saudská Arábie, produkty nabízené v souladu s islámským právem se těší velké oblibě i v západních zemích. V roce 2014 zaznamenal svět islámského finančnictví zásadní krok ve svém vývoji, když se Velká Británie rozhodla vydat první státní *sukuk* – islámskou alternativu dluhopisu. Jeho vydání v celkové hodnotě 200 miliónů liber přilákalo investice v hodnotě 2,3 miliardy liber. Ani soukromé společnosti nezůstaly pozadu a Sociéte Générale, Bank of Tokyo-Mitsubishi UFJ nebo Goldman Sachs oznámily, že v dohledné době také chystají vydání *sukuk* dluhopisů.

S ohledem na tento vývoj se zdá nejvýše vhodné přiblížit některé aspekty islámského bankovnictví a představit je i v evropském kontextu. Tato diplomová práce je rozvržena do několika částí. V prvé řadě představím některé základní principy islámského práva, zvláště ty, které jsou relevantní pro pochopení pojetí financí a obchodu v islámu. Dále se podívám na několik vybraných produktů, které jsou obvykle nabízeny islámskými bankovními institucemi. Ve druhé části své práce se zaměřím na problematiku regulace islámských bankovních institucí a popíši zásadní mezinárodní organizace, které vydávají regulační standardy. Druhou stranou regulace islámských bank je potřeba vnitřní i vnější

kontroly souladu jejich činností s islámským právem. I tento aspekt krátce popíši a oba úhly regulace představím na případu islámských bank v Pákistánu. Jako příklad uvedu i nově založenou, první plně islámskou banku v Evropě – německou KT Bank AG. V závěru práce se věnuji i obecnému srovnání islámského a konvenčního bankovnictví a výzvám, kterým čelí islámské banky v budoucnu.

Primárním zdrojem islámského práva neboli šaríi je Korán, o kterém muslimové věří, že jde o přímé zjevené od Boha. Je to ústřední náboženský text, který komplexně pokrývá všechny aspekty života jednotlivce i společnosti. Korán je doplněn sunnou, neboli skutky Mohameda, hlavního proroka islámu. Jako sekundární zdroje je považován především konsensus (*idžmá)* a analogie na základě právního odůvodnění (*qijás*). Přestože slouží sekundární zdroje pouze k vyjasnění sporných nebo nepřesných míst v Koránu či sunně, tak mají ve svém důsledku zásadní vliv na vývoj a chápání islámského práva. Přesná definice sekundárních zdrojů jakož i pravidla jejich používání se liší v rámci islámských právních škol a přispívají tak k značné fragmentárnosti islámského práva. Jako další zdroje jsou používány kritéria veřejného zájmu či blaha (*maslaha)*, nezbytné nutnosti či potřeby (*durara)* nebo lokální zvyk (*urf)*.

Zdroje islámského práva jsou využívány k tvorbě *fiqhu* neboli islámské jurisprudence na které se podílí především právníci a obecně právní učenci. Soudci jsou v rámci islámského práva chápáni spíše jako ti, kteří aplikují právo, ale nevěnují se přímo jeho interpretaci. Tu mají na starosti právě právníci, jejichž reputace, a tím i obecné přijímání jejich interpretace, závisí především na jejich úrovni znalostí a schopnosti argumentace. Celý život muslimského jednotlivce i muslimské společnosti je obsažen v normách islámského práva. Záležitosti, které se týkají vztahu mezi člověkem a Bohem, jsou odlišeny od záležitostí v rámci komunity. Právě tato druhá kategorie norem je otevřená k extenzivní interpretaci a je tak náchylná k snadnějším změnám v čase. Pouze tyto záležitosti mohou také být podrobeny sankcím vynucovaným státní nebo náboženskou autoritou. Vzhledem k těmto charakteristikám je zřejmé, že islámské právo je flexibilním a pluralitním systémem, který umožňuje vývoj dle nových skutečností a reálií moderního světa.

Pluralita islámského práva je dána i skutečností, že v islámu neexistuje jediná centrální náboženská autorita, která by mohla podávat autoritativní výklad. Islámské

právo, přestože je založeno na stejných principech a zásadách, může nabývat značně různorodých podob a to nejen v čase a v místě, ale i mezi jednotlivými právníky žijícími ve stejnou dobu na stejném místě. Tento aspekt islámského práva je v praxi dále podtržen různou historií jednotlivých zemí, které v současné době aplikují v různé míře islámské právo. Některé země zdědily ze své kolonialistické minulosti anglické common law, jiné dobrovolně zvolily francouzské či německé zákony, jako předlohy pro své kodexy. Je důležité mít na vědomí tuto různorodost, která vedla k vytvoření tolika různých systému islámského bankovnictví, kolik je zemí aplikujících tento systém. Neexistuje žádný jednotný systém, který by se dal aplikovat všude na světě a který by byl interpretován jednotně.

Základní principy islámského finančnictví mají svůj základ již v primárních zdrojích – Koránu a sunně. Přestože byly rozvíjeny ve starověkém i ranně novověkém muslimském světě, byly následně téměř zapomenuty pod vlivem evropského kolonialismu v regionu. Až doba po druhé světové válce přinesla změny nejen v postavení arabských zemí, ale i v obnovené intelektuální činnosti islámských právních učenců. První islámské finanční instituce byly založeny v 60. a 70. letech v Egyptě. V roce 1973 došlo také k založení významné nadnárodní instituce – Islámské rozvojové banky, která existovala pod správou Organizace islámské spolupráce. V následujících letech vznikaly další islámské finanční instituce, z nichž část byla vlastněná soukromě a část státem. Několik většinově muslimských států také oznámilo plnou islamizaci svého finančního sektoru – Pákistán v roce 1979 (tento první pokus nicméně selhal a byl obnoven až v roce 2001), Írán a Súdán v roce 1983 a ve stejném roce představila částečnou islamizaci i Malajsie, která se ovšem rozhodla vydat cestou dvojího sektoru – koexistujícího islámského a konvenčního finančnictví.

První islámské banky ovšem nezaznamenaly automatický úspěch. Naopak, během prvních pokusů najít možný model pro fungování islámského bankovnictví došlo k řadě skandálů a bankrotů, které poznamenaly důvěryhodnost celého odvětví. Tyto první nezdary vedly k řadě změn v chápání role islámských bankovních institucí a umožnily současný, mnohem příznivější, vývoj. Zatímco arabské země Perského zálivu byly při vývoji systému islámského bankovnictví motivovány především svým nebývalým ekonomickým rozvojem a velkým národním bohatstvím, Malajsie přistoupila k vytvoření

duální, konvenční a islámské, sktruktury jako k příležitosti podpořit svůj ekonomický rozvoj.

Korán podporuje obchod založený na oboustranném souhlasu a preferuje ho před jinými způsoby získávání majetku jako například dědictví nebo darování. Základními předpoklady jsou právě souhlas obou stran a také výměna předmětu obchodu přinášející zisk. Islám dává důraz na souhlas a na úmysl a upřednostňuje obsah před formou. Korán tak podporuje podnikání a násobení majetku. Neodsuzuje ani dluh za podmínek, že je smluvený v písemné formě a není v rozporu s právem. Chápe zadlužení jako způsob překlenutí nepříznivého období a nabádá věřitele k strpění a i k odpuštění dluhu, což je chápáno jako forma ctnostné dobročinnosti. Bohatství je považováno za kladnou vlastnost, majetek je respektován a tvorba zisku je podporována za předpokladu, že při rozmnožování svého majetku nezapomenu na svou komunitu a její méně majetné členy.

Středověcí Arabové byli zkušení obchodníci a nezadali si s moderními kapitalisty. Přesto měli zásadně odlišný přístup k jednomu aspektu obchodu – k penězům. Podle islámských učenců jsou peníze pouze prostředkem k dosažení určitého cíle a nemohou být cílem samy o sobě, neboť nemají žádnou vlastní hodnotu. Podle středověkého učence Ghazaliho byly peníze vytvořeny proto, aby mohly cirkulovat mezi lidmi, používány jako způsob poměřování hodnoty zboží a jako prostředek pro získávání věcí. Peníze nemohou být použity ke tvorbě dalších peněz – nemohou být tedy ani půjčovány na úrok. Právě tento předpoklad je často vnímán jako základní pravidlo islámského finančnictví. Ve skutečnosti je ale doplněno řadou dalších zásad, které budou vysvětleny v následující části.

Jeden z hlavních všeobecně známých principů islámského bankovnictví je zákaz úroku (*riby).* Ten je založen na interpretaci několika veršů v Koránu. Ve své podstatě se ale jedná o velmi složitý problém, který byl a bezpochyby i nadále bude předmětem mnoha rozdílných, až protichůdných interpretací. Termín *riba* pochází z arabského slova pro nárůst či růst. V Koránu se objevuje v kontextu několika veršů, které se věnují povinnosti majetných muslimů pamatovat na své bližní, především sirotky, vdovy a nemajetné, a ilustrují tak princip společenské odpovědnosti, na kterém je islám založen. *Riba* je tak převšinou v tomto kontextu chápána jako antiteze charity, kdy místo dobročinného daru vyžaduji po nemajetném spolubližním úroky (hraničící s lichvou) ze

zapůjčené částky. Na dalším místě se zákaz *riby* objevuje v situaci, kdy dlužník žádá po věřiteli odložení splatnosti dluhu výměnou za navýšení splatné částky. Muslim by měl žádat navrácení pouze původně zapůjčené částky, bez jakéhokoliv navýšení. Další zmínky o *ribě* můžeme nalézt v sunně, která se problému úroků věnuje o něco důkladněji. Zde se vyskytuje požadavek na výměnu určitého typu zboží (zlato, stříbro, ječmen, datle, sůl a pšenice) pouze z ruky do ruky, v rámci jednoho druhu zboží a bez navýšení množství.

V moderní době se problematice *riby* věnovala řada učenců/právníků. Někteří z nich, jako například Muhamad Abduh, Rashid Rida, Abd al-Razzak nebo Maaruf al-Dawalibi, shledali úrok, na rozdíl od lichvy, jako zcela přijatelnou součást islámského práva. Rozšířili ovšem naše chápání lichvy například i na složený úrok, v souladu s principem ochrany slabšího. I další současní právníci, například Abdullah Saeed, se zaměřili právě na teleologický výklad zákazu *riby*, který vidí jako způsob zabránění zneužití silnějšího postavení věřitele, a poukazují na původní důvod tohoto zákazu – zabránění nespravedlnosti. Tento výklad nicméně není zásadněji rozšířený a významné nadnárodní regulatorní instituce islámského finančnictví většinou úrok zakazují. Příkladem může být The Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI), která explicitně zakazuje používání kreditních karet založených na používání úroku. Bezpochyby můžeme ale očekávat další vývoj v oblasti výkladu pojmu *riba*, který bude určující i pro další směřování islámského bankovnictví.

Dalším obecně zakázanou činnosti je v islámu spekulace (*gharar*), která je ve svém významu úzce spojená se zbytečným rizikem, zavádějící nejistotou a přesouváním rizika. AAOIFI považuje *gharar* za nedovolený pouze v rámci dvoustranného právního jednání, většina islámských právních škol nicméně spekulaci zakazuje plošně. V sunně se termín *gharar* objevil v souvislosti se zákazem stanovení výsledků losem nebo zákazem prodeje ptáka ve vzduchu, ryby ve vodě, uprchlého zvířete nebo otroka nebo čehokoliv, co prodejce nemusí být schopen splnit v důsledku chybějící držby. Podle některých regulatorních institucí, např. pákistánské centrální banky, je *gharar* neplatný pouze pokud se jedná o nepřiměřené riziko.

Dalšími nepovolenými činnostmi jsou hazard a právní lest neboli obcházení zákona. Obecně jsou všechny aspekty lidského chování rozřazeny pěti kategorií –

zakázáno, nedoporučováno, povoleno, doporučeno a vyžadováno. Pouze zakázané jednání ve společenské oblasti je sankcionováno. Zakázáno (*haram)* je například obchodování s alkoholem, pornografií, drogami, vepřovým masem nebo používání bankovních produktů, které nejsou v souladu s islámským právem.

V následující části své práce stručně popisuji vybrané produkty islámského bankovnictví. Nejprve se budu věnovat nástroji zvanému *mušáraka*, která může být popsána jako partnerství. Může se jednat i o partnerství v rámci vlastnického práva neboli spoluvlastnictví ale typicky pojmenovává obchodní partnerství. *Mušáraka* se dá rozdělit mezi smluvní partnerství a spoluvlastnictví a může vzniknout jak na základě práva, tak na základě smlouvy. V její nejjednodušší podobě oba partneři přispívají určitou částkou na společné vlastnictví a každý z partnerů může přitom nakládat s celým vlastnictvím. Zisk i ztrátu sdílejí oba partneři podle svého podílu na společném vlastnictví. *Mušáraka* je natolik univerzální koncept, že může nabývat mnoha podob a tím se stává značně flexibilní možností spolupráce a financování. V Saudské Arábii je například typicky používaná pro založení obchodních korporací obdobných společnosti s ručením omezeným. Speciální a široce používanou variantou *mušáraky* je tzv. snižující se *mušáraka.* Jedná se o takové partnerství, kde jedna strana je identifikovaná jako financující společný projekt a druhá strana jako správce projektu. Financující strana (banka) zpočátku poskytuje až 99 % potřebných finančních prostředků a obdrží odpovídající podíl hlasů i zisku. V průběhu pokračující spolupráce odkupuje aktivní strana podíly financující strany, a tak snižuje její zapojení do společného projektu a naopak zvětšuje svůj podíl. Na závěr může dojít k plnému odkoupení podílu financující strany a zániku *mušáraky.*

Dalším produktem, který nabízí islámské banky je *mudáraba.* Jedná se i společný podnikatelský počin dvou a více stran, při kterém jedna ze stran přináší kapitál ve formě peněžitého vkladu nebo vkladu hmotné věci, zatímco druhá strana vkládá do společného projektu především osobní zkušenosti, know-how, práci a čas. Strana vkládající svou práci je aktivní při správě společného projektu a má volnou ruku při přijímání rozhodnutí souvisejících s obchodním vedením. Přesný rozsah této svobody je vymezen jednotlivými právními školami i mezinárodními a národními standardy různě. Podíl na zisku je definován smlouvou uzavřenou mezi stranami a může být měněn s ohledem na měnící se okolnosti. Musí být nicméně stanoven v poměrně, nikoliv jako pevně daná částka.

Financující strana ručí pouze do výše svého kladu a za závazky, které tento vklad převyšují, ručí druhá strana. Ztrátu nese pouze financující společník, neboť druhý společník utrpí ztrátu především na investovaném čase a na ušlých příležitostech. Na Blízkém východě je *mudáraba* používána islámskými bankami k financování krátkodobých podnikatelských plánů. Banka poskytne finance, obvykle pocházející od jejích investorů, klientovi, který je využije ke svému podnikatelskému záměru nebo nákupu zboží. Po ukončení dohodnuté transakce jsou zisky rozděleny dle smlouvy poměrně mezi klienta a banku (a její investory). Přestože banky obvykle žádají dostatečné záruky od svého klienta, že daný plán bude ziskový, nemůže jim být návrat jejich investice předběžně garantován. Vzhledem k opatrnosti bank při poskytování financí pomocí *mudáraby* se ovšem jedná o investici s velmi nízkým rizikem.

Murábaha je jedním z nejčastěji používaných nástroji financování. Jedná se o obdobu prodeje s obchodní přirážkou, ale není omezená pouze na nákup zboží, surovin nebo majetku, ale i jako nástroj pro správu likvidity a kapitálu. Ve své nejjednodušší formě nakoupí banka (prodejce) zboží dle požadavků svého klienta, budoucího kupce. V průběhu tohoto procesu získává banka nejprve vlastnictví nad daným zbožím, i když nemusí být jeho držitelem. Poté zahájí druhou část *murábahy*, když zboží prodá svému klientovi za původní cenu navýšenou o předem dohodnutou částku. Tato druhá transakce bývá zpravidla uzavřena na základě úvěru poskytnutého ze strany banky. Dohodnutá cena a přirážka nemůže být v proběhu *murábahy* měněna a do přirážky může banka zahrnout i náklady vynaložené na přepravu, skladování a pojištění. Předmětem *murábahy* může být jakékoliv zboží s výjimkou zakázaných věcí (*haram*), hotovosti a jejích ekvivalentů (např. zlata a stříbra). V současnosti představují až 87 % portfolia nabízeného islámskými bankami.

Idžára neboli nájem či pacht je používán jako alternativa k nákupu na splátky při financování vybavení. Pronajímatel, v tomto případě banka, si zachovává vlastnický titul k pronajímané věci. Při uzavírání *idžáry* vysloví klient banky přání zakoupit určité zboží. Banka toto zboží následně zakoupí a pronajme jej svému klientu.

Islámské bankovní produkty mohou být islámskými finančními institucemi nabízeny ve dvou podobách. Buď může banka celá fungovat zcela v souladu s islámským právem a poskytovat komplexní bankovní služby obdobně jako její konvenční

alternativy. Druhou možností je tzv. islámské okno konvenčních bank, které umožňuje nabízet pouze vybrané produkty, které jsou jednotlivě v souladu s islámským právem. V obou případech musí banka ustanovit islámskou dozorčí radu, která posuzuje soulad nabízených produktů a služeb s islámským právem. Způsob jakým se státy s regulací islámského bankovnictví vyrovnávají je dán i rozdílným přístupem k jeho přítomnosti v jejich jurisdikci:

(1) země, které transformovaly celý svůj finanční a bankovní sektor dle principů Islámského práva – Irán, Pákistán (který se nachází v procesu transformace) a Súdán;

(2) země, které podporují islámské bankovnictví jako státní politiku, ale zároveň umonují existenci duálního systému (koexistence islámského a konvenčního bankovnictví) – Bahrajn, Brunej, Kuvajt, Malajsie, Turecko, Spojené Arabské Emiráty;

(3) země, které islámské bankovnictví ani aktivně nepodporují ani nekladou překážky jeho vývoji – Egypt, Jemen, Singapur, a Indonésie; a

(4) země, které kladou překážky vzniku islámského bankovnictví – Saudská Arábie, Omán.

Ve všech výše zmíněných případech můžeme hovořit o dvou dimenzích regulace finančních institucí. Zaprvé, islámské finanční instituce podléhají regulaci národních i mezinárodních regulátorů stejně jako jejich konvenční protějšky. Zadruhé, islámské bankovnictví, postavené na základech islámského práva, podléhá regulaci a kontrole souladu právě s normami islámského práva. Tato regulace je vykonávání interními orgány i národními a nadnárodními institucemi. V obou případech je v systému islámského bankovnictví zřetelná snaha přijmout a implementovat standardy a pravidla, která by umožnila překonat národní a názorové rozdíly a vytvořit skutečně globální systém.

Za tímto účelem byla vytvořena řada mezinárodních regulačních institucí, z nichž v současnosti dvě nejvýznamnější jsou Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI) a the Islamic Financial Serviced Board (IFSB). Jejich význam může být snadno dokázán skutečností, že standardy a pravidla přijatá těmito institucemi jsou využívaná většinou národních regulačních autorit zemí s islámským bankovnictvím. AAOIFI sídlí v Bahrajnu a byla založena v roce 1991 za účelem přípravy standardů v oblasti účetnictví, auditu, správy, etiky a islámského práva pro islámské

finanční instituce. V současnosti má 200 členů ze 40 zemí a její standardy jsou přímo aplikovány v Bahrajnu, Jordánsku, Libanonu, Kataru, Súdánu a Sýrii. Další země přijali vlastní pravidla založená na dokumentech vydaných AAOIFI. Těch bylo přijato již téměř 90 a více než polovina z nich se věnuje otázkám islámského práva, čtvrtina pak účetnictví. IFSB je novější organizací – byla založena roku 2002 v Malajsii, která se také zaměřuje na vydávání standardů, vztahujících se na bankovnictví, kapitálové trhy a pojišťovnictví. Za dobu své existence přijala IFSB 22 dokumentů různé povahy.

Mezinárodní regulační rámec, který zasahuje jak konvenční tak islámské banky, je nastaven opatřeními Basilejského výboru pro bankovní dohled. Ten v roce 2011 v reakci na světovou finanční krizi přijal nejnovější set opatření nazvaný Basel III. Přestože primárním cílem Basilejského výboru jsou konvenční banky, jeho rozhodnutí dopadají i na islámské banky. Ty se basilejskými opatřeními musí řídit jednak v případech, kdy se nachází v zemi, která je členem Basilejského výboru a aplikuje jeho standardy, ale i tehdy řídí-li se standardy vytvořenými IFSB, který zapracovává basilejská opatření do svých dokumentů.

IFSB reagoval na přijetí Basel III vypracováním nových standardů, které byly představeny v roce 2013 pod názvem IFSB-15. V tomto dokumentu byly basilejské požadavky přizpůsobeny potřebám islámských bank s jejich specifickými vlastnostmi především v oblasti kapitálu a likvidity. Například Katarská centrální banka rozhodla o přijetí obou opatření – Basel III i IFSB-15 a vyžaduje od katarských bank implementaci všech požadavků v nich opatřených. Obdobnými cestami se vydali i další země Perského zálivu.

Pro islámské banky znamenalo přijetí opatření Basel III zásadně méně komplikací a nutných změn než pro banky konvenční. To je dáno především důrazem, který Basel III klade na kapitálovou přiměřenost. Islámské banky přitom již nyní mají vzhledem k povaze svých produktů většinu svého kapitálu (průměrně přibližně 80 %) uloženého v původním kapitálu spadajícím do Tieru 1. Zvýšení minimálních požadavků na poměr kapitálu v Tieru 1 tedy nemá na islámské banky zásadnější význam. Problematičtější jsou změny s ohledem na likviditu bank. Islámské banky se již dlouhodobě podílejí s problémy s likviditou a to je i jedním z hlavních nedostatků celého islámského bankovního systému.

Obecně ale mají islámské banky vůči svým konvenčním protějškům určitou výhodu, neboť již nyní plní v řadě bodů požadavky stanovené Basel III.

Na jednu stranu je vhodné, aby islámské banky byly zapojeny do systému mezinárodních standardů a účastnily se tak globálního bankovního systému, na druhou stranu je ale potřeba uvědomit si, že basilejská opatření byla vytvářena pro konvenční banky a nereagují tak na výzvy, kterým skutečně islámské bankovnictví čelí. Do budoucna můžeme pravděpodobně předpokládat větší důraz na problematiku islámského bankovnictví i v rámci basilejského systému, a to ze dvou důvodů. Jednak již nyní je řada centrálních bank zemí s islámským bankovnictvím a IFSB členy poradního výboru a za druhé budeme v tomto roce svědky otevření první islámské banky na území Evropské unie.

Vnitřní regulace jednotlivých islámských bank i celého systému islámského bankovnictví je dána jeho specifickou povahou založenou na náboženském právu. Pro tyto účely jsou zřizovány šaría dozorčí rady, které působí jak při jednotlivých bankách, tak při centrálních bankách a mezinárodních organizacích. Jejich role je posoudit každý nový produkt či transakci s ohledem na jejich soulad s islámským právem. Následně mohou vyslovit souhlas či nesouhlas s jejich zavedením. Kromě toho plní i další funkce, které jsou vysvětleny v této kapitole.

V další části práce se blíže věnuji dvěma případům islámského bankovnictví. Nejprve je představena situace v Pákistánu, kde v současné době existují vedle sebe jak konvenční, tak islámské finanční instituce, i když vláda dlouhodobě směřuje k zavedení čistě islámského bankovního systému. Klíčovou roli v této snaze hraje Státní banka Pákistánu, která má za cíl podporovat rozvoj islámského bankovnictví. Za tímto cílem připravuje takový regulační rámec, který bude flexibilní a orientovaný na potřeby trhu. Zároveň prosazuje takový mechanismus posuzovaní souladu s islámským právem, který bude komplexní a uznávaný v rámci státu i na mezinárodní půdě. K tomu jí slouží šaría dozorčí rada, která má mimo jiné i možnost rozhodovat o konfliktech v rámci šaría dozorčích rad soukromých islámských bank. Spíše pro orientaci v problematice se velmi stručně věnuji i případu banky KT Bank AG v Německu, která bude 1. července 2015 otevřena jakožto první zcela islámská banka v Evropě.

V samém závěru práce se věnuji porovnání problémů, kterým čelí islámské banky a konvenční banky a nastiňuji možný další vývoj v tomto novém a rostoucím odvětví. Islámské banky se potýkají s řadou problému, velmi odlišných od problémů konvenčních bank, jejichž vyřešení bude klíčové pro další vývoj tohoto nového sektoru. Tyto specifické výzvy přispívají k menšímu zisku i k potřebě hledat možnosti takových mezinárodních standardů a regulačních opatření, která by umožnila vytvořit sjednocený systém. Především tento aspekt bude klíčový pro další rozvoj islámského finančnictví.

Veřejná regulace finančních trhů: srovnání islámského a konvenčního finančnictví

Abstrakt v českém jazyce

Ve své práci se zabývám povahou islámských bank a jimi nabízených produktů v kontextu regulace finančních trhů a bankovnictví. Islámské bankovnictví může být chápáno jako bankovní činnost, která je v souladu se *šaríou*, islámským právem. I přes značné překážky, kterým islámské bankovnictví v minulosti čelilo, zaujímá nyní podstatnou a stále rostoucí část světového finančního systému. Nejprve jsou představeny zásady islámského práva, na jehož základě je islámské bankovnictví vystavěno, spolu s klíčovými zásadami islámských financí. Pozornost je věnována i novodobé historii islámského bankovnictví. Na tento úvod navazuje část zabývající se vybranými bankovními produkty nabízenými islámskými bankami, jejichž pochopení je klíčové pro porozumění specifickým problémům, se kterými se islámské bankovnictví potýká. Druhá část této práce je věnována otázkám regulace islámských bank. Nejprve jsou představeny mezinárodní regulační instituce působící v oblasti islámského finančnictví a dále je prozkoumána otázka dopadu přijetí opatření Basel III na islámské banky. Vzhledem ke své povaze je v případě islámských bank potřeba i další vnitřní i vnější kontroly souladu jejich činností s islámským právem. Tuto činnost vykonávají tzv. dozorčí rady pro soulad s islámským právem, které existují interně i externě na národní a mezinárodní úrovni. Vybrané aspekty problematiky regulace islámských bank jsou ilustrovány na dvou příkladech. Prvním je islámský bankovní sektor v Pákistánu a druhým je v roce 2015 otevíraná první islámská bank v Evropě. Závěr práce se zabývá především shrnutím poznatků a poukázáním na vybrané problémy, kterým v otázce regulace bude islámský bankovní systém čelit v budoucnu.

Klíčová slova

islámské finančnictví, islámské bankovnictví, bankovní regulace

Key words

Islamic finance, Islamic banking, banking regulation