

Guarantee by the Islamic Bank of the Investment Deposit

MOHAMMAD ALI ELGARI

Associate Professor

Department of Economics

Faculty of Economics and Administration

King Abdul Aziz University, Jeddah, Saudi Arabia

ABSTRACT . While commenting on the topic of discussion "Guarantee of Islamic Bank for Investment Deposit" a few questions have been raised that seek their answers:

- Is there a need for such a guarantee by the Islamic bank? What is that? and why is that?
- Is it possible to hold Islamic bank guarantor of the capital of investment deposit on the ground that the bank itself is the *Mudarib* while it hands over the capital to another *Mudarib* involving violation of the rule?
- Can monetary authorities check Islamic bank from exposing depositor's money to the risk of loss?
- Are there accepted *fiqhi* evasions on holding the *mudarib* (working partner) guarantor of *Mudarabah* capital?
- Are there accepted *fiqhi* evasions / elusions for holding the *Mudarib* (working partner) guarantor of *Mudarabah* capital in addition to lumpsum amount of money?
- In what way these evasions / elusions differ from the bank interest?
- Is it permissible for the bank to voluntarily provide this guarantee?
- Is it permissible for a third party to voluntarily provide with such a guarantee?

First Question: Is such a guarantee necessary to obtain from the Islamic Bank? What is the nature of this necessity? How is it justified?

The appropriate approach to this question does not lie in whether bank deposits are guaranteed or not, but rather in the extent of risk the deposit owner is willing to take. Existence of such guarantee from the bank does not necessarily mean a low rate of risk if the Islamic bank offering it is itself not financially strong. We know that the best and least risk-laden of bank loans are those which banks extend to their best customers

without a collateral or guarantee. What should be of concern to the investor then is the extent of risk involved; he should look into the guarantee as part of several means of risk minimization. In this context, the level of risks involved could be reduced to its minimum through investment diversification, good and prudent management, control of investment periods and choice of parties that are credit-worthy etc. These diverse measures could be taken to the extent that would enable the investor reach a suitable and acceptable level of risk-taking without the need to have a guarantee of the investment deposit from the deposit-receiving bank. Furthermore, one would undertake these measure while bearing in mind that the receiving bank bears full responsibility for the investment deposit in case of any transgression or default on its part, without this constituting a violation of the principles of Shari'ah. Acceptance of the bank to guarantee the capital of the investment deposit explicitly in the deposit contract would revert the investment contract into a loan contract. This would, in turn, lead to treating any increase in the amount deposited as a form of unlawful interest.

This leads us to a very important issue that has escaped attention of the observers of Islamic banking, namely the difference between the legal and the economic aspects of the issue at hand. Shari'ah requirements in contracts are a legal reality and significance; they come in the form of injunctions: "do" and "do not do" and not in the form of an economic theory. Therefore, many transactions, which do not differ from other transactions from an economic perspective (such as the extent of risk involved), are prohibited or labeled unlawful, while other similar counterparts are lawful. The reason for this distinction is ascribed merely to differences in the contracting aspects of the two groups of such similar transactions. Shari'ah has no objection to any efforts made for the sake of risk management and risk minimization to the extent that would bring such efforts close to those exerted when considering the risks involved in a loan. The objection of Shari'ah is centered on the contract form; once the condition of guarantee is stipulated in the investment deposit, the contract automatically changes into a loan contract.

Second Question: Is it possible for the Islamic bank to guarantee the capital of an investment deposit in its capacity as a *Mudarib* (Manager) who has extended such capital to another *Muadarib* for investment?

The *Mudarib* does not guarantee capital of the investment deposit on the basis of giving his capital to another *Mudarib* for investment, unless he does this without the permission or consent of the original investor, or without such conduct being customary. This is very unlikely in the work of banks, for their function as financial intermediaries is well known and constitutes common knowledge to customers. Thus the general Shari'ah rule, which reads "*That which is known to be an observed custom has the force of a legally binding stipulation*", applies here. Based on this, the bank receiving the investment deposit has an implicit authorization from the deposit owner (*Rabb-ul-Mal*) to give the capital of this deposit to another *Mudarib* for investment. As there is no violation of any contractual obligations involved here, such bank will not be obliged to guarantee the capital extended to another *Mudarib*. Hence, there is no legal basis or case for making the bank responsible for guaranteeing the investment capital.

Third Question: Do monetary control authorities prevent the Islamic bank from exposing depositors' funds to the risk of loss?

What concerns the monetary control authorities is to prevent banks from defrauding their clients by giving them the impression that their deposits are guaranteed at the time when they are really not. The monetary authority, which oversees the work of banks, ensures that the depositor is fully aware of the nature of an investment deposit when he deposits his funds in an investment account in an Islamic bank. In other words, these authorities' main concern is to ensure that the depositor is aware of the nature and extent of the risks he is taking when he places money in an Islamic bank for investment. This is not limited to Islamic banks. The funds banks receive from individuals in time deposit accounts are guaranteed by these banks. The same holds true about funds received by banks in trust. The bank receiving an investment deposit should ensure that the investor knows and understands well the nature of risk inherent in the investment process.

Fourth Question: Are there any acceptable juristic attempts to make the *Mudarib* (Manager) liable for payment of the *Mudarabah* capital in case of its loss?

There have been many attempts in that direction, but none of them was accepted. Most notable among these attempts was that advocated by Dr. Sami Hasan Humoud, in which the *Mudarib* was given, by analogy, the status of a common workman. It is well known that the Caliph Ali Bin Abi Talib (May Allah be pleased with him) made a common workman liable for his work in case of transgression or default, contrary to a private workman, who is not held liable. Adherents of the Maliki School of Islamic Jurisprudence deal with the issue of guaranteeing workmanship or services by artisans in a different way. They distinguished between those who work under close supervision of the employer and those who do not. Those who do not work under the direct supervision of their employers are made liable for compensation in case of transgression or default, whereas workmen who do work under the direct supervision of their employers are not.

In all respects, the common *Mudarib* is different from the common workman and the considerations on the basis of which the common workman has been made liable for what he does do not apply to the bank.

Once more, it should be emphasized that the issue here is an issue of measuring risks, where the guarantee is no more than one of several means at the investor's disposal to minimize risks.

Fifth Question: Are there any acceptable juristic attempts to make the *Mudarib* (Manager) liable for payment of the *Mudarabah* capital in addition to a lump sum ?

There are attempts to make the investment account oscillate between a loan contract and a *Mudarabah* contract in the sense that it would first start as a loan to the *Mudarib*, which would be treated, in this case, like a current account. Once an investment opportunity arises and profit is realized, the loan would be automatically converted into a *Mudarabah*. Those who suggested this arrangement have as their

authority the story of the two sons of Caliph Umar Bin Al Khattab, Abdullah and Ubaidullah. However, the analogy on which this suggestion is based is an imperfect one; it is an analogy with a difference. Therefore, this trend did not receive jurists' acceptance and was even totally rejected by many resolutions issued by Shari'ah boards.

Sixth Question: In what way do these attempts differ from bank interest?

I have no doubt that all these attempts revert to the same end result, namely conversion of the *Qirad* contract into a loan contract, even if there were some variations in the contractual relationships at the beginning or at the end.

Seventh Question: Can the Mudarib volunteer to offer such a guarantee as a gift?

The answer is affirmative. However, attention should be paid to the meaning of a donation or a gift. In order to ensure the validity of such offer of guarantee as a gift, it should not be stated in the *Mudarabah* contract, neither explicitly nor implicitly, nor should it be given except after the *Mudarabah* contract has already been concluded. In other words, conclusion of the *Mudarabah* contract should not be based on the condition of offering such a guarantee. Besides, offer of the guarantee, as a free voluntary act, should not be binding on the *Mudarib*, because it is a form of voluntary gift or donation. The contract should not be abrogated as a result of the absence of such voluntary offer of guarantee, for if this happens it would be, in reality, as if the guarantee has been made a condition of the contract.

In the work of banks, this would entail abstaining from making such an offer recur, for its recurrence would mean that it has become an established custom, which would have the force of a condition according to the general Shari'ah rule quoted earlier. There is no harm in such a guarantee being offered as a pure gift or donation, which happened once with one of the big Islamic banks. The bank sustained big losses and its Board of Directors decided to have the bank's owners shoulder this loss on behalf of the owners of the investment accounts. The bank's Shari'ah Supervisory Board approved such measure, which was done once. Thus it was a donation meeting all conditions of validity.

Eighth Question: Could a third party volunteer to offer such guarantee?

No doubt that donating such guarantee by a third party is a permissible act. But could a third party exist without being a party having an interest or stake in the investment? If this is very unlikely, and the third party envisaged would most likely be an interested party, then such party is no longer considered a third party any longer. Thus a real disinterested third party is inconceivable. We were informed that the Jordanian Government accepted to offer guarantees in respect of the *Mudarabah Sukuk* (investment certificates), which the Department of *Awqaf* wanted to issue for the rehabilitation of some of the Department's *Awqaf* properties. Such an offer of guarantee by a third party is acceptable, though very rare, and thus merits no consideration to establish a rule. In most cases, such third party would not be a party independent of the two contracting parties; he is either a partner, a seller or a buyer etc. and thus would not serve as a legally acceptable donor of the guarantee.

ضمان المصرف الإسلامي للوديعة الاستثمارية

محمد علي القوي

أستاذ مشارك

قسم الاقتصاد - كلية الاقتصاد والإدارة

جامعة الملك عبدالعزيز - جدة - المملكة العربية السعودية

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- هل يمكن أن يضمن المصرف الإسلامي رأس مال الوديعة الاستثمارية على أساس أنه مضارب دفع مال رب المال إلى مضارب آخر ؟
- هل تمنع السلطات النقدية المصرف الإسلامي من تعريض أموال المودعين لخطر الخسارة ؟
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- فيم تختلف هذه المحاولات عن الفائدة المصرفية ؟
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