

**Overview of the services of Islamic Banking System and
potential for implementation problems in Lebanon.**

By:

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A research project submitted in partial fulfillment
of the requirements for the degree

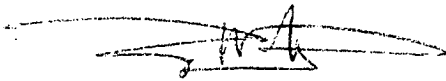
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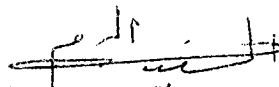
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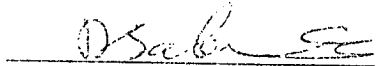
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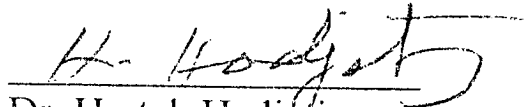
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Abstract

Overview of the services of Islamic Banking System and potential for implementation problems in Lebanon.

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This study presents a brief and a quick overview of the Islamic banking system which is finding its way as a new competitive system. Islamic banking is mainly directed towards fulfilling and respecting Islamic fundamental laws of monetary relations among Muslims. This study concisely summarizes services offered by Islamic Banking, then determines potential problems that could be encountered by this new system in the Lebanese economy.

(74 pages)

Glossary: *

Murabaha:

This is a contract sale between the bank and its client for the sale of goods at a price which includes a profit margin agreed by both parties. As a financing technique it involves the purchase of goods by the bank as requested by its client. The goods are sold to the client with a mark-up. Repayment, usually in installments, is specified in the contract.

Mudaraba:

This is an agreement made between two parties: one which provides 100 per cent of the capital for the project and another party known as mudarib, who manages the project using his entrepreneurial skills. Profits arising from the project are distributed according to a pre-determined ratio. Any losses accruing are borne by the provider of capital. The provider of capital has no control over the management of the project.

Musharaka:

This Islamic financing technique involves a partnership between two parties who both provide capital towards the financing of a project. Both parties share profits on a pre-agreed ratio, but losses are shared on the basis of equity participation. Management of the project may be carried out by both the

parties or by just one party. This is a very flexible partnership arrangement where the sharing of the profits and management can be negotiated and pre-agreed by all parties.

Quard Hassan:

An interest-free loan given either for welfare purposes or for bridging short-term funding requirements. The borrower is required to pay back only the amount borrowed.

Riba:

Literally, an increase or addition. Technically it denotes, in a loan transaction, any increase or advantage obtained by the lender as a condition of the loan. In a commodity exchange it denotes any disparity in the quantity or time of delivery.

Shariah:

Islamic canon law derived from three sources - the Quran, the Hadith (sayings of the Profit Muhammad), and the Sunnah (practice and traditions of the Profit Muhammad).

Zakat:

There are two types of Zakat:

- Zakat al fitr, which is payable by every Muslim able to pay, at the end of Ramadan (the month of fasting).
- Zakat al maal is an annual levy on the wealth of a Muslim (above a certain level). The rate paid differs according to the type of property owned. This tax is earmarked, among others, for the poor and needy.

**(source: Islamic Banker, May 1997)*

Chapter I

Introduction

In recent years, the world has witnessed active movements in the Islamic world: political, social and economic. Our main interest is to follow these movements on the economic side; Muslims proclaimed that an economic system based on the principles of the Islamic law is feasible even after fourteen centuries of the emergence of their religion. In order to practice what they preach, Muslims have decided to put the system into effect. And the major movement that was realized is the establishment of Islamic financial institutions and other business enterprises. The basic purpose of this research is to detail and discuss one of the Islamic financial institutions which is the Islamic banking system, whose main operations and services do not oppose the Shariah. The Shariah position is quite simply that if you lend money, then you do not get interest at all. However, if you want to go into a venture with him, then you share in the risk with him. In the Islamic system the capitalist enters in the risk with the party doing the work, while in the Riba system (see the glossary for definition), the owner of the capital puts his money at no risk at all. The basis

of Islamic banking is therefore risk-sharing, hence the profit-or-loss system (PLS).

This document contains five chapters, a bibliography, and three appendices.

The first chapter, which is the introduction, is subdivided into two major parts; the first part gives us a general definition of Islamic Banks, their objectives and their aspects. And the second part covers the features of Islamic banks which are the interest and the Zakat.

The second chapter, justifies why this paper was to be conducted and provides information about the establishment and the evolution of the system in countries like: Pakistan, Egypt, Kuwait, Iran, Bahrain, and Saudi Arabia.. Islamic Banks became a necessity for Muslim people who believe in their religion and want to live in subordination to the Islamic beliefs and values, moreover it is to be introduced to Lebanon sooner or later. These potential customer who want to deal with such a system, don't know how it is operating, therefore this study was necessary to explore the justifications behind establishing an Islamic Bank.

In the third chapter, two main objectives to be met were listed. The first one is to list and define the operations and services offered by the system which are mainly: Musharaka, Murabaha, Mudaraba, Mutajara, Ijara, and social services. And the second objective is to determine the problems that might face the system if it is to be introduced in the Lebanese economy. That include:

legislative problems, competitions with the commercial banks and the relation with the central Bank.

The fourth chapter talks about the methodology that was adopted throughout the research, in order to meet the two objectives of the previous chapter, interviews were held with religious figures in the country, with the First Vice Governor of the Central bank, with the manager of external relation in Banque du Liban (Banque Du Liban is also referred to throughout this research as the Central Bank), with deputies in the parliament, and with researchers that have been conducting similar research. In order to support this research, many readings were done from books available in Lebanon, and from books, magazines, and articles imported from London and Saudi Arabia.

The fifth and the last chapter of this research includes the results and the recommendations. The appendices are attached to this thesis due to their pertinence and relevance for any further research in this field.

A part of this research is going to tackle the different features of a new financial system which is trying to find its own way and its own position in the international financial market. This financial system is the Islamic Banking System whose main purpose is to exclude interest, known in Islam as "Riba", from the financial transactions and relations among the different sectors in the whole economy.

The economy as we know it today is mainly the heritage of the western commercial practices. Following the commercial revolution and mainly following the industrial revolution, the west gained more amplitude in the

world's economy. Thus, subsequently western culture had an increasing effect on the world's commercial culture till the stage was reached where the world's economic and commercial concepts are the pure results of western thought (Al Shirazy, 1994, p 9).

Before going any further we have to define what is meant when using the word "western"; this word is used to refer to Europe and U.S.A starting the late 18th century. The west's concept of an economy consists of factors of production and of products. Therefore, one of the most important pillars of this economic system was the rate of return which measures the success of any commercial transaction. What I do mean to say is that the economic and commercial cultures took a deviant trajectory from that of human culture in the sense that the purpose of the commercial-economic culture is its continuity and self perpetuity. This represents the view of many people and many scholars that reproach to the western economic and commercial culture its lack of humanity (Al Shirazy, 1984, p 15). Furthermore, during the past decade many scholars predicted the collapse of the western financial and monetary system that was gradually being metamorphosed to rely on financial and money market instruments that increase wealth through denominating values to instruments that are not very much attached to any physical presence of any assets that denominate future value allowing speculation. And this fact will allow entire sectors of the world's economy to rely on debt and to proliferate on speculation and interest. This issue is of a very controversial nature and historical precedents till present proved neither right nor wrong. However my aim is to

show that many people share this vision of the world's economy and among those are the adepts of Islam.

Islam for Muslims organizes the believer's relation with God as well as his practical life. They believe that Islam includes the norms for any social conduct and activity among which is commerce or the economy from Islam's perspective. The western hegemony has to be repelled and Muslims have to go back to Islam to organize their practical life. From this logic there was a necessity to develop the economic and commercial concepts that abide to shariaa (Qur'an, Sunnah, Ijmaa') in order to form an Islamic economy (Chambour, 1997). And what is meant by Islamic economy is an economy that doesn't contradict the teachings of Islam. The major point within this context is the interest concept for that according to Islam interest is one of the ugliest facets of the inhuman economy as we know it today. Muslim believers argue that Islam provides the basis for commercial and economic activities that are fair in the sense that they include the human factor as a moral goal where the benefit of humanity should be the ultimate goal of any economic activity and where this human factor is not considered only as one of the factors of production. It is fair to say that western scholars acknowledge this lack of humanity but concluded that out of this conglomeration of selfish individual acts a positive social impact will be distilled through the incremental creation of wealth (Chambour, 1997). Therefore there was the need for financial institutions that could operate conformingly or in a non contradictory manner with the Shariah. From this perspective we can say that there is an Islamic

financial activities but not an Islamic banking sector in the sense that the word banking is inconsistent with the activities performed by a financial institution that performs Islamic financial activities. Furthermore the word banking comes from the Latin, western and Judeo-Christian commercial concepts. This objection was raised by many Islamic scholars who just wanted to show that the use of the phrase “Islamic banking” was just for practicality services despite the contradiction in principles (Al Sadder, 1990, p 16).

Before going into details with objectives, aspects and features of Islamic banking, we have to give an overview about the time value of money in the western and in the oriental culture, and the money multiplier.

Time value of money :

In the Webster’s Collegiate Dictionary, “interest” is defined as: “money paid for use of money lent or for forbearance of debt, a charge for borrowed money that is generally a percentage of the amount borrowed”. In biblical times, interest on money was considered to be usury (Islamic literature makes no distinction between usury and interest, referring to both as “ Riba”). Usury was forbidden between Jews but not for aliens who borrowed money from Jews to develop trade. Generally, the Christian rules relating to interest, as well as to loans, were tied to spiritual rather than economic aspects of society. The interpretation was that interest was usury and therefore forbidden because a greater value was taken from the borrower than was given, resulting in an injustice to the borrower. This view prevailed into the 14th century but was

modified later in order to accommodate industrial and exchange development. Buyers on credit, discounts on bills of exchange, partnerships combining money with labor, and other related dealings gradually were allowed as the influence of the Church declined and the individualism of Protestantism rose (Abdeen and Shook, 1984, p 16). Protestantism advocated entrepreneurialism leading to a growing importance of capital and means to evaluate the marginal benefit that would accrue from lending any accumulated capital to any person in order to invest it. From this point it is quite easy to observe the origins of the concept of time value of money, where accumulated wealth was transformed into money earning assets. On the other hand, the oriental culture viewed the means by which to increase any accumulated amount of money was through the mechanisms of changing hands. So time in the west became the ultimate measuring criteria for profits to be incurred on any accumulated money thus the dichotomy was done between money and its owners. While on the other hand the oriental culture still identified the money with its owners and lenders rather than aggregating the whole of the personally accumulated wealth into what is later to be known as the economy's savings (Taky, 1988, pp. 318-325). Several stages in the philosophical development of the interest concept took place during the 18th, 19th and early 20th centuries. The French Physiocrats, led by Jack Turgot, began the process by distinguishing between money and capital. Turgot argued that the productivity of capital and abundance of capital were necessary for all enterprise and that low money interest rates were both the cause and index of abundant capital (Abdeen and Shook, 1984, p16).

Classical economists, including Adam Smith and David Ricardo, contended that interest was the compensation which borrowers paid lenders for the profit made by use of the borrowed capital. Smith adopted the position that interest was the reward or inducement paid for utilizing savings, and that employing capital in production resulted in an increased value of the product over the labor value. Ricardo on the other hand, attributed all value to labor (Abdeen and Shook, 1984, p 17).

Money multiplier:

Throughout this paper, whenever we refer to conventional bank we implicitly define conventional banks as Fractional Reserve Banking System, which is a system in which banks hold reserves that are only a fraction of their deposits. Speaking of reserves, it is useful to mention that the Required Reserve Ratio, RRR (which is the minimum portion of deposits that must be legally held as reserves) in the USA approximates 18 to 20 % of the bank's total deposits. As to Lebanon, till 1995 the RRR was 60 % and then it was adjusted to 40 % of the bank's total Lebanese deposits. The importance of the RRR stems from the fact that this ratio determines the amplitude of the money multiplier which is the ultimate change in checking deposits (bank money) caused by a \$ 1 initial change in bank reserves: in a simple banking system, equal to $1/RRR$. Since the money multiplier is inversely related to the Required Reserve Ratio, the larger the RRR the smaller is the multiplier and the smaller the multiplier, the smaller is its effect on growth of the money supply, since in each round a bank would have to hold back more and lend out less of

new deposits (Mc.Connell and Brue, 1990, pp. 314-315). What is meant by the definition of the money multiplier, is that each one dollar in deposit will result in a certain amount in loan that is one minus reserve, and this loan will go into deposits again. Aggregating this process, the result would be that this one dollar will be transformed to one dollar plus the amount that is added through the multiplier effect which is $1/R$. So the one dollar will be transformed into $\$ 1 * \text{multiplier}$ or $\$ 1 * (1/R)$.

Objectives and aspects of Islamic Banking

The Islamic Bank is a banking establishment that solicits funds and employs them in accordance with the Islamic Shariah, for the purpose of building Islamic solidarity and insuring justice of distribution and employment of funds in accordance with the Islamic principles. It is a financial, investment, development and social institution that follows Islamic principles in all of its operations and it generally has the following objectives: to remove the burden of the sin of Riba from Ummat Al Islam (Islamic Nation), to promote economic unity, to assist Muslim States, to promote Islamic religious, political and cultural unity, to assist Muslims in the development of their commercial and industrial potential and to provide an innate Islamic basis for full economic

cooperation with the non-Muslim “people of the book” in conformity with the Holy Quran’s law (Abdeen and Shook, 1984, p 171).

The ideology of Islamic banks derives its logic and beliefs from Islamic Shariah and these banks don’t consider their purpose to be only economic but rather spiritual and religious. When accepting deposits, the purpose is not to increase its power to lend and collect interest but to make the Muslims think about savings and to plan for their families future. Due to the prohibition of interest from its operations, Islamic Bank is forced to search for investment opportunities in all sectors of the economy: agricultural, industrial, commercial, service and others, and for investment projects that give a long term social return such as those in infrastructure (Abdeen and Shook, 1984, p 173). These projects are evaluated by the research division which is responsible of preparing the feasibility study and making the appropriate recommendations for the selection of investments. The research department team has to be equipped with technical know-how, knowledge of the market, the financial conditions, and the Islamic principles.

Features of Islamic Banking

The Islamic financial system thus has two basic features: the prohibition of interest and the imposition of the Islamic religious tax (zakat).

1- Interest:

The equivalent of interest in Islam is Riba, which is according to the Sheik Abdul Latif Ziadeh, former judge in the Islamic Court in Tripoli, is defined as the exploitation of the person who is in need of money by taking interest, as a cost of the money borrowed (Ziadeh, 1996). The fact of giving a loan for the purpose of receiving a certain amount of money is deemed, in Islam, an unlawful act. The interest of the cost of money deposited in commercial banks is considered bluntly as Riba, and the depositor must refuse to receive interest on his money or to get any type of benefits (Ziadeh, 1996). Riba connotes the meaning of increase, the verb of which is "yarbu" meaning it increases. This is the general linguistic meaning of the word which is not necessary confined to the act of lending money at interest. But when used in the Qur'an the word is defined by the article "al" meaning "the" in a particular reference to the act of giving money at a fixed increase. Hence, the verb "yurabi" refer to the act of giving loans at a fixed increase, and "murabi" is the person who does such an act (El Ashker, 1987, p 38). Riba is the cause of immorality and other social and economic ills because it breaks the bonds of natural relations between human beings, and it leads to inequality between the lender and the borrower. It unjustly enables the rich to continue to dominate the poor and needy (Abdeen and Shook, 1984, p 164). The prohibition of interest is mentioned in the Qur'an in 4 references:

In the first, the Qur'an states: "That which ye give in usury in order that it may increase on people's property hath no increase with Allah; but that which ye

give in charity, seeking Allah's countenance, hath increase manifold" (Qur'an, 30:39).

In the second, it states that the taking of interest is forbidden and will surely be punished (Qur'an, 4:160,161).

In the third, it states: "Devour not usury, doubling and quadrupling (the sum lent) (Qur'an, 3:130,131).

In the fourth, it states: "Those that live on Riba (interest) shall rise up before God like men whom Satan has demented by his touch; for they claim that Riba is like trading. But God has permitted trading and forbidden Riba" (Qur'an, 2:275). In Islam those who deal with interest the eternal fire penalty is severe. However gains that are derived from trading are permitted because they are the result of risk and effort, and traders are blessed because the seller offers the buyer his commodity in which he invested his labor and his capital (Euromoney, 1979, p 53).

Riba is classified into 2 main types: loan Riba (stipulated in the Qur'an), and commodity Riba (stated in the Traditions).

Loan Riba is referred to in the Islamic literature as Riba al-Jahilia (al-Jahilia is a description of the period before Islam), Riba al-Duyun (Duyun means loans), Riba al-Nasia (meaning Riba associated with the payment period), and Riba al-Qur'an (as stated in the Qur'an).

Commodity Riba is divided into 2 types: Riba which is associated with the exchange of an object for the same kind of object for an increase in quantity

(this is called Riba al-Fadl), and Riba which is associated with the exchange of an object for the same object or for a different object of the same kind with a delayed delivery (this is called Riba al-Nasihah) (Taky, 1989, pp. 10-17).

2- Zakat:

Because of the historical importance of the zakat institution, it is essential to explain briefly its meaning and its role in Islamic economic and social well-being. The exact meaning of the word Zakat is: growth and by extension, growth is the purity of the soul through honest actions and dealings. The literal meaning of Zakat is purity and there is no equivalent word that has the same meaning in other languages. Zakat is a form of tax on the net accumulated wealth, the rate of which ranges between 2.5% (on net worth which includes industrial assets and real estate) and 10% (on agricultural production) (Yakan, 1997).

Zakat is one of the devices to help proper allocation of wealth in the community, Islam is not against being rich, but is concerned how wealth is used; and whenever it is used in ways that do not promote economic development in the community it is highly condemned. The Qur'an states: 'Proclaim a woeful punishment to those that hoard up gold and silver and do not spend it in God's cause. The day will surely come when their treasures shall be heated in the fire of Hell, and their foreheads, sides and backs branded with them. Their tormentors will say to them: "These are the riches which you

hoarded. Taste then the punishment which is your due” (Qur’an, 9:34,35) (El Ashker 1987, p16).

The basis of an Islamic economic system is the belief that God is the creator of the earth and of man whom He has made His vice-regent on earth and it is wrong for a man to treasure money, it should be put to productive use for the good of himself and the community (Proctor, 1980, p 31). Moreover a Muslim businessman would not seek to maximize profits for the purpose of accumulating wealth, money is seen as an agent which may be employed in commercial or industrial investment, it is used as a measurement of the value of physical and financial capital (Metwally, 1987, p 2).

Zakat is the third in importance among the five pillars of Islam, it is obligatory to every Muslim, man or woman in order to satisfy the needs of all those who are unable to help themselves because of some inability one which they have no control. Those who don't pay zakat will be burned with their hoarded wealth on their foreheads, sides and backs in hell. It also subsidizes establishments and works of public welfare for the benefit and progress of the Islamic states. The state does not benefit from zakat and even not impose it ,however, it is the responsibility of the state to watch over the institution in charge of collecting zakat (Najjar, 1996, p 4). Besides its social role, it purifies the soul of the giver, it has been called spending in the name of Allah (God) and it is indicative of its real spirit. It is widely believed by all Muslims that once the able gives Zakat to the poor, God will bless its wealth and may double or triple it in size (Najjar, 1996, p 1).

Chapter II

Islamic Banking

The Islamic economic system is based upon a set of principles found in the Quran. It has to be based on the Quranic concept of social Justice. The Islamic financial system, therefore, cannot be introduced totally by eliminating Riba but by adopting the Islamic principles of social justice and introducing laws and instruments that will help in maintaining justice, equity and fairness.

The Islamic Banking System was established because the Muslims felt that they are in need of a certain banking system which does not deal with interest and does not contradict with "Al-Sharia'a". In this situation, there was an unanimous agreement among the Sharia'a scholars on the issue of preventing Muslims from dealing with interest in order that they do not contradict the Islamic doctrine and for the purpose of keeping individuals closer to their values and customs (Obeidy, 1996).

Therefore, Islamic Banking became a necessity for Muslim believers. The idea came to implementation in many Islamic countries like Pakistan, Egypt, Iran, Kuwait, Saudi Arabia..., the gulf states became the primary

advocates for the proliferation of the system. According to Dr. Obeidy, the introduction of a new Islamic Bank in Lebanon would be a very constructive step toward improving the economic life cycle and enriching the current banking system. Moreover, he stated that this bank should have the opportunity to enter the Lebanese market in order to evaluate its prospective local performance, especially because Islamic banks are expected to decrease the level of unemployment in the economy and to present more investment opportunities to people (Obeidy, 1996). Lebanon is a country where many religions co-exist, however Lebanese Muslims form the majority of the population. Therefore Islamic banking was to be introduced in Lebanon, sooner or later, as it is gaining ground in countries like Pakistan, Egypt, Kuwait, Iran, Bahrain and Saudi Arabia, where the Muslim population has significant demographic weight (Chambour, 1997).

The Islamic Development Bank (IDB) and the Kuwait Finance House (KFH) made the initiative by submitting to the Lebanese parliament a law proposal to establish an Islamic bank in Lebanon in which they will be the main investors. However this proposal was refused and a parliamentary committee was formed to establish a law that would bind and govern any Islamic bank that is to be opened in Lebanon. And what is worth mentioning is that on the 18th of September 1997 the Lebanese parliament voted to postpone the project (Chambour, 1997). Recent studies by the central bank have shown that about \$900 million to \$ 1 billion are being saved by Muslims without depositing them in any financial institutions due to the Shariah teaching where interest is

prohibited (Al Anwar, 1996). Eventhough Islamic banking system is necessary for Lebanese people, the practicality of its implementation is still a controversial matter. Moreover, many Muslim believers do want an Islamic Banking System but don't know how it operates and whether opting to it could be feasible. Therefore, this study was necessary to explore the justifications behind establishing an Islamic bank and to inform about its operations and to discern some of the problems that might face this system in Lebanon.

Furthermore, Lebanese Christians were kind of opposed and skeptical towards this systems and this study could be useful to someone having this skepticism in order to be informed on this issue in a more global manner. One more point to be added is that this study tried to follow the law proposal in the political and parliamentary maze so as to assess the prospects of this project in Lebanon.

Establishment of Islamic Banking System

Until the early part of the 20th century, Islamic banking was subject to many theoretical discussions, It was not possible to initiate a program of practical implementation of Islamic banking on a scale that could produce a solution of the economic problems confronting the world and offer greater social benefits to the Islamic world. Most efforts to introduce Islamic banking in earlier years were through isolated private and individual initiatives. These efforts, accompanied with the huge and extremely powerful operations of non

Islamic banks, were unable to make any significant impact (Mallat, 1988, pp. 47-48). However, the individual and private initiatives in the field of Islamic banking thus provided an excellent example on which the infrastructure of interest free banking could be built .

Few pioneering Islamic banks were established in Egypt in 1963, on a very limited scale, and operated as rural social banks along the Nile Delta. These Islamic banks proved to be worth pursuing and had as an inspiration to people to promote more substantial movements toward a new Islamic economy and financial system (Siddiqui, 1983, pp. 87-88). However and because of the lack of government support to these banks, they suffered from many problem , but the system was revived in 1970 when Egypt and Pakistan proposed the establishment of Islamic banking during the second meeting of the foreign ministers of Islamic countries. The proposal was approved in 1973 and 1974 when the ministers of finance of the Islamic countries held 2 meetings in Jeddah and announced the establishment of the Islamic Development Bank (IDB) and the bank formally opened in October 1975 (Abdeen and Shook, 1984, p 165). The purpose of the IDB is to encourage economic development and social progress of member countries and Muslim communities in accordance with the principles of the Shariah. The bank has many functions such as to participate in equity capital of productive projects in member countries and to invest in their economic and social infrastructure projects. Also it makes loans to the private and public sectors for the financing of productive projects and enterprises in member countries. Moreover, it is also

required to establish and operate special funds for specific purpose including a fund for assistance to Muslim communities in non member countries (Islamic Development Bank, 1975-1976 pp. 2-5).

Evolution of Islamic Banking System

Many Islamic financial institutions are now functioning in various parts of the Muslim world. They fall into two broad categories: they are either Islamic commercial banks or Islamic investment and international holding companies. The first category includes Faisal Islamic Banks in Egypt and Sudan, the Kuwait Finance House, The Dubai Islamic bank, the Jordan Islamic Bank...etc. The second category is having either a national or an international mandate like Dar Al-Mal Al Islami (Geneva) and the Islamic Investment Company (Bahamas) (Siddiqui, 1983, pp. 91-92)

The main objectives of these institutions include the undertaking of all financial operations required by Muslims in the framework of the principals of the "Shariah".

As time passes, the Islamic banking system showed a greater expansion in different Islamic and non Islamic countries. Achievements that have taken place in different countries are the following:

1) Pakistan:

The first attempt at establishing an Islamic financial institution in the modern Islamic world began in Pakistan in the late 1950s with the establishment of a local Islamic bank in a rural area. The process of islamisation of the financial system in Pakistan was initiated in 1979, when the specialized credit institutions in the public sector reoriented their financial activities toward non-interest bearing operations (El Ashker, 1987, p 32).

Many steps were done in order to Islamise the economic system in the country such as: The application of an Islamic taxation system, the establishment of the Zakat institution and the elimination of interest from the financial system and its substitution by a system of profit and loss sharing. However many difficulties were facing the application of these steps, so the government in Pakistan decided to go in several phases (Arabia, 1984, p 44). The first phase was in July 1979, when interest was eliminated from the operations of three institutions:

1) The National Investment Trust, which was established in November 1962 under the auspices of the government to mobilize savings for investment in the corporate sector in order to broaden the base of holdings. After the Islamized conversion, the NIT income from dividends and capital gains increased by 34% in the year 1979-80;

2) the House Building Finance Corporation, which was established in 1952, its interest based transactions were substituted by profit and loss sharing schemes, the scheme has been very well received, and ;

3) the Mutual Funds of the Investment Corporation of Pakistan, which was established in 1966, it has been performing the functions of an investment bank whose main objectives are to develop the capital market and broaden equity investments. After the conversion, the performance of ICP was successful. Small business finance corporations were put on interest free basis added to interest free loans to farmers (El Ashker, 1987, pp. 33-37) . The second phase was done in 1980 when there was the promulgation of the Mudaraba ordinance and the amendment of banking laws to allow for the elimination of interest. In January 1981, all branches of the Pakistan nationalized commercial banks started business based on profit-loss sharing, and an interest free loan (Quard Hassan) was introduced to finance students' studies . By June 1984, \$22 billion had been deposited in Islamic banks accounts. At the beginning of 1985, the entire banking system of Pakistan was converted to the Islamic system. The investment Corporation of Pakistan has offered from 1980 to its investors a sharing account program (Presley, 1988, p 119).

2) Egypt:

After Pakistan, Islamic banks expanded their operations to Egypt by the year 1963 by establishing the Mit Ghamr Savings Bank in a rural area of the Nile

Delta. The operations were based on the same Islamic principles of no interest to depositors or from the borrowers. The borrower had to have a deposit in the bank for a certain period before he could be considered for credit facilities. After that, more and more branches were opened in different parts of the country implying the success of the system. However and because of the changes in the political atmosphere in the country, the project suffered a setback, but was revived in 1971 under Sadat's regime with state funding and a new name, the Nasser Social Bank (El Ashker, 1987, p 38).

After that there was the Faisal Islamic Bank of Egypt who started operations in 1978. It has an impressive performance with total assets in excess of \$2 billion by 1986 and net profits of \$106 million. Faisal Islamic Bank has 24 branches which is the largest network of any Islamic Bank from Iswan to Alexandria in addition Islamic International Bank for Investment and Development which was founded in 1981 as a separate firm has 7 branches mainly in Cairo and Delta. These institutions account for 17% of private deposits in Egypt and pose a real challenge to the four big public Egyptian banks which resulted from Jamal Abdl Nasser Nationalization of the financial system (Presley, 1988, p 125).

3) **Kuwait:**

Kuwait Finance House was established in 1977 and operated on interest free basis from the beginning. It is the largest and the most successful of the

Islamic commercial banks which have been established in the last 2 decade. It accounts for almost one-fifth of total bank deposits in Kuwait, the highest market share of any Islamic commercial bank in a national market. It is the leading Islamic bank in terms of assets and 30th in the league of Arab commercial banks. Only 5 years after being established, the KFH was the 6th amongst Kuwait's banks in terms of deposits (Wilson, 1990, pp. 129-132). The KFH was set up as an Islamic investment bank operating under a special government decree which recognized the Islamic nature of the institution. The government played an important role in the establishment of the KFH subscribing 49% of the paid up capital. Its eight branches in Kuwait made rapid progress and their deposits rose from 149 million Kuwaiti Dinar in 1980 to 474 million (KD) in 1982. Moreover, in 1985, their total assets exceeded (KD) 803 million and its net profit was 17 million (KD) (Presley, 1988, p127). Its success shows that it serves much more than a niche market, and it has aimed to attract customers by emphasizing its Islamic identity while at the same time stressing its modernity. It has aimed to win clients by providing as full a range of banking services as the other commercial bank in Kuwait (Wilson, 1990, p 173).

4) **Iran:**

Islamic banks have begun to play an important role in Iran in January 1984 following a bill approved by the Iranian government in August 1983.

After that date no customer was allowed to open a new interest-earning account or make a new interest-bearing deposit, neither were the banks allowed interest-bearing loans. As of March 1985, interest had been abolished and transactions were conducted on an Islamic basis. The Islamic banking transactions have amounted to over 100 billion Iranian Rial. By October 1983, 20,000 bank employees had attended training courses (Wilson, 1990, p 151)

5) Bahrain:

The Massraf Faisal Al-Islami of Bahrain began operations in December 1982, and in 1985 its total assets had grown to \$677 million with profits of 2.6 million dollar. Moreover, the Bahrain Islamic Bank is also successful; it operates with three branches and accounts for around 16% of total deposits in Bahrain (Presley, 1988, p 130).

6) Saudi Arabia:

Prince Mohammed Al Saud funded the dar Al-Mal Islami banking group which is today registered in the Bahamas, with group administration in Geneva, Switzerland, and a wide ranging of an international network of subsidiaries and affiliations.

Islamic Development Bank in Saudi Arabia represents the only aid institution which operates in accordance with the Sharia law and which was specifically created to bridge the gap between rich and poor Muslims countries. In

addition, Al Rajhi group, the largest chain of money changing establishments in Saudi Arabia, is now a designated Islamic financial institution which claims that all its transactions are conducted in accordance with the Sharia law (Presley, 1988, p 131).

The operations of the Islamic banking system are not restricted only to the Arab world. They have expanded toward the Western countries. For instance, Al Baraka group have their own outlets in London through Al Baraka International Limited which is fully licensed deposit taker (trade union) in the United Kingdom providing a range of mainly trade-related banking services such as documentary credits. A separate investment company run by Al Baraka group has also operated from London since 1983. An advisory office for Islamic investment is also maintained in London by the Saudi Arabian Al Rajhi group through a U.K registered company named Al Rajhi company for Islamic Investments. There are commercial banks in UK and other European countries which serve both interest based and non interest based operations. Most of the Euro-Arab banks; for example, offer Islamic trade and finance on Murabaha basis. The Union Bank of Switzerland adopted an Islamic Unit Trust in 1986 which used the principles of ethical investment to construct a portfolio that would be considered "Halal" for Muslim clients (Iqbal and Mirakhor, 1987, pp. 65-66). Recently in 1994, Chase Manhattan bank in the United States of America has opened a department that works according to Islamic principles.

Moreover, the Islamic Bank International (IBI) in Denmark has recently opened an account in 3 major foreign currencies namely, the US dollar, the

Deutsch Mark of Germany and the pound sterling of UK, and the minimum funds accepted for the opening of these accounts must not be less than \$10,000 or its equivalent. (Mallat, 1988, p 51) .

In addition, the Murabaha financing (see the definition in the Glossary) has gained momentum in Islamic banking operations. For example, Al Rajhi group, London branch, a subsidiary of Al Rajhi Islamic Bank of Saudi Arabia has so far confined its operations to Murabaha with a turn over of US \$3 billion in the first 3 years of operations. Furthermore, in the Islamic bank in Luxembourg, Murabaha financing reached around 37% of its total financing in the year ending 30th of June 1994 (Mallat, 1988, pp. 55-56).

Chapter III

Objectives

The research has two main objectives: the first one consists of defining the operations and services of the Islamic Banking System, and the second one consists of determining the potential problems that faced the Islamic banking System, in countries where it is functioning, and might face the system in Lebanon.

Defining the services of Islamic banks.

The paper's first objective is to list and define the main instruments of Islamic Banking namely: Musharaka, Murabaha, Mudaraba, Mutajara, Ijara and social services. According to advocates of the Islamic Banking System most of the conventional bank services can be provided through the above mentioned instruments, yet with small modifications (Muad, 1997). Therefore they advocate that the system is practical and achievable. It is the purpose of this study to define each individual service provided by the Islamic banking system.

*Determining the potential problems, and their effect
on the market potential*

The second objective is to try to discern the problems that might face and that are facing Islamic Banking. In spite of the great achievements that Islamic Banks have succeeded to reach in different countries, many problems limit their expansion not because of the Islamic Banking System itself, but because of the environment in which they are operating which is in most of the countries-except Iran, Sudan and Pakistan- a non Islamic economic environment. These problems fall mainly into two categories: legislative and cultural. The cultural clash is inevitable for Islamic Banking as it is, is a whole new system based on Islamic doctrine in a world already formatted on a totally different system. Even in Islamic countries (like Iran, Sudan, Pakistan and Egypt), the system faced serious problems, so what could be the extrapolation for a multicultural and multi religious country. Providing a legislation for Islamic banking proved also to be very problematic and controversial. The point was to put this system under the supervision and monitoring of the Central Bank, like any other, yet to ensure that none of the Shariah rules would be violated and all of this should be done under the equity umbrella that should be provided to all by the legislative process. One further point the compatibility of this system with the conventional system in an interactive economy where both have to mutually interact.

Chapter IV

Methodology

Field survey and research.

The same methodology was followed for both objectives; to determine and find the possible problems that might face the Islamic banking system once it is established in the Lebanese market, and to list and define the operations and services of an Islamic Bank. Interviews were conducted with experts in the field, like deputies in the parliament who were and still are following up the case, religious figures, scholars, and researchers in the same topic. First of all I have taken appointments with them, and went personally to conduct the interviews. Many commercial bank managers didn't have any substantial information concerning the subject. Subjects that were discussed had been prepared in advance and were almost the same for all the interviews; Issues of interest included:

- a) a general overview of the Islamic Banking system and its international expansion and evolution;
- b) a general overview of its services;
- c) problems in general that faced the system worldwide in Islamic and non Islamic countries;
- d) specific problems that might face the Islamic banking system if established

in Lebanon and its possible implications on the Lebanese economy and society; e) patterns of behavior of Lebanese people and the interest rate; f) advantages of the System and; g) its applicability in the Lebanese Market.

Interviews were done with:

- Dr. Zouhair Obeidy, former deputy in the Lebanese parliament who is following up the case in the parliament. The interview was held on April 18, 1996 for almost an hour and a half, in Beirut in his office in the “Islamic Jamaa” headquarter.
- Dr. Maher Moraaby, Chairman of Sociology Faculty at the Lebanese University. The interview was held on May 7, 1996 for one hour at the Lebanese University in Tripoli.
- Sheikh Abdul-Latif Ziadeh, former Judge of the Islamic Court in Tripoli. The interview was held on May 24, 1996 for almost half an hour.
- Dr. Fathi Yakan, a former deputy and very influential member in the “Islamic Jamaa” The interview was held on July 25, 1997 for almost half an hour in his office in Abu Samra.
- Mr. Hicham Tabach, Credit and Marketing Manager in Bank Al Baraka . The interview was held on August 17, 1997 for one hour in the bank’s office in Beirut.
- Miss Souha Mu’ad, a lecturer at A.U.B, a scholar and a researcher on this issue. The interview was held on August 17, 1997 for almost half an hour in Bank Al Baraka Beirut.

- Dr. Nasser Saidi, Premier Vice Gouverneur in Banque Du Liban. The interview was held on August 15, 1997 for almost ten minutes.
- Mr. Toufic Chambour, external relations manager in Banque Du Liban. The first and second interview were held respectively on August 25, and September 8, 1997 in his office in Banque Du Liban. The third interview was held on September 14, 1997 in his sister's house in Bechmezzine, El Koura.

Chapter V

Results and Conclusion

The following are the results of the two objectives of the research: to define the operations and the services of the system, and to determine the potential problems and their effect on the market potential.

Operations and Services of the System

The Islamic Banking System, like the commercial banking provides the following services:

Current Accounts:

Like commercial banks, Islamic banks offer current accounts to their depositors for the purpose of keeping liquidity with them and paying checks drawn on them through the normal and international clearing system used by commercial banks. The current accounts are payable on demand, and they do not yield interest or profit to their owners. Unlike some conventional banks, the Islamic system does not apply the value date system to the current accounts. This type of account is an interest-free account (Qard Hassan) as it is considered as a service to the depositors (El Ashkar, 1987, p 123). Islamic banks may open a current account to a second party in any foreign currency;

however the bank retains the right to reject to perform this service for a certain customer without divulging the reason, and this right also exists for conventional banks (this account must be in credits all the time and there will be no over drafts).

Saving Accounts:

The saving accounts excluding blocked accounts, are payable on demand. The procedures and formalities used for depositing and withdrawing are almost identical in both systems. However, in the Islamic bank, the depositor who opens a saving account may or may not give the bank the right to invest the deposited money (Wilson, 1990, p 29). Due to the fact that interest is prohibited in Islamic banks, profits or losses are incurred achieved from investing a certain part of these types of deposits in short-term projects or investments. Usually, the profits of saving accounts are less than the profits of fixed investments deposit accounts because of the short range nature of the projects the funds are allocated to and because the saving deposits can be withdrawn on demand at any time. But savings account are less risky; the account fund cannot be reduced by any losses the bank may suffer. However, if the depositor chooses not to give that right to the bank, the saving account would be similar to a current account, and a check account may be used (Abdeen and Shook, 1984, p 175).

Investment Deposit Accounts:

The investment deposit accounts are also called “Islamic Participating Accounts”. Islamic Banks accept deposits in the form of investment accounts, and invest the deposited funds on behalf of the depositors in economic sectors or projects whose operations conform to Islamic principles. The investment deposits are entitled to a portion of the return on investment according to the amount of the deposit and the time involved. For this reason, the investment accounts are grouped into two main kinds: specified and unspecified. (The account also bears its share in losses).

In the specified accounts, the depositor authorizes the bank to invest the deposited sum in particular projects or sectors. Therefore, these accounts are sometimes called “conditional” or “limited investment accounts”, for they are assigned to specific projects or sectors (Wilson, 1990, p 32). In the unspecified accounts, the depositor gives the Islamic bank an unconditional authorization to invest the deposited money without any restriction as to projects or sectors. These accounts are held for short-term periods (ranging from three to twelve months), or for long term period (up to 5 years).

Financial services:

With the conventional banking system loans are performed through a simple financing mechanism where the banks act as financial intermediaries by accepting deposits from people and lending them to the borrowers, regardless

of whether these borrowers are individuals or business entities. In this system, the main profits of the bank are gained from the difference between the interest earned from borrowers and the interest paid to depositors (Wilson, 1990, p38).

With the Islamic banking system, the bank's profits are earned in a different and a more complicated way. In this system, money does not earn money without a collaboration between capital and effort. Therefore, depositors do not earn an automatic fixed return on their deposits as in the conventional system. The expected earnings of depositors are directly related to the profits earned by entrepreneurs (Khan and Mirakhor, 1987, p 76). Moreover, financing instruments vary to suit the financial needs in the market and to provide short, medium and long-term funds. These Islamic instruments are: Mudaraba, Musharaka, Murabaha, Mutajara, Ijara and social services.

Mudaraba:

This mean of financing is the Mudaraba or "capital trust" which was a pre-Islamic custom used to finance a significant portion of the caravan trade in the Arabian Peninsula, where the savings of the elderly, women, children and sick people were given to merchants of the Quresh tribe for an agreed-upon part of the generated profit from certain trade or venture activities. The Mudaraba is a contract in profit sharing, with one party providing funds and the other the work. These operations tend to concentrate on small businesses that depend heavily on expertise with small capital such as small art and craft workshops. The Mudaraba is a contract between two parties: The

Islamic bank as the investor (Rabbal-Mal) providing a second party, the entrepreneur (Mudareb), with financial resources to finance a particular project. In this case, profits are shared between the two parties in a proportion agreed upon in advance, profits range on average between 20 % and 60 % and may be distributed during or at the end of the contract. Any profits received by the Mudareb become his, even if a loss occurs later. Losses are the liability of the bank, and the Mudareb loses only his efforts and his expected share in profits (Tabach, 1997). The Mudaraba is adopted in different medium to long term project trade financing. If the partners of the Mudaraba want to renew it, a new contract must be negotiated, but only after the old one has been terminated and the rights and liabilities of the parties concerned have been reached. Moreover, before the liquidation and the distribution of profits, the Mudareb possesses the right not only to his share in the profit but also to any gain or appreciation in the value of the output or the assets that might occur during the life of the Mudaraba contract (Khan and Mirakhor, 1987, p 78).

Mudaraba might be considered as a solution to the economic dilemma of how the owner of monetary assets and the businessman can be brought together on common ground, it coordinates the interests of the two parties and fits the objectives of Islamic system. It also offers an opportunity for collective investment to those who lack managerial, technical skills, and the ability to take risks because of the small size of their savings (Abdeen and Shook, 1984, pp. 188-189).

Musharaka:

The second mean of financing is the Musharaka which is a well established partnership contract in Islamic law and was operating in the early Islamic period. The Musharaka financing ranges from 7 to 10 per cent of the total financing instruments of Islamic banks. The Musharaka is also a contract between an Islamic bank and a customer or business entity for achieving certain operations and may terminate within a specified period of time or when certain conditions are met (Tabach, 1997). The customer has to provide extensive data to the bank on entrepreneurial results, capital structure, balances, profit and loss records, and income records covering the last 3 years. Moreover he shall provide a description of the project to be undertaken, stating the capital to be provided by the bank, and estimates of profits for each yearly quarter for as long as the project is to run (Khan and Mirakhor, 1987, pp. 80-81). Unlike the Mudaraba, the two partners in the Musharaka participate in the capital of the project. Profits are shared and allocated according to an agreed proportion, these shares are not uniform in all cases; for example, a client may participate with the bank in financing a commercial or industrial project whereby he contributes 25% and the bank 75% of the needed capital. The agreement provides that the client manages the project, and in return he receives 20 - 40% of the actual realized profit. It would be expected that the greater the amount of work and the higher the level of expertise, the higher the percentage. However, if losses occur, they are distributed on the partners in proportion to

their contribution to the capital (Tabach, 1997). So as we can see the difference between Mudaraba and Musharaka lies in the fact that in the Mudaraba, the Mudareb bears the loss; the entrepreneur loses the reward for his efforts but does not bear any of the financial loss as long as he is not negligent (in case of negligence, the entrepreneur has to repay the original sum to the Mudareb). While in the Musharaka, if the business incurs a loss, both parties bear the loss. As the profits and losses need to be recorded, only those companies with regular bookkeeping are eligible for Musharaka contracts. The bank here doesn't usually interfere in the business unless the profit drops below the planned level, though this depends on the amount of capital supplied by the bank. In all cases, the bank maintains the right to inspect business operations with a direct access to accounting records, and to ask for guarantees and collateral from the client, not in the capacity of the client as a participating partner but as a manager of the project, in order to assure the bank of honest and efficient management (Wilson, 1990, p 186). The Musharaka does not guarantee a fixed return for the partner; it also finances private or public companies for both short and long-term periods. The Musharaka consists of two main types of agreements:

- 1) Musharaka related to certain projects and terminating with the project's completion; and 2) The redeemable Musharaka which could be renewed after the mutual assent of both parties. This renewal is usually done when the project is still beneficial for both the bank and the customer.

Murabaha:

The third financing instrument in Islamic banks is the Murabaha which is mostly for short term operations, it is a resale contract named by jurists as “Bai Maujjal” or deferred sale. It is used for financing the purchase or import of capital goods, consumable goods, raw materials, or equipments (Tabach, 1997). In the Murabaha, the customer provides the bank with the specifications of the goods to be purchased, and the Islamic bank studies the documents with reference to the price, specification, and conditions for payment. In many cases the bank may be able to obtain the same goods or equipments at more favorable conditions than those obtained by the customer. After the agreement of both parts, the bank and the customer, on the terms of the deal, the bank purchases the goods or equipments, and the customer receives the ownership at a later date when the installment of value of the deal has been completed (Khan and Morakhor, 1987, p89). The sale price which is agreed upon in advance is calculated as follows: purchase price + mark up = sale price. We should note here that the mark up is not the same for all the operations, when calculated, many factors are taken into account such as the profitability of the commodity (the higher the profitability the higher the mark up), the necessity of goods to the average consumer (mark ups on alimentary goods are lower than those on other goods), the amount of work involved (imported goods have higher mark up than locally purchased goods), and the degree of risk involved (risk from buying goods abroad is higher than risk from buying locally). The average annual mark up rate is between 10 and 15% (El

Ashker, 1987, p 132) . Payment by the client may be made in installments and the bank may ask for collateral or some other guarantee. However the bank should not increase the price of the sale in any circumstance, and if the client makes a late payment he should not be penalized with an extra charge . In case the banks succeed in getting a discount on the purchase price, the bank should notify the customer and safeguard his rights. This method is most suitable for commercial operations and corresponds in a way to trade credit. Usually, the credit is provided for a period between 3 and 6 months. Murabaha has been criticized that it may open the door for dealing on fixed interest basis under the name of mark up. However, Islamic banks believe that Murabaha is not a risk-free operation because there is a risk during the purchase transaction due to unacceptable quality, delivery delay,... and a risk during the collection of debt. Moreover, and since the client is not in the same position as the bank in obtaining discounts from suppliers, the sale price offered by the bank to the client will be lower than the price the client would pay if he depended on commercial banking finance. Adding to this, the client benefits from the speed at which these transactions take place because Islamic banks pay quickly and without risk to the suppliers, and save them from having to arrange trade credit themselves on behalf of their Islamic clients with their ordinary banks (El Ashker, 1987, p 133). In Murabaha operations, the bank does not necessarily handle the goods physically, they are directly sent to customers. The bank only takes the paper work as a proof of its ownership until the client pays off his debt. If the client refuses to receive the goods, without reason, the bank has the

right to sell them in the open market, deduct its due from the proceeds and refer to the client with difference, since the goods were purchased in the first place at the request of the client (Tabach, 1997).

Mutajara:

The fourth financing instrument is the Mutajara which is very close to Murabaha. Mutajara arises when the client finances the purchase of the goods by using his own funds, and the bank acts as an agent which charges a service fee only (Khan and Mirakhor, 1987, pp. 95-96).

Ijara:

The fifth financing instrument is the Ijara which occurs when an individual or a company requests the bank to buy a certain equipment that the client intends to rent. When there is an Ijara financing, the bank evaluates the financial position of the client and the expected inflows of the lease contract in the same way as in lease financing in a conventional bank with one difference which is the exclusion of interest (Khan and Mirakhor, 1987, pp. 99-100).

In the Islamic Banking System there are two types of leasing: 1) the direct leasing finance that occurs when the Islamic bank allows the client to use a certain amount of the bank's funds for a limited period of time ranging from few days to few years. The bank purchases a capital asset and leases it to the lessee in return for an agreed upon annual or monthly rent; and 2) the lease and purchase finance which is also called Ijara Wa Iktina, and it occurs when the Islamic bank buys the capital asset and rents it to the customer who promises

to purchase the asset within a certain period. The rental payment may be either a certain fixed amount or a combination of a certain percentage of the profits generated by the asset and the rental charge. When the total rental charges equal the cost of the asset, the asset ownership will be transferred to the lessee.

The transfer of the ownership of the assets depends on the nature of payment. If the two parties agree on a lump sum payment, the transfer of the ownership to the lessee when the amount agreed upon is paid. However, if the lessee is to pay the price on an installment basis, the transfer of the ownership will be gradual and the bank's title decreases proportionally, as well as the rental fees. with the successive payments (Iqbal and Mirakhor, 1987, pp. 187-189).

Social Services:

The other main part of the Islamic Banking operations is the social services which include a) beneficial or Benevolent loans (Kard Al-Hasan), b) Funds for social purposes, c) Zakat and donations, and d) other social services . it is important to notice that Islam prohibits interest, but it allows, lending and borrowing of money among people for the purpose of helping needy people. these loans are payable within a specified period either by installment or lump-sum amount (Khan and Mirakhor, 1987, p102).

a) The most important and used social services in the Islamic Banking System is the Benevolent or beneficial Loans, where the bank does not expect any direct return when these loans are made . This service embodies one of the most important objective of Islamic Banking which is the economic welfare of

society. Benevolent Loans are made for productive purposes in various fields in order to help the needy people to start independent lives and to raise their standard of living, and to help needy students (Repayment starts two years after the completion of studies and is to be finished within ten years) (Al Shirazy, 1994, pp. 198-201).

b) Funds for social services have independent management and their accounting will be separate from the accounting of the other operations of the bank. Almost all the existing Islamic banks offer these funds, for example the Islamic Development Bank allocates funds for the Islamic Research and training Institutes, the war refugees in many countries around the world, the educational assistance to schools and colleges in occupied Palestine and other countries, for special assistance for construction of mosques and for many other Islamic causes (Al Sader, 1990, p 165).

c) Zakat and donations are collected from individuals and organizations by Islamic banks, and special departments will be responsible of distributing the zakat on their behalf in accordance with the Islamic Shariah. The amount of Zakat may be distributed to deserving individuals either by the government who receives the Zakat amount from the Zakat fund of the country, or directly by the banks (Al Sader, 1990, p 169).

d) Other social services offered by the banks include social, cultural, scientific, educational, and health services. The Islamic banks may lend money on an interest-free basis to a number of beneficiaries which might include: a) depositors who maintain regular accounts; b) shareholders; c) companies or

clients who have already been financed by the bank; and d) education, marriages, and other social purposes.

Problems facing the system.

Problems that faced the Islamic Banking system, in countries where it is applicable now, and might face the system in Lebanon are determined as follows: legislative and cultural problems, competition with conventional banks, interaction between Islamic and conventional banks, and lack of planning.

Legislative and cultural problems

Islamic banks faced in many countries major problems at the establishment and branching out phase. In order to open an Islamic bank in any country, a special law must be promulgated by the legislative authority, which is not always easy. For example in Syria, the Damascus government has refused to let any Islamic institution challenge the monopoly of the state owned Commercial Bank of Syria. In Iraq, the negotiations with the Kuwait Finance House about opening a branch in Baghdad have been stopped because of the recent Gulf war (Wilson, 1990, p 198). Moreover, many countries adopting the conventional banking system are either refusing or discouraging the establishment of Islamic banks on their territories because of religious and ethnic causes like in France or due to political causes as in many Islamic

countries like Algeria and Tunisia where the Muslim fundamentalists have threatened the local governments.

Problems may arise when Islamic banks are established especially in a non Islamic social environment. In many countries, the Central Bank obliges the commercial banks to invest a certain amount of money in governmental securities. This issue creates a big problem for Islamic banks since their principles prevent them from dealing in any kind of securities that generate predetermined interest or Riba (Tabach, 1997). In addition to this difficulty, many other problems between Islamic banks and the local Central Bank will also appear such as the federal funds and the legal reserve issues. With relevance to Islamic banks from the legislative perspective, and if the proposed law doesn't set a required reserved ratio, regardless of the fact that Islamic banks don't aggregate their deposits and then lend out of them, so, in this case the money multiplier effect will be ambiguous in the amplitude. This ambiguity results from the fact that if Islamic banks were left with the freedom to determine the reserve amount, if any, to be held from each deposit, then the money multiplier will be the aggregate result of those bank determined reserves, thus the multiplier will change according to the bank's will and with it will change the Central Bank's ability to control the money supply. Again if Islamic banks would still operate under the fiduciary deposit legislation, then these activities will be considered as off balance sheet activities, then their deposits will not be subject to reserve rate requirements leading to the same result where the Central Bank will not be able to control completely the money

supply in the market by increasing or decreasing the legal reserve, or the discount rate (Obeidy, 1996). The Lebanese legislative process began in January 1996 when the fiduciary deposits law was passed allowing the Al Baraka Bank to offer Islamic Banking instruments while operating as a conventional bank. This was done by accounting to these operations as off balance sheet activities. This process was incomplete and did not satisfy neither the Central bank, who was not quiet satisfied with the accounting treatment of the bank's activities as off balance sheet, nor those who wanted an Islamic bank because Al Baraka bank activities in Lebanon didn't conform totally with the Shariah and we are referring to Shariah as the basic teachings of Islam based on Qur'anic texts which specifically forbid dealing with interests, on this reference, there is a general consensus on the part of Islamic scholars. The second step was mentioned earlier; when the Kuwait Finance House and the Islamic Development Bank submitted a law proposal that was rejected then a parliamentary committee was formed and came up with a new law proposal that was to be the basis for monitoring and regulating any Islamic bank to be opened in Lebanon. Again this proposal was subject to controversy and criticism and it was postponed on the 18th of September. The main reason for the law proposal's postponing was that the Central Bank didn't quiet approve of it since it wanted a foreign institution (like Kuwait Finance House) to be the guarantor of such a bank, especially that their deposits are not protected by the deposit insurance funds. Furthermore, many experts in the field criticized the proposal because according to their view it diminishes the Central Bank's

authority and blur the authority lines especially between the central bank's prerogatives and that of the committee to be formed (the committee consists of monetary and Shariah experts).

The following are: 1) the proposed plan for establishing an Islamic bank in Lebanon with the cooperation of Kuwait Finance House (KFH) and the Islamic Development Banking (IDB); and 2) the difference between the old and the new proposal law.

A proposed plan has been put by the KFH with the cooperation of IDB to establish an Islamic bank in Lebanon. The proposed plan consists of establishing a Lebanese corporation through a special decree and this corporation is to be known as Kuwait and Lebanese Finance House, and we will refer to it as "the company" throughout the text.

The company's activities:

- The company will perform banking operations that don't operate on the basis of predetermined interests. Also the company will perform investments, financing, exchange, fiduciary operations and all the operations that can be described as Islamic banking tools namely Musharaka, Murabaha, Mudaraba and leasing. The company will perform its operations either for its account or for the account of 3rd parties, and those operations will be done either from the company's private funds or from the clients deposits and this is to be done in a manner that do not contradicts with the Shariah.
- The company has to put at least 30 % from the company's capital and funds into investment in Lebanon.

- The company has the right to deposit the excess money in any currency, at the Banque Du Liban (BDL) also this latter has the same reciprocal right. And those transactions are to be done according to an agreed upon system that is to be made by BDL.

The company's legal framework:

- The company is to be exempt from the first two paragraphs of the article 152 from “ قانون النقد والتسليف “ or “Legislation on Money and Credit“ and it is permitted for the company to go into partnership and contribution investments without abiding by the decree 153 of the same law.

- The company has to abide by all the laws and decrees and those of the “ قانون النقد والتسليف “ , the commerce law and the bank secrecy law.

The company's monitoring:

- The central administration of BDL and the banking monitoring committee have the responsibility and the right to set and adjust all the legal elements that are related to the budget and its different branch outs. This is meant to insure the good relations between the company and its depositors as well as those dealing with it so as to preserve the company's liquidity and good performance.

The company's operations:

- The company can acquire physical assets including real estate to achieve the objective stipulated within the law in condition that the acquisition period do not go beyond 20 yeas.

The company's capital:

- The company's capital was determined to be \$50 million to be divided as 40 % owned by the KFH, 20 % owned by the IDB and the remaining 40 % will be subject to subscription from the part of Lebanese companies and individuals. No single investor other than the KFH and the IDB has the right to possess directly or indirectly more than 5 % of the company's capital.

The divulge of the company's information:

- The company has to inform its customers and to get their approval when she is doing any consultancy work for the benefits of its agents.

- The company has to write down its operations and the implementations of these operations on a daily basis and in a detailed accurate manner. This also applies when the company is doing operations for its own account. As for the operations for any 2nd party, the central administration of BDL and the bank monitoring committee will provide samples of the necessary paper work to write down these operations in an accurate detailed and traceable manner so as to be able to show all the information needed to all those that are concerned.

The founding and the management company:

- The company's founder committee consists of :

- a representative of KFH.
- a representative of IDB.

- an appointed representative from the part of the Ministry of Finance.

This committee will establish the company's rules and regulations that have to get the approval of the BDL central administration.

The company's consulting committee:

The founding committee and henceafter the regular committees will appoint a consulting committee that consists of 3 specialized advisors in the Shariah and in monetary and banking transactions. This appointment will be for 3 years and is renewable. The committee's duties will consist of reviewing the regulations, operations and contracts to make sure that nothing will be contradictory with the Shariah. Furthermore, the committee would submit suggestions to the stockholders committee and the company's board of directors for the same reason mentioned above. Also it has the right to review any demand that is submitted to it by any second party dealing with the company and thus providing the appropriate recommendation to the company's management.

The parliamentary committee that was responsible to study the KFH and IDB proposal issued a law proposal for establishing any Islamic bank in Lebanon. This proposal was submitted after rejecting the KFH and IDB proposal. The 2 proposals were very similar however the first proposal was meant to establish a branch of the KFH in Lebanon with the cooperation with the IDB. The second was meant to form a legal framework upon which Islamic banks would operate in Lebanon. Another major difference was that 30 % instead of 40 % of any

Islamic Bank stock has to be owned by Lebanese nationals. Furthermore not one person can directly or indirectly can acquire more than 10 % of the company's stock while in the KFH proposal 60 % was to be owned by KFH and IDB and 40 % by Lebanese companies and individuals. (source: Souha Mu'ad, 1997)

Competition with conventional banks

From the most serious obstacles limiting the expansion of Islamic Banks is the competition with conventional banks. People who are used to dealing with conventional banks for a long period of time find it difficult to deal with a new system whose principles are vague or new for them. In addition, people who are generally risk averters prefer to earn fixed interest rates rather than unknown and variable profits or losses. This is because of the misunderstanding of the real concept of the Islamic Banking System along with the inadequate available information concerning the operations of these banks (Chambour, 1997).

The interaction between Islamic and conventional banks

Other problems facing Islamic banks operating under a non Islamic banking system result from the relationship between the Islamic and conventional banks. Business relations among depositors in both Islamic and conventional banks imply financial transactions between those two different kinds of banks. These transactions like check clearing, and money value of

drafts, usually involve interest rates which violate the basic principle of the Islamic banking system (Chambour, 1997).

The absence of a complete network of Islamic banks around the world is also another disadvantage to the new system since it creates a problem for those banks: for example, many depositors who are willing to import goods from foreign countries should open a credit letter. Other depositors in Islamic banks want for example to transfer a certain amount of money to their parents or friends in other countries (Moraaby, 1996). These two and other possible cases oblige the Islamic banks to cooperate with conventional banks in different countries to fulfill their transactions. This cooperation forces Islamic banks to enter the world of interest which contradicts with the basic elements and principles on which Islamic bank exist.

Lack of Planning

Moreover, another drawback to the Islamic banking system is the lack of planning that threatens Islamic Banks by causing serious financial problems for some banks and by destroying the reputation of others. An illustration of this lack of planning occurred in Kuwait with the "Kuwait Finance House" in Souk El Manakh in Kuwait in 1987. During that year, the "Kuwait Finance House" which is an Islamic bank was offering to its depositors a profit level of 15% while the interest rates in Kuwaiti conventional banks were only around 4%. In addition to that, one conventional bank went bankrupt and the whole chain of conventional banks in Kuwait was affected. Thus, a big number of people

withdrew their deposits from the conventional banks and deposited them in the “Kuwait Finance House”. This wide transfer of funds caused a surplus of money in that Islamic bank which was not prepared for such a case. In this situation “The Kuwait Finance House” was obliged to store huge amounts of uninvested funds because the bank was neither allowed to deposit funds in other institutions nor permitted to give loans on an interest basis (Beauge, 1990, pp. 55-56). Then, the profit generated by the bank’s investments during that year was quite low especially after the distribution of profits among all the depositors. and the average profit was less than 3 %. As a result, a real problem has risen for both the bank and the depositors and caused the bank’s crisis.

Recommendations:

Islamic Banking in Lebanon like in many other countries, faces many problems even before its establishing. this problem has a larger amplitude in Lebanon since it is a multicultural and a multi religious country. The legislative maze in which the Islamic banking law passed is a clear illustration of the political factors that were intermingled in this legislative process. Islamic banking in itself could be a viable and a practical system if the proper legislation permits it to be established and then soundly regulates its activities

to ensure the proper functioning of this system. Islamic banking needs to be developed in the sense that it needs to fine tune its services and policies in order to be more interactive and competitive with commercial banks in an economy that is going global by the day. Furthermore, advocates and practitioners of such a system should find better means of communication with the populus to properly convey the purpose, functioning, and practicality of the Islamic Banking System. Again the importance of this latter point should be emphasized in a country where there was a religious civil war for over 17 years and where prejudgments proliferate on the very fertile ground of sectarianism and fundamentalism.

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Appendices

Appendix A

مشروع قانون

يتعلق بإنشاء "بيت التمويل اللبناني-الكويتي":

المادة ١:

تنشاء شركة مغلقة لبنانية تسمى "بيت التمويل اللبناني-الكويتي" شركة مغلقة لبنانية منشأة بموجب قانون خاص، تعرف فيما بعد بالشركة، موضوعها القيام بالتالي:

-العمليات المصرفية غير المستندة إلى تحديد مسبق للفائدة.

-عمليات التمويل والاستثمار والتوظيف والصيرفة والمساهمات والمشاركات وإدارة الأموال والتركات والصناديق وعمليات الإيجار التمويلي والعمليات الائتمانية. تجري "الشركة" عملياتها، سواء لحسابها أو لحساب الغير، من أموالها الخاصة، ومن الودائع المتلقاة من الجمهور على سبيل التملك أو الإدارة، وذلك على النمط الذي لا يتعارض مع أحكام الشريعة الإسلامية.

المادة ٢:

تعفى الشركة من موجبات أحكام الفقرتين (١) و(٢) من المادة ١٥٢ من قانون النقد والتسليف. ويجاز لها إجراء المشاركات والمساهمات دون التقيد بأحكام المادة ١٥٣ من القانون المذكور. يكون للمجلس المركزي لمصرف لبنان ولجنة الرقابة على المصارف أن يحددا ويعدلا كلما رأيا ذلك ضروريا، قواعد تسيير العمل والنسب الواجب توافرها بين مختلف عناصر الميزانية وخارجها والتي على الشركة الالتزام بها لتحقيق أغراضها، ولتأمين حسن علاقتها بمودعيها والمتعاملين معها وللحفاظ على سيولتها وملاءتها.

المادة ٣:

للشركة أن تكتسب الحقوق العينية والعقارية لتحقيق أغراضها المنصوص عليها في هذا القانون، شرط أن يحصل الاكتساب بموجب ترخيص مسبق من المجلس المركزي لمصرف لبنان الذي عليه أن يتحقق من جديته وان يحدد في ترخيصه اجل التملك بحيث لا يتعدى في مطلق الأحوال العشرين سنة.

تعفى الشركة من الحصول على التراخيص القانونية المتعلقة باكتساب الأجانب الحقوق العينية والعقارية في لبنان وذلك بعلم مديرية الشؤون العقارية في وزارة المالية وإطلاعها.

المادة ٤ :

يتعين أن تتمثل ٣٠٪ على الأقل من عناصر الأصول والحقوق المبينة في ميزانية الشركة وخارجها باستثمارات و توظيفات في لبنان.

للجنة الرقابة على المصارف أن تقدر ما إذا كانت بعض العناصر تدخل في النسبة السابقة أم لا. و لا يخضع تقديرها في هذا المجال لأي طريق من طرق المراجعة.

المادة ٥: حدد رأسمال الشركة بما يوازي خمسين مليون دولار أميركي.

يمكن زيادة رأس المال ، مرة واحدة أو مرات عدة وفقا" للأصول المعتمدة بزيادة رأسمال المصارف التجارية . على أن تحفظ "بيت التمويل الكويتي " و "البيت الإسلامي للتنمية " على دوام نسبة ٦٠٪ من مجموع اسهم أي زيادة في رأس المال قد تقرر خلال مدة الخمس سنوات المنصوص عليها في المادة الثامنة من هذا القانون .

المادة ٦: يكتب "بيت التمويل الكويتي " شركة مساهمة كويتية في رأسمال الشركة بنسبة ٤٠٪ من مجموع الأسهم .

يكتب "البنك الإسلامي للتنمية" -جدة في رأسمال الشركة بنسبة ٢٠٪ من مجموع الأسهم.

- تطرح الأسهم العائدة للجزء المتبقي من رأسمال الشركة والبالغ ٤٠٪ على الاكتتاب من قبل الأفراد اللبنانيين والشركات اللبنانية بمفهوم قانون تنظيم تداول اسهم المصارف .

-يقفل باب الاكتتاب حكما عند بلوغ مجموع الاكتتاب كامل اسهم الشركة. إذا كان الاكتتاب اكبر توزع الأسهم على المكتتبين كل بنسبة اكتتابه من مجموع الاكتتاب بالمقارنة مع مجموع الأسهم القابلة للاكتتاب.

- يكتب "بيت التمويل الكويتي " بالأسهم التي يحق الاكتتاب بها من قبل الأفراد والشركات اللبنانية خلال المهلة المحددة لاكتتابهم على أن لا يجوز التفرغ لاحقا عن الأسهم المصدرة نتيجة هذا الاكتتاب إلا للبنانيين بمفهوم تنظيم تداول اسهم المصارف اللبنانية.

-يتم تحرير كامل الرأسمال نقدا عند الاكتتاب لدى مصرف لبنان.

المادة ٧:

تشكل مجموع الأسهم المحفوظة لاكتتاب اللبنانيين المنصوص عليها في الفقرة السابقة فئة خاصة من اسهم الشركة ينبغي التفرغ عنها واكتسابها عن طريق سوق مالي منظم. لا يجوز لأي مساهم باستثناء "بيت التمويل الكويتي" ش.م.ك. و "البنك الإسلامي للتنمية" أن يمتلك بصورة مباشرة أو بصورة غير مباشرة أكثر من ٥٪ من رأسمال الشركة. ويعتبر زوج وزوجة المساهم وفروعه القاصرون بمثابة الشخص الواحد. يعد باطلا بطلانا مطلقا حتى بين المتعاقدين كل عمل أو عقد يخالف ذلك.

المادة ٨:

لا يمكن أن تتدنى مجموع مساهمة "بيت التمويل الكويتي" وبنك التنمية الإسلامية "عن نسبة ٦٠٪ من مجموع أسهم الشركة طوال مدة الخمس سنوات اللاحقة لتمويل التأسيس النهائي للشركة، وبعد التأكد من تحقيق أرباح صافية لا تقل عن نسبة ١٠٪ من قيمة رأسمال الشركة المحددة في النظام الأساسي.

المادة ٩:

يتوجب على الشركة، عند قيامها بعمليات لصالح عملائها، إعلام عملائها بمخاطر هذه العمليات خصوصا إذا كانت لأجل ، وبكل ما يمكن أن يشكل تعارضا في المصالح بينها وبينهم يكون متعلقا بهذه العمليات.

المادة ١٠:

يتوجب على الشركة تدوين عملياتها وتنفيذها بشكل واضح ودقيق على أن تظهر يوما فيوما، وبصورة خاصة، وفي كل أن، وبشكل مفصل وثابت المعلومات التالية:

أ- في ما يتعلق بالعمليات التي تقوم بها لصالحها:

التاريخ الدقيق لتنفيذ كل عملية ورقمها المتسلسل والحقوق التي جرى بشأنها التعامل بموجب هذه العملية، ماهيتها، وأسعارها، وجميع العناصر التي تفيد التعرف عليها.

ب- في ما يتعلق بالعمليات التي تقوم بها لصالح عملائها:

- اسم كل عميل والرقم الخاص المعطى لهذا العميل وشهرته وعنوانه، على أن لا يعطى ا لعميل أكثر من رقم واحد ولا يجوز استعمال هذا الرقم مرة أخرى لعميل جديد وان انقطعت العلاقة مع العميل الذي كان يحمل هذا الرقم.

- التاريخ الدقيق لتنفيذ كل عملية ورقمها المتسلسل.

- الحقوق التي جرى بشأنها التعامل، ماهيتها، وأسعارها، وجميع العناصر التي تفيد التعرف عليها.

يضع المجلس المركزي لمصرف لبنان وكذلك لجنة الرقابة على المصارف نماذج وأصول تدوين هذه العمليات بشكل واضح ودقيق يمكن من إظهار جميع المعلومات اللازمة لكل المعنيين بها.

المادة ١١:

يتوجب على الشركة مسك حسابات عملاتها على وجه يميز فيه، عند الاقتضاء، بين حسابات الودائع المصرفية المفتوحة لدى صناديقها وفقا لأحكام المادة ٣٠٧ من قانون التجارة وبين حسابات الاستثمار الأخرى المفتوحة لديها بأسماء ولصالح عملاتها. يجب أن تبين حسابات الاستثمار المفتوحة بأسماء العملاء ولصالحهم بوضوح خصائص القيم والحقوق العائدة لكل واحد منهم، ولا تدخل هذه القيم والحقوق ضمن أصول الشركة.

المادة ١٢:

تعين الجمعية التأسيسية ومن بعدها الجمعية العمومية العادية هيئة استشارية مؤلفة من ثلاثة مستشارين أخصائيين في الشريعة والفقه والعمليات المصرفية والمالية، ويكون تعيينهم لمدة ثلاث سنوات قابلة للتجديد.

لا يجوز لإدارة الشركة اعتماد أي نظام يتعلق بأعمالها أو بعملياتها ولا أي نموذج عقد للتعامل مع الغير قبل الحصول على موافقة الهيئة الاستشارية التي عليها التأكد من عدم وجود تعارض مع الأحكام والقواعد الشرعية الإسلامية المستقرة في مجال المعاملات المالية. وللهيئة أن تقترح تلقائيا على الجمعية العمومية للمساهمين ومجلس الإدارة كل ما تراه مفيدا من أجل تحقيق الشركة لموضوعها على الوجه الشرعي المناسب.

كما لها أن تنتظر في أي طلب يقدم إليها من قبل أحد المتعاملين مع الشركة وتتخذ بصدده التوصية المناسبة وتبلغها إلى إدارة الشركة ومفوضي المراقبة.

المادة ١٣ :

يقوم بدور المؤسسين هيئة تشكل على النحو التالي:

- مندوب عن "بيت التمويل الكويتي".
- مندوب عن "بنك التنمية الإسلامي".
- مندوب معين من قبل وزير المالية.

تضع الهيئة النظام الأساسي للشركة الذي لا يصبح نافذاً إلا بعد موافقة المجلس المركزي لمصرف لبنان وتستكمل بعد صدور هذه الموافقة جميع إجراءات تأسيس الشركة.

المادة ١٤ :

تطبق على الشركة جميع الأحكام القانونية والنظامية المعمول بها والتي لا تتعارض مع هذا القانون ولا سيما تلك الواردة في كل من قانون التجارة وقانون النقد والتسليف وقانون السرية المصرفية.

المادة ١٥ :

يعمل بهذا القانون فور نشره في الجريدة الرسمية.

Appendix B

مشروع قانون

يتعلق بإنشاء مصرف اسلامي في لبنان

المادة ١

المصرف الاسلامي هو مؤسسة موضوعها القيام بالعمليات المصرفية والمالية غير المسندة الى تحديد مسبق للفائدة وبمختلف عمليات التمويل والاستثمار والتوظيف والصيرفة والمساهمات والمشاركات وإدارة الاموال والتركات وصناديق الاستثمار المشترك وعمليات الاجار التمويلي والعمليات الانتمانية .
يكون للمصرف القيام بجميع العمليات المتصلة او المتممة لموضوعه .

المادة ٢

يخضع لترخيص من " المجلس المركزي " لمصرف لبنان تأسيس اي مصرف اسلامي في لبنان .
يضع " المجلس المركزي " نظاما خاصا يتضمن جميع الشروط الواجب توافرها لمنح الترخيص .
يمنح " المجلس المركزي " الترخيص اذا رأى أنه يخدم المصلحة العامة ، وهو يتمتع بسلطة استثنائية في منح الترخيص او رفضه .

المادة ٣

يجب ان تكون اسهم المصرف كافة اسهما اسمية تعود ملكية ثلثها على الاقل الى اشخاص لبنانيين بمفهوم القوانين والانظمة المتعلقة بتنظيم التداول باسهم المصارف اللبنانية .
يخضع للموافقة المسبقة للمجلس المركزي لمصرف لبنان كل تفرغ عن اسهم يؤدي الى اكتساب احد الاشخاص ، بصورة مباشرة او بصورة غير مباشرة ، نسبة تفوق ١٠٪ من مجموع اسهم المصرف .

المادة ٤

يجري المصرف عملياته ، سواء لحسابه او لحساب الغير ، من أمواله الخاصة ، ومن الاموال المتلقاة من الجمهور على سبيل التملك او الادارة ، وذلك على النمط الذي لا يتعارض مع أحكام الشريعة الاسلامية .

المادة ٥

يعفى المصرف من موجبات احكام الفقرتين (١) و(٢) من المادة ١٥٢ من قانون النقد والتسليف . ويجاز له إجراء المشاركات والمساهمات دون التقيّد باحكام المادة ١٥٣ من القانون المذكور .

يكون " للمجلس المركزي " لمصرف لبنان ان يضع الانظمة الخاصة لجمل ولكل من عمليات المصرف ، كما له ان يحدد ويعدل كلما رأى ذلك ضروريا ، قواعد تسيير العمل والنسب الواجب توافرها بين مختلف عناصر الميزانية وخارجها والتي على المصرف الالتزام بها لتحقيق أغراضه ، ولتأمين حسن علاقته بمودعيه والمتعاملين معه ، وللحفاظ على سيولته وملاءته .

المادة ٦

للمصرف ان يكتسب الحقوق العينية والعقارية لتحقيق أغراضه المنصوص عليها في القانون الحاضر . يتم الاكتساب بموجب ترخيص مسبق من المجلس المركزي لمصرف لبنان الذي عليه ان يتحقق من جديته وأن يحدد في ترخيصه أجل التملك . تعفى الشركة من الحصول على التراخيص القانونية المتعلقة باكتساب الاجانب الحقوق العينية والعقارية في لبنان .

المادة ٧

يتعين أن تتمثل ٣٠٪ على الاقل من عناصر الاصول والحقوق المبيّنة في ميزانية المصرف وخارجها باستثمارات وتوظيفات في لبنان . للمجلس المركزي لمصرف لبنان أن يعدل هذه النسبة وفقا لمقتضيات المصلحة العامة وان يقدّر ما إذا كانت بعض العناصر تدخل في النسبة السابقة أم لا . ولا يخضع تقديره في هذا المجال لأي طريق من طرق المراجعة .

المادة ٨

يجوز للمصرف ان يودع فوائض امواله بالعملات المختلفة لدى مصرف لبنان ويكون لهذا الاخير ان يودع لدى المصرف مبالغ بالعملات المختلفة وذلك وفقا لنظام خاص يضعه مصرف لبنان بخصوص الايداع التبادلي على اساس النقط الدائنة والمدينة .

المادة ٩

يتوجب على المصرف ، عند قيامه بعمليات لصالح عملائه ، إعلام هؤلاء العملاء بمخاطر هذه العمليات ، خصوصا إذا كانت لأجل ، وبكل ما يمكن أن يشكل تعارضا في المصالح بينه وبينهم يكون متعلقا بهذه العمليات .

المادة ١٠

يتوجب على المصرف تدوين عملياته وتنفيذها بشكل واضح ودقيق على أن تظهر يوما فيوما ، وبصورة خاصة ، وفي كل أن ، وبشكل مفصل وثابت ، المعلومات التالية :

أ- فيما يتعلق بالعمليات التي يقوم بها لصالحه :

التاريخ الدقيق لتنفيذ كل عملية ورقمها المتسلسل ، والحقوق التي جرى بشأنها التعامل بموجب هذه العملية ، ماهيتها ، واسعارها ، وجميع العناصر التي تفيد التعرف عليها .

ب- فيما يتعلق بالعمليات التي يقوم بها لصالح عملائها :

- إسم كل عميل والرقم الخاص المعطى لهذا العميل وشهرته وعنوانه ، على أن لا يعطى العميل أكثر من رقم واحد ولا يجوز استعمال هذا الرقم مرة أخرى لعميل جديد وإن انقطعت العلاقة مع العميل الذي كان يحمل هذا الرقم .
- التاريخ الدقيق لتنفيذ كل عملية ورقمها المتسلسل .
- الحقوق التي جرى بشأنها التعامل ، ماهيتها ، واسعارها ، وجميع العناصر التي تفيد التعرف عليها .

المادة ١١

يتوجب على المصرف مسك حسابات العملاء على وجه يميّز فيه ، عند الاقتضاء ، بين حسابات الودائع المصرفية المفتوحة لدى صناديقه وفقا لاحكام المادة ٣٠٧ من قانون التجارة وبين حسابات الاستثمار الاخرى المفتوحة لديه باسماء ولصالح العملاء .
يجب أن تبيّن حسابات الاستثمار المفتوحة باسماء العملاء ولصالحهم بوضوح خصائص القيم والحقوق العائدة لكل واحد منهم ، ولا تدخل هذه القيم والحقوق ابدا ضمن اصول المصرف .

المادة ١٢

تعيّن الجمعية التأسيسية ومن بعدها الجمعيات العمومية العادية هيئة استشارية مؤلفة من ثلاثة مستشارين أخصائيين في احكام الشريعة والفقه والعمليات المصرفية والمالية ، ويكون تعيينهم لمدة ثلاث سنوات قابلة للتجديد .

لا يجوز لادارة الشركة اعتماد أي نظام يتعلق بأعمالها أو بعملياتها ولا أي نموذج عقد للتعامل مع الغير قبل الحصول على موافقة الهيئة الاستشارية التي عليها التأكد من عدم وجود تعارض مع الاحكام والقواعد الشرعية الاسلامية المستقرة في مجال المعاملات .
والهيئة ان تقترح تلقائيا على الجمعية العمومية للمساهمين ومجلس الادارة كل ما تراه مفيدا من اجل تحقيق الشركة لموضوعها على الوجه الشرعي المناسب .
كما لها أن تنظر في أي طلب يتقدم اليها من قبل أحد المتعاملين مع الشركة وتتخذ بصده التوصية المناسبة وتبلغها الى إدارة الشركة ومفوضي المراقبة .

المادة ١٣

تطبق على المصرف جميع الاحكام القانونية والنظامية المصرفية المعمول بها والتي لا تتعارض مع هذا القانون ولا سيما تلك الواردة في كل من قانون التجارة وقانون النقد والتسليف وقانون السرية المصرفية .

المادة ١٤

يعمل بهذا القانون فور نشره في الجريدة الرسمية .