

Islamic Banking Muḍārabah Review from Depositors' Funds Security Perspective

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ABSTRACT

Islamic banks use Muḍārabah to collect money into their saving and term deposit investment accounts. While doing so these banks stipulate in their terms and conditions that the customers as money providers will solely bear the loss. The banks who manage these funds will neither bear the loss, nor guarantee these funds. Additionally, the customers have no course to the profit distribution or investment decisions. The banks quote that these terms and conditions are in line with Muḍārabah Sharī'ah principles. On the contrary, they use the same terms and conditions as an excuse for not providing financing to the customers based on the Muḍārabah. This double standard draws attention of the researchers to analyze the situation with the aim to protect the depositors in Islamic banks. This is a qualitative study that used unrestricted interview methods to collect data. It was found from research that the current banking Muḍārabah has been altered completely and that the banks don't qualify to continue using same loss terms and conditions. It is inevitable for the financial and social safety of society to update the Muḍārabah terms and conditions to make them comply with Maqāṣid al Sharī'ah. The study recorded the view of few scholars; however, it opened the doors for Islamic banks, regulators and Fiqh councils to further discuss the legitimacy of the banking Muḍārabah terms and conditions to protect relationship with the customers who deposit money in trust of being Islamic and to avoid the usury offered by the interest based conventional banking.

Keywords: Muḍārabah, Islamic saving accounts, Islamic investment deposits, Islamic Finance and Banking.

INTRODUCTION

Islamic banking witness rapid growth all around the world with assets of USD 3.38 trillion in 2023 (IFSB, 2024). Obviously, this backed by growing levels of deposits through profit sharing investment accounts (PSIA). Muḍārabah is the most famous structure for collecting money by Islamic banks. Muḍārabah common definition in the Islamic finance is that it is a partnership contract. Whereby the capital provider (rabb al-māl) would contribute capital to an enterprise or activity that is to be managed by the entrepreneur (Muḍārib). Profits are shared in accordance with the percentage specified in the contract between parties. (IFSB, 2024). This part is fine; however, the problem is about the loss treatment. Bank happily communicate that in case of loss the customer will bear it. This term is the reason that banks like to extensively use Muḍārabah to collect money from customers, on the other hand, they don't provide financing based on Muḍārabah partnership for the same reason. The banking contract typically stipulate that as per the Muḍārabah terms and conditions, capital provider will solely bear the losses unless it is due to Muḍārib breach of contracted terms, misconduct or negligence (IFSB, 2024). The alarming fact is that banking Muḍārabah is not that sample as the traditional classical Muḍārabah used to be. In reality it shares many challenges, details of operations and banking risks due to the unlimited mandate to collect the deposits money. Hence, there is need to revise the definition, terms and conditions and treatment of loss in light of the banks using Muḍārabah as a financial product. This point was discussed in many contemporary studies, such as (Aslan *et al*, 2024, Miah *et al*, 2023, Öznur & Erdal, 2023, Yustiardi *et al*, 2020, Yurista & Ardi, 2019, Afzal & Hassan, 2018, Sapuan, 2016 & Rammal, 2003) however, its discussion context was to find the reasons that Islamic banks have very limited use of Muḍārabah to finance

their customers. These studies have not paid attention to the fact banks are not willing to finance due to risk but it is exposing the billions of deposits to the same risk. This study aimed to address this point through the core Sharī'ah condition of the Sharī'ah contract of Muḍārabah. Under the Muḍārabah contract, the Bank may act either as Muḍārib or as Rabb al-Māl, as the case may be and the whole process is managed based on the interest rates. Islamic banks pay almost equivalent to interest rates paid on deposits and saving accounts by the conventional banks. The result is that the return and profits paid to depositors are not the actual performance of Muḍārabah profitability. There is no better explanation of the impact of the above-mentioned situation than the words of 'Usmānī (2008), who stated that in the modern economic system, banks advance depositors' money as loans to industrialists and traders. Industrialists invest 10 million of their own and acquire 90 million from the banks. It means that 90% of the project used the money of the depositors, and only 10% was their own capital. To embark on a project that brings enormous profits. However, only a small proportion not exceeding 14 or 15% will go to the depositors through the bank, rest will be gained by the industrialists against a contribution not more than 10%. Even this small proportion of 14 or 15% is included by them in the cost of their production. On the contrary, if in an extreme situation, the industrialists go insolvent, their own loss is no more than 10%, while the rest of 90% is totally borne by the bank, and in some cases, by the depositors. The net result is that all the profit goes to the enterprise capital 10% of the total investment, while the people owning 90% get the fixed rate of interest which is often paid into the increased prices of the products. In this way, the rate of interest causes imbalances in the system of distribution, which has a "constant tendency in favour of the rich and against the interests of the poor." ('Usmānī, 2008). Due to the fiqhi and ijtiḥād approach of the discussion two of the top senior Sharī'ah scholars were interviewed; however, it forms a call for the regulators and practitioners to forward this discussion to Fiqh councils to get majority opinion on the matter in the interest of Islamic banking and finance and its stakeholders.

This study used qualitative method of research by conducting open ended unrestricted interview. The literature review, discussion and interviewed revealed the necessity of looking into the matter from view of providing protection to the customer and their funds that are deposited in banks. It finds that concentration of billions of monies in treasuries of few banks does not comply with the Maqāṣid Al Sharī'ah. It also doesn't comply with the original aim and goals of Muḍārabah contract. Hence, call for through revision of terms and conditions in light of the current Islamic banking and finance realities. Muḍārabah in the banking sphere shall consider the learned opinions of scholars who call for making the Islamic banks guarantee the deposits collected under Muḍārabah contract without following any tricks or indirect structures to achieve the goal. This all falls under the objectives of wealth preservation and its components of the corresponding objective of money circulation (rawāj), clarity of terms of words (wuḍūḥ), protection of parties' rights (ḥifẓ), firmness (thabāt), and justice ('adl) for contract parties (Ibn 'Āshūr, 2013).

LITERATURE REVIEW

AAOIFI has given a very brief definition of Muḍārabah by stating that: "Muḍārabah is a partnership in profit whereby one party provides capital (Rabb al-Māl) and the other party provides labour (Muḍārib)." (Sharī'ah Standard No. 13, page 370). However, these definitions are not exhaustive because it did not mention the loss scenario. As per common Islamic banking definition, Muḍārabah is a contract for a specific pre-agreed share in the resultant profit, if any, between the (Rabb al-Māl) who would provide funds (Muḍārabah Capital), to the other party (Muḍārib). The Rab al-Māl is not involved in the management of the Muḍārabah activity, while Muḍārib role is to invest the Muḍārabah Capital deploying its experience and expertise. (IFSB, 2024).

In general, the Islamic banking theory was based on profit and loss sharing, and the contemporary Islamic economic under the profit-loss sharing model refers to the Muḍārabah and Mushārah (Aslan *et al*, 2024, Miah *et al*, 2023, Öznur & Erdal, 2023, Yustiardi *et al*, 2020, Rammal, 2003, Yurista & Ardi, 2019, Afzal & Hassan, 2018, Mazuin, 2016, Sapuan, 2016). The Muḍārabah contracts provides opportunities for growth through legitimate cooperation between the investor who looks for growth opportunities and the skilled worker to enable him invest this money and reach a common goal of getting profitability and financial returns. It is a pure Islamic real partnership in real projects with aim to creating value and income from them when designed apart from interest rate mentality (Dewaya, 2024).

It is found that studies mostly discuss the issue of unpopularity of Muḍārabah as a financing product. Afzal and Hassan (2018), conducted interview with 23 senior Islamic banking practitioners in Pakistan and concluded that they think that the main reason to avoid *Muḍārabah* financing in banking practice is the operational difficulties (Afzal & Hassan, 2018). Sabrina and Abd Majid (2020) deemed that lack of banking product of Muḍārabah is affiliated with factors such as risk, human skills, operational complication, lack of innovation, lack of transparent data and lack of regulatory support (Sabrina, S., & Majid, M., 2020). Similarly, Yustiardi *et al* (2020), mentioned that Islamic banks may have intermediary role in Muḍārabah as the agent of the investor to channel financing to entrepreneurs in a two-tier Muḍārabah contract (Yustiardi *et al*, 2020).

Abdul-Rahman and Nor (2016), considered the difficulty in dealing with the low credit worthiness customer as a non-appropriate partner, in other words due to risk of capital security (Abdul-Rahman & Nor, 2016). Meanwhile, Islam and Ahmad (2020), found that it is viable to finance entrepreneurs using the Muḍārabah risk-sharing principles. However, it needs improving the commitment related to entrepreneurial skills in compliance with Sharī'ah principles (Islam & Ahmad, 2020).

Most studies noticed that Muḍārabah is replaced with other debt financing structures that are developed to mimic conventional interest-based products and contracts that borrowing and lending based (Aslan *et al*, 2024, Miah *et al*, 2023, Öznur & Erdal, 2023, Yustiardi *et al*, 2020, Yurista & Ardi, 2019, Afzal & Hassan, 2018, Sapuan, 2016).

Academically, industry should be guided to draw the attention towards distinguishing between Islamic finance contracts original characteristics and their employment in IFIs to keep the Islamic banking contracts up to the level of current Sharī'ah, commercial and legal requirements. The bank customers should be given the option to select, understand and take responsibility of their real investment decision through Islamic banks based on true letter and spirit of Mushārah and Muḍārabah (Dewaya, 2024).

Muḍārabah is based on trust (Sadique, 2009). The investor depends on the honesty of the manager for profit share payments (Schoon, 2010). Iwona Sobol (2019), concluded that judgement of managers of Islamic banks is no better than that of their conventional counterparts, in this scenario the theory of profit and loss sharing means uncertainty that the depositors will gain profits, while they are exposed to the loss. For examples in 1982 Kuwait Finance House lost millions of dollars during the stock market bubble (Seznec, 1999, Sobol, 2019).

Some studies have discussed the critical aspects, raised due to lack of transparency regarding the performance and profit sharing (Archer & Abdel Karim, 2009). Jais *et al* (2019), conducted a study that concluded that use of Muḍārabah in Islamic banks requires a parallel awareness and capacity building with their customers as their partners to develop skills and experience required for practice of Muḍārabah (Jais *et al*, 2019).

On the other hand, the studies have critically discussed the use of Muḍārabah in the liability side by the Islamic banks. But without much focus on the core problem. The aims should be to provide maximum protections to the depositors and to the society and not mere mention that the loss will be borne by customers who provide the funds (Dewaya, 2024). The risk includes potential abuse from shareholders against the depositors based on Muḍārabah. Given that depositors have no knowledge or authority to discuss the performance and profit sharing (Åström, 2012). Damak and Mensah (2016) noted that in restricted accounts bank secures some amount for its asset management services, while it reports off-balance sheet the underlying asset without taking any risk related to it (Damak & Mensah, 2016).

In 2004, the concern of the safety of deposits, based on a Muḍārabah mechanism was discussed in the UK. The UK Financial Services Authority (FSA) raised this concern because the customers have the legal right to a guaranteed refund of the deposit. The solution was to get the written consent of the depositors to waive the demand of the guaranteed refund under the profit and loss sharing Muḍārabah (Ainley *et al*, 2007).

This is not a new issue, the risk of money loss in Muḍārabah was genuine concern from inception. Unfortunately, the remedy was always by way of finding tricks. Ḥammad (2000), mentioned some tricks from

the old Fiqh books. For example, structuring the deal to loan/ Qarḍ so that the capital can be protected. The Ḥanafī scholar Al Sarkhasi suggested that “If a man wanted to invest some money on basis of Muḍārabah with another man. But, at the same time he wanted the money to be guaranteed by Muḍārib, then he can use a trick ḥilla. The Rabb al-Māl will give the full amount minus one dirham to the Muḍārib as a loan. In this way the Mustaqrīḍ became the guarantor of the loan money after he gets its possession. Next the Muḍārib pays one dirham to become his partner with the amount that he has already gave him as Qarḍ. The total amount will be invested or used as working capital based on an agreed profit share. He added that this is a valid partnership and the profit will be distributed as per the partnership agreement (Ḥammād, 2000).

Study concludes from the literature review is that the banking Muḍārabah is not the same like it was practiced for last 1400 years. Today the Muḍārib is a bank. The customers don't know who works in that bank and who is taking the Muḍārabah actions that will determine the safety of their money. The analysis of the previous studies reflected a limited discussion of Muḍārabah issues purely from Islamic banking perspective as a financing product. Studies often mix between the Mushārah and Muḍārabah while arguing in the context of Profit and loss Sharing. However, they end up without providing any significant solution or offering improvements for the long-time risen matters that critical impact the mass majority of customer who trust these banks and the fatwas that encourage them to place their funds on Muḍārabah basis.

RESEARCH METHODOLOGY

This study followed qualitative method. In this context it used unstructured open ended interview method to collect the opinions of learned scholars through interviews. According to Saunders *et al.* (2011), interview falls into three main types namely (1) structured interviews, (2) semi-structured interviews, and (3) unstructured interviews (Saunders *et al.*, 2011). Different between structured and unstructured interview is that the earlier depends on a formalized set of questions, while the unstructured aims for open and free conversation. (Easterby-Smith *et al.*, 2012). Interviews are a method for collecting data, the interviewees participants are asked questions to find out what they think (Collis and Hussey, 2013). Interview is the most effective method for fruitful extraction of data/ information of respondent's knowledge, view of point and robust insight of the interviewee (Kvale, 1983, Bryman, 2012).

Further, along with analytical method of the published or recorded view on the subject. It included combination of classical and contemporary writings. A detailed literature review using the online library review method and searching for the relevant academic articles in journals using the key words Muḍārabah, profit and loss sharing and Islamic banking investment accounts.

In this context, two of the contemporary learned scholars namely Dr. Hussein Hassan and Dr. Nazīh Ḥammād were interviewed by the researcher to record their answers for the questions regarding the mitigation to make the Islamic banks guarantee the customers' money collected under the Muḍārabah contract? Their opinion was recorded both on Fiqhi and contemporary terms and conditions of the banking Muḍārabah contracts.

DISCUSSION AND ANALYSIS

It is inevitable to comprehensively analyse the impact of collecting money under the Muḍārabah. Hence, discuss practical multi-dimensional aspects of the use of Muḍārabah by the banks as a liability product to receive the money. Islamic banks highlight a very important terms and condition point in case of Muḍārabah that the financial loss is solely borne by the customers i.e. investors (IFSB, 2024). Accordingly, banks who are in controlling positions articulate some remedies that arise the concerns highlighting that the customers are the weakest contractual party and protection of their rights in terms of capital protection and also calculating and paying profit in a transparent way in Muḍārabah based accounts.

Banking Muḍārabah review

The holy Quran has clearly instructed the forbiddance of concentrating the money in the control of few and depriving its circulation to the less fortunate people.

“And what Allah restored to His Messenger from the people of the towns - it is for Allah and for the Messenger and for [his] near relatives and orphans and the [stranded] traveler - so that it will not be a perpetual distribution among the rich from among you. And whatever the Messenger has given you - take; and what he has forbidden you - refrain from. And fear Allah; indeed, Allah is severe in penalty.” [59:7] Quran Karim.

Original Sharī'ah contracts are just and promote circulation of wealth; hence, should not be neglected in the Islamic finance structures ('Usmānī, 2005). The Muḍārabah contract was originally designed by Sharī'ah to be an effective tool against the concentration of wealth in limited hands.

Islamic banks use the Muḍārabah for accepting deposits in saving accounts and term deposit accounts, the impact of this use of 'Muḍārabah' is that it results in concentrating billions of dollars of public money in the treasuries of a few banks, similar to the conventional banks. Eventually, this will create the same impact as conventional banking that gathers billions of deposit money in its treasury and lends the same to the public with higher rates. As a result, in both cases, the impact is to putting billions of public monies into banks' treasury and exposing billions of dollars that belongs to millions of people to the risk of loss in case of any credit, banking or global crisis that creates global economic crisis such as the one witnessed in 2008 (Hassan, 2010). This concentration of money is in contradiction to the object of circulation\ Rawāj (Ibn 'Āshūr, 2013). This shows the Islamic financing contracts as applied in Islamic banks lack the Sharī'ah contracts inherited features of justice and equality. Resulting is that this money has no much social impact or opportunity offered for skilled workers or development projects. Based on this fact, the income gap keeps growing between the rich who have access to financing and between the poor who are barred from financing.

Similar to conventional banks, the Islamic banks also prefer to mostly provide credits to rich capitalists and industrialists. In the case of corporate clients these credit facilities reach up to billions. banks prefer the party which fits into their collateral's workout. similarly, the individual customers who are well salaried and have proven consistent income are welcomed for excessive loans. Hence, such category is often getting money from banks with desired negotiated terms and rates. Subsequently Islamic banks like the conventional work for recovery of debt or take over the available collateral of credit (Chapra, 1985).

On the other hand, rejecting most deprived persons and SMEs or creating difficulties and charging high rates for them is similarity of conventional and Islamic banks. Providing funding with the same methods risk policies often lead the Islamic bank works as a capitalist (Chapra, 1985). In this case, Islamic finance structures should find solutions for this in light of the true Sharī'ah spirit. It means that Islamic banks should not avoid to creating any assets or joint ventures in the form of partnership between a party who is capital deficient, but skilful.

The fact is Islamic banks, financing eligibility is for those who meet the credit criteria similar to conventional banks. Islamic banks impose high rates of profits and creates similar impact like conventional banks when financing people who don't meet the conventional credit scores (Rosly, 2005, 'Usmānī, 2005).

Rosly (2005), mentioned that Islamic banks credit criteria include history with banks, salary and income record, collateral capacity. These are known as 5Cs; therefore, the poor cannot get facilities from Islamic banks because they do not meet the 5Cs. This exposes them to exploitation of the corrupt lenders high rate of profit is tantamount to of taking advantage of the poor and charging excessive amounts of profit based on interest benchmark is contradiction of many Islamic principles and condemnable (Rosly, 2005).

This results that current financing facilities are for the rich and super-rich. The majority who do not have collaterals and don't meet the banking conditions face the same faith in Islamic and conventional financing environment; they are not welcomed to obtain the facilities. Islamic banks should not follow the greediness of capitalists ('Usmānī, 2005).

Ever since, banks prefer to collect money on Muḍārabah basis and don't wish to fund using the Muḍārabah. Banking Muḍārabah was developed to collect money for the investment pool of Islamic banks it has become

a tool of money concentration in hands of some controlling monopoly limited Islamic financial institutions by collecting millions and billions of dollars. Islamic banks (IBs) use the Muḍārabah contract to collect money under an unrestricted mode of Muḍārabah. Under the Islamic banking practices Muḍārabah became a tool to maximize the banks' deposits by collecting money into Islamic banks' treasury (Dewaya, 2024).

IBs use Muḍārabah based saving accounts and investment accounts also known as Un-Restricted Investment Accounts (URIA) as alternatives to conventional banking interest-based term deposits. While, banks do this as a controlling party, they also enjoy the terms and conditions that were intended by Sharī'ah to protect the Muḍārib considering him the weaker party. These conditions were applicable when the Muḍārib was an ordinary real personality not legal and commercial entity like a bank. The bank is not an entrepreneur who requires funding, rather, it is a commercial entity that is found by government or rich businesspersons. In this case, how it is justifiable to provide money to it on Muḍārabah bases with the same degree of protection i.e. from losses that are given to an entrepreneur or individual. This logically violates the concept of 'Adl or justice (Ibn 'Ashur, 2013).

The difference between the impact of Muḍārabah original Fiqhi Sharī'ah contract and Muḍārabah as applied by Islamic banks and funds is felt loudly under the theme of financialization of the different Sharī'ah contracts in terms of their impact and compliance with form and substance of Sharī'ah principles. This situation needs a Maqāṣid analysis, to suggest remedy in order to avoid possible violations to the rights of customers who are providing their funds on Muḍārabah basis to equally save and safeguard customer rights and money (Hassan, 2010).

Preserving money is requirement of Maqāṣid al-Sharī'ah also includes multiplying investment opportunities and save its value from inflation. Hence, it is urged that banks should go for Muḍārabah financing to provide cash to customer especially the corporate and SME, however, it is banks' responsibility to do the necessary due diligence through multiple scrutinizes and not only rely on the Relationship manager who might be more motivated by getting his financial target and incentive (Dewaya, 2024).

Muḍārabah alterations & financialization by banks

The banks attitude generally is to shift all the risks to customers only and Muḍārabah contract gives them good pitch to do that. Hence, it states and focus that in case of loss the Rabb al-Māl i.e. the customer will bear the loss. The reason that the Islamic banks use it only to receiving money in shape of fixed investment deposits and don't use it to provide financing to customers is the risk factor (Chapra, 1985). Nevertheless, avoiding risk is a valid concern under the Maqāṣid al Sharī'ah of preserving the money, wealth and whatever falls under the Sharī'ah definition of al Māl. The risk should be equally weighted when the banks are collecting billions of public monies.

The alarming fact is that the circumstances of banking Muḍārabah are very different from fiqhi Muḍārabah because banks have added so many changes to it. However, it is a reality that banks stay the controlling party while the customers have much limited options. In all cases the banks use their own designed and customized contracts that become one sided adhesion contracts, forcing contracts that are similar to monopoly of the banks over the customer. The customer has no choice but to sign the account opening forms and provide consent and asked to sign lengthy terms and conditions which are often drafted for the interest of banks as priority and not the customers. It offers very little to protect the ordinary or the individual customers, there are no rules to protect the depositors collectively or individually against any misconduct or manipulation in the profit distribution by the bank (Hammad, 2000).

Literally, the Muḍārabah under Islamic banking product imitates the impact of fixed terms of conventional banking as eventually the profit distribution is done based on the interest benchmarks prevailing in the market. Islamic banks list Muḍārabah as a 'Liability' product when used for collecting money into banking investment and saving accounts, they also list it as 'Asset' if used as financing product (IFSB, 2024). This is done exactly on same conventional banking bases that considers the customer deposits as liability because it is a loan that has to be returned to the customer.

Given that now the bank is always the strong party, whether, it acts as Muḍārib or Rabb al-Māl, if Islamic banks consider this a liability, then they should also guarantee it for the interest of customers. This is a serious demand for real revision of Muḍārabah terms and conditions and not depend on following some tricks or adding cosmetic clauses to the contracts. Also calls for stop substituting Muḍārabah and Mushārahah with commodity Murabaha Tawarruq with justification of risk.

There are regulations to protect the shareholders and compensate them on priority basis, on the contrary, the loss would be borne by the Rabb al-Māl as fundamental rule of Muḍārabah. Some banks add the provision that the Muḍārib would bear the loss in case of his misconduct, fault, negligence or violation of any of the terms and conditions of the Muḍārabah contract. However, they don't provide enough explanation for the exception of loss due to misconduct of the bank. Making this type of additional clause just a formality that adds further to the ambiguity to the Muḍārabah contract under the Islamic banks. For this purpose, some suggest to add that the Rabb al-Māl receives satisfactory evidence that such loss was due to force majeure and that the Muḍārib neither was able to predict the same nor could have prevented the negative consequences of the same on the Muḍārabah (Hassan, 2010).

The money of the customers' is being used by the banks' is comingled with money of Shareholders or the owners of the bank in common pool. This is derived by a conflict of interest as the bank management has more tendency to focus on the shareholders' interest and please them with higher returns on their shares in order to get hefty incentives for the senior executives of the bank. Correspondingly, in case of loss, the bank transfers it to the customer by reducing the profit rates on the Muḍārabah deposits and accounts or compensating it from the reserves which are against money of depositors.

In this context, there are so many issues related to the point of profit and loss distribution. The profit calculation and distribution method of Muḍārabah common investment pool in Islamic banks include many arrangements that make its impact mimic the conventional interest-bearing accounts and term deposits. Given that, there are many other contemporary additions to the Muḍārabah contract such as adding to it features such as Profit Equalization Reserve PER, Investment Risk Reserve IRR, and other reserves. Regularly money is cut from the profits payable to the account holders to be put in reserves such as IRR and PER. Hence, Islamic banks make sure that saving and deposits account holders gets the same profit that is being distributed by conventional banks in the market or maybe less (Yustiardi *et al*, 2020). This contradicts to the Maqāsid al Sharī'ah of growing the Māl, the return paid often is not even or enough to pay 2.5% of the capital as the Zakat of money.

To facilitate adjustment of the 'profit' payable in order to match it with interest paid by the conventional banks or the market rate, these banks keep the ratio of profit distribution between Rabb al-Māl at a ridiculous level. In some types of accounts, the share of the bank in the profit reaches up to 85% or 95%, leaving thousands of depositors to distribute the remaining 15% or 5% as per their weightage after deducting the reserves. Some supervisory bodies issue regulations with regard to this ratio. In Turkey the minimum profit share for investor's is 75 percent, and remaining 25 percent for the bank (Song & Oosthuizen, 2014). On the other hand, Malaysian central bank set the limit of 50 to 75 per cent (BNM, 2012, BNM, 2015, Yustiardi *et al*, 2020).

The profit distribution to the Muḍārabah based investment account holders is also affected by the distribution of the expense. Hence, one of important issues that should be carefully standardized is the distribution of expense. If Islamic banks deduct all expense from Rabb al-Māl (customer), then it is a doubtful practice, because, not all the expenses of the bank are occurred due to management of Muḍārabah. On the contrary, in the case of profit, banks take its share before distribution to the 'Rabb al-Māl'. According to Taqī 'Usmānī (2008), the Muḍārib are authorized to do anything which is normally done in the course of business. However, if they want to do work that is beyond the normal routine of the traders, they require permission from the rabb al-Māl ('Usmānī, 2008). This can be achieved through restricted Muḍārabah. however, most of the investment accounts and deposits in Islamic banks are based on unrestricted Muḍārabah.

The challenge is that the classical fiqh books discuss the expense in situation of Muḍārabah between individuals and banks. Multiple learned Fiqh books that includes Ibn Qudāmah, al-Mughni, 5:186, al-Sarakhsi, al-Mabsūt, 22:149–50, al-Kasāni, Bada'i' al-Sanāe'i, 6:109, stated that the Ḥanafī jurists restrict the right of deducting expense by the Muḍārib only in a situation when he is on a business trip outside his own city. In that case he can claim his personal expenses, accommodation, food, etc. However, he is not entitled to get anything as daily allowances when he is in his own city. This is in case of single Muḍārib, which is the principal situation. Maliki scholars don't put any restrictions on number of investors and entrepreneurs with the condition of prior permission by the fund provider. Al-Sarakhsi has explained the situation in which Muḍārabah is between multiple sides or parties. In that case they should be bound to act with approval of the investor as per mutual agreement. The Muḍārib is held responsible for any losses for his unauthorised actions without approval of the Rabb al-māl ('Usmānī, 2008, Borhan, 2004).

'Usmānī (2008), explained that Muḍārib is only eligible for the agreed profit proportion. He is not allowed to charge any other remuneration, salary or fee against the work done by him for the Muḍārabah. This is a unanimous opinion of all schools of Fiqh, with the exception of Imām Ahmad who allowed to take daily food expense for the Muḍārib from the Muḍārabah account. ('Usmānī, 2008). It is clear that these classical opinions about the Muḍārabah are difficult to apply on the contemporary banking within the financialization sphere. Taking daily allowance of food was more relevant when Muḍārabah was between individuals. This doesn't fit in case of institutions such as a banks' whose staff are already being well-paid and work for the owners of the bank or the shareholders and not for the Muḍārabah. This is one of the matters that Islamic banks should declare in detail and make sure that customers consent was recorded on.

Despite the alterations done in the Muḍārabah makes some sitting members of Sharī'ah committees and Sharī'ah board members take a negative stance. Instead of trying to comply with Maqāṣid al-Sharī'ah and moral theory of Islamic finance, they find it easier to escape from applying the Muḍārabah and Mushārah and shift the industry to the debt based tricky products such Commodity Murabaha Tawarruq or the organized banking Tawarruq. In a recorded interview, Sheikh Niẓām Ya'qūbi highlighted the challenges that accompany the application of Mushārah and Muḍārabah in the Islamic banking. According to him full Mushārah full Muḍārabah is applied in Islamic finance investment banks, where lots of people who have accepted the loss and profit-sharing method lost their funds because it was a risky business and they knew about it.

INTERVIEWS & FINDINGS

The researcher focused on the alterations that took over the Muḍārabah when developed by the Islamic banks under the current financial circumstance. Hence, for the discussion it was important to select some most senior fiqh scholars with background of Islamic banking. Use of Muḍārabah to collect funds from public into few investment pools is a problem due to risk size. The major issue is to analyse if the Muḍārabah under Islamic banking investment accounts qualify to be continued with the same style and terms and conditions as discussed in the fiqhi books for the Muḍārabah that was done between two or more individuals. With in this context the most important factor is the treatment of loss situation and the security of funds provided by people under Muḍārabah contract (Dewayā, 2024).

The interview approach was to explore the fiqhi possibility of updating the terms and conditions of Muḍārabah in Islamic banking contracts to provide more protection to the customers who deposit their funds on Muḍārabah basis. Researcher asked interviewee to explain his position to make the Islamic banks guarantee the money collected based on the Muḍārabah Investment and saving accounts?

Firstly, Dr. Hussein Hamed Hassan was interviewed. His age at the time of interview was 82 years old out of which he spent more than half decade in teaching and research related to Fiqh, Islamic banking and finance. He was also pioneer of most innovative products, Sukuk and chairman of a large number of Islamic finance institutions. In one of his research papers (Hassan, 2010) presented the idea of changing and modification of Muḍārabah terms and conditions to make the banks in their capacity as Muḍārib liable in case of financial loss or at least shift the burden of proving the reason of loss should be on the bank in its capacity as the Muḍārib.

It means that bank will be asked to give clarification about the reason of the loss. Accordingly, the account holders “Rabb Al-Māl” will have the rights to demand that the Muḍārib should prove that the loss was not due to his negligence, misconduct or violation of the terms and conditions of Muḍārabah.

Dr. Ḥussein Ḥassan elaborated that as per the Fiqh al-Mu‘āmalāt the Muḍārib is Amīn which means trusted party, in fiqhi term his liability is known as “Yadd al-Amānah” he is “deposit intrust” or trusted party. Subsequently, as per the traditional Fiqh rules he is not asked to guarantee the money or cannot be guarantor.

In this context, he applied a very wise analogy based on the Fatawa of Imam Ali to Ṣani‘ as Ḍāmin guarantor, while the original fatwa was that Sani‘ was Amin. In case of Istisnaa‘, Ṣani‘ was Amīn when the people dealings were based on Amānah and trust, but when the people have lost trust, integrity and Amānah he gave the Fatwa to make the Sani‘ guarantee the material of Istisnaa‘. This change in Fatwa was to protect Mustaṣni‘ the people who supplied the raw material such as leathers or the textile, in order for the worker to use it to manufacture and create the requested product. He modified his Fatwa to make the Ṣani‘ as Ḍāmin guarantor, if the Ṣani‘ was not asked to guarantee these materials provided by the Mustaṣni‘ then there was a big chance of loss of due to Sani‘ misconduct or negligence.

Dr. Hussein added that in case of Istiṣnā‘ the Ṣani‘ has the Yadd al-Amānah similar to the Muḍārib. However, Imām Ali (may Allah blessed him) gave a Fatwa to make the worker or the trusted party was asked to guarantee the money or the Māl. Similarly, there is need to assess the situation of Muḍārib in the Muḍārabah contract in Islamic banking terms and conditions in which the loss is borne by the customers.

The prevailing practice and Fatāwa do not put the onus of proving negligence, misconduct or violations of Muḍārabah terms and conditions in case of loss on the banks. It is too risky business to tell that the bank in his capacity as the Muḍārib does not guarantee the money of customer or Rabb al-Māl. It is too risky for the safety of the hundreds of billions of peoples’ money collected by these Islamic banks. This matter certainly deserves to be looked upon to protect the depositors’ position.

Additionally, the problem is that the customers ‘Rabb al-Māl’ who deposited their money in Islamic banks through Muḍārabah structure have no legal representative association to take action in case of loss. They don’t have the legal and technical capacity to prove the misconduct or negligence of the bank in its capacity as the Muḍārib to hold it responsible in case of loss.

Researcher well noted that, Dr. Ḥussein Ḥassan opinion was that the onus of proving the reason of loss should be on the bank / Muḍārib and not the customers /Rabb al-Māl. Banks will be legally required to prove that loss was not due to their negligence, misconduct or violation of Muḍārabah terms and conditions. This means that the Muḍārib will have the upfront right to defend his position by providing the justified reasons that lead to loss. On the flipside, the investors or the Rabb al-Māl will get sufficient evidences to investigate the Muḍārib role and the reasons of the financial loss. His Ijtihād was very sound to mitigate the risk of loss and to place more controlling terms and conditions to protect the customers.

Secondly, researcher interviewed Dr. Nazīh Hammad, a senior scholar of Islamic banking and finance. Dr. Nazīh have many research and contribution that discuss the options to update Muḍārabah contract as applied in Islamic banks is good example of contemporary Fiqh to update the financial and banking. His book has chapter about the impact of change from a natural personality to the commercial or legal entity. Also, he built his opinion based on the maxims that the Ahkām can be changed according to the change of circumstances and time. His Ijtihād fits into the Maqāsid al-Sharī‘ah methodology of evaluating the benefits/ Maṣlahah and harms/ Mafsadah in the contemporary transactions/ Mu‘āmalāt.

Dr. Nazih categorically and openly called to doing necessary changes in Muḍārabah to make the Islamic banks in their capacity as Muḍārib guarantee in case of loss. In fiqhi terminology his opinion is that “Yadd al Amānah” can be changed to “Yadd Al Ḍamān” In light of the absence of knowledge, commitment of banker about Sharī‘ah principles among and the absence of trust.

Dr. Nazīh Ḥammād, mentioned number of facts including that because banks are not a real personality. Banks are legal entities. In case bank declares insolvency, seal the doors and dismiss the employees, the customers ‘Rabb al-Māl’ will not have any person to talk to.

Bank employees’ poor decision reflects on depositors or the customers. The money is not protected from any bad decisions of banks. On the other hand, customers didn’t have any role in decisions to manage their funds. Dr. Nazīh Ḥammād added that there are examples of Islamic banks that went into insolvency, in Egypt, in Malaysia and other countries, hence, the public lost all the money. There are some precedents that Islamic banks lost amounts above USD 500 million. When the people came to ask the Sharī’ah board, the Sharī’ah boards of these Islamic banks gave the ruling that, since the contract was Muḍārabah the bank doesn’t guarantee their money and that loss was to be borne by the customers in their capacity as Rabb al-Māl.

He added that Muḍārabah terms and condition in case of banks should restrict the bank in his capacity as the Muḍārib to guarantee the capital in case of loss. It should be responsible to protect the money of customers in their capacity as the Rabb al-Māl. Also, the terms and conditions should stipulate that banks will not invest Muḍārabah money in risky deals. He thinks that this is a straight forward approach. According to him such terms will be Ṣaḥīḥ i.e. valid and Mulzim i.e. binding. It is much closer to the Ḥājah (necessity), Maṣlaḥah (interest) and Sadd al Darā’eh (blocking the means) to avoid loss of peoples’ money. He added that he is against structuring tricks to follow fiḥi Muḍārabah that was for the individuals and applying the same on the banks that are commercial entities.

He supported his argument with some good references in the Fiqh that sought to secure the position of the Rabb al-Māl as a solution to deal with the declined honesty/ Amānah level of people. He mentioned that Omar ibn Khattab (may blessing of Allah be on him) the second Khalīfah (ruler), ordered his two sons to guarantee the money that was paid to them by one of the governors for investment purpose. The agreement was to return the capital to Bait al-Māl and keep the profit. But Omar changed the agreement to a Muḍārabah with a fifty percent profit sharing ratio and at the same time guaranteeing the capital.

In this context, to examine Muḍārabah logically and deduce the Maqāṣid al Sharī’ah we may question the ḥikmah (wisdom) of the Sharī’ah to give such a formula of loss in a way that the financial loss will be borne by the Rabb al-Māl. One of the wisdoms is that Islam aims to protect the worker as he might be the weaker party that is poor or short of funds, hence, he cannot be put financially under the double burden in case of loss due to force majeure or reasons that are out of control. Because in that case the worker will lose his time, reputation, and effort which itself is consider a material lose under the contemporary good will value. If all the due diligence is followed and still some loss happened, the loss of money will be borne by the Rabb al-Māl. unless it occurred due to the negligence, misconduct or violation of the terms and conditions by the Muḍārib (Hassan, 2010).

Although there is high chance that many banking and Fiqh scholars will stick with the traditional opinion of Madāhib, study supports the Ijtihād to make the banks guarantee the money of account holders and update the accordingly the Muḍārabah terms and conditions (Hammad, 2000). This arrangement is motivation to urge the Rabb al-Māl to do his best research, investigation about Muḍārib credibility, reputation, historical achievements and honesty. In addition, ask for feasibility and risk study before entering into the Muḍārabah contracts. This applies to both customer and bank in sphere of applying Muḍārabah in Islamic banking and finance.

CONCLUSION

The research concludes that it is utmost important to give highest importance and priority to the security of the depositors’ money. In line with the growing banking challenges, it is noticed that collecting billions of dollars into few banks carries similar massive hazards for the safety of depositor money. However, Islamic banks have some further distinction that makes it not guarantee any collected money in its Muḍārabah Islamic investment and saving accounts as stipulated in its terms and conditions. By doing so they claim that they are

complying with the Shariah principle of Mudarabah. At the same time, they take Shariah approvals to do what ever alteration they require to Muḍārabah to make it favourable for banks own operations, profitability and in net shell perform same like conventional interest-based banking accounts. The study discussed these double standards of Islamic banks by shifting all the risks to the funds providers or the customer and advocated their protection as a requirement of Maqāṣid al-Shariah. Hence, researcher provide full insight of the Mudarabah from Fiqh, banking, operations and ethical perspectives and suggested direct and transparent fiqhi solution for the matter. As a matter of principle, comparing to finding tricks and indirect paths to reach to same results the right approach is by updating some Mudarabah traditional terms and condition. Upon careful examination of the current practices of common investment pool of banking unrestricted Muḍārabah, study calls for a review of classical terms and conditions of Muḍārabah to make them more rational and suitable with current financial environment of Islamic banking and finance. It recommended more transparent practices by Islamic banks and to provide equal chances under the original aims and objectives of profit loss sharing method and shift towards the restricted Muḍārabah that creates investment pools for projects models. The Islamic banks accounts should distinguish itself from borrowing and lending model, accordingly, the profit distribution should not be linked with interest rates. Eventually, this will lead to using Muḍārabah in particular and Islamic banking for promoting production, moral and fair money circulation and towards a model that is based on production and money circulation as per Maqāṣid al-Sharī'ah. The study limitation was that the opinion was based on the ijtihad of two learned scholars; therefore, in order to make it more enforceable it is recommended that such opinion is discussed by central banks, regulators and practitioners on the level of fiqh councils, AAOIFI and IFSB.

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