

**CONFERENCE OF ISLAMIC PERSPECTIVES  
ON MANAGEMENT AND FINANCE**

**2- 3, July 2009**

**CHARITABLE INVESTMENT BANKING  
MODEL:  
AN ISLAMIC PERSPECTIVE**

**Abdel Fattah M. Farah (Ph.D. Econ.)**  
*Economic Advisor,  
Ajman Chamber of Commerce  
United Arab Emirates*

**ORGANIZERS:**

**The School of Management  
University of Leicester**

## **TABLE OF CONTENTS**

- 1. INTRODUCTION**
- 2. ISLAM AND THE SOCIO-ECONOMIC VALUES**
  - 2.1. Prohibition Of Usury And Alternatives Values
  - 2.2. Qardh- Hassan As A Business Value
- 3. CHARITABLE INVESTMENT**
  - 3.1. Socio-Economic Returns Of Charitable investment
  - 3.2. Profit Rate In Charitable Investment
- 4. THE CHARITABLE INVESTMENT BANK MODEL**
- 5. THE CIB DEPOSITS**
  - 5.1. Charity Accounts**
    - 5.1.1. Zakaah Account
    - 5.1.2. In-Advance Paid Zakaah
    - 5.1.3. Sadaqat Account
  - 5.2. Charitable Investment Accounts**
    - 5.2.1. Investment Account
    - 5.2.2. Saving Account
  - 5.3. Waqf Accounts**
    - 5.3.1. Qardh-Hassan Account
    - 5.3.2. Waqf Account
    - 5.3.3. Current Account
- 6. EXTERNAL ZAKAAH AND CHARITY ORGANIZATIONS**
  - 6.1. External Zakaah & Charity Funds
  - 6.2. Settlement Of Defaulted Debtors
- 7. THE USERS & THE AREAS OF USE**
- 8. CONCLUSION**

## 1. INTRODUCTION:

Vital projects in poor countries suffer from lack of adequate finance and management. This research attempts at forming an appropriate mechanism utilizing positive normative values to help achieve modernization and sustainable socio-economic development programs in poor rural areas<sup>1</sup>.

Voluntary interest-free loans and charitable investments are assumed to be the cornerstone for establishing a model of a charitable investment Bank ("CIB") as a professional financial tool for achieving such a goal. The research also aims at streamlining external funds to guarantee that the CIB qardh-hassan (interest-free) loans are in accordance with deeply rooted values that Muslims share with the rest of the world cultures.

The CIB is expected to reduce poverty and build stronger local and international foundations for justice, welfare and confidence.

## 2. ISLAM AND THE SOCIO-ECONOMIC VALUES:

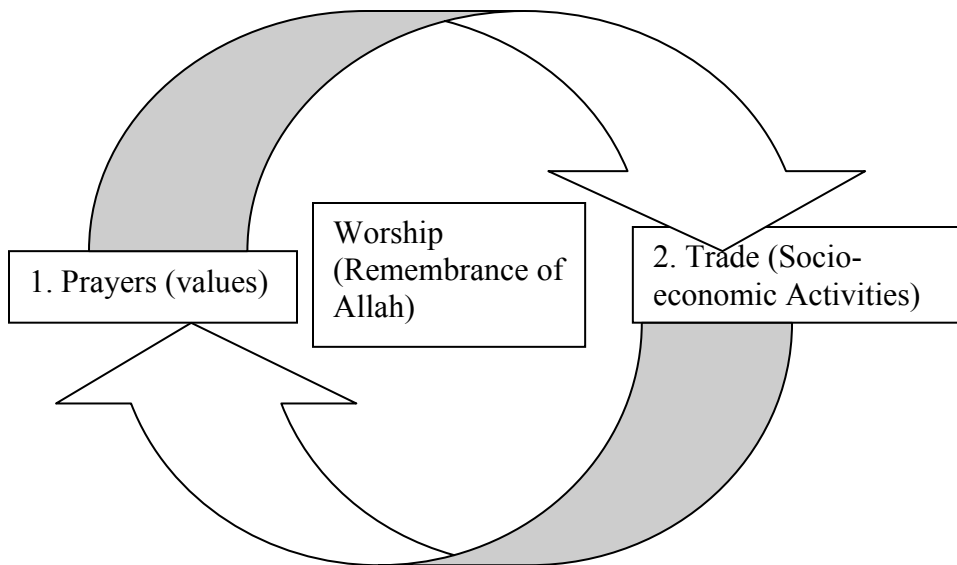
The returns of any investment could either be profits or social benefits. Both are recommended in Islam whenever the means to attain them are ethical. Performing prayers as worship, for example, imbues individuals with the socio-economic values necessary for the daily life. The following Qur'anic verse identifies the significance of performing both socio-economic activities and prayers consecutively:

**"Believers, if the Friday prayers are called for, hasten to remembrance of Allah and *cease trading*, that is best for you if you but knew it. Whenever the prayers are over, *disperse on earth in quest of Allah's bounty*. Remember Allah much so you may prosper".61: 10.**

**Figure 1 illustrates** the link between prayers and trade as worship of Allah.

---

<sup>1</sup>See: Michael and Stephen, *Economic Development*, 8th Ed. 2003, pp. 12-14



A prophetic hadeeth narrated by Tabrani states that:

*"Some sins are unforgivable by prayers or fasting or visiting the house in the time of Hajj or at other times -umrah-, except by effort (ethical) to make a living".*

Similar to other textual contexts, this hadeeth recommends ethical means of livelihood and shows its significance as worship of Allah.

## **2.1. PROHIBITION OF USURY AND ALTERNATIVE VALUES:**

The proposed CIB is extremely dependant on the prohibition of usury and the recommendation and worthiness of charity in Islam. Some Qur'anic verses in this regard are:

2.1.1. **"Allah will deprive usury of all blessing but will give increase for deeds of charity; for He loves not creatures ungrateful and wicked". (2: 276).**

2.1.2. **"Allah permitted trade and forbade usury" (2: 275)**

2.1.3. **"Fear Allah, and waive what is still due to you from usury, if ye are indeed believers or war shall be declared against you by God and His Apostle. If you repent, you may retain your principal, deal not and not be dealt unjustly. " (2: 278-279).**

The cyclical global crises are reflections of the above mentioned deprivation of blessings and declaration of war by Allah.

Several people in Muslim communities refuse receiving usurious returns and bestowing them as charity is also undesirable. The Machiavellian philosophical statement of "**Ends justify means**" is rejected in Islam, because usury is excluded from charity according to the Qur'anic verse: "**Believers, give in alms (charity) of the good wealth you have earned**". (2: 267)

Profit-loss sharing, advancing interest-free loans and offering charity are the Islamic alternatives for usurious loans. Based on such normative values was the movement of the Islamic banks in the early seventies of the last century with positive contributions to international finance. A similar situation is expected with regard to the CIB within the coming decade.

## **2.2. The Business Value of Qardh- Hassan:**

Qardh-hassan is the loan offered without any additional returns where the initial amount only is repaid. Several Qur'anic verses praise lenders of Qardh-hassan.

A verse states: "**Allah will multiply for whoever lends Him a good loan (without usury)**". (2: 245, 57: 11) The concept of "**lending to Allah**" refers to almsgiving and offering qardh-hassan.

Many Prophetic Hadeeth consider advancing Qardh-hassan as equivalent to, or even better than, giving a part of it as *Sadaqah* (almsgiving/Zakaah). The reasons for this include the following:

1. The required loan amount is normally more than the sadaqat/charity offered
2. The loan is circulated frequently as a revolving fund
3. Debtors tend to increase production in order to repay the loan
4. The velocity of money circulation will be more because the marginal propensity to consume for the category of poor people is higher.

## **3. CHARITABLE INVESTMENT:**

Charitable investment is a profit making process in socially responsible projects aiming at elimination of poverty in poor societies. It contributes to expanding supply of necessities including food, shelter, drinking water, and electricity, as well as building infrastructure and facilitating educational and health services. A Prophetic Hadeeth praises those who

provide such good social services stating that: *"The best of people are the most beneficial to people"*<sup>2</sup>

### **3.1. Socio-Economic Returns Of Charitable Investment:**

Charitable investment funds would be channeled to finance development projects with long term socio-economic benefits that include the following:

1. Increasing per capita income and raising standards of living for poor citizens
2. Best utilization of unemployed human and natural resources
3. Increasing the supply of hygienic quality food products
4. Provision of good nutrition, drinking water and food for poor people and facilitating for them health and educational services
5. Reducing prices of necessities by increasing supply
6. Expanding demand and finding new local markets for products
7. Expansion of foreign trade
8. Increasing investment, national income and flourishing the economic activity
9. Funding stock markets with real shares thereby reducing speculations
10. Leading towards technological transfer and advancement
11. Building good international commercial relations
12. Reducing violence, instability and terrorism

### **3.2. Profit Rate In Charitable Investment:**

The profit rate in charitable investment will not be exploitative and could be equal to, or less than the normal rates prevailing in the market, depending on the nature of the product and the real forces of supply and demand.

While the market forces direct investors towards the higher profit rates, the intention of a charity doer will be towards attaining social benefits in spite of the profit rates.

The profit rendered from charitable investment falls under charity because:

1. The investor willingly directs the investments towards none usurious dealings
2. A highest profit rate is not the best alternative for the investor
3. The investor values the socially beneficial projects

---

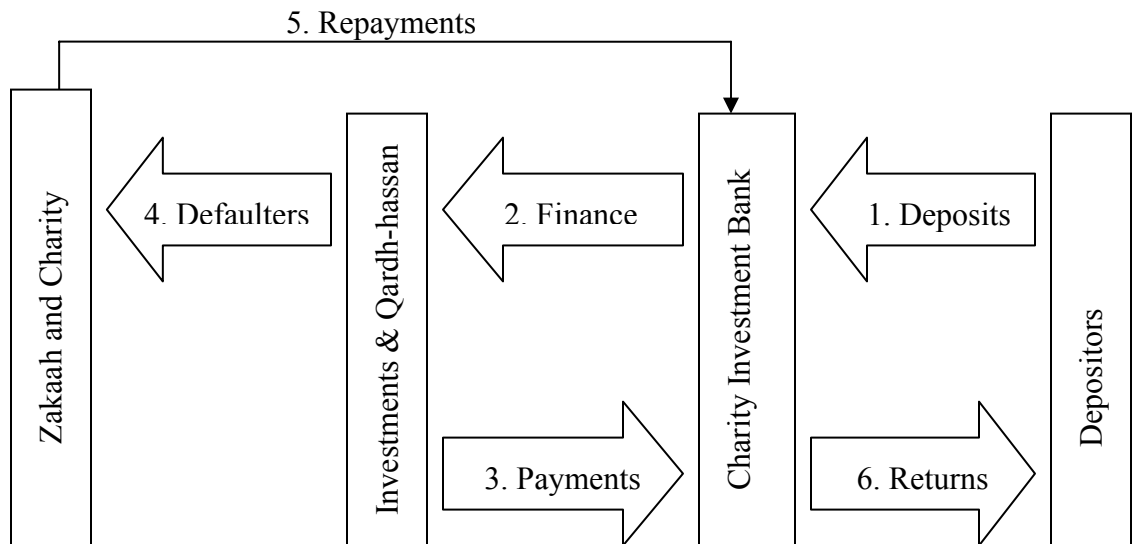
<sup>2</sup> Recommended as correct by Suyooti and Albani.

#### 4. THE CHARITABLE INVESTMENT BANK MODEL:

Figure 2 below illustrates the operational linkage between the four main elements of the CIB Bank Model as explained below:

- a) **Depositors:** Arrow 1 represents all the deposits of the CIB while arrow 6 represents the returns to the holders of charity investment accounts.
- b) **The CIB:** It receives deposits, finances investment, offers qardh-hassan, and pays returns to the holders of investment accounts. Arrow 2 represents the finance provided while arrow 3 represents the settlements.
- c) **The users:** Some users receive, invest, and payback the funds while others receive qardh- hassan.
- d) **The charity institutions:** Defaulters communicate with the charity organizations which make repayments to the CIB as represented by arrows 4 and 5 respectively.

**Figure 2: Elements of the CI Banking Model.**



#### 5. THE CIB DEPOSITS:

As illustrated in Table 1 below, the CIB offers a variety of accounts used either for Charity, Waqf (endowment) or Charitable Investment purposes.

##### 5.1. Charity Accounts:

These accounts are entirely charity accounts where the principal amounts and their returns are non-refundable i.e. charity and zakaah accounts.

### **5.1.1. Zakaah Account:**

Zakaah is a religious obligatory commitment, charged on wealth on lunar year basis at the rate of 2.5%, in the case of financial wealth when it equals or exceeds *Nisab*<sup>3</sup>. The zakaah account is utilized for the sake of the eight beneficiaries as specified in the Holy Qur'an (9: 60). Zakaah account is either funded from internal or from external sources.

5.1.1.1. The **internal sources** include collection of Zakaah within the CIB from charitable investment and saving accounts in accordance with the formats signed between the CIB and the depositors. Zakaah is not chargeable from the current accounts because such accounts are used by the CIB for financing charity projects.

5.1.1.2. The **external sources** include the funds received in this account from various zakaah payers.

If there is a specialized official house for zakaah in a country the situation would differ. The CIB would be authorized for collection and spending of zakaah or otherwise the deposits of the whole zakaah account would be channeled towards the official house of zakaah.

### **5.1.2. In-Advance Paid Zakaah:**

Zakaah could be collected or paid in advance for the period of three years or more if there is a need for advancing them to zakaah spending areas. Clearly stated development projects in rural areas or for poor citizens would encourage payers to advance Zakaah for all or a part of their wealth<sup>4</sup>.

### **5.1.3. Sadaqat Account::**

Sadaqat account within the CIB is a revolving fund utilized in charity and charitable investment. The account is subsidized from both internal and external sources. The internal sources refer to the profits rendered from the use of all accounts within the CIB. The external sources include the funds newly received from various donors. Charity account differs from zakaah account with regard to the following aspects:

---

3 Qaradawi; Yousuf.

4 Ibn Gudamah, Al Mughni. Hajr Press, Cairo, 1986. V4. p 85.

1. Areas of charity spending are general while that of Zakaah are specific.
2. Zakaah is compulsory and has specific conditions to be fulfilled (e.g. Nisab, payment time, collection and distribution authority, and payment rate) while charity is voluntary and has no such conditions.

## **5.2. Charitable Investment Accounts:**

Charitable investment accounts include investment and saving accounts where holders own the principal and share profit pro rata with the CIB. Restricted withdrawal from these accounts provides stability for better planning.

### **5.2.1. Investment Account:**

Funds in investment account are deposited for any number of agreed periods of 3, 6, 9, 12 months or their multiples. The CIB is entitled to find the best charitable investment opportunities decided by their socio-economic returns.

### **5.2.2. Saving Account:**

The CIB is authorized by the holders of saving deposits to invest their savings on their behalf as charitable investment funds. Saving account does not offer cheque books and drawing from it, although possible, is restricted. If more than a specific number of monthly drawings (usually twice) is made, the account doesn't deserve a share in the profit during that month.

The minimal balance of a saving account during each month shares in the profit/loss as per its contribution ratio in the overall investment pool. The Investment pool refers to the total amounts participating in investment during a specific period (normally a calendar year).

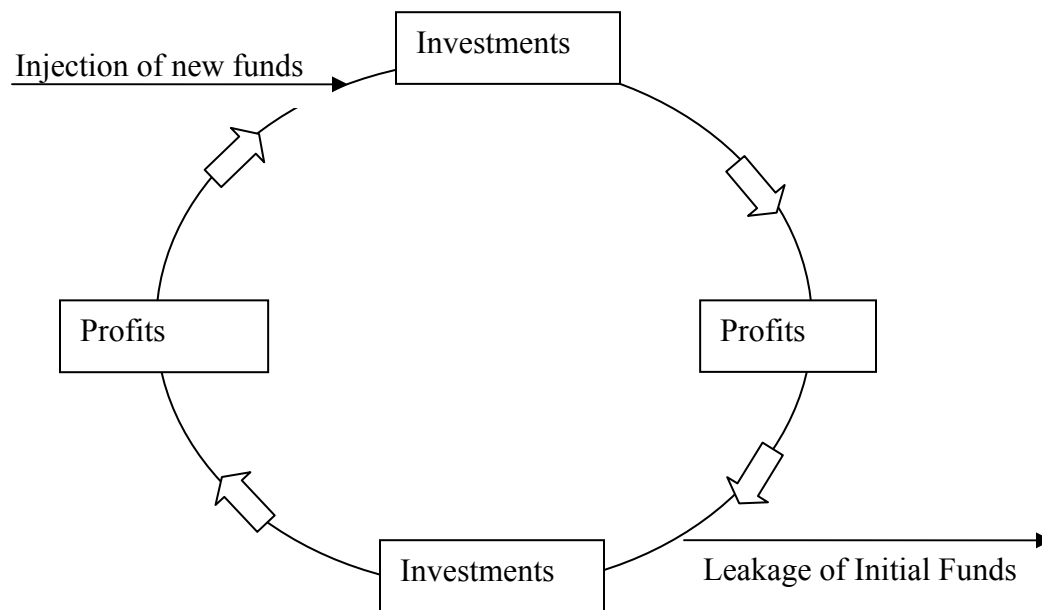
## **5.3. Waqf Accounts:**

Waqf accounts include waqf, qard hassan, and current accounts. The principal deposits are guaranteed deposits offered for utilization by the CIB in areas with high social returns but their holders do not share any profit.

### 5.3.1. Qardh-hassan Account:

Qardh-hassan is an interest-free loan from the depositor to the CIB for utilization in charity. As per the Maliki and early Hanafi Schools of fiqh qardh-hassan accounts or cash-waqf are encouraged forms of charity deposits<sup>5</sup>.

The charity deposits can either be channeled directly towards covering defaulted accounts and qardh-hassan (interest-free) requisitions, or indirectly towards charitable investments where their returns will again be channeled towards charity account. The movement of these accounts circulates from investment to profit and again to investment in a continuous loop while the initial funds are either injections when they are newly deposited or leakages whenever they are withdrawn from the concerned accounts, as illustrated in figure 3.



**Figure 3: The Investments and Profits of Funds.**

There will be transparency and specified criteria for offering the interest-free loans or leakages including the area of expenditure, the attitude of the requester, the credibility, fund availability, relation with the CIB...etc.

---

<sup>5</sup> Ad-Dirdiri, Ahmad bin Mohamed. *A-Sharh a-Ssagheer*, Eisa alHalabi Press. 1952. V4. p379. see Zuhaili, Wahbah. *Al-Wasaya wa al-Waqf*, Dar al-Fikr Press, Damascus, 1987, pp-162-164

### 5.3.2. Waqf Account:

The area of charity for a waqf account is wide and any of them could be specified or the CIB could be authorized by the depositor to select the relevant area. A waqf account with unspecified area of charity is a qardh-hassan from the depositor to the CIB while a qard hassan account is specified to be offered to the needy lenders on interest-free basis.

### 8.1.1. Current Account:

Current account is a short-term unspecified waqf account. It is an interest-free cash-waqf loan from the depositors to the CIB that it can use towards charity the way it wants. The holder of a current account in the CIB enjoys all the facilities provided in other Islamic banks.

**Table 1: Difference between Various CIB Accounts.**

Purpose	Investment Accounts		Waqf Accounts			Charity Accounts	
	Saving	Charitable investment	Current	Waqf	Qard Hassan	Charity	Zakaah
Deposit Period	Unlimited	Fixed	Unlimited	Fixed	Fixed	Open	open
Withdrawal	Restricted	Fixed	Unlimited	Fixed	Fixed	No	No
Cheque books	None	None	Available	None	None	None	None
Profit Share	Yes	Yes	No	No	No	Yes	Yes
Share in Charity	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Project area	Not specified	Specified	Not specified	Not Qard hassan	Qardh-hassan	Open	Specified

## 6. EXTERNAL ZAKAAH AND CHARITY ORGANIZATIONS:

The CIB coordinates and builds strong relations with external Zakaah and Charity Organizations on strategic partnership basis. Both the CIB and such organizations share the same goals and work cooperatively to extend their development mission.

### **6.1. External Zakaah & Charity Funds:**

Zakaah and Charity accounts of the CIB will be working closely coordinating with external zakaah, charity, and Takaful (Islamic Insurance) organizations in order to guarantee the current and saving accounts of the CIB and support its defaulters which are classified as one of the eight categorizes of zakaah beneficiaries<sup>6</sup>.

### **6.2. Settlement Of Defaulted Debtors:**

Under the supervision of the Central Bank and specified criteria, other charity organizations would partially settle the defaulted payments that the CIB alone would not be able to.

A portfolio system containing data of all dealers with the banking system will be maintained for reference whenever charitable investment or interest-free loans would be offered. Unless the justifications of default are accepted from an Islamic jurisprudential view point, a defaulter would not be liable for any sort of financial support in future.

## **7. THE USERS & THE AREAS OF USE:**

The end users of the CIB services (i.e. investment funds or qardh-hassan) are the individuals and private or community organizations that contribute to achieving the social development goals of the bank. They normally execute the projects that are targeted by the bank and are carefully selected with transparent policies and clear criteria.

Such projects are not usually financed by commercial banks because of their societal nature. Therefore, areas of competition between the CIB and the commercial banks whether Islamic or conventional are obscure, due to the difference of roles.

---

<sup>6</sup> Farah, Abdel Fattah M. *The Orientated Investment Of Zakaah: A Comparative And Analytical Economic & Jurisprudential Study*, Dubai Islamic Bank Printing Press, 1st Ed. 1997, pp. 116- 126.

## **8. CONCLUSION:**

This paper proposes a Charity Investment Bank (CIB) model aiming at facilitating sustainable development in rural areas of underdeveloped countries in a variety of charity investment fields.

Quranic verses, hadeeths and scholarly opinions as well as tables and figures are introduced to illustrate the idea of the CIB model. The positive utilization of Islamic values that praise qardh-hassan (interest-free loan), waqf (endowments) and charity and condemn usury represent the core philosophy on which the CIB is based.

The interaction between the depositors, the CIB, the users and the charity organizations as the four elements of the model is illustrated.

The model presents a mechanism for offering qardh-hassan and charitable investment funds, settlement of defaults and guarantee of saving and current accounts in a Shariah compliant manner. Eight sorts of CIB accounts are discussed under the three main categories of charity, charitable investment and waqf.

## 9. REFERENCES:

### A. References (English)

1. Abel, Andrew B, Ben S. Bernanke. "Macroeconomics". 2nd ed. Adison-Wesley P.C., USA. 1995.
2. Campbell R. McConnell. Stanley L. Brue. "Economics, Principles, Problems and Policies". 11<sup>th</sup> ed. Singapore: McGraw-Hill Book Co, 1990.
3. Dawood, N. J., *The Koran*, Penguin Books, 5<sup>th</sup> Ed. 1990.
4. Michael and Stephen, *Economic Development*, 8th Ed. 2003.
5. The Holy Qur-an English Translation of the Meanings and Commentary. King Fahad Holy Qur-an Printing Comlex, Al-Madinah Al-Munawarah, 1410 H.

### B. References (Arabic)

6. Abdul Baqi, M. Fuad, *Al-Mujam Al-Mufahras Li Alfaz Al Quran Al Karim*. Dar Ihya Atturath Al Arabi, Beirut. No year.
7. Abu Obaid, Al Qasim Ibn Salam (D\* 225 H). *Al Amwal*. 2nd ed. Cairo: Azhar Colleges Library, Dar Al Fikr, 1975.
8. Ad-Dirdiri, Ahmad bin Mohamed. *A-Sharh a-Ssagheer*, Eisa alHalabi Press. 1952.
9. Al Bukhari, Abu Abdalla Mohamed Bin Ismail Al Jaafi, (D 256 H). *Saheeh Al Bukhari*. 3rd ed. Ajman: Ulum Al Quran, 1987.
10. Al Dusuqi, Shams Uddin Arafa Mohamed Bin Ahmed. *Al Hashiya Ala Al Sharh Al Kabeer*. Cairo: Al Khayriyah Press, 1905.
11. Al Nasafi, Abdulla Bin Ahmed (D 710 H). *Madarik Al Tanzil Wa Haqaiq Al Ta'aweel*. 1st ed. Beirut: Dar Al Qalam, 1989.
12. Al Qaradawi, Yousuf. *Fiqh Al Zakaah*. 1st ed. Beirut: Muassat al Risalah, 1981.
13. Al Qurtubi, Abu Abdulla Mohamed Bin Ahmed Al Ansari (D 671 H). *Al Jami Li Ahkam Al Quran*. 1st ed. Beirut: Dar Al Kutub Al Ilmiya, 1988.
14. Al Sarkhasi, Shams Uddin Abu Bakr Mohamed Ibn Sahl (D 483 H). *Al Mabsoot*. Beirut: Dar Al Marifa, 1986.
15. Al Tirmizie, Abu Eisa Mohamed Bin Eisa Bin Sawrat (D 892 H). *Sunnan Al Tirmizi*. 1st ed. Hams, Syria: Al Fajr Al Hadeetha Press, 1967.
16. Al Zuhaili, Wahba. *Al Wasaya wa al Wakf Fi Al Shariah Al Islamiya*. Damascus: Dar al Fikr, 1987.
17. Farah, Abdel Fattah M. *The Orientated Investment Of Zakaah: A Comparative And Analytical Economic & Jurisprudential Study*, Dubai Islamic Bank Printing Press, 1st Ed. 1997.
18. Ibn Hajar, Abu Al Fadhl Ahmed Bin Ali Hajar Al Asqalani. *Fath Al Bari*, 1st ed. Cairo: Dar Abi Hayan, 1996.
19. Ibn Qudama, Muwafag Uddeen Abu Abdulla Bin Ahmed Bin Mohamed Al Maqdisi (D 620 H). *Al Mughni*. Cairo: Hajr press, 1986.
20. Ibn Rushd, Abu Al Walid Mohamed Bin Ahmed (D 595 H). *Bidayat Al Mujtahid Wa Nihayat Al Muqtasid*. Cairo: Modern Nahdha Press, 1960.
21. Malik, Ibn Anas. *Al Muwatta*, 1st ed. Cairo: Dar Al Rayan Litturath, 1988.
22. *Readings in the Islamic Economics*. Islamic Research Center. 1st ed. Jiddah: King Abdul Aziz University, The International Press Center, 1987.

\* D: Refers to the writer's year of Death. H: Stands for Hijri calendar.