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Challenges in the Application of Partnership Contracts in Islamic Banks: A Theoretical Analytical Study

A Thesis Submitted in Partial Fulfilment of the Requirements for the
M.Sc.Degree in Islamic Banking and Finance

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Defense Committee's Approval

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☐ Without making any changes to the thesis.

☒ After making the modifications attached with this decision.

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Abstract

Objective: This study aims to demonstrate the challenges associated with implementing the contract of participation in Islamic banks in the Kingdom of Bahrain and explore the extent to which the contract of participation and Islamic banks achieved the purposes of Maqasid al-Shariah. The study also presents the applications of the engagement contract in Pakistan and Oman.

Methods: Using qualitative research, 10 Islamic Shariah experts, including Islamic bankers who have served in their bank for more than 15 years, were interviewed. Risk professionals with sufficient knowledge of the meaning and structure of the participatory contract were also interviewed. NVIVO software was used to analyze the data collected.

Findings: The results of the study showed that the reasons for the rarity of Musharaka financing were the difficulty of implementing monitoring and its higher risks compared to other contracts, laws, and regulations. There was also a lack of awareness among staff and individuals of Musharaka financing. Results showed that the partnership contract based on the principles of profit and loss sharing achieves the purpose of Maqasid al Shariah more than other contracts.

Implications: The study contributes to understanding the constraints that have led to the restricted use of Musharaka financing in Islamic banks in the Kingdom of Bahrain. The findings of the thesis also assist finance decision-makers and policymakers.

Keywords: Islamic Banks, Musharaka, diminishing Musharaka, Maqasid al Shari'ah, Challenges of Musharaka.

Dedication

To the one who raised me, taught me values and principles, and my inspiration in the field of Islamic Finance.

(My Father).

To my first teacher, the first supporter of my ambitions, who gave me love and contributed to my success with her advice.

(My mother).

To the person who encouraged and supported me to pursue my Master's degree, who witnessed the beginning of my journey, and whom I hoped would witness the end of it.

(My grandfather: may his soul rest in peace).

To those who supported my stumbling footsteps

(My sisters and brothers).

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1.0 Chapter 1 – Introduction to the Study

1.1 Introduction

Islamic financial systems are an alternative approach to conventional finance. They offer financial instruments based on principles derived from shariah laws, such as the prohibition of interest (Riba), uncertainty (Gharar), and gambling (Maiser). They also promote risk-sharing, social justice, and ethical investment. Over the last 30 years, Islamic banking and finance have expanded and prospered in Bahrain and globally to become a major worldwide business (Al-Sadah, 2019).

Bahrain has established itself as a major hub for Islamic financial activities and is recognized globally as a trailblazer in the sector. It boasts the highest concentration of Islamic financial institutions in the Middle East and hosts several leading global organizations that set standards for Islamic Finance. Bahrain's dynamic Islamic finance landscape includes 6 retail banks, 13 wholesale banks, and 9 Islamic branches of traditional banks (Banking | CBB, n.d.; Erdoğan et al., 2018).

Despite the challenges facing Islamic banks, they have continued to succeed. Islamic banks play the role of financial intermediation between the receipt of deposits and the granting of loans, but they differ from conventional banks by restricting transactions to the provisions and principles of Islamic law. They are distinguished from their conventional counterparts in that they are banks based on the principle of participation in profit and loss sharing (PLS), which is that the profits that Islamic banking receive are in line with an agreed ratio. This arrangement delivers a large reward when the customer's business profit is strong, but it carries a significant risk when the customer loses, leading to the parties bearing the loss of their shares (Wahyudi et al., 2019).

In practice, Islamic banks tend to reduce their involvement in contracts based on participation in profit and loss and increase debt contracts to minimize their risks. It is important to recognize the extent of the use of Murabaha finance in Islamic banks in Bahrain. The following table represents the ratio of Murabaha financing to financing assets for the main five Islamic banks in Bahrain as of December 31, 2021. The data were compiled manually from each Bank's annual reports.

Table 1: Ratio of Murabaha financing to finance contracts

Bank Name	Murabaha to Financing Asset
Bahrain Islamic Bank	85.31%
Al Salam Bank	48.59%
Kuwait Finance House	42.97%
Al Baraka Bank	36.96%
Khaleeji Bank	99.69%

This study explores why Islamic banks are hesitant to utilize partnership contracts, analyzes the challenges Islamic banks encounter when employing Musharaka partnership contracts for investment purposes, and the key risks inherent in this financial arrangement. Additionally, the study explores partnership contracts, defining and categorizing their types, and offers an overview of the contracts from a Shariah perspective. It presents the researcher's viewpoint on which types of contracts fulfill Maqasid al Shari'ah.

1.2 Research problem

Islamic banks' funding methods come in a variety of styles and forms, each of which is an alternative to the activities carried out by conventional banks. While Islamic banks utilize equity-based partnership contracts such as Mudarabah and Musharaka, they also use other contracts such as Murabaha (cost-plus financing) and Ijarah (leasing).

There has been a record of restricted availability and scope of partnership contracts in Islamic banks; the percentage of debt contracts in Bahrain Islamic banks in 2016 was 48.1% compared with partnership contracts at 28.6% (Tashkandi Al Jelassi, 2016). Limitations are attributed to a range of factors, including high risk, asymmetric knowledge issues, moral hazards, and challenging financial evaluation procedures (Yustiardi et al., 2020). There was also a lack of interest by bank management in Musharaka financing; a shortage of loyal, honest, and skilled entrepreneurs; and a lack of expertise and government assistance (Farooq & Ahmed, 2013).

This study emphasizes the limited use of partnership financing in Islamic Finance due to the challenges associated with this type of contract. The research problem lies in quantifying the extent of implementation of partnership contract financing in Islamic banks in Bahrain and the significant obstacles that restrict its application.

The financial practices in Islamic finance are guided by the principles of Maqasid al-Shari'ah, which aim to ensure justice, welfare, and the protection of wealth, faith, life, intellect, and progeny. In this context, two primary forms of financial contracts are prevalent: debt contracts (e.g., Murabaha, Ijarah) and partnership contracts (e.g., Mudarabah, Musharakah). Each contract type has distinct mechanisms and implications for the participants involved.

Despite the theoretical alignment of both contract types with Maqasid al-Shari'ah, there is limited empirical research comparing their effectiveness in achieving these objectives. It is unclear how each contract type contributes to or hinders the goals of economic justice, equitable wealth distribution, and social welfare. This study seeks to address the gap by examining the differences between debt contracts and partnership contracts in achieving the purposes of Maqasid al-Shari'ah.

1.3 Research Questions

The following are the research questions that this study addresses:

1. How do partnership contracts and debt contracts in Islamic finance compare in achieving the objectives of Maqasid al-Shari'ah, especially in terms of economic justice and wealth distribution?
2. What is the reality of implementing partnership contracts in Islamic banks?
3. What are the reasons for limiting the financing of partnership contracts in Islamic banks?
4. What potential solutions can be implemented to enhance the utilization of partnership contracts in Islamic banks?

1.4 Research Objectives

The primary objective of this study is to explore partnership contracts from an Islamic perspective, focusing on their applications within the Bahrain Islamic banking sector. The research aims to evaluate the extent to which these contracts, particularly Musharaka, align with the principles of Maqasid al-Shari'ah, such as promoting economic justice, equitable wealth distribution, and social welfare. The study also assesses the risks and challenges associated with implementing partnership contracts in Islamic banks and identifies effective strategies to mitigate these risks. By examining both theoretical and practical aspects, the study seeks to provide comprehensive insights into how partnership contracts can be optimized to better serve the goals of Maqasid al-

Shari'ah, ultimately contributing to the advancement of Islamic finance practices in Bahrain.

1.5 Research Significance

The study will address a question which is often asked: Why do Islamic banks use debt contracts more than partnership contracts, and why are they reluctant to use partnership contracts more widely? The study also offers insight into partnership contracts, identifies factors influencing the limited adoption of partnership contracts in Islamic banks in Bahrain, and proposes alternative solutions, policies, and strategies to enhance their utilization.

1.6 Research terminology

Islamic banks: Islamic banks are financial institutions offering a wide variety of financial services in accordance with the principles of Islamic law and rules. They are subject to the supervision and control of the central banks.

Partnership Financing: A type of Shariah financing product known as equity financing is predicated on profit sharing. Typically, working capital or investments are used for this kind of funding (Effendi, 2018).

Debt Financing: Debt financing is based on underlying contracts, which are commonly employed in Islamic Finance. This type of finance is derived from sales transactions (Maikabara, 2018).

Musharaka : Musharaka is a contract where partners invest money in a project and share the risks and profits. Profits are split evenly among partners according to a predetermined ratio, but losses are split exactly in proportion to the capital contributed by each partnership (M. Kabir Hassan & Lewis, 2004).

Maqasid al Shari'ah: The general objectives of Islamic legislation consist of the deeper meanings (ma ani) and inner aspects of wisdom (hikam) considered by the Lawgiver (Shari) in all or most of the areas and circumstances of legislation (ahwal al-tashri) Ashur, M. A. T. I. (2006)

Risk/Challenges: The frequency of interactions between employees and their supervisors and colleagues when working remotely, including factors that can obstruct the attainment of specific objectives (Kanchu & Manoj Kumar, 2013).

Chapter 2 – Literature Review

2.1 Background

Islamic finance is based on Islamic principles. For example, Islamic banks are not permitted to pay interest on deposits or loans or to fund Shariah non-compliance projects, but this does not exclude them from lending. They offer loans through sales, leases, and Profit-Loss Sharing. The Islamic system is based on asset ownership on the one hand and profit and loss sharing on the other (without guaranteeing the profit). Islamic finance is also built on concepts and methods originating from Islamic law.

Islamic banks have unique characteristics such as license variations; a Shariah Supervisory Body (SSB); and sale and purchase transactions, rather than money exchange. There is no guarantee of capital or profit for investors in the bank and subject to a particular law in the courts (Bahrain) other than the other banks that try in the commercial law. Islamic banking is built on the Islamic financial system. It is a banking system with rules and regulations based on Shariah laws, or Islamic jurisprudence derived from the Quran and the Sunnah of the Prophet Muhammad. Its functions must be consistent with Shariah regulations and principles (Muhammad, 2014).

Most theoretical models of Islamic banking are based on Musharaka, although current Islamic banking practice deviates from these models. Almost all Islamic banks, investment businesses and investment funds provide trade and project financing on a mark-up, commission manufacturing, or lease basis. PLS only has a small role in Islamic banking and finance. This is due to the prohibition of interest in Islamic financial transactions and the structure of Islamic banks, which is based on the idea of profit and loss sharing. However, there is increasing evidence that Islamic banks prefer debt-based over equity-based securities. (Farooq, 2007; Ariffin et al., 2015); Sadique, 2015).

Islamic banks are currently applying for more debt-based financing, especially in Murabaha and Ijarah. Equity financing by Islamic banks is less widespread than debt financing. Furthermore, the application of equity financing mechanisms is less developed.

2.1.1 Debt contracts vs. Equity contracts

Islamic finance offers a range of financial instruments, each with a particular function, to fulfill the unique demands of businesses and individuals. These financial instruments can be classified into debt financing (Financing to be indebted to the customer) and equity financing. According to Aggarwal & Yousef (2000), Tashkandi and Al Jelassi (2018), Iosco (2004), and Jusoh & Khalid (2013), alternative "interest-free *riba*" Islamic banks and monetary authorities have developed funding mechanisms in numerous countries. The financing formats derived from Islamic jurisprudence and used by Islamic banks are divided into Trade-off Contracts and Participatory Contracts.

Two main types of contracts define the financing operation of Islamic banking: the contract of PLS (*Ukud al-Isytirak*) and the contract of exchange (*Ukud al-Mu'awadhat*). Muhammad (2014) divided the financial activities conducted by Islamic banks into three basic types of Shari'ah-compliant contracts: Profit and Loss Sharing (PLS) Base, Trade Base, and Lease Base. Nugraheni and Alimi (2022) categorized Islamic financial contracts into four groups of transactions: profit and loss sharing, lease, sale, and purchase and loan.

Equity finance is the agreed profit Islamic banking receives in proportion to the customer's business earnings. Equity financing will deliver a large reward when the customer's business profits are substantial, but it also carries a significant risk if the customer loses money. This occurs because this finance does not guarantee revenue (return). Equity-based finance is a type of financing used in partnership arrangements where two parties share profits and losses (Maikabara et al., 2020).

A sale contract contrasts the idea of debt financing with a contract that guarantees certainty of payment, both in terms of quantity (amount) and time (Wahyudi et al., 2019). Because debt instruments are asset-backed, Islamic debt finance is organized with contemporaneous underlying exchange contracts, such as sale and buy agreements. In Islamic finance, an underlying asset must be used as the subject of the contract (Iosco, 2004). The contract of exchange permits the bank to utilize its funds to conduct economic transactions, which often include purchasing products or assets from a third party and reselling them to its customer on a delayed basis, creating a responsibility to pay later. The delayed exchange contract allows Islamic banking to

develop a variety of debt-based financing arrangements. (Jusoh & Khalid, 2013): Debt-based, through a sale-repurchase arrangement or back-to-back sales of borrower or third party-held assets; asset-based via a sale-leaseback arrangement (operational lease); or the lease of third-party purchased assets with purchase obligation components (financing leasing) and equity-based future assets (Jobst, 2007).

Islamic banks thus offer four financing mechanisms: equity financing, sale (debt-based financing), lease financing, and, at the institution level, Al Qard al Hassan. Financial contracts in Islamic banks can be divided into two types: debt and equity contracts. Murabaha, Ijara, Salam, and Qard Hasan are all considered debts since they generate responsibilities between a creditor and a debtor, regardless of how the contract is structured. Equity contracts encompass both Musharaka PLS and profit-sharing Mudaraba. This study focuses on equity-based contracts, especially Musharaka.

Table 1- Differences between debt and equity contracts

Basis for comparison	Debt base	Equity base
What is it?	Loan Funds	Own Funds
Reflects	Obligation	Ownership
Term	Comparatively short-term	Long-term
Status of holders	Lenders	Proprietors
Risk	Less	High
Return	Installment/ limited	Dividend/unlimited
Collateral	Essential to secure loans, but funds can be raised in other ways.	Only third-party collateral is allowed
Islamic financial instrument	Murabaha	Musharaka
	Ijarah	Mudharaba
	Istisna	
	Salam	

2.2 Concept of Partnership in Islamic Jurisprudence

2.2.1 Definitions of Sharika

Sharika can be defined linguistically, and in Fiqh scholar.

2.2.1.1 Sharika in linguistics

Sharika means to merge or to mingle; it comprises two shares, and neither can be distinguished from the other (Al-Shubaili, 2010).

2.2.1.2 Sharika in Fiqh scholar

1. Hanbil scholars define Sharika as an involvement in entitlement or disposition (Bin Qudamah, 1969).
2. (Al-Shirbini, 1994) Sharika, according to Shafi scholars, is evidence of a right in something shared by two or more participants over a common property.
3. Hanafi scholars define Sharika as a contract between participants in property and profit (Effendi, 1911).
4. Sharika, according to Malikiah scholars, is permission from each partner to disposition, whether that act is for himself or for his partner (Al Dosari, 2019).

2.2.2 Legality of Musharaka

2.2.2.1 The legitimacy of the Musharaka based on the Qur'an:

1. "...but if more than two, they share in a third..." (Al-Nisa':12).

The passage emphasizes the norm of Islamic inheritance. However, Muslim jurists have generally interpreted it to include the broad permissibility of any sort of partnership.

2. "Verily many are the partners (in business) who wrong each other except those who believe and work deeds of righteousness and how few of them." (Sad: 24).

Tafsir Ibn-kther (Abu Dawud) said: "He has wronged you in demanding your ewe in addition to his ewes. And, verily, many partners oppress one another, except those who believe and do righteous good deeds, and they are few." This verse is often cited as evidence for the permissibility of companies and partnerships in Islam, even though it relates to conflict. It establishes the existence of the company without denying its contract.

2.2.2.2 The legitimacy of the Musharaka based on the Sunnah

Abu Hurayrah (RA), trusted companion of Prophet PBUH, said: “Allah says: I am the third [partner] of the two partners as long as they do not betray each other. When one of them betrays the other, I depart from them”. [Reported by Abu Dawud and graded Sahih (authentic) by Al Hakim].

This means that, “Allah, the Exalted and Most High, blesses partners in their riches who are trustworthy with each other's money and exhortations to participate without betraying the partner” (Al-Khayyat, 1994).

Islam places a high value on honesty and truthfulness; this is especially relevant in commercial transactions. When two or more individuals form a partnership, they effectively place their faith in each other. They trust that each other will operate in good faith and not endanger the partnership's success. This shows that Allah permits financial transactions in the interests of citizens. Some people have enough experience but lack money. Some have money, but there is insufficient expertise to run a project. There are also those who have money and expertise but need more finance. By partnering with these groups, solidarity and cooperation is created to achieve people's interests.

2.3 Classification of Sharikah

2.3.1 Sharika in Fiqh

Sharika, which means “sharing”, is classified into three groups in Islamic Fiqh terminology: permissibility company, partnerships by ownership (Sharikat al-Muilk), and partnerships by contract (Sharikat Alaqd). Permissibility company involves the public being collectively entitled to ownership by taking and possessing permissible features of nature that originally belonged to no one, such as water, fallen leaves, and trees growing on permissible mountains (Book of Jurisprudence of Transactions): “And in this came the hadith of Abu Khirash al-Hudhali: I went on an expedition with the Prophet (ﷺ) and heard him say, ‘People are partners in three things: grazing pasture, water, and fire.’”(Reported by Ahmad and Abu Dawud, (Thiqah)).

Partnerships by ownership (Sharikat al-Muilk) and partnerships by contract (Sharikat Alaqd) are also important; partnerships by ownership means ownership of a property or obligation by two or more individuals not designed for commerce or profit. It can arise from inheriting, purchasing, giving, or combining capital, and it ends in division of the proceeds. Consequently, Sharikat al-Muilk is divided into two kinds based on how it develops: discretionary and compulsory (Usmani, 1998). Discretionary arises without the will of the partners, whereas compulsory is developed with the will of the parties.

Partnerships by contract (Shirkat-al-Aqd) are defined as contracts established between two or more partners to share money, work, or security, and the permission to dispose of them. The profit is shared between them; this type of contract is what the jurists meant when they used the word "Shirkah" (Company in Islamic jurisprudence).

According to the Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI), Shirkat al-'Aqd (Contractual Partnership) refers to an agreement between two or more parties to pool their assets, labor, or liabilities to create profit (Shariah Standards, 2017). Sharika is a cooperative contract concluded between two or more partners to manage a joint business operation for the purpose of profit, often used in Islamic banking and in the financial system (Khan et al., 2020). Additionally, the Journal of Judicial Rules No. 1329 defined Sharikat Alaqd as a contract between two or more people in which the capital and profit are divided.

Sharikah is called Sharikat al-Amwal when participants share in the capital and profit. All signatories to the contract provide capital for the business (Farooq & Mushtaq Ahmed, 2013). The partners enter into either a Mufawadha or Innan. Innan means that two or more people share their capital and profit whether both labor with their own hands, or one of them labors and has more profit than the other. In this regard, Al-Anan is permissible (Al-Fawzan, 2002). This form of Sharika is common among individuals because equality in money, management, or business operations and the kafala are not essential conditions (Al-Shubaili, 2010).

Sharikat al Mufawadah is when two or more persons agree to form a commercial partnership on the premise that they have equal capital, expenditure, and liabilities, which means that both partners are accountable to the other in purchasing and selling.

In commercial dealings, each partner is responsible for fulfilling the obligations of the other. They are jointly accountable for the rights and responsibilities associated with their trade. Each partner is regarded as an agent for the other in terms of what is owed to them and what they are accountable for; they act as guarantors for one another (Al-Zuhaili, 1997).

When all members or partners collectively engage to supply services for their customers and the profit is shared among them according to an established ratio, it is called Shirkat-al-Aamaal (Muhammad et al., 2017).

In Shirkat-al-Wujuh, partners agreeing to cooperate conduct business based on their market reputation and goodwill rather than their talent and capital (Farooq & Mushtaq Ahmed, 2013).

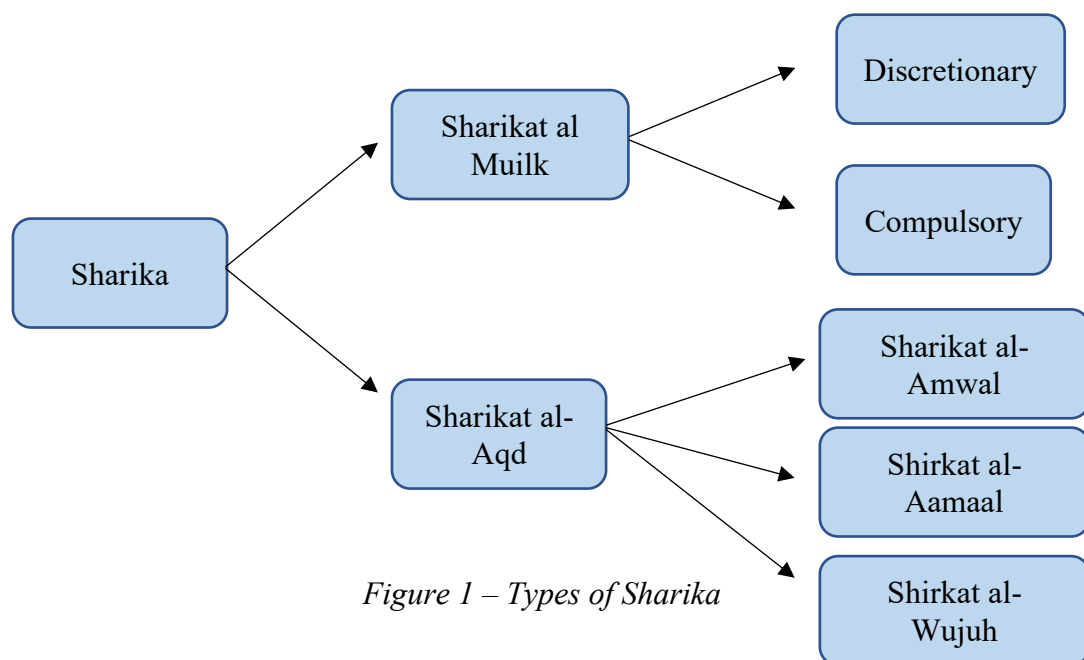


Figure 1 – Types of Sharika

In Sharikat al Muilk, the partners might decide to engage in commerce, even though this was not their intention at the outset. Because this agreement is implemented without a Sharikah contract, there is a missing investment characteristic. While the purpose of Sharikat al-Aqd is to promote commerce and to increase the capital between the two parties, as explained above, this type of Sharikah is an investment.

Sharikah is defined as a collaboration between two or more parties to put their capital and effort into fulfilling profit by sharing profits and losses between them.

2.3.2 Modern companies

(The International Islamic Jurisprudence Academy, 2003; Shariah Stander, 2017; Al-Shubaili, 2010).

Table 2- Types of modern companies

Financing partnership	Personal company
- Stock company	- Joint liability company
- Company limited by share	- Partnership in commendum
- limited liability corporation	- Muhassah partnership

A **stock company** is one whose capital is divided into equal marketable shares, and each partner is liable for the amount of capital he contributes. The shares are an indivisible and negotiable stock. A **company limited by shares** is a firm whose capital is made up of tradable shares, and its members are separated into two categories: joint partners, who are jointly liable for the company's obligations, and silent partners, whose responsibility is restricted to the value of their shares. A **limited liability corporation** is one in which a small number of partners owns the capital, usually no more than a specific number (50 partners); the size of each partner's stake in the capital determines their obligation, and its shares are non-tradable. These types of companies are under Sharikat al-Amwal since they rely on partner money for their establishment and formation, independently of each shareholder, and their shares are transferable.

A **Joint-Liability Company** is a firm formed by two or more people for the purpose of trade; they share the capital and are individually and jointly liable for all of their private finances before creditors. It is mostly based on personal acquaintance between the parties. A joint-liability corporation is a private partnership; this collaboration must be publicly stated as a registered corporation with a distinctive name (trademark). A joint-liability firm has its own legal identity and financial obligation separate from the partners' liabilities. However, if the company's assets are insufficient to pay its liabilities, all partners are individually liable. **Partnership in commendum** is a company formed by one or more partners who are jointly responsible, as well as by one or more partners who are shareholders outside of management and are known as limited partners, and whose liability is limited to the amount of their capital shares. This firm

comprises managing and sleeping partners; the controlling partners in this partnership are jointly accountable for the company's obligations under the theory of joint responsibility. Each sleeping partner's obligation is limited to the number of lots he owns and does not include his assets. The responsibility of some investors is allowed to be restricted without any payment for doing so, in which case the company is made up of joint-liability partners and limited liability partners. Sleeping partners are not permitted to interfere with the firm's activities.

The law prohibits identifying the names of the investors on the date of the company's registration. Only the amounts raised from sleeping partners are reported (Shariah Standers, 2017).

A **Muhassah partnership** is a hidden company that has no legal personality and is formed between two or more people, each of whom has a known share of the capital; the partners agree to share the profits and losses arising from one or more commercial activities carried out by the partners together or separately. Liability is limited to the person who carried out the activity. This sort of collaboration falls under the umbrella of personal or private companies. This is because, before entering into a partnership, the partners consider each other's financial strength and capacity to satisfy financial responsibilities using personal assets. In Sharikat al-Muhassah, there is a lack of juristic personality since persons other than the partners are unaware of it; as an entity, this partnership bears no independent financial liabilities. Joint-liability companies, Partnerships in command, and Al Muhassah partnerships are individual companies whose entity is built by partners, where each knows, respects and trusts the other.

The fundamental rule governing business is permissibility; every trading arrangement is acceptable provided their operations are devoid of Shariah restrictions. If their activity is banned, such as usurious banks or corporations that deal in forbidden goods, such as selling narcotics, honor, and pigs in all or a portion of their transactions, they are forbidden companies whose shares cannot be owned or traded. Companies must also be free of dishonesty, ignorance and conflict and any other grounds that would render the company illegitimate or corrupt according to Shariah law. Companies are also not permitted to issue preference shares, Tamattu shares, and bonds.

2.4 Musharaka financing

The Central Bank of Bahrain (CBB) explains Musharaka as an agreement between an Islamic bank licensee and a customer to contribute various amounts to a current or new firm or to acquire real estate or movable assets, either permanently or on a decreasing basis. Profit generated by this contract is shared, following agreement between the parties, while losses are distributed according to the contribution to the capital. Musharaka is a partnership agreement between two or more parties, such as an Islamic bank and its clients, in which they contribute capital to a specific venture and share profits based on pre-agreed terms.

In contrast, losses are shared based on each party's capital contribution ratio (Onagun, 2017). Musharaka finance involves the entrepreneur and the bank working together to provide cash and manage the project; losses are borne according to capital contributions, although profit proportions are freely negotiated (Aggarwal & Yousef, 2000). According to Smolo & Kabir Hassan (2011) and Astrom (2013), Musharaka refers to a partnership where partners share profits based on an agreed ratio, while losses are shared in proportion to the money contributed by the partners.

The profit ratio must be indicated at the time the contract is drawn up. It is not permitted to postpone calculating the ratios until the profit has been earned since it may lead to ambiguity and disagreements among the partners. This does not exclude the change in profit ratios or the transfer of one party's stake to another. Further, profits must be allocated in such a way that each partner receives an undivided share of profit rather than a lump sum of money or a percentage of capital; moreover, a maximum profit limit can be established, with any surplus being ceded to the other party.

Ghayad and Hamdan (2021), Iqbal et al., (2023), and Hassan & Lewis (2004) described Musharaka as the affiliation of one capital with another capital to share the gains and losses that may emerge from this arrangement. Musharaka is a type of Islamic finance that comprises a partnership between two or more parties in which earnings and losses are divided according to predetermined percentages.

The loss ratios concerning capital contributions must be agreed upon. It is not acceptable to agree on a loss ratio that differs from the ownership shares since this contradicts the provisions of Islamic law and is considered a form of guaranteeing the capital, which is also prohibited in Islam; it would be unfair and an illegal theft of wealth, and all partners must bear responsibility for accounting and auditing for Islamic

financial institutions. AAOIFI requires that the proportions of losses suffered by partners match the proportions of their contributions to Sharika capital. It is therefore not authorized to agree to make one or more partners accountable for full losses, or liable for a proportion of the loss, that does not correspond to their share of ownership in the partnership. However, it is permissible for one partner to accept responsibility for absorbing the loss at the moment of the loss without any previous conditions.

2.4.1 General Rules of Musharaka Financing

Important principles and Shariah rulings that define Musharaka financing are discussed below, derived from the work of Sheikh Usmani (1998); Shari'ah Standards AAOIFI (2017); Islamic company jurisprudence; Onagun (2017); and Al-Harran (2009):

1. **Musharaka financing:** As with any Islamic financial arrangement, Musharaka financing must be completed with the parties' consent and the parties must be competent to engage in a contract. Furthermore, the project or business sponsored by Musharaka must be Halal and Shariah-compliant.
2. **Capital:** The capital shall be known, and the proportion of each partner in the capital should be decided, whether it is provided in the form of a single lump amount or in many payments over time, i.e. when additional funds are required to raise the capital. Failure to do so will result in uncertainty; it is not acceptable for Sharikah's capital to be confusing since knowledge about capital size is a prerequisite for profit sharing. Additionally, the capital must be available when concluding the contracts and must not be subject to a debt. It is not authorized to use debts (receivables) alone to contribute to Sharika's capital. The reason for rejecting payment of partnership capital in receivables is that debts due to a partner by another partner cannot be used in partnership activities since they are not assets in possession. However, if the receivables are merged with other assets and the debt-to-total-assets ratio is small, debt and other assets might be considered contributions to partnership capital.
3. **Management of the venture:** All partners can work in the Musharaka endeavor, and no partner may be barred from participating in the business's management or operations. Unless they agree otherwise, it is acceptable for the partners to choose a third party as a manager and give him a defined fee that is included in Sharika's costs. It is not authorized to set a fixed payment for a

partner who contributes to the management of Sharikah funds or offers other services, such as accountancy, because this may lead to securing its capital and not sustaining the loss to the extent of its capital if it occurs. However, unless he had been assigned to a separate contract from the Sharika contract, it is acceptable to offer the manager a greater share of the profit than he would earn if he just had a share of the partnership capital.

4. **Guarantee:** Each partner acts as a trustee for the other partner's finances but only guarantees them against negligence or misuse. A Sharika contracts, however, allow a partner to require another partner to offer a personal guarantee or a mortgage in the event of misbehavior, carelessness, or breach of contract. Also, a third party may give a guarantee to compensate for any or all of the partners' capital losses.

5. **Termination of the company's contract.**

According to Islamic scholars, Sharika contracts terminate with one of five conditions:

1. **Termination:** Each of the partners may terminate the company's contract as long as there is no harm to the other partner after giving the partner due notice to this effect, in which case the partner shall be entitled to his share in the partnership, and this withdrawal would not necessitate the termination of the partnership of the remaining partners. This is contrary to Malki academics, who declare that the Sharika contract is bilateral and cannot be terminated without the other party's approval.
2. **Expiration of the period:** If the company's contract is fixed for a period, it expires on the expiration date, or the completion of the work or the project for which the company was founded. In this case, it is permissible for the partners to enter into a binding promise for the continuity of the partnership for some time and to agree to terminate the partnership before a fixed period has expired. The obligations and actions that took place before termination remain unaffected and continue to exist.
3. **Death:** If a partner in a firm dies, those who object to inheriting the right to participate, the heirs and legatees, have the choice of splitting the shares or joining the company, provided the surviving partners agree. Furthermore, if a corporation has more than two partners and one of them dies, the surviving partners do not lose their positions.

4. **Total incapacity:** One of the partners is incapable of running the company due to a serious physical or mental illness.
5. **Loss of the capital:** Loss of the whole Sharika capital before purchase. After purchase, the contract remains valid even if the capital is destroyed.

2.5 Types of Musharaka

2.5.1 Fixed or continuous participation: Continuation without a predetermined deadline is where banks are co-owners and manage and monitor the project, sharing in the gains and losses. Participation continues throughout the project. Following the completion of the project, the bank continues to participate by committing to financing a portion of the capital of a future specific project, which implies becoming a co-owner of the project as well as a participant in all of the subsequent profit or loss in the proportions specified in the agreement. Each partner has fixed shares (Jaafar, 2009). This arrangement takes the legal shape of a Joint-Liability company, a limited liability corporation if its shares are not tradable, or a company limited by shares if its shares are tradable. Financing through Musharaka never means the advance of money. It means participation in the business.

2.5.2 Diminished Participation (Meslier et al., 2020; Mustafa, 2015) refers to a financing arrangement where the bank grants the partner the right to acquire its share of the participating project incrementally. This arrangement reduces the bank's stake while simultaneously increasing the partner's share, ultimately leading to the partner's full ownership of the project. This method also represents a financing contract in which clients agree to gradually purchase a portion of the assets, initially bought by the bank on their behalf, until they attain full asset ownership.

Two or more persons participate in ownership of an asset or services/work, or one partner pays the other partner for working on the company to invest and share the results between them. One partner sells his share to his partner from the project's returns or outside payments, either in full or in installments based on the pre-agreed conditions, until the ownership of the project is transferred to him at the end of the contract (Abushareah & Mohamed Naim, 2015).

Diminishing Musharaka (DM) may be used in various finance cases, particularly for financing assets that can be leased. As a variable or floating rate of return is possible in leasing transactions, Islamic banks can use it for long-term financing even in

economies with an inflationary trend. For example, financial institutions can use Diminishing Musharaka to provide house financing, auto financing, plant and machinery financing, factory/building financing, and financing of all other fixed assets with different structures.

However, Islamic banks can also use Musharaka financing with Ijarah sub-contracts or a Musharaka with a Murabaha sub-contract. The Central Bank of Bahrain rule book (CA-4.8.19) states that an Islamic bank licensee may create joint ownership of tangible fixed assets (such as automobiles, machinery, and so on) with a client on a Musharaka basis, with the assets leased or sold on an Ijarah or Murabaha basis.

2.5.2 Types of Application of Musharaka:

Before discussing the way that Musharaka financing can apply, it should be emphasized that Musharaka can either be financing or investment, as explained below:

1. Musharaka financing:

is a contract in which the partner (customer) approaches the bank with a proposal for a specific project and offers to be a partner by sharing profits and losses.

2. Musharaka investment:

is different from Musharaka financing in that the banks propose a venture, and the customer enters as a partner or investor.

These types of Musharaka can be ended by transferring ownership to the partner, or continued as the partner wishes. This research paper is interested in Musharaka financing.

Musharaka might take one of two forms: equity participation or joint venture projects. According to **the equity participation form**, the bank will become one of the company's shareholders. This is comparable to venture capital investments, where the bank receives returns in the form of dividends or the disposition of shareholdings. However, by project financing, Musharaka can be utilized for project finance if the fund giver participates in equity and shares in the profits after the project generates revenue. Musharaka can also be used in financing corporations by using Islamic Venture Capital (IVC); from an Islamic perspective, venture capital focused on equity financing comes within the scope of Islamic finance as long as it invests in permitted industries and enterprises with zero traditional debt capital structure. It blends economic viability with Islamic preference, making it an appealing alternative for Islamic financial organizations. Providing equity-based finance to SMEs is consistent with Islam's aim

of broader economic expansion and more equitable wealth distribution. That is why venture capital financing is recognized for its capacity to foster expansion while ensuring financial stability (Mokakha, 2017; Mohamad et al., 2023). While Musharaka is therefore related to venture capital, its core concepts differ.

Musharaka and VC have four characteristics: definition, high risk, information asymmetry, and monitoring and assistance.

In **joint venture initiatives**, the Bank will finance specific projects and share the profits and losses depending on the agreed-upon percentages. Musharaka may be employed to assist with the finance requirements of commerce and industry in both the short and long-term (Billah, 2019; Ali & Zada, 2019; Mustafa, 2015; Ali & Hussain, 2017; Al-Harran, 2009). Joint ventures are mostly used to reduce participation between the bank and the client.

In general, participation financing is applicable to large State funding, instruments, or working capital, such as the acquisition of raw materials for manufacturing companies. Musharaka can also be utilized to fund imports and exports that benefit the industry. It can also function as a Sukuk; Musharaka Sukuk represents undivided ownership of the Sukuk holders in the business venture. This Sukuk is typically issued to fund a specific project or to gain ownership of the issuer's firm. As a result, cash raised by Sukuk investors is invested in the issuer's business or project. The venture's profits are then divided between them following the terms of the agreement. At the end of the period, the issuer purchases a portion of the Sukuk investors' stake in the enterprise, and they receive their investment.

Sukuk al Musharaka: “are certificates of equal value issued with the aim of using the mobilized funds for establishing a new project, developing an existing project or financing a business activity on the basis of any of partnership contracts so that the certificate holders become the owners of the project or the assets of the activity as per their respective shares.” AAOIFI

After all, Participation can be defined as a contract in which the partners' money is combined to profit from a given activity. This action must be based on Shariah and adhere to Islamic legal standards. Such agreements separate the participation contract from other contracts, such as the loan contract. The parties must intend to enter into a joint venture with many partners. A participation contract requires a minimum of two partners.

Capital contribution: The partners must provide capital to the company.

Profit and loss sharing: All partners must share the business's gains and losses. The participation contract is important for firms seeking to run or expand their operations. It allows firms to obtain cash while also sharing the risks and profits with their partners.

The participation contract is useful for firms looking to expand their operations. It allows firms to obtain financing while also sharing the company's risks and profits with its partners. Moreover, by financing Musharaka, the banks contribute to economic development; create job opportunities; achieve justice; distribute money rather than amassing it; help small and medium businesses to start and grow; and achieve social solidarity. Musharaka financing has led Islamic banks to achieve their purposes by fulfilling Islamic economic principles and Maqasied characteristics and support the Islamic economic vision and mission. Dr. Mohamed Abdel Moneim Afar has defined Islamic economics as the science of identifying how humans used different resources to meet the needs of society over time. Moreover, Islamic economics governs and controls economic activity according to the roots of Islam. Thus, it is a set of economic principles based on the writings of the Quran and Sunnah (Al-Fangary, 1997).

2.6 Structures of Musharaka contracts in Islamic banks

2.6.1 Structure of Musharaka

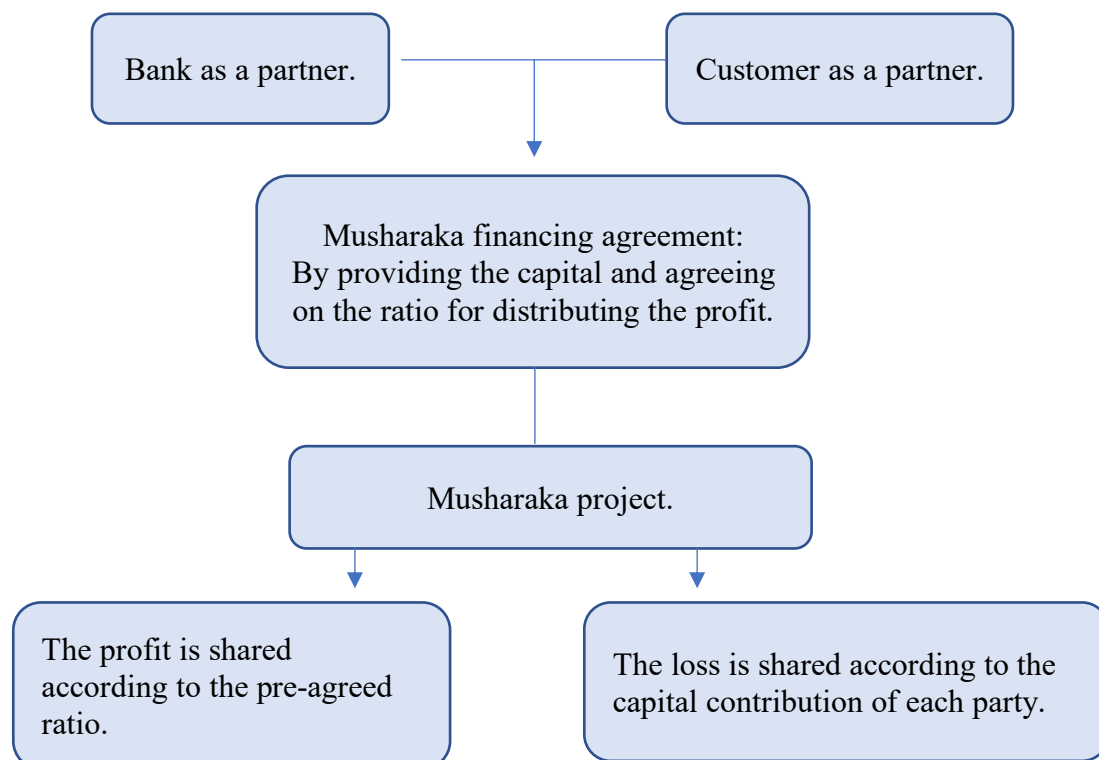


Figure 2- Steps of Musharaka contract

2.6.2 Structure of diminishing Musharaka

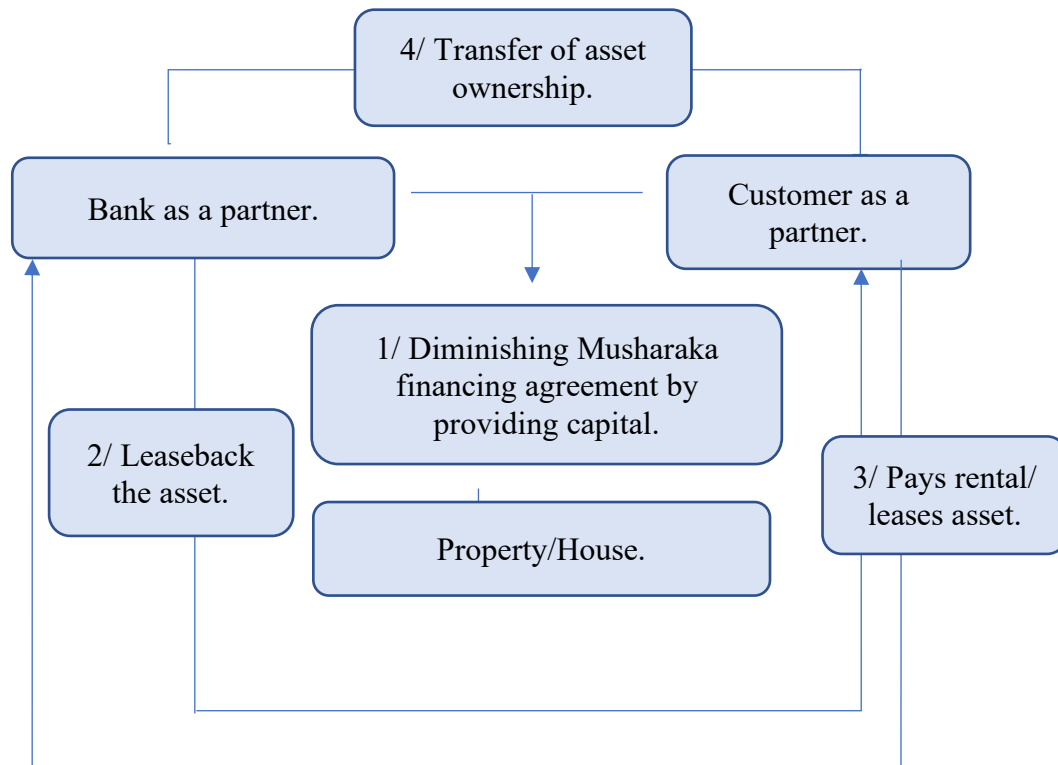


Figure 3- Steps of Diminishing Musharaka Contract

2.7 Case Study of Musharaka Financing

2.7.1 Application of Musharaka in Pakistan

Nouman et al. (2019) conducted a study to evaluate the increase of participatory finance in Pakistan from 2012 to 2018 in terms of its areas of application and important components. Lately, the pattern identified has begun to change in Pakistan, where participatory finance has grown dramatically in Islamic banks' financing portfolios. Table 3 demonstrates that Islamic banks' financing portfolio composition has begun to shift and grow.

Table 3 - Musharaka percentage in Pakistan banks (2012-2018)

Modes	Dec 2012	Dec 2013	Dec 2014	Dec 2015	Dec 2016	Dec 2017	Dec 2018
Musharaka	0.8	6.7	11.0	14.0	15.6	22.0	19.9
Diminishing Musharaka	36.2	30.8	32.6	31.7	34.7	30.7	33.3

Table 4 - Musharaka percentage in Pakistan banks (2019-2023)

Modes	Dec 2019	Dec 2020	Dec 2021	Dec 2022	Dec 2023
Musharaka	19.8	22.7	24.9	25.2	25.3
Diminishing Musharaka	34.1	33.6	33.8	34.8	32.1

Source: State Bank of Pakistan (2019-23).

Based on the preceding five years, it can be seen that Musharaka financing is still growing in Pakistan. Table 4 shows that the percentage of Musharaka financing increased from 19.8% to 25.3% in less than 5 years (December 2019 to December 2023).

Five reasons contribute to the growth of participatory funding, including the introduction of new kinds of funding in Musharaka, increased application, large-volume projects, government initiatives, and regulators' participation.

1. **Varieties in Musharakah** were introduced by adapting the standard Musharakah mode and creating new variants, such as diminishing Musharakah and running Musharakah (The implementation of Running Musharakah allowed Islamic banks to join their clients' businesses as sleeping partners by signing a contractual agreement). By implementing Running Musharakah, Islamic banks in Pakistan were able to meet the business sector's working capital needs at relatively lower and fixed rates that were equivalent to the rates offered by conventional banks for overdraft lending. As a result, Running Musharakah has become a popular financing option, accounting for around 25% of Islamic bank financing in Pakistan (Akram, 2019). Additionally, the profit rate in running musharaka (RM) is set at two levels. At the first level, Islamic banks establish a

target rate (known as a profit ceiling) that is typically equivalent to the Karachi interbank offered rate (KIBOR). It is mutually agreed that earnings up to this profit limit will be allocated depending on the bank's and client's investment shares. At the second level, Islamic banks agree to lower their profit share to as little as 0.00001 percent. At the same time, the customer receives the remaining profit, 99.99999 percent—a sum that typically exceeds the profit shared between the bank and the client at the first level. These new products have made Musharaka finance more sustainable in a range of contexts, attracting more participants and promoting the overall adoption of participatory modes.

Steps in implementing Running Musharaka: A fictitious example (Siddique & Zahid, 2022)

1. Initial Agreement:

Mr. Khalid, a corporate customer, requires working money, so he contacts an Islamic bank for funding via an RM facility. After reviewing Khalid's company's financial accounts, the bank decides to become a sleeping partner in Khalid's firm under a contractual agreement for an agreed period of time.

2. Profit determination:

In RM, profits are defined by two levels:

Level one: Profits up to a predetermined limit (typically KIBOR) are divided depending on investment shares.

Level two: The remaining profit is allocated at the second level by previously agreed ratios between the bank and Khalid.

3. Setting up the RM facility

- Khalid's account is credited once the bank approves a certain amount under the RM facility.

- Khalid withdraws various sums on an "as-needed" basis.

4. End of the contract

- The total amount taken by Khalid is subtracted from the allowed limit, representing the Bank's investment.

- Khalid delivers company information to calculate his capital share.

5. Profit Distribution:

- Stage 1 profit is distributed according to the pricing ceiling.

In Stage 2, the remaining profit will be distributed as a pre-percentage agreed upon in running Musharaka, usually 0.00001 and 99.99999.

An illustration of the financial calculations

Let us assume that the Islamic bank gives an amount limit equal to 100 million with an agreed period equal to 1 year; after one year, the total amount withdrawn from the clients is equal to 72 million, and the client's share is a 30-million-dollar total investment of joint business equaling 102. Stage -1 of profit Distribution is calculated by multiplying the percentage of KIBOR by the total investment. Assuming it is 14% ($14\% \times 102 = 14.28$); this is the profit ceiling (whatever the amount of profit, the partner distributes it according to this ceiling). The Islamic bank's profit is equal to $72/102 = 71\%$. ($71\% \times 14.28 = 10.08$). The client's share of the profit is $30/102 = 29\%$, $29\% \times 14.28 = 4.2$. The stage - 2 profit is distributed between the parties. Assuming that the profit of the project is 20, the remaining profit = $20 - 14.28\% = 5.72$ million. This remaining profit is distributed between them according to the agreed ratio.

This illustration shows that the Islamic bank will know its capital contribution at the end of the contract period. Shariah scholars argue that the capital contribution of the bank is unknown, and as previously discussed, knowing the capital is vital in avoiding disagreements and ignorance. This is not the case in the RM example because the bank allows the customer to withdraw the whole amount from the account. Determining the first-level distribution of the profit is also considered an issue. Table 5 shows the proponents and opponents of this deal.

Table 5 - Opinion on the legality of running Musharaka

Proponents	opponents
<i>Ahmed et al. (2016)</i> discussed the volume and operational elements of RM in the Islamic banking business; however, Shariah compliance issues were not addressed.	<i>Tahir and Khan (2016)</i> criticized RM, claiming that when an Islamic bank registers an RM account for a corporate customer, it is viewed as the client's account rather than a shared account handled by the Bank.
<i>Ali (2020)</i> refuted opponents' claims by outlining AAOIFI's Shariah criteria and	<i>Akram (2019)</i> highlighted issues such as the indeterminate nature of investment

saying that RM adheres to Shariah requirements for Musharaka. The two levels of profit determination and profit ceiling were defined as allowed under Shariah.	shares and profit ratios, profit giving, and divergence from Islamic norms. RM was chastised for mimicking traditional finance and concentrating wealth in corporate hands. Akram concluded that RM is neither Musharakah nor a superior method of finance compared to sales-based modes with set rates of return.
<i>Ullah et al. (2017)</i> noted that some Islamic banks' finance working capital needs through RM, which incurs a set charge to the client and is similar to traditional overdraft facilities.	<i>Javaid et al. (2018)</i> argued that RM is built without regard for the essence of Musharakah, implying that it deviates from Islamic norms.

Opponents object to the contract technique because the distribution of profits is defined by a specified index, ensuring that the maximum limit of the investors' profit share is not surpassed. However, there is no issue as long as this condition is applied for profit determination without any condition for the losses. Reviewing the meaning of running Musharaka in Faysal banks (FBL), the FBL and customer will enter into a Musharaka transaction in which FBL, from time to time, will invest in identified primary and operating business activities of the customer. This product offers customers the flexibility of drawing and depositing funds with FBL. At the end of the transaction period, the FBL and customer will share the profits according to the agreed profit-sharing ratios. In contrast, any losses are shared according to the investment ratio. The Shariah board in the bank confirms this agreement (see Appendix 1).

1. Enhanced Applicability: Musharaka finance's increased relevance in working capital financing, commodities operations financing, and high-volume projects has made it a more appealing alternative for enterprises and financial institutions. The greater use of Musharaka has created prospects for larger finance transactions and cooperation, increasing participatory financing activities.

2. Financing high-volume projects: Running Musharaka is often supplied to major enterprises for working capital funding and government entities for commodities operations financing.

3. Function of SBP: The State Bank of Pakistan (SBP) has helped promote participatory financing in Pakistan:

Firstly, the SBP aids the government in establishing investment possibilities for Islamic banks to address the surplus liquidity problem. The Islamic Banking Promotion Committee, chaired by the federal finance minister, includes the deputy governor of the State Bank of Pakistan. The committee's primary goal is to convince the government to take action to promote Islamic banking and finance. These initiatives contribute significantly to the expansion of Islamic banking and Musharaka finance.

Secondly, government interventions. The government has played an essential role in expanding Islamic banking in general and participatory finance specifically. To address the surplus liquidity problem facing Pakistan's Islamic banking industry, the federal government urges its subsidiaries to finance a percentage of money for commodities activities through Islamic banks. Because of the Islamic banking industry's extremely low asset creation, Islamic banks experience liquidity management issues, particularly in the near term. As a result, in places where Islamic banking structures may be easily implemented, the government directs various ministries to seek financing from Islamic banks to protect them from failure.

By utilizing these elements, Pakistani Islamic banks have been able to promote and execute participatory finance more successfully, which has contributed to the industry's recent development and expansion.

4.2 The principal fields of application for Musharaka finance in Pakistan's

Islamic banking business include the following:

- Islamic banks in Pakistan provide working capital funding for SMEs and corporations through Musharaka financing, in which the bank invests cash in the firm on a profit-and-loss-sharing basis to satisfy operational requirements. Musharaka Finance meets the working capital requirements of both small and large businesses. Six Islamic banks in Pakistan conduct business using this Islamic method (N. Iqbal et al.,

2014): Alsalah Bank, UBL, Dubai Islamic bank (Pakistan), Bank al Habib, Mezzan Bank, and the National Bank of Pakistan,

- Financing fixed assets: Islamic banks provide Musharaka finance for fixed assets such as land, buildings, machinery, and cars. In this arrangement, the bank and the business become joint owners of the asset, with the latter using it and paying rent to the bank.
- Consumer financing products: Islamic banks' house and auto financing schemes are Musharaka-based. Customers and the bank become joint owners of the asset, with the client utilizing it and paying the bank a recurring rental fee.

2.7.2 Musharaka Financing in Oman

2.7.2.1 Nizwa bank

2.7.2.1.1 Overview of the Bank:

Bank Nizwa is Oman's first Islamic Bank, offering completely Shariah-compliant goods and services. The bank provides a comprehensive range of commercial banking services in compliance with the license provided by the Central Bank of Oman (CBO) and the Banking Law proclaimed by Royal Decree No. 114 of 2000. Individuals, small and medium-sized businesses, companies, and government entities benefit from the bank's comprehensive range of banking options.

2.7.2.2.1 Analysis of Musharaka of Nizwa Bank

Table 6 shows that the percentage of Musharaka financing in Nizwa Bank in Oman increased by 4% between 2018 and 2019, from 7% to 11%, and the contract increased by 4% from 2019 to 2020; this indicates that growth continued despite market problems. The contract increased by 4% between 2020 and 2021, from 15% to 19%. Between 2012 and 2022, the contract increased by 6% from 19% to 25%. This growth shows long-term stability in contract growth, demonstrating market strength and the ability to adjust to economic and political developments.

Table 6- Musharaka percentage in Nizwa Bank - Oman (2018-2022)

	2018	2019	2020	2021	2022
Musharaka Financing	7%	11%	15%	19%	25%

Source: Financial report for Nizwa Bank (2018-22).

Musharaka financing in Nizwa refers to a contractual connection formed by mutual consent of parties for profits and losses deriving from a joint venture or company. Investments are made by all partners/shareholders, and earnings are dispersed following the contract terms. If one or more partners opts to become non-working or silent partners, their profit ratio cannot exceed the ratio of their capital investment to Musharaka's total capital investment. Under the agreement, both partners mutually agree to contribute money to the Musharaka business activity and share any profits derived from assets or business operations following a predetermined ratio. At the same time, losses are borne in proportion to their respective capital contributions. Capital from the Bank (financing amount) can be disbursed in a single sum or via progressive payments, as agreed by both parties.

The Musharaka Asset is co-owned by the bank and the client following their respective capital contributions. In such a transaction, the bank assumes the risk in the Musharaka Asset equal to its part/capital contribution. The bank's exposure (and hence the associated risk) decreases during the transaction when the client purchases back units of the bank's ownership stake in the Musharaka Asset. In the event of a loss, the bank bears the loss according to its part/capital contribution in the Musharaka Asset. This is only relevant if the loss was not caused by the customer's gross negligence or willful wrongdoing, in which case the customer is completely accountable for the loss.

Diminishing Musharaka is a Shirkat-ul-Mulk-based contract between a bank and a client for shared ownership of a fixed asset (for example, a house, land, equipment, or machinery); the bank divides its share in the fixed asset and progressively transfers ownership to the client (at carrying value).

- a) The SSB-approved DM contract template is utilized for DM transactions.
- b) If the standard DM contract template is not utilized, the revised contract is evaluated and authorized by the Internal Shari'ah Reviewer or Internal Shari'ah Reviewer Compliance Structuring Unit to certify the inclusion of suitable terms required for a Shari'ah-compliant transaction.
- c) Only physical assets can be converted into Diminishing Musharaka (DM).

DM is confined to specific assets rather than the entire organization. Nizwa Bank also provides diminishing Musharaka for SMEs. In this financing arrangement, the capital does not have to be in cash; it can be capital in kind. This funding is used to construct or acquire fixed assets in a firm. When assets are generated or acquired, the bank's part

of the assets is regularly returned to the client, reducing the bank's ownership of the assets (see Appendices 2 and 3).

2.7.2.2 Musharaka financing in Muzn Islamic bank in Oman

2.7.2.2.1 Overview of the bank

Muzn Islamic Banking is a licensed Islamic Banking Window based in the Sultanate of Oman that provides Shari'a-compliant financial solutions to clients.

2.7.2.2.1 Analysis of Diminishing Musharaka of Muzn Islamic window

Table 7 shows that Muzn Bank has a great proportion of diminishing Musharaka in the Bank, where DM sharply increased by 20% between 2018 – 2019, from 19% to 34%; and increased by 5% between 2019 – 2020, from 34% to 39%. It continued to increase - by 7% between 2020 – 2021, and between 2021 – 2022 from 39% to 46% and from 46% to 53% respectively.

Table 7 - Diminishing Musharaka percentage in Muzn Islamic Window Bank- Oman (2019-2022)

	2018	2019	2020	2021	2022
Diminishing Musharaka	19%	34%	39%	46%	53%

Source: financial report for Nizwa Bank (2018-2022).

DM, offered by the Muzn Islamic Window, is a form of partnership in which both the customer and Muzn contribute capital in varying proportions to either develop a new asset or share an existing one. Both parties become owners of the capital, with their ownership being permanent or declining, and they receive a share of profit and losses.

Muzn enters a DM based in Sharikat al-Muilk with the customer to finance an agreed-upon share of fixed assets such as land or a house. They then enter into periodic profit payment agreements on an Ijara basis to utilize Muzn's Musharaka, which the customer shares. Over the agreed period, one partner's investment in the partnership decreases as the other partner's investment increases.

The DM agreement between the Muzn bank and the customer includes conditions such as purchase undertaking, undertaking to pay, providing guarantees from a third party, and creating Takaful insurance.

As part of the process of purchase, acquisition, or construction of assets at the request of the customer, the parties have to agree as follows:

- If the customer has entered into a sale and purchase agreement with the seller to acquire the asset at the time of the execution of the agreement, the bank agrees to jointly purchase rights, interests, and benefits in the asset with the customer up to the Bank's Initial Acquisition Payment to facilitate the acquisition of the asset from the vendor.

- If the customer is the legal owner of the asset and intends to obtain financing for the purpose, the bank agrees to acquire from the customer the rights, interest, and benefits in the asset for consideration up to the bank's Initial Acquisition Payment by executing a sale agreement with the customer and making the payment in accordance with the customer's instructions.

If the asset needs to be constructed at the time of executing this agreement, the bank and the customer agree to jointly construct it based on the agreed ownership of shares. For further details, see Appendix 4.

2.8 Maqasid al Shari'ah

2.8.1 Concept of Maqasid al Shari'ah

Maqasid al-Shari'ah is thought to be the foundation or guiding concept of Islamic finance. It covers everything associated with it: laws, conduct, views, products, transactions, activities, and services. It defines the goals and knowledge (Hikmah) that Shari'ah prescribes in all of its rulings to defend and maintain society's advantages and interests (Maslahah). Furthermore, Maqasid al-Shari'ah facilitates human needs; ensures that wealth is distributed fairly to as many people as possible; avoids conflict; ensures stability; promotes Maslahah; avoids haram; promotes transparency and accountability; and upholds and promotes justice in wealth acquisition to help the protection of wealth in Islam (Vejzagic & Smolo, 2011).

Ibn Ashur and Alal al-Farsi are prominent in divided the purposes of Maqasid al-Shariah. Ibn Ashour divided the purposes of Shari'a into two sections: firstly, the purposes of Shariah were defined as the general purposes of the legislation, the meanings, and the judgments of Shariah law in all or most of the conditions of the

legislation. Secondly, the purposes of special legislation are defined as "How the Shari'ah law is intended to achieve people's useful purposes or to preserve their public interests in their actions".

Alal al-Fassi defined Maqasid al-Shariah as the purpose of Shari'ah and the secrets set by the shariah law in each of its provisions (Al Fassi, 1963).

Shari'ah aims to promote people's wellbeing by protecting their faith (dīn), lives (nafs), intellect ('aql), posterity (nasl), and wealth (māl). Whatever protects these five serves the public interest and is desirable, and whatever harms them is against the public interest and should be removed (Al- Shatabi, 1997).

The definition of Maqasid al Shari'ah emphasizes the epistemic (Aqedah) dimension. The ultimate purpose of Shariah is to liberate man from his whims and preferences so that he might choose to be a servant of Allah, just as he is without it (Al Shatabi,1997). Moreover, Maqasid al Shari'ah seeks to achieve Maslahah by applying Shariah rules. Al-Ghazali initially described this concept in terms of preserving five fundamental parts of life: din (religion), nafs (soul), aql (intellect), nasab (progeny), and maal (property). However, Ibn Taymiyya determined that the Shariah's purpose is not confined to the five criteria outlined earlier, and its purposes include obtaining benefits and averting harm.

"Maslaha" literally means "benefit" and is one of the techniques of Islamic jurisprudence, but it has also been recognized as "Maqasid," which implies an al-Dharuri scenario or essential degree of advantages (Awang & Jusoh, 2014). Maslaha sometimes connotes the same meaning as Maqasid, and scholars have used both names virtually interchangeably (Dusuki & Abdullah, 2007).

2.8.2 Classifications of Maqasid al Shari'ah

Maqasid al Shariah is classified into Necessities, Complements, and Embellishments.

Necessities (Darūriyyah) refers to the five purposes of Shariah: religion, life, intelligence, posterity, and money. These necessities serve as the foundation for establishing welfare in this life, and ignoring them leads to confusion, unrest, and loss in this world and the hereafter (Dusuki & Bouheraoua, 2011). Some scholars have proposed additional necessities such as equality, freedom, and environmental

preservation, arguing that while the five Maqasid are important for human happiness, they are not the only necessities.

The adoption of the aforementioned principles is required to guarantee society's regular operation and people's wellbeing. Society and individuals are responsible for taking all necessary steps to avoid or eliminate all impediments to the attainment of these values. Shari'ah is always working to accept and endorse these ideals and improve processes for their continuance and advancement (Vejzagic & Smolo, 2011).

Complements (Hājiyyah): Al-Shatibi defined Complements as what is lacking in terms of expansion and lifting tightness, which frequently results in hardship and difficulty due to a failure to take the necessary action. If the need is not considered, the hardship and difficulty will fall on the person responsible. For example, in commercial transactions, Shari'ah validates specific contracts, such as the Salam (postponed sale, in which an early payment is made for products to be delivered later), because people need it. Although the origin is the prohibition of the Salam contract because it is the sale of the non-existent, the sale of the non-existent shall not be permitted because the sale article of the contract is required to be presented at the time of concluding the contract (Ali, 2010).

Need or complementary interests supplement essential interests. This refers to interests whose neglect leads to hardship but not to total disruption of the normal order of life. In other words, these interests, other than the five essentials, are needed to alleviate hardship so that life may be free from distress and predicament. It also acts as provisions that aim to remove hardships and/or facilitate life (Dusuki & Bouheraoua, 2011).

Embellishment (Taḥsīniyyah) is described as interests that, when realized, generate an improvement, and contribute to attaining a desired outcome. The absence of Tahsiniyyah does not interfere with daily life, yet it may make it unpleasant (Elahi & Alam, 2015). Moreover, the interests are suited to good customs and morals (Al-Khadimi, 2001).

2.8.2.1 Protection of Wealth

Acquiring property is an essential human necessity. Everyone wants safety and security for their possessions. Islam has decreed that no one shall violate and gain the property of another without good cause and a lawful contract. The Qur'an emphasizes

this point when it states: “And eat up not one another's property unjustly (in any illegal way, e.g., stealing, robbing, deceiving, etc.), nor give bribery to the rulers (judges before presenting your cases) that you may knowingly eat up a part of the property of others sinfully” (Al-Baqarah: 188). The Qur'an also cautions that individuals who wrongfully acquire the possessions of others will face severe punishment on the Day of Judgment: “Verily, those who unjustly eat up the property of orphans eat up only a fire into their bellies, and they will be burnt in the blazing Fire!” (Al-Nisa: 10). Islamic jurisprudence defines money as “what a person's nature is oriented towards and may be stored till the moment of necessity, whether it is moveable or immovable” (Effendi, 1934).

Maqasid scholars have decided that conserving money is one of the most important goals drawn from essential sources. It is ranked a fifth concern after religion, self, intellect, and progeny. Ibn Ashour stated that Maqasid al Shari'ah means five things: circulation, clarity, preservation, proof, and justice. Dr. Yusuf al-Qaradawi classified Maqasid al Shari'ah in financial matters, breaking it into six groups with twenty-seven financial purposes (Al Qardawi, 2008).

1. Maqasid al Shari'ah is related to the value and status of money. It demonstrates the importance of money, and Islam emphasizes the preservation of wealth, while warning against becoming fascinated with money and tyranny.
2. Linking money and the economy to faith, ethics and morality.
3. Maqasid al Shari'ah urged the production and earning of money from legitimate methods, such as agricultural production, industrial production and trading, and outlawing malicious earning. Earning money from Haram sources does not become pure through charity. Wealth should be increased through lawful means; and the manufacture of hazardous products is prohibited.
4. Maqasid al Shari'ah regarding the consumption of money: Allowing beneficial and lawful activities; rationalizing the consumption and expenditure of money; forbidding extravagance; and preserving the environment and its components.

5. Maqasid al Shari'ah related to the circulation of money: Financial transactions should be regulated and include legitimate provisions, applying Maqasid al Shari'ah to monetary wealth.

6. Maqasid al Shari'ah related to the distribution of money: Justice in the distribution of money among groups and individuals; looking after the poor and vulnerable; employing Zakat as one of the pillars of Islam; reducing differences in society; respect for the private ownership of money; preventing private property in matters necessary for the general public; solidarity in society; liberating people from poverty; and seeking to eliminate the necessity of caring for citizens, problems and emergency needs.

Shari'ah has developed subsidiary laws to preserve money by regulating its development system and circulation techniques, as well as avoiding harm due to lack of money, consuming/taking property through falsehood, and ensuring its security (Hussein, 2009). Avoiding harm also entails shielding it from excessive expenditure, illicit consumption, or damage, and can also include preventing a mentally impaired person from its use due to legal incompetence. The prohibition of illegal wealth consumption refers to the consumption of money without a genuine Islamic entitlement. Usury, fraud, dishonesty, bribery, high interest, gambling, coercion, and ingratitude are some examples. As a result, creating social security by protecting people's wealth in a community seeking economic growth helps its members. Shariah has taken great care in this respect, and one of the most stringent and powerful laws in this area is the punishment for stealing (Belouafi, 2008; Al-Huthayfi, 2022).

Shariah has many Maqasid in funds; the objectives include the principle of trading, clarity, justice, and protecting it from abuse. Maqasid al Shari'ah in wealth circulation means that money is shared among individuals and is mobile through consumption or investment (Siddiq, 2017). It is defined as an equal distribution of money to the largest number of people (Pusparini, 2022; Khattak, 2014; Dasuki, 2015; and Ghozali, 2012).

Islam promotes wealth distribution, encourages investment, and strongly opposes wealth concentration in a few hands. It also serves the goal of safeguarding financial transactions and encouraging circulation so that a wide number of individuals have access to funds. Shari'ah does not consider money acquisition to be prohibited as long as one fulfills one's duty to Allah, mankind, and society through humanitarian and Zakat actions. Ibn-e-Ashur stated that the legitimate distribution of money among most of

society creates prosperity and contentment. Shari'ah has made all financial transactions and activities permissible, unless otherwise mentioned, in order to empower people and assist society to thrive and prosper. According to Islamic law, money should circulate amongst individuals and be in motion through consumption or investment. This aim is achieved through various processes, one of which is to prevent wealth hoarding and monopolizing important daily necessities.

Clarity in Maqasid al Shari'ah means transparency in ownership and obligations (Al-Khaloufi, 2013). Ghozali (2012) and Elahi & Alam (2015) defined clarity in finance as both transparency in transactions and wealth acquisition - the purpose of clarity is to prevent conflicts and controversies. Islamic law achieves this by recording transactions and contracts in writing, witnessing agreements, and through mortgages:

“O believers! When you contract a loan for a fixed period, commit it to writing. Let the scribe maintain justice between the parties. The scribe should not refuse to write as Allah taught them. They will write what the debtor dictates, bearing Allah in mind and not defrauding the debt. If the debtor is incompetent, weak, or unable to dictate, let their guardian dictate for them with justice. Call upon two of your men to witness. If two men cannot be found, then one man and two women of your choice will witness—so if one of the women forgets, the other may remind her. The witnesses must not refuse when they are summoned. It would help if you were not against writing ‘contracts’ for a fixed period—whether the sum is small or great. This is more just for you in the sight of Allah and more convenient for establishing evidence and removing doubts. However, if you conduct an immediate transaction among yourselves, you do not need to record it but call upon witnesses when a deal is finalized. Let no harm come to the scribe or witnesses. If you do, then you have gravely exceeded your limits. Be mindful of Allah, for Allah is the One Who teaches you. And Allah has perfect knowledge of all things.” (Al-Baqarah:282).

Financial transparency aims to prevent Islamic finance from being abused, squandered, or contested, as well as to avoid communal grudges and conflicts over financial concerns. Passages on this topic emphasize the need for a witness while performing financial transactions and the qualifications expected of people involved in financial administration.

Justice in Maqasid al Shari'ah refers to the aim of acquiring wealth in a just manner; to place it where it is intended to be used, as ordered by the wise legislator; and to increase it in appropriate ways (Al Jazairi, 2001), creating a safe environment that respects

property rights and distributes wealth and opportunity properly (Pusparini, 2022). Justice in finance includes justice in acquiring money and spending it without harm, including in commercial transactions and contracts (Al-Khaloufi, 2013).

Maqasid al Shari'ah is stable and has proof of commitment in contracts and agreements. A claim of ownership or a contract may only be certified as accurate if it is accompanied by legal paperwork. Maqasid al Shari'ah growth, development and wealth creation is achieved via effort, investment, and lucrative commerce (Pusparini, 2022).

2.8.3 Musharaka and Maqasid al Shari'ah

1. Musharaka and Maqasid and the circulation of funds.

As explained earlier, the circulation of funds is rotation of money through legitimate investment and consumption, in the interests of individuals and communities (Khalladi, 2016).

Islam encourages money circulation and fluctuation in people's hands. As for gains granted by Allah to His Messenger from the people of other lands, they are for Allah and the Messenger, his close relatives, orphans, the poor, and needy travelers so that wealth may not only circulate among the rich. Whatever the Messenger gives you, take it. And whatever he forbids you from, leave it. And fear Allah. Surely Allah is severe in punishment (Al-Hashr:7).

Musharaka contributes to the movement of money through trade and to the volatility of money in people's hands by encouraging investment projects and offering entrepreneurs the opportunity to extend their ventures, fund development and invest their money.

2. Musharaka and Maqasid and clarity

One of the aims of Islamic law in financial transactions highlighted by Ibn Ashur is clarity. This means that transactions between persons must be precise, detailed, and clear. They should be free of harm and, as far as possible, avoid arguments and confrontations. This ensures their protection against denial and rejection.

When the partners in the Musharaka contract conclude agreements, each partner's percentage of the profit and capital contributions will be clear and transparent; in case of losses, each partner knows that he will lose the same percentage of his contribution.

Transparency in the Musharaka agreement: each partner in the contract clearly understands their rights and obligations. The partner, in the case of DM, will increase his portion in the venture; the period of the venture and the actions of each participant are defined by the type of Sharika, or project.

3. Musharaka and Maqasid: stability and proof

Stability and proof comprise the laws, contracts and transactions that create a stable framework for ownership, trade, and transfer of commodities and services, ensuring wealth preservation (Kamali, 2017).

Statements in the contracts ensure avoiding damage to the parties and eliminating disputes. Every condition mentioned above of Musharaka financing is documented and signed by all the partners to ensure their rights.

The stability and clarity of funds are the economic purposes of Islamic law. Transactions must be characterized by precise identification and conditions and be as far away from harm and exposure to disputes as possible, and this is proof of their preservation (Al-Alem, 1994; Bin Ashour, 2004).

4. Musharaka and Maqasid of justice in funds

Justice and the prevention of injustice is vital in contracts (Ibn Taymiyyah, 1995). Ibn al-Qayyim said, “Allah, subhanahu wa ta'ala (SWT) has clearly revealed His books and sent His messengers to enable people to firmly maintain justice. This very equity establishes the earth and the heavens.” (Ibn Qayyim, 1350). Justice in funds is achieved by collecting them in a manner devoid of injustice and placing them in the location for which they were created (Belouafi, 2008).

“God Almighty said, ‘Indeed, Allah commands justice and goodness and gifts to relatives and forbids immorality and evil and the transgressor will admonish you so that you may remember’” (An-Nahl:90). Ibn Ashur interprets Justice in this verse as giving rights to its owner. It is the comprehensive principle of rights that relate to what is necessary, from intrinsic rights and rights of transactions, as “the Muslim is commanded to be just in and of himself..., and he is commanded to be just in dealing, which is a transaction with his Creator by acknowledging his attributes. Performing his rights and dealing with creatures is one of the principles of family cohabitation and social mixing, and that is in words and deeds.” (Bin Ashour, 1404).

Musharaka achieves justice and equality between the partners in many ways:

- Where profit or loss is achieved, it will be divided among the parties fairly, guaranteeing that revenues and expenditures are distributed equally. As explained

above, in a Musharaka, any profit achieved is distributed between the partners based on an agreed-upon percentage. The distribution of losses depends on each party's contribution.

- It achieves social justice by establishing and offering job opportunities for individuals.
- The provisions of participation contracts are negotiated and agreed. Each contractor is free to determine the circumstances appropriate for his or her talents and capabilities, ensuring justice and equality in the contractual relationship.

5. Musharaka and the protection of money

Shariah urged the development of money and increased production by legitimate earnings. Participation helps to achieve this by investing and entering into trade to increase wealth. This benefits both society as a whole and the individuals within it.

Quran urged to trade by saying: “Believers, do not consume your wealth among yourselves in falsehood, except there be trading by your mutual agreement. And do not kill yourselves. Allah is the Most Merciful to you” (An-Nisa: 29). Shari'a ensures the development of money, and the prophetic commandment came from trading the money of orphans so that it would not be consumed by charity. Islam emphasizes not allowing trade to distract the individual from a duty toward God and his messengers and writers. What is important in earning is to be Halal, within the framework of Islamic financial transactions.

2.8.4 Maqasid al Shari'ah in Islamic financial transactions

Isa et al. (2015) In their study, aims to examine Shariah academics' perspectives on Islamic ideals and Shariah's purposes and to determine if they are used in the creation of Islamic financing products. This study combined both written and face-to-face interviews using open-ended questions. Isa et al. (2015) found that respondents agreed on the significance of justice, openness, and Maqasid al Shari'ah in Islamic finance. However, when it came to current Islamic financial practices, they believed that certain banks do not adhere to these ideals in their goods and operations. Nouman et al. (2020), examined the relationship between participatory finance and Maqasid al Shari'ah through an interpretive systematic review based on critical interpretative synthesis principles. They discovered that participatory finance is consistent with the Islamic ethos and value system.

"Social wellbeing" serves as a link between the Maqasid al-Shari'ah and participatory finance which is defined by social commitments and ethical standards, and is based on Shariah's moral and ethical foundation. Social commitments and ethical standards can be employed as effective ways of constructing a just society and achieving socioeconomic goals within the larger framework of Maqasid al-Shari'ah.

Additionally, many academics agree that Musharaka is a fulfillment of Maqasid al-Sharia, including Yusof et al. (2009); Iqbal (1997); Al-Khaloufi, 2013); and Ariffin et al., (2015). Equity funding is the way forward for accomplishing the social welfare or economic welfare paradigm espoused by both Muslim academics and non-Muslim scholars, as established in Maqasid Al-Shari'ah. Equity financing does not camouflage debt-based financing contracts prevalent in conventional banking. Thus, equity financing achieves the objectives of shari'ah, which is the fulfillment of justice in society.

If there is no risk, effort, or responsibility in a specific contract, it cannot be deemed to have any aspect of justice. Equity financing includes the components of risk, effort, and obligation, making it evident to all that these financing arrangements are reasonable and more in keeping with Maqasid or Shariah principles. Justice requires that borrowers and lenders share both gains and losses equally and that the economic process of wealth building and distribution in the economy be fair and reflective of real production (Iqbal, 1997).

Islam strongly encourages profit from commerce and constructive investment; money must be put to useful use, and risk must be taken to justify a return (Akacem and Gilliam, 2002). This is one of the reasons why many scholars hold the view that unless Islamic banking institutions resolve to use PLS financing instruments, socioeconomic justice, as envisioned by the Islamic banking system, will never happen (Yusof et al. 2009).

Equity-based finance supports economic activity and equitable property distribution, aligning with Shariah's wealth management goals. In addition, these types of partnership contracts are the most successful in accomplishing Maqasid al Shari'ah because they are based on the notion of partnership, which is a genuine Islamic basis for achieving circulation. Such partnerships fulfill the goal of prosperity because they

entail collaboration between the parties, resulting in the movement of money between owners and entrepreneurs interested, for example, in establishing a factory or engaging in commerce. Justice aims to guarantee that each party obtains its fair portion of profits and, more significantly, that each party bears their share of losses. These contracts also achieve the goal of openness, as each partner understands their capital ownership, profit entitlement, and loss accountability. However, in numerous aspects, participatory models of finance are more favorable to the circulation of wealth (*rawaj*), clarity and transparency (*wudu*), stability and proof (*thubat*), and growth and development (*tanmiyah*) than other types. *Musharaka*, for example, has far more sophisticated and diverse applications. It may be used efficiently for venture funding, but its true potential is seen when higher ethical goals are utilized in Islamic finance markets where idle monies are channeled. Thus, it can potentially be an effective tool for ensuring wealth circulation and creation (Soualhi, 2018).

Although some Muslim economists do not completely reject the use of Shariah-compliant debt-based contracts combined with participatory finance, they contend that the socioeconomic aims of Islamic finance, including social justice and economic stability, growth, and efficiency caused by the protection of all parties' wealth, may be better fulfilled if Islamic banks turn to largely participatory financing. Scholars have concluded that each contract in financial transactions has its own distinct purposes and characteristics for achieving *Maqasid al Shari'ah* (Isa et al., 2015). Al-Khaloufi (2013) argues that debt-based contracts are the least efficient way to achieve the objective of Shariah. However, this is not to say that they serve no purpose. Providing people with cash, products, and commodities satisfies one of Islamic law's aims. They therefore meet the less important financial objectives. However, In Islamic law, several requirements must be completed for a lawful sale contract. To enhance openness, decrease the possibility of conflict, and achieve transparency, the contract must contain many key parts (buyer, seller, subject matter, and *aqd*). According to Islamic law, these ingredients must meet specific prerequisites.

Furthermore, in Islam, a selling transaction entails the transfer of ownership, which cannot be separated from the danger of loss. If the assets stay with the sellers, they are responsible for the risk until they are transferred to the purchasers. In addition to quality, all parties must be aware of the amount and specifications of the subject content (Isa et al., 2015).

To summarize, Maqasid al Shariah is a science that tells us the meaning of Islamic law, rules, and their wisdom and provision. Furthermore, Shari'a protects five necessities: religion, self, posterity, mind, and wealth. Islam urges people to earn and grow money not only by investing it but also by giving it. Islamic law bans the hoarding of money and extravagance based on it. Islamic law is a law of moderation and mediation, with neither excess nor negligence. Allah, SWT said and “{eat and drink, but be not excessive. Indeed, He likes not those who commit excess} [Al-Araf:31]. And in Surah Al-Isra {And do not make your hand [as] chained to your neck or extend it completely and [thereby] become blamed and insolvent} [al-Isra:29].” According to the achievement of Maqasid al Shari'ah in financial transactions, Islamic banks can contribute to Maqasid by trading and developing money by investing in projects and achieving justice by distributing the profits and losses. Participation contracts may indeed be the closest contracts to achieving Shari 'a purposes, but they are not the only contracts. By providing financing loans without interest, banks are preserving money and not wasting it, as well as ensuring Halal and good earnings.

2.9 Challenges in Islamic Finance

The Islamic financial services industry has grown exponentially and is spread across a wide geographical area worldwide. According to the Islamic Finance Development Report 2023, the global Islamic finance industry increased its asset volume by 11% to USD 4.5 trillion in 2022, with Islamic banking holding 72% of its total assets (ICD – LSEG Islamic Finance Development Report, 2023). Islamic banking is of great importance in Bahrain, accounting for 38.3% of the assets of the domestic banking system and 18.5% of its total assets (including foreign assets) at the end of 2022. Bahrain's Islamic banking market is ranked seventh globally, with total assets amounting to US \$41.6 billion or 92.4% of the Kingdom's GDP (Al-Bilad, 2023). When the first publications of the Islamic Bank model appeared in the 1950s, supporters believed that partnership contracts were the true alternative to interest finance and that they could provide the community with the positive outcomes of the Islamic finance formula, such as income and wealth distribution fairness, poverty reduction, and economic stability. Participatory finance is one of the most influential ideas proposed by Islamic banks, as it is very adaptable to various investment structures.

As discussed above, Islamic banking is founded on the notion of equitable wealth and income sharing and the avoidance of exploitation, with the aim of enhancing the circulation of money and transparency in commerce. Nevertheless, the emphasis on social and ethical dimensions in investment creates an extra hazard to Islamic financial institutions, in addition to traditional risks. In the case of Islamic finance, the risk canvas is larger and includes many more aspects related to participation, purpose, and other limits on payment capabilities. The most prevalent hazards, such as credit, market, operational, and liquidity risks, also exist in Islamic banking. Credit Risk appears to be higher in Islamic banking due to the lack of legal remedy for defaults, which increases the likelihood of defaults occurring. The risks associated with using profit-sharing instruments for financing purposes do not contain credit risk in the traditional sense. However, they share a critical characteristic of credit risk in the form of capital impairment (IFSB).

Furthermore, credit risk is higher in Islamic banking due to limited access to credit derivatives. Market Risk is posed by commodities, indexes, and foreign exchange. Operational Risks are another level of Shari'a risk that might be managed differently from operational risk. Liquidity risk is perceived to be higher due to the lack of availability of money markets, limited access to overnight borrowing, and increased market and client sensitivity.

Additional issues such as a defective legal framework, and lack of standards, processes, skilled workforce, and competent government backing raise risk exposures. (Kumar, 2009).

As we have seen, Musharaka is one method of funding projects in Islamic banking. Under Musharaka, the bank forms a joint venture with the client for a specified purpose. The bank administrates the financed activity which is closely related to the project's aims and impact. This introduces new aspects, such as monitoring and control. The bank is impacted by four risks: credit risk, market risk, operational risk, and liquidity risk. Because it involves participatory finance, the bank is subject to credit risk if the partner fails to honor their agreement. Market risk exposure is represented by the commodity prices under consideration. Operational Risk exposes the bank to various hazards that might arise from partners or outside sources. Liquidity Risk is crucial because, if the bank employs Musharaka to raise funds but does not create sufficient returns, investors may demand their money, resulting in a liquidity crisis (Kumar, 2009). Among the most significant issues that Islamic banks face are risks associated

with financing formulae and Shari'a-compliant banking, particularly investment risks, the technique of implementing Basel II suggestions, capital market, and financial derivatives risks.

Islamic banks also face a variety of hazards that differ from those encountered by commercial banks (Khorshid, 2009). However, referring to a real case of a risk matrix for DM contracts in Bahrain Islamic Bank (BISB), the process taken by the bank to mitigate the risk of the contract is long and divided into three aspects: before concluding the agreement, during the period of the contract, and at the end of the contract. In the pre-contract stage, the banks faced the risk of asymmetry of information, as well as ensuring that they calculated the administrative fees correctly. The bank has to ensure that they calculate the administrative fees by complying with the pre-approving process from the Shariah supervisory body, ensuring that the DM contract meets all the requirements, conforming to the bank's entitlement mechanism for participation quotas. The bank must also ensure that it doesn't make a deduction from the customer until after signing the sale or lease contract, while ensuring that the lease of contract is concluded with, or after, the contract of diminished participation. Additionally, during the period of cancellation or amendment of the contract or in the case of deferral, installments or early payment, the bank faces a higher matrix of risk, such as ensuring that it has not calculated additional fees or profits on schedule at deferral of installment or during early payment. The bank's main purpose in conducting these monitoring activities is to ensure that the contract is in compliance with Shariah at all stages. For more details, see Appendix 5.

2.9.1 The Obstacle Factors of Musharaka Application

Many studies, such as Billah (2019); Muhammed (2014); Yustiardi et al. (2020); Fianto et al., (2018); Mukhibad et al. (2023); and AbdulRahman & Nor (2016) have shown that the primary reasons why Islamic banks do not offer financing products with profit and loss sharing is because of high risk, asymmetric information difficulties, and moral hazards.

As previously explained, Islamic banks can serve as capital providers and entrepreneurs. Both subject Islamic banks to risk, as banks and clients share profit and loss equally. As a result, banks require improved company performance because of operational risks. The company may be unable to generate the expected cash flow. This circumstance is known as credit risk. If a company needs more cash, it will face

liquidity issues, necessitating additional funding for future initiatives. As soon as the partners believe that the company cannot continue owing to the large losses experienced, they must sell their stocks to the market, exposing themselves to market risk, which means that the market price of the equity may be lower than its nominal price (Hassan et al., 2023). Consequently, operational challenges identifying and monitoring risk transformation at various phases of Musharaka investment life cycles, and the operation of the contract, divestment, and liquidation, are all challenges related to financing Musharaka (Orhan, 2017); Onagun, 2017). Furthermore, Al-Jarrah et al. (2021) found that there are challenges related to the conditions of the Musharaka itself regarding the partner's permission in the management of the financed venture, including its limited share of capital and inability to require the guarantee from the clients.

Several experts found that the factor causing low Musharaka financing in Islamic banks is the lack of efficiency either on the client's side or by the bank employees. Yustiardi et al., (2020) found that the finance selection procedure might be one of the most difficult problems for Islamic banks when providing funding, where they must pick the ideal partner to operate the business. Furthermore, the lack of awareness and knowledge from the customer might be one of the reasons for the insufficiency of participant financing in the market. In addition, the customer is sometimes unwilling to have a business partner because they do not wish to share the project's profits; instead, they prefer the fixed return financing option. Regarding Farooq & Ahmed's (2013) study, which seeks to identify the factors that lead Islamic banks to limit the expansion of Musharaka financing to a minimum in Pakistan, they found a range of factors related to clients: lack of committed, honest, and skillful entrepreneurs; lack of expertise' customers unwilling to share high-profit ventures; and a lack of interest from customers.

Meanwhile, alternative, less dangerous, and less tedious financing methods are available. Abdulrahman and Nor (2016) found that Islamic banks in Malaysia face challenges when offering PLS financing. One of the main challenges is identifying the right partner for financing. Islamic banks must choose a partner with a proven track record and acceptable financial performance before providing financing. This is important to ensure that the selected partner can fulfill their obligations in the PLS financing agreement.

In summary, selecting the right partner is a crucial and a key challenge in PLS financing for Islamic banks in Malaysia. Kayed (2012) noted that the lack of suitable clients is a problem facing Islamic banks in offering Musharaka financing. Ascarya and

Yumanita (2006) agree that adverse selection occurs when an entrepreneur is unwilling to share his highly lucrative firm with an Islamic bank when cheaper interest-based funding is accessible. One solution to overcome adverse selection and disclosure of information is using guarantees or collateral, but this approach does not comply with the PLS contract. Musharaka exposes investors to operational difficulties, credit problems, liquidity, and market risks, among other issues Astrom (2012).

According to Muhammad (2014), some of the significant variables that have resulted in the limited usage of Musharaka-based financing by Islamic banks are internal elements such as management's monitoring, management's risk-averse approach, and the effect of Shariah supervision. These factors are significantly more important than external factors which are determined by customer performance and government policies. However, external factors also limit the use of Musharaka financing in Islamic banking and finance (Al-Jarrah et al., 2021). Bank employees lack an understanding of Musharaka financing, have weak technical and administrative competence, and lack expertise. There is no real desire on the part of Islamic banks to carry out a technical study of the market, and they are unwilling to establish companies with partners. In a study conducted by Ascarya and Yumanita (2006), the authors came to the same conclusion as Al-Jarrah et al. (2021), that the quality of human resources is lacking to handle, process, monitor, and audit PLS projects.

The regulation and unavailability of Legal and Government Support are also factors limiting the use of Musharaka. Ascarya and Yumanita (2006) conducted a focus group discussion to analyze problems in the PLS contracts in Indonesia. They found that the lack of supportive regulations and the lack of support from government and other institutions are some of the main. While government and other institutions' impediments are present, such as the lack of supporting policies to encourage PLS financing for public projects and the absence of a secondary market for Islamic financial instruments, Islamic banks are limited in their ability to allocate or acquire cash following Shariah ownership rights, as PLS funding requires clear and efficient ownership rights and lack of uniformity in religious principles. Political, legal, and regulatory environments (i.e. government support and the importance of the project/business venture for the country; a favorable and stable regulatory environment; well-defined property rights; and unfair taxation are also regarded as major impediments. Secondary markets for trading in Islamic financial instruments, particularly Musharaka, do not exist, and contracts are unenforceable) (Onagun,2017).

Additionally, Islamic banks operate in a dual system, which keeps them in a competitive environment. Islamic banks are therefore driven to exit participating contracts and join less hazardous ones (Dar & Presley, 2000; Billah, 2019). However, Islamic banks that are exposed to the risks associated with Musharaka activity are required to hold onto enough capital to cope with adversity.

The Capital Adequacy Standard (IFSB-2), which completes Pillar I of Basel II, provides guidelines on minimum capital requirements of Musharaka, allowing an Islamic bank to measure the extent to which its capital position is commensurate with its overall risk profile and business strategy, thereby assessing its ability to absorb a reasonable level of unexpected losses before going bankrupt. These regulations address the danger of losing invested capital as a result of engaging with contracts or transactions based on Musharaka, as well as reducing Musharaka in cases where the banks and their customers/partner(s) contribute to the capital of the partnership and share its profits or losses (Onagun, 2017).

The IFSB distinguishes between three types of Musharaka to determine the minimum capital adequacy requirement: a) Private business enterprise to conduct trading activities in foreign exchange, shares, and/or commodities: the RW is based on the relevant underlying assets as specified in the market risk. An 8% capital charge is imposed on the larger of the net long or net short holdings in foreign exchange, as well as the net long position in gold/silver. A Musharaka that invests in quoted shares is measured, using the equity position risk approach. Positions in tradeable assets are treated as equity position risks in the trading book, resulting in a total capital charge of 16% (equivalent to 200% RW).

b) Private commercial enterprises to conduct a business venture (other than (a)): IIFS are supposed to apply the standard risk-weight approach to determine equity exposures in this sort of transaction. The RW applies to equity-based risks in the banking book, except provisions. The basic risk-weight technique for calculating equity position risk in a business venture requires a 400% RW for non-publicly traded shares, excluding any impairment provisions. If a third party agrees to make good on impairment losses, the third party's RW will be substituted for the assets for the undertaking.

c) There are two sections for joint ownership of real estate or moving assets (such as vehicles): i) In Musharaka in an Ijarah contract, the partnership can generate rental revenue by leasing assets to other parties through Ijarah contracts. The risk of the

Musharaka investment is mostly related to the underlying Ijarah contracts. Each partner's capacity to repossess the leased assets mitigates credit risk. However, in other circumstances, the lessee is not a third party but rather an IIFS's partner as a client. Having an Ijarah sub-contract in addition to a Musharaka exposes the IIFS to credit risk because of the partner's commitment to service lease rents. ii) Musharaka in a Murabaha contract: The IIFS receives a portion of revenue by selling assets to third parties through Murabaha contracts. This exposes the IIFS to credit risk for the buyer/counterparty's receivables. Furthermore, these Musharaka investments are risk-weighted depending on the counterparty/lessee's credit status and on the counterparty's or buyer's credit standing. In a declining Musharaka, equity exposure is calculated as the remaining amount invested (measured at historical cost, including any portion of undistributed profits), less any impairment provision. This exposure is risk-weighted based on the nature of the underlying assets. If a third party agrees to make good impairment losses, the third party's RW is substituted for that of the assets in the amount of any such undertaking.

In short, the challenges that limit the use of Musharaka financing can be classified into three main categories: the contracts themselves, internal factors, and external factors. Contract processes and conditions are complicated. For example, in Diminishing Musharaka, the bank must create a new contract at the end of each period when its share decreases and the client's share increases. Internal factors are lack of efficiency; customer unwillingness to share their profit with the bank; and operational risks where Musharaka finance, especially in shares, needs to be regularly monitored; External factors include legal regulations and the competitive environment; and the necessity of the Islamic Bank to maintain its reputation to attract customers, especially its presence in a competitive environment by entering participant financing

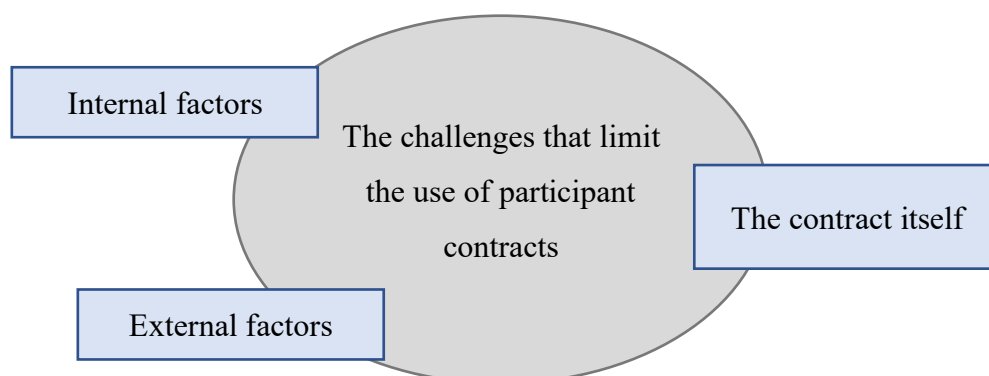


Figure 4- challenges in Musharaka financing

2.10 Chapter Summary

This chapter has provided a detailed literature review on Sharika, Musharaka, Maqasid al Shari'ah, and challenges in applying participant contracts in Islamic banks. The section on Sharika focused on defining the meaning of Shariah as well as the legality of Sharika, the types of Sharika in Islam, and modern companies. Musharaka financing in Islamic banks was then explained, including its types, the ways in which it can be applied, and real cases of applying the Musharaka in Bahrain. Subsequently, an overview of Maqasid al Shari'ah was provided, explaining the meaning of protection of wealth in Islam and how Islamic banks achieve the purpose of Maqasid al Shari'ah in the types of financing provided, followed by identifying the challenges. All the aforementioned points were supported by results from recent and relevant studies. Chapter 3 presents the research methods employed to execute the research objectives.

3.0 Chapter 3 - Research Methodology

3.1 Introduction

The primary goals of this chapter are to explain the study's research strategy and methodology and describe the research instruments developed and employed to achieve its aims. This chapter includes a description of the target population, sampling techniques, and the sources used for data collection.

3.2 Research Methodology

A qualitative research methodology using in-depth interviews was employed to achieve the study's objectives to detect the constraints that limit the application of Musharaka in Islamic banks. The methodology is appropriate because it uses qualitative data, in the form of interviews to comprehend and explain a social phenomenon.

The methodology included conducting intense individual interviews with a limited number of respondents to investigate their perspective. The advantage of in-depth interviews is that they give far more specific and detailed information than other data-gathering methods. They also may create a more personable environment in which to gather information — for example, participants may feel more comfortable having a discussion with the researcher than completing a survey (Boyce & Neale, 2006).

3.3 Philosophical paradigm and approach

The selection of the research model was based on the research questions and objectives: namely, to reveal the reasons and challenges that limit the use of the participation contracts in Islamic banks and to examine the relationship between Musharaka investment and Maqasid al Shari'ah by gathering views of Shariah experts and Islamic bankers. The study is underpinned by an explanatory practical perspective, which is utilized to extrapolate the research findings. The study takes an interpretative approach, arriving at conclusions which recognize the experiences and contexts of Islamic banks in Bahrain when adopting the participation contract.

3.4 Data collection

Data collection is acquiring and systematically assessing information on variables of interest that allows one to answer research questions and evaluate outcomes. Data

gathering aims to capture quality evidence, translate it to rich data analysis, and create a persuasive and credible response to the research question(s) posed (Kabir, 2016). There are two types of data: primary and secondary. Primary data refers to information obtained directly by the researcher; it can be gathered through surveys, observations, questionnaires, focus groups, case studies, and interviews (Ajayi, 2023). Secondary data refers to sources previously acquired by someone else. Secondary data sources include websites for government publications, books, journal papers, and internal documents (Ajayi, 2023). This study is based on primary data collected through structured interviews, using open-ended questions.

3.5 Target Population

The term "target population" refers to all participants who matched the criteria for a research study (Mohsin, 2016). The sample should fit the study's purpose to provide the most trustworthy results. Participants in this research were selected from the target population. The study's research population included Islamic bankers, particularly managers in the Shariah department and risk/credit review management, as well as Shariah specialists, such as Shariah supervisory members.

3.6 Study community

The study community was selected carefully to ensure the quality of research results, compiled from Shariah experts and banking experts with sufficient experience in Islamic banking and financial risks.

3.7 Research Instrument

This study employed interviews, using open-ended questions. The questions were divided into two sections: the first section related to the participation contract; the impediments to its use; and the differences between the challenges of the Musharaka financing and the other debt contracts. The second section concerned the Maqasid al Shari'ah and to what extent participation contracts achieved the objectives of Shari'a.

3.8 Statistical Methods

The study data were analyzed thematically using NVIVO 14. The emphasis of the dataset was to depict respondents' perspectives and experiences in applying the Musharaka and explain the challenges the banks faced in doing so. Participants' opinions were sought relating to the Shariah objectives and Islamic banks. Participants'

specific contracts were analyzed by coding the language and classifying common ideas and opinions.

3.9 Chapter Summary

This chapter has presented the research methodology and the steps taken to conduct this study. A qualitative research design was employed, and in-depth interviews were conducted with individuals from different levels and qualifications in Islamic finance. NVIVO 14 was used to analyze the data. Data collection and analysis is discussed in Chapter 4..

Chapter 4 - Analysis and Discussion

4.1 Introduction

This chapter reviews the findings obtained from 10 participant interviews by analysing the data using Nvivo14. The analysis is divided into two sections. The first section outlines the analytical challenges faced in applying the Musharaka. The second section presents and analyzes the questions related to Maqasid al Shari'ah. This is followed by a discussion which compares the study's findings to those published by authors who have conducted research in the same field.

4.2 Descriptive Results and Participants' Socio-demographic Characteristics

As seen in Table 1, each participant's experience in Islamic banks is summarised, as well as information about their gender, and their job role. The majority of participants were male (n=8); only two were Female (n=2). Their roles were as follows: Shariah Supervisory Board (SSB) member (n=1); Head of Corporate Banking (n=1); Chief risk Officer (n=1); Head of Credit Management (n=1); Head of Shariah Coordination and Implementation (n=2); Head of Shariah Internal Audit (n=2); Head of Risk Management (n=1).

Table 8 - classification table

Participants	Gender	Position	Years Of Experience
Participant 1	Male	Head of Shari'ah Coordination and Implementation	Over 30 years
Participant 2	Female	Head of Credit Management	Over 24 years
Participant 3	Male	Head of Shari'ah Coordination and Implementation	Over 19 years
Participant 4	Male	Head of Risk Management	Over ten years
Participant 5	Male	Chief Risk Officer	Over 13 years

Participant 6	Male	Head of Shari'ah Audit	Over 16 years
Participant 7	Male	Head of Internal Audit	Over 17 years
Participant 8	Male	Shariah Supervisor	Over 23 years
Participant 9	Female	Head of Shari'ah Audit	Over 23 years
Participant 10	Male	Head of Corporate Banking	Over 15 years

The interview themes were summarized using Nvivo's thematic analytical technique. The themes were compiled using the hierarchy chart tool and displayed in Figure 6. The tool shows each theme in a box and the sub-codes used to code the files.

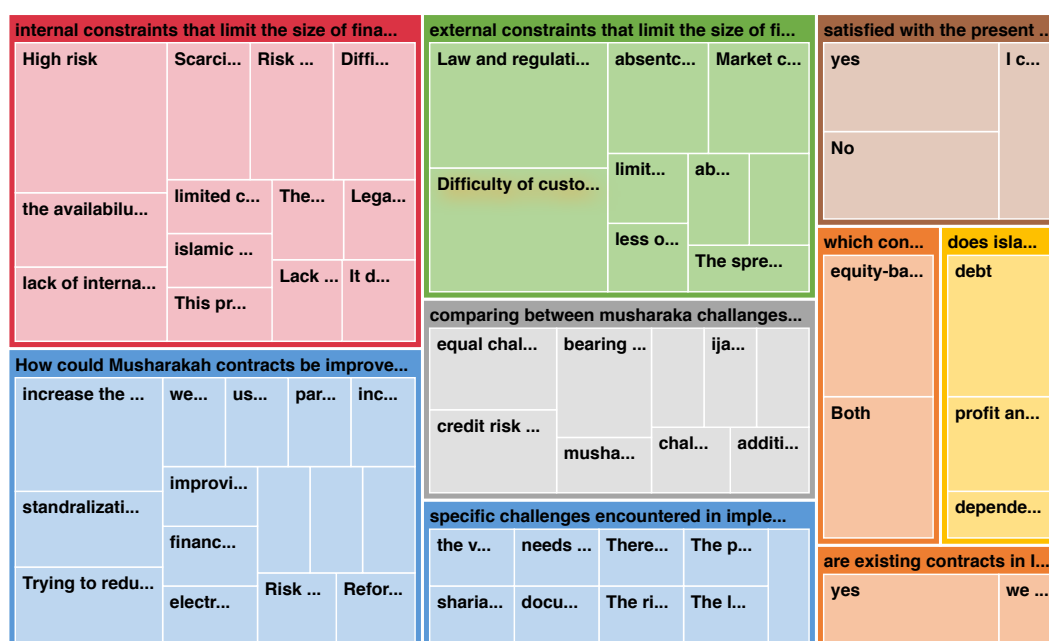


Figure 5 - Hierarchy chart for all themes using Nvivo

A word frequency tool was also employed to display the words used most frequently in the unstructured interview files. The word cloud is displayed in Figure 6. The most frequently used words are contract, Musharaka, partnership, challenges, Islamic banks, and banks. The words displayed by the tool describe the study's primary goal; this shows the integrity of the results.

- **No**

Some participants believed that Islamic banks have a role besides being financial intermediaries between debtors and creditors: they must carry out their intent or mission, contribute to the economy, and promote more fairness in money and transactions.

“No, Yeah, although Islamic finance has experienced significant growth over the years, the Musharaka is still very low compared to the total Islamic financing.”

“No, it’s true that every type of contract in Islamic banks has its needs. But still, Islamic banks have to enter into Musharaka more, and they must draw to their mission, which is a part of Islam's integration for the development of society.”

“No, but at the same time, if we want to increase the proportion of Musharaka financing, we should be more interested in correcting how to apply the Musharaka contract.”

“No”

- **I cannot decide**

Several participants agreed that the main issue is what is suitable for the client’s needs, stating that if Musharaka is applied, it should be because there is a real purpose for it, and not to apply Musharaka just to prove that we have it.

“It is difficult to answer the question of satisfaction because we are interested in providing funds given what is appropriate and convenient for the consumer and suitable to the bank, especially if there is a second product that meets the same requirements of the participant's contract.”

"I cannot decide. Therefore, the topic is governed by what management deems appropriate and meets client requirements. Nevertheless, I think that the Musharaka is an important contract, but it is not the only one in Islamic banks."

4.3.2 The internal constraints that limit the size of financing by a partnership (Musharaka)

4.3.2.1 Complicated process

A Musharaka needs more than one step to be concluded, and sometimes it needs to have a buy or rent component for some shares, which means having a new signature in each contract. Furthermore, a Musharaka is a contract that differs from one client to another depending on the project that the bank and the customer will be cooperating on. This means that the contract is not standardized for all customers. as emphasised in the following statements:

"Difficulty of application"

"More operational requirements: (complicated process) every client needs a new contract that is different from the previous one due to the difference in the fees, which needs the team for the Musharaka only to be sure about every step and monitor."

"The Musharaka contract is not straightforward. Also, the complicated Musharaka contract needs to be monitored and followed up, as well as P/L allocation."

"Longer process than other types of contracts"

"The process for the Musharaka contract is longer than other contracts."

"The participant's contract includes more than one party who needs to formulate the contract to the parties' consent and in which the contracts of adhesion cannot be applied in Musharaka."

4.3.2.2 Lack of internal awareness

Most participants agreed that bank employees lack sufficient knowledge and skills in Musharaka transactions; the Musharaka contract needs an expert employee who is

more qualified and knows what types of contracts will be suitable for the customer's needs. This theme is reflected in the following statements:

"Lack of internal awareness, Lower educational awareness than other contracts, Musharaka always needs expertise and specialized."

"Difficulty of understanding the contract by bank employees"

"Difficulty of understanding the contract by bank employees (employees in Islamic banks don't have enough understanding of Musharaka financing)"

"The contract is difficult to understand."

"Lack of awareness by bank staff; they should know how to organize the steps specification system of the contract changes for each client, which is different from others."

4.3.2.3 Scarcity of the contract

Musharaka is not given prominence. Islamic banks are more interested in other types of contracts. The following verbatim comments were documented during the interviews:

"Scarcity of the application of Musharaka even in the Islamic world as a financing or even investment method"

"This product has not been practised and has not been given the right to properly study in terms of operations, legal, treasury, and risk."

4.3.2.4 Risk management department in banks

The risk management department in banks does not allow other departments to complete Musharaka due to the increased risk associated with these types of contracts, especially when an alternative contract may perform the same function. They may also require limiting the financing size by asking for collateral or additional guarantees, leading to clients' hesitation to accept a Musharaka:

"Risk management department might ask for collateral or additional guarantees for some time in partnership because it's high risk."

"Risk management encourages the bank to deal with trade contracts because they are the least risky and are guaranteed (a sale that turns into a fixed debt in the customer's possession)."

"Risk department/risk framework management - they want to (mitigate the risk) and always lead the banks to lower risk contracts."

"Risk management in the banks refuses to enter the banks into higher risk contracts when there is another contract that can be accomplished and is considered lower risk."

4.3.2.5 Higher risk

Participants said that the original Musharaka is exposed to some risk whereby, in concluding the Musharaka, the banks will consider the losses they may incur, especially since the percentage of losses is determined by the proportion of the capital, and usually the banks will side with the partner who contribute the bigger shares, especially in the beginning. Some of the notes taken from the interviews:

"Banks think about profit and loss sharing and partnerships they will share in profit, so maybe sometimes the bank will hesitate to take the larger share of losses in the Musharaka."

"Partner with the customer in taking the risk of an incomplete project: As a financier, I prefer the client to take this risk himself."

"Higher risks attached to construction and valuation of the property."

"High risk and increases from day to day."

"It's important for the Bank Management to measure risk; they may consider that the subject of participation carries the risk that the Bank doesn't want to deal with and losing."

4.3.2.6 Bank management

Some results showed that the bank management can decide whether to have Musharaka financing for institutions. If the bank's management or board of directors (BOD) truly wants the Musharaka to be available, they will support it. Occasionally, the board of directors or bank management overlooks the significance of this contract and its position as an Islamic bank. Thus, because most bank executives are finance experts and there is a lack of genuine culture in Islamic financial institutions. This theme is embedded in the following statements:

"It depends on whether the bank management prefers the contract or not."

"Lack of understanding of the contract by executives or bank-holders from the Board of Directors"

"The absence of a legitimate culture in Islamic financial institutions (A large part of the employees and officials of Islamic banks lead through a mindset formed on a capital that wants to inhibit and earn money and lose sight of the importance of the participatory contract for the community by its development and the creation of employment opportunities for the community)."

4.3.2.7 Availability of alternative contracts

Few participants thought that the availability of other types of contracts in Islamic banks with more flexibility in application, lower risk, and suitability for customer needs is a reason for the limited use of Musharaka, especially since sometimes it is difficult to ensure that the project is fully Shariah compliant. Excerpts from the interviews:

"Having easier options to apply, less risky, and Shariah compliant."

"Availability of alternative contracts that meet needs more easily"

"It's hard to be sure that we are 100% avoiding shariah compliance risk, standards, and rules."

4.3.3 The external constraints that limit the size of financing by a partnership (Musharaka)

4.3.3.1 Law and regulations

The predominant external constraint that limits the financing of Musharaka in Bahrain Islamic banks is the law and regulation environment that governs participants' contracts, whether it is the regulations from Bahrain's central banks, such as the higher risk weight effect in the capital adequacy ratio, or the laws in court. The interview findings show that:

"According to the laws and regulations of CBB, Islamic banks are required to focus on a particular type of product, and their use percentage is required for each type of contract, so Central Bank hinders the right use of participation."

"Regulatory environment and legal framework governing in partnership with the financing can impose a constraint and sizeable financing regulatory requirement such as the capital adequacy ratio, risk management guideline. Banks should be ensuring and monitor the attachments of partnership agreements are under the local regulation."

"Higher risk weight of the central bank of Bahrain: affects the capital adequacy ratio."

"Regulation from CBB"

"Maybe some laws and regulations from the Central Bank may lead to avoiding the contract."

"The law in Bahrain doesn't give the Islamic bank Privacy in enacting laws necessary for the financing process."

"No special law governs the contract, especially in the courts."

4.3.3.2 Constraints from the perspective of the customer.

Another common point mentioned by participants was that challenges were caused by the Islamic bank's clients' lack of knowledge of the process and conditions of the Musharaka. Furthermore, they preferred the other types they were accustomed to. Thus, customers are unwilling to partner with banks and share their profits. However, Islamic banks are encouraged to enter Musharaka with customers if they have assets or funds. Sometimes, the customer wants to conclude a Musharaka with limited capital or without assets, leading Islamic banks to conclude the contract.

- Customer/institution lack of awareness

"Customer lack of knowledge."

"Difficulty of customer's understanding of contract."

"The unwillingness of companies or institutions to undertake cooperative projects based on the participating contract due to the lack of awareness of the participating contracts and they're accustomed to the Ijarah contract as the main producer of Islamic banks".

"Lack of awareness in Musharaka financing."

- Customer contract preferences

"Customers don't prefer the contract because it needs more than one step

- Customers unwilling to share the profits with the bank

"Difficulty in the customer understanding that the property to be financed by the bank will be shared between them. And they will become a partner."

"Customer unwilling to share the profit with the bank."

- Limitation of funds by the clients

"Limitation of funds by the clients; sometimes the customer does not have the assets, making the bank discouraged from concluding the contract."

4.3.3.3 Account standards

Several participants expressed the view that Musharaka financing lacks an accounting standard that is suitable for participant contracts and that the global account standard does not serve the banks in concluding and entering into Musharaka. The following statements are verbatim comments:

"Absence of accountant system that suitable for Musharaka contract"

"Account standards"

4.3.3.4 Market conditions

Other factors mentioned by participants were market conditions, price volatility, and the power of the real estate market; they faced each of these challenges by applying Musharaka financing. Examples of related comments:

"Market risk/ project risk; cost of the structure not only the evaluation"

"The real estate market is not booming, and banks are hesitant to enter partnerships or profit-sharing ventures due to the lack of economic stability in some countries, which could result in loss of assets."

"The valuation of the assets"

"Project valuation (decrease in property values)"

4.3.4 Comparing the challenges faced in Musharaka to those faced in debt contracts such as Murabaha/Tawarruq/Ijarah)

By comparing the challenges faced in Musharaka to those in debt contracts, it is possible to discover whether the constraints identified above are also applicable to other types of financing but can be measured and mitigated.

The following statements are the participants' opinions. Their viewpoints can be classified into five groups:

1. One participant believed that all types of contracts accomplished in Islamic banks take account of risks. However, Musharaka financing is more complicated in practice, while debt contracts are more straightforward:

"Murabaha applications are easier than sharing in risk. All of this contract is conscious of risks; in Murabaha, for example, the assets are possibly damaged and gone."

2. Unlike other participants, this second group of respondents considered that the challenges handled by Musharaka exceed those experienced by debt contracts. Debt contracts will end with an indebtedness associated with the solvency of clients, which means the banks have strategies and ways to mitigate the risk and take it into account before entering into the contract. As explained previously, the reality of Musharaka financing is to be a partner in profits and losses. This entails the banks bearing the risk from the beginning until the end of the partnership. Moreover, Musharaka financing includes additional market risk, especially since evaluating property is much easier in the other types of contracts:

"Challenges in asset-based contracts are lower, as risk is lower than in Musharaka because they result in indebtedness; the risk becomes paying the debt by the clients. And the risk can be taken into account. Unlike participation, risk is at the origin of the contract, not its consequence."

"More risk than debt contract"

"The idea of sharing the risk keeps Musharaka riskier."

"Debt contracts do not require the bank to take part in the risk, in contrast with the Musharaka, where the basis of the contract is to bear the risks."

"In the Musharaka, an additional market risk will be attached to the banks."

"Evaluating the property for other products is much easier than Musharaka."

3. Other participants thought that Islamic Banks always prefer to enter contracts that are more guaranteed and easily monitored; debt contracts provide these two features more than Musharaka:

"Debt contracts are more guarantee than equity contracts."

"Assets always will be collateral in debt contracts, and collateral management is easier in debt contracts."

4. One participant disagreed with other participants. In his opinion, both types of contracts are similar in terms of challenges:

"The risks and challenges in both types of contracts are equal; it's not exceeded and not less than each other."

5. Another participant explained that most of the challenges have been eliminated because of the frequent use and handling of debt contracts:

"Today, debt contracts have become easy to apply, so there are no longer challenges that may affect the application of these contracts, unlike the general and special challenges facing them."

4.3.5 How could Musharaka financing be improved to better serve the interests of banks and customers?

4.3.5.1 Musharaka cannot be improved

One participant was very satisfied with the position of Musharaka financing, and he did not believe that Islamic banks should increase the percentage of Musharaka financing in Islamic banks, especially with the law governing the banks in Bahrain.

"It's hard to apply Musharaka financing in Islamic banks."

4.3.5.2 increased awareness

Many participants agreed that the level of knowledge and familiarity with Musharaka financing should be increased and the banks, CBB and government should accept this brief. Islamic bank employees should also be more qualified in Islamic bank transactions, especially in Musharaka financing. Their knowledge should be developed so that they are familiar with every step of the contract:

"Market awareness is very important; we have to increase the market awareness about partnership contracts and more promotions to be launched in the market, such as campaigns and seminars to explain and encourage our clients to conclude Musharaka contracts."

"Party arrangements between the banks, clients, and contractors will help each party to understand his role and responsibility."

"Increased consumer awareness"

"Increase the awareness."

"Increasing the legitimate culture in Islamic financial institutions"

4.3.5.3 Reducing the Contract Process

According to the respondents, Islamic banks must consider ways to make the contract less complicated and easier to apply. As discussed earlier, the contract needs more than one signature from the customers at each step, thus encouraging the customer to enter the contract. This should be overseen by the Shariah supervisory board:

"Trying to reduce the contract process."

"The contract should be more flexible, especially if there is some delay in delivering the property rather than the signature of another contract."

"Using technologies, specific application, the benefit from governance app by making an electronic connection between what customers' information."

4.3.5.4 Risk appetite

If an Islamic Bank wants to expand its use of contracts, it must be willing to take risks and be more prepared to conclude Musharaka financing:

"Risk appetite"

4.3.5.5 Using Musharaka Financing correctly

Some respondents believed that, to increase the value of a Musharaka, Islamic banks should use the Musharaka in what would now be considered to be inappropriate contexts, such as for investors with less liquidity who wish to have more cash without selling their assets. Islamic banks can also improve Musharaka by entering into agreements with small and medium businesses:

"Use the contract to enter merchants into their assets they do not wish to sell but face a lack of cash flow."

"Banks must enter special development projects for SMEs to encourage them and help the community while at the same time helping to move the bank's funds."

4.3.5.6 Standardization of Musharaka Financing

Several participants said that, to improve the contract, Islamic banks must try to standardize the contract:

"Standardization of the contract."

"Standardized contracts, standardized application of the participatory contract mechanism."

4.3.5.7 improve the quality of contract structure

Another suggestion from a participant was that, if Islamic banks can have clearer risk-sharing arrangements or can decide the limit of risk, they would be more willing to enter into a Musharaka contract. This would inspire Islamic banks to increase the position of Musharaka in their institutions, and they could increase or decrease the extent of Musharaka depending on their situation. However, Islamic banks cannot decide the percentage of loss because it is incompatible with Islamic law.

"To have a clear sharing arrangement."

"Improve the quality of contract structure."

4.3.5.8 Specific law

"The Musharaka contract must be governed by a specific law that is different from the law governing other conventional participants' agreements; this will make Islamic banks more confident in applying the contract."

"Special Law on Contracts for Participation in Islamic Banks"

4.4 Maqasid al Shari'ah and Islamic banks

4.4.1 Do Islamic banks operate on the principle of profit and loss sharing or the principle of debt?

- **Based on the principles of debt**

Most participants perceived that Islamic banks today operate according to the principle of debt:

"Based on the principle of debt."

"Mostly in the principles of debt."

- **Based on the principles of PLS**

Only one respondent believed Islamic banks adhere to profit and loss-sharing principles and procedures.

"According to the principle of profit and loss sharing."

- **Both PLS and Musharaka**

One participant expressed how Islamic banks operate according to the PLS principles and Musharaka.

- **Dependent on the bank's management**

One participant viewed this issue as dependent on the bank's management, who could decide whether their bank operates according to the principles of profit and loss sharing or debt. The following statements are some of the participants' verbatim comments:

"In Islamic banks, this varies according to the bank's management because each management has its own viewpoint. Management with insufficient awareness of the various Islamic financial products tends to have more debt instruments, unlike those who are open to the Islamic financial market and have sufficient legitimate awareness of the products and their risks. There is an acceptable risk-taking limit. They will consider the participants to be an important means of doing this."

4.4.2 Do existing Musharaka in Islamic banks already fulfill the purpose of Maqasid al Shari'ah?

- **Yes**

Most participants believed that Musharaka financing provided by Islamic banks achieved the purpose of Maqasid al Shari'ah. Musharaka financing contributes to money circulation and will help economic growth, especially if applied correctly. The comments below illustrate this theme:

"Yes, achieved and strongly"

“Yes”.

"Yes, there is no doubt that all Islamic banks always pursue the purposes of Shariah through the preservation and development of money."

- **Islamic banks do not provide Musharaka financing.**

Only one participant thought that very few Islamic banks do not provide Musharaka financing.

"Today, Islamic banks don't provide Musharaka financing, but in previous dealings, yes, it fulfilled the needs and purpose of Maqasid al Shari'ah."

4.4.3 In your opinion, which contract assists in achieving Maqasid al Shari'ah more: equity-based or assets-based contracts such as Murabaha, Ijrah. And why?

- **Equity-based contracts assist in achieving Maqasid al Shari'ah more than assets-based contracts.**

Two participants believed that equity-based contracts assist in achieving Maqasid al Shari'ah more than assets-based contracts:

"Equity-based contracts more than assets-based contracts."

"Equity more than debt contract".

- **Both contracts achieve the purpose of Maqasid al Shari'ah.**

The majority of participants perceived that both contracts fulfilled the purpose of Maqasid al Shari'ah. One participant thought that one could not be chosen over the other, that both achieve Maqasid al Shari'ah, but the equity-based contract is more related to Maqasid al-Shari'ah. Examples of the related comments are presented below:

"There is no specific purpose for the participants that is distinct from the purpose of the debt's contracts; ultimately, the two contracts will preserve money by investment or Halal financing."

"I don't think there is a product that achieves the purposes of Shari'a more than the others. All of them are financing formulas that have legal support. I think all of them are on one degree and equal in achieving the purposes of Shari'ah."

"Both play a role in the purposes of Shari'a, but the contracts for participation have the issue of wealth distribution, which is an important purpose. As in the Musharaka contract, profit is distributed to more than one side."

Table 9: Respondents' Answers

participant	Question 1: In your opinion, do Islamic banks operate according to the principle of profit and loss sharing or on the principle of debt?	Question 2: Do existing contracts in Islamic banks already fulfill the purpose of Maqasid al Shari'ah?	Question 3: In your opinion, which contract assists in achieving Maqasid al Shari'ah more, equity-based contracts such as Musharaka, Mudarabah, etc. (عقود المشاركات) or assets-based contracts such as Murabaha, Ijrah (عقود المدائنات). And why?
Participant 1	- According to the principle of profit and loss sharing.	- Yes, achieved and strongly	- Equity-based contracts more than assets-based contracts.
Participant 2	- Based on the principle of debt.	- Yes	- Equity
Participant 3	- Based on the principle of debt.	- Yes.	- There is no specific purpose for the participants that is distinct from the purpose of the debt contracts; ultimately, the two contracts will preserve money by investment or Halal financing.
Participant 4	- Depends on the bank's management	- Yes, there is no doubt that all Islamic banks always pursue the purposes of Shari'ah through the preservation and development of money	- I don't think there is a product that achieves the purposes of Shari'ah more than the others. All of them are financing formulas that have legal support. I think all of them are on one degree and equal in achieving the purposes of Shari'ah.
Participant 5	- Both.	- Today, there are no Musharaka financing, but in previous dealings, yes, it fulfilled the needs and purpose of Maqasid al Shari'ah.	- Equity more than debt contract.
Participant 6	- Mostly in the principles of debt.	- Yes.	- Both play a role in the purposes of Shari'ah, but the contracts for participation have the issue of wealth distribution, which is an important purpose. As in Musharaka financing, profit is distributed to more than one side.

4.5 Discussion of the Research

The main objectives of this qualitative research were to explore the challenges faced by Islamic banks in Bahrain when applying participation contracts; to investigate whether Islamic banks operate on the principles of equity contracts or debt contracts; and determine whether the contracts adopted today by Islamic banks are in line with Maqasid al-Shari'ah.

Of the 10 participants, five were not satisfied with the proportion of Musharaka finance. In their opinion, Islamic banks should increase Musharaka and cooperate with the investors in their projects.

Three participants fulfilled the percentage of Musharaka financing, and they believed that Islamic banks should not enter into higher-risk projects or agreements because they are ultimately responsible for saving depositors' money.

The remaining participants were unsure whether institutions offered Musharaka financing, as it was more important that the banks offered what was appropriate for their clients.

Islamic banks should try to increase the principles of Musharaka financing but in a way that is consistent with the interests of enterprise and depositors. Allah's Messenger (ﷺ) said: "There should neither be harming (of others without cause) nor reciprocating harm (between two parties)." (Reported by Ahmad and Ibn Majah.)

In this study, the complicated processes of Musharaka financing, the conditions of the contract and Shariah compliance of the financing were raised frequently, resulting in the need for Islamic banks to have more expert employees not only in Shari'ah but also in the investment and feasibility study at every project stage to monitor the status of the project. Al-Jarrah et al. (2021), Orhan (2017), and Onagun (2017) are in broad agreement about the obstacles to achieving this.

Another issue raised by respondents was the lack of employee knowledge and understanding of the various types of contracts that the organization could offer and the difficulty in choosing a contract that matched the customer's needs. This coincides with the findings by Al-Jarrah et al. (2021) and Ascarya and Yumanita (2006). This is because most employees in Islamic banks are not Islamic finance or Shariah-qualified.

Musharaka financing also carries a higher risk than other agreements applied in Islamic banks, thus leading the bank's management or risk management department to avoid it and use more guaranteed contracts. This challenge is in line with the conclusions of Muhammad (2014). As Islamic banks operate in a competitive environment, the bank's management are more cautious about entering Musharaka.

This study found that the biggest external obstacles were the law and regulation. The majority of participants agreed that the laws and regulations governing Islamic banks are reasons for the low percentage of participant contracts; this aligns with the findings of Ascarya and Yumanita (2006). In addition, the accountant standards that require Islamic banks to commit to regulation do not support Musharaka.

A lack of awareness also adversely affects the position of Musharaka financing in Islamic banks in Bahrain. Islamic banks face challenges related to the lack of awareness of subjects in the kingdom regarding the types of financing offered by the Islamic banks. Yustiardi et al. (2020) concurred with this view. Respondents were clear that customer challenges were the absence of knowledge and expertise and not adopting a moral standpoint. This was contrary to the findings of Farooq & Ahmed (2013) and Kayed (2012).

Similar results were reported in the Hassan et al. (2023) study regarding market conditions. The instability of the economy and the absence of property valuation are difficulties banks face when entering Musharaka. As the real estate market is not flexible, it moves up and down, making banks hesitant to enter into a contract. Musharaka financing is a long-term agreement, and it is difficult to predict the real estate market.

Participants were asked for their opinion on which types of financing in Islamic banks face more challenges. The majority of participants agreed that Musharaka financing is riskier; this might explain why Islamic banks are avoiding Musharaka contracts as they are not a sales contract. Few participants believed that both types of contracts face the same type of risk. This is because, in their opinion, the sales contract or Ijarah contract is more guaranteed. It is still related to market risk where, in the case of the customer's default, the banks can take action to sell the product. There is still a risk that the commodity may fall in price when the bank withdraws it from the customer and sells it to pay the customer's remaining debt.

Maqasid al Shari'ah

The main reason the respondents were asked whether Islamic banks operate according to the principles of debt or equity was to determine whether Islamic banks operate on profit-and-loss-sharing principles. The results show that three participants argued that Islamic banks operate according to the principle of debt: one participant emphasized the principle of equity, while another responded that he believed that Islamic banks operate according to both principles.

In question three, we asked the participants which type of contract achieves Maqasid al Shari'ah: the contract of debt or the contract of equity. Three participants concurred that both contracts have their role in Maqasid al Shariah; this agreed with the study of Isa et al., (2015) and Al-Khaloufi, (2013). Three participants agreed that the equity contract achieves the objective of Maqasid al Shari'ah more than Musharaka; this is in line with the studies of Nouman et al., (2020); Yusof et al., (2009); Iqbal (1997); Ariffin et al., (2015); and Al-Khaloufi, (2013).

By comparing answers to the first and third questions, we can summarize that Islamic banks achieve the Maqasid al Shariah even if they operate according to the principles of debt. If banks increased the percentage of the Musharaka, they would contribute more to society and economic development. They would assist in the circulation of money between the individual and enhance investment. This can be evidenced by illustrating the answer for participants to question two, who all agreed that Musharaka financing achieved the purpose of Maqasid al Shari'ah.

4.6 Chapter Summary

This chapter reviewed the findings from a thematic analyses of participants' replies to questions posed during the interviews. The interviews focused on the challenges Islamic banks face in implementing Musharaka financing in their institutions and the involvement of Maqasid al Shari'ah in the participation contract. The focus of the analysis was to identify the internal and external challenges faced by Islamic banks in the Kingdom of Bahrain that led to limiting the use of Musharaka and whether Islamic banks achieve the purpose of Maqasid al Shari'ah. The findings were discussed in relation to Bahrain's context and studies conducted in other countries.

5.0 Chapter 5 – Conclusion and Implications

5.1 Introduction

This chapter will summarize the chapters of the study, its main points, research methodologies, research findings, limitations of the study, and recommendations.

5.2 Summary of the Research Findings

This study examined the challenges in applying Musharaka financing in Islamic banks in the Kingdom of Bahrain and the relationship between the principles of PLS and the objectives of Maqasid al Shari'ah.

After providing an overview of Islamic banks, Chapter 2 discussed the results of previous studies on Sharika in Islamic jurisprudence, the legality of the Sharika, the classification of Sharika in Islam, and the modern types of Sharika. The chapter discussed Musharaka financing in Islamic banks, identifying the general rules and types of the contract, and the ways that Musharaka can be applied in Islamic banks. The chapter also identified a significant increase in Musharaka financing in Islamic banks in Pakistan and clarified the types of Musharaka they used, compared with the agreements of diminishing Musharaka in the Nizwa Bank in Oman.

The chapter also described Maqasid al Shari'ah in general and explained the concept of protecting wealth. Results from previous studies in the same field showed different opinions and reviews regarding Maqasid al Shari'ah in Islamic financial transactions. The chapter concluded by discussing the challenges related to applying Musharaka financing, and presented results from a range of research studies.

Chapter 3 elaborated on the methodology, data collection design, and target population. Sections on research instruments and statistical methodology were also included.

In Chapter 4, each respondent's answer was displayed and analyzed by Nvivo 14. Data were analyzed to provide a greater understanding of the challenges in Musharaka from the perspective of risk, the treasury and investment. Also considered were issues related to corporate banking holding a different position than that of Islamic banks and the extent of Shariah expertise and implementation.

The remainder of Chapter 5 will conclude the research paper and propose recommendations for increasing the use of Musharaka financing.

5.3 Implications of the Research Findings

The main problems impeding the adoption of the participation contract are as follows:

The contract is classed as high-risk in relation to the bank's overall capital. The bank is exposed to risk by virtue of the participation arrangement. When a bank enters into a participation contract, it effectively exposes itself to risk since it recognizes that the danger of losing money equals the probability of profit, and the risk of losses can be much greater.

Laws and regulations neither enable nor encourage senior management in Islamic banks to increase the use of participation contracts owing to a lack of support from relevant authorities.

Employees at Islamic banks are unaware of the many forms of contracts that Islamic banks might offer to better serve the interests of their clients and society. This results in a lack of information among members of the community regarding the sorts of contracts offered by Islamic banks, making clients unwilling to accept participation contracts from Islamic banks owing to their unfamiliarity with the contract's benefits.

5.4 Recommendations

- Islamic Banks should allocate a certain proportion of their capital at the beginning of the year to finance participation contracts, even if it is low to begin with, and gradually increase it as it deems appropriate. They can also take a guarantee in cases of misconduct or negligence.

- The Central Bank of Bahrain (CBB) should encourage Islamic banks to enter into Musharaka financing with its corporation. The CBB should decide the capital an Islamic bank could use but only if it entered into Musharaka contracts.

- Islamic banks, in general, are considered a lower risk than conventional banks because their transactions are linked to buying and selling. This CBB should lower the capital requirement ratio for Islamic banks.

- A competent body should be established to study the feasibility of projects to be guaranteed to Islamic banks.

- Increasing the bank's capital to enable it to engage more extensively in participation contract.

- Good Conduct Certificate Services should be provided by the Bahrain Chamber.

- Employees' awareness of the range of contracts that are available should be increased by introducing them to specialized and in-depth courses in Islamic financial products. Society's awareness of the contracts available will follow increased use of the range of contracts.

5.5 Limitations

There were limitations associated with this study. Firstly, determining the target group was difficult since it required selecting specialists in risk management and credit review who are well-known for Musharaka financing and its structure and the Shariah prohibitions of the contract. Secondly, scheduling interviews with participants was difficult because most members have operational positions in the bank and some worked abroad.

5.6 Conclusion

This study summarized the main internal and external constraints that cause Islamic banks to avoid submitting participating contracts to the client and small investors. This is despite the agreement of most respondents that the participant's contract, if applied appropriately and used in the right context, would provide benefits and advantages at an economic and developmental level and would further assist official banks in achieving Shariah objectives.

The findings show that the contract of participation conforms to the principles of the Maqasid al Shari ah and achieves it more than other types of contracts. However, the overriding conclusion of the study is that it is difficult for Islamic banks to implement the participation contract in the face of economic and real estate volatility. If Islamic banks are to increase Musharaka financing, their presence in a highly competitive environment requires cooperation and intervention from other institutions and bodies.

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APPENDICES

Appendix 1: Faysal Bank Shariah Certificate of Running Musharaka

Faysal Bank Limited
7th Floor, Faysal House
ST-02, Shahrah-e-Faisal
Karachi, Pakistan

UAN 021 111 747 747
TEL 021 3279 5168
FAX 021 3279 3122

faysalbank 

August 31, 2016

barkat islamic banking

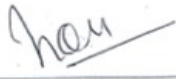
Hasan Junaid Nasir
Head Islamic Banking
Faysal Bank Limited

Subject: Shariah certificate for Running Musharakah

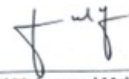
This is to confirm and certify that the Shariah Board has reviewed the product policy, financing facility agreements & other related documents pertaining to the proposed "Running Musharakah" financing and have found them to be in compliance with the Shariah Principles.

And Allah knows the Best.

Regards


Mufti Khawaja Noor ul Hassan
Resident Shariah Board Member


Dr. Mufti Khalil Ahmad Aazami
Member Shariah Board


Mufti Muhammad Mohib ul Haq
Chairman Shariah Board

Registered Office
Faysal House
ST-02, Shahrah-e-Faisal
Karachi, Pakistan
www.faysalbank.com

Appendix 2: Diminishing Musharaka Ending with Ownership Agreement

Contract No:
Diminishing Musharaka (Partnership) Contract
This contract is made and entered into at the latest of the signatures date, by and between:
1. Bank XYZ, established under the laws of COUNTRY of XYZ; Address: P.O. Box (), PC (), , COUNTRY of XYZ; Here-in-after referred to as the (First Party, Bank).
And
1. Customer: Address: represented by Mr.: in his/her capacity as: Here-in-after referred to as the (Second Party).
Both parties, with their full legal competence to conclude such actions, declare and agree to the following:
Preamble
Whereas the First Party is an Islamic Bank, licensed by the Central Bank of XYZ, to practice Islamic Banking and provide Islamic Banking products in compliance with Islamic Shariah principles and rules; and whereas the Second Party wishes to sign a Musharaka Agreement with the First Party to purchase goods as per the terms and specifications of this Agreement in Annex (1);
both Parties being legally competent to enter into this contract, hereby agree on the following:
1- Nature of Preamble
The above Preamble, and all supplements to this agreement signed by the parties are integral and complementary to the contract, to the extent it does not conflict with its provisions.
1. Musharaka Conditions
(2-1) The Musharaka capital in XYZi Dinars is the amount mentioned in Annexure (1), and each of the First Party and Second Party shall contribute to the Musharaka capital the percentage as mentioned in Annexure (1). (2-2) In case utilization of the Musharaka partnership capital is executed on various time schedule, it is permitted for the Bank to pay the capital participation gradually simultaneously with these periods, and it is permitted to adjust the capital participation percentages as agreed between both parties. The second party's share in cash will be deposited in the special account opened at the Bank on or before the signing of this agreement. In the

event the second party's share is in kind such as in the form of the value of the land, the same will be reflected as the second party's share from the Total Musharaka Capital.

(2-3) A special account shall be opened at the Bank to manage the Musharaka after concluding this contract directly whereby each party deposits its cash participation after concluding contract directly. For avoidance of doubt, the Bank on behalf of the Musharaka shall operate the account including the payment to contractor. However, the Second Party will sign the Supervisory Contract and deal with the contractor as well as other roles as stated in that Contract.

(2-4) The Customer shall present suitable security for cases of transgression or underperformance or violation to the terms and conditions of the Musharaka partnership contract. Securities are mentioned in Annex (1).

(2-5) The partnership starts and terminates on the dates mentioned in Annexure (1) unless one of the two parties sends a written notice to the other party, and is subject to renewal or extension for a period as agreed between both parties.

(2-6) Both parties agree that management of the partnership and the power of signature is entrusted to the Customer provided that such transactions are executed to realize the objective of partnership and within its objectives and on behalf of the partnership. Any legal actions shall be issued by all partners.

(2-7) Losses, if any, are distributed among partners respectively to the capital participation of each partner. The Second Party shall not guarantee the capital of the First Party except in cases of negligence and transgression and violation of the terms and conditions of the Musharaka partnership contract.

(2-8) In case the Customer refrains from paying its obligations due to any reason, the First Party is entitled to pay any of the obligations and register it to the account of the Customer held at the Bank, and reserves the Bank's rights stipulated in this agreement arising or related to the violation of the Customer to these obligations, and account for it in the Musharaka account unless related to the Second Party.

(2-9) Each partner shall bear respectively to each capital participation various operating maintenance expenses, and the Second Party is permitted to take sub-lease for first party and shall be solely liable for any obligations towards third parties.

(2-10) In the event that the implementation of the property is not completed and it is decided to terminate the participation, any change in the value of the property increased or decreased will be divided between the parties according to their share in the participation

(2-11) The right of the bank in the absence of completion of the building and the desire to end the participation to be evaluated from the property and the sale of the bank's share of the property to the client or to a third party
(2-12) If the bank's share cannot be sold on its own, the client will be entitled the bank to sell all the shares as completed after evaluating them to a third party. Profit or loss will be divided between the parties in proportion to their ownership.
2- Musharaka Capital
(3-1) The total Musharaka capital amount subject of this contract is mentioned in Annex (1). If one party incurs expenses and expenses related to participation, it is added to its share of participation (capitalization of expenses).
(3-2) The First party shall pay its capital participation gradually to the Customer or his designates as per the Customer's written and signed instructions, as per progress of each period independently as per the attached schedule. The Bank is entitled to request that these contributions shall be preceded by a report from the responsible or supervisory entity or both. The Bank is also entitled to refrain from paying its contributions until the Bank confirms progress and the related payment. For avoidance of doubt, Bank's Capital Participation will be credited into the Musharaka Special Account' as per clause 2.3 above.
4-Obligations of the Second Party
(4-1) The Second Party undertakes not to perform any transaction similar to the Musharaka partnership transactions or to compete to the same objective. And in case such violation by the Customer is confirmed to this clause, the Bank is entitled to abrogate the partnership contract and terminate it.
(4-2) The customer undertakes that he will establish a first degree mortgage over the property, as described in Annexure 1, in favor of Bank XYZ at his own cost. The Original Title deed/ Mulkiya will be kept with Bank at all times till the termination of the Musharaka agreement. Further the Customer undertakes not to create any additional mortgage/ pledge/ charge on this property without taking prior written consent from the Bank then it will be for shariah compliant activities
(4-3) Withdrawal and Transfer of shares: a) All partners are not entitled to withdraw from the partnership before the end of its term except with the approval of the other partners. b) All partners are not permitted to sell or mortgage or transfer its share or part of, except with written approval of the other partners who shall have right of priority to purchase the offered share. c) In case of violation of the preceding clause, the sale of the share shall not be valid for the rights of the other partners, and they maintain all their rights.

(4-4) If the Second Party defaults in any of its obligations stipulated in this contract, the Bank is entitled to act as substitute to the Second Party to perform the defaulted obligation, the cost of which shall be deducted from the entitlements of the Second Party, if any, or debited to the Customer's account.
(4-4-1) The First Party is entitled to request a guarantor to guarantee the Bank's existing or future rights or which shall arise or are relevant to this contract. The guarantee of the guarantor is conditional in case gross negligence or wilful misconduct to all transactions relevant to this contract, and any due obligations.
(4-4-2) The Musharaka partnership contract shall terminate due to the demise of second party. Accordingly, upon such event, the Bank shall invoke the Takaful policy to recover the relevant portion of its Musharaka ownership share at that time.
(4-5) The Musharaka partnership may be terminated before the end of its duration in case of losses, by unanimous decision of the partners.
2. Other Conditions
(5-1) Address The address written in this contract for each of the parties to this contract is the address chosen for sending all correspondence and notices related to this contract to each party; any change of address shall not be considered unless with a written notification sent by either party to the other by registered mail, or any other means agreed to at the time, containing the alternative address.
(5-2) Law and Jurisdiction This contract in its interpretation, implementation and resolution of disputes arising between its parties, is subject to the terms and rules of the First Party and to the relevant applied regulations and laws of XYZ not in contradiction to Islamic Shariah principles and rules. The courts of XYZ shall have the jurisdiction to resolve any dispute that may arise about the interpretation or execution of this contract.
(5-3) Authority and Power of the Second Party The Second Party declares that he/she has the full authority and power to enter into the contract and fulfill the obligations set out therein, and such, fulfillment shall not conflict with any law, promise or obligation of the Second Party.
(5-4) Obligatory of fulfillment of the Contract Not claiming fulfillment of any condition or obligation in this contract by the First Party at any time, or non-execution any of its confirmed rights herein, shall not be construed as waiver of that right and its execution surrender of claiming total fulfillment at any subsequent time. And any item not mentioned in this contract shall be subject to the laws and trade norms of the COUNTRY of XYZ, and the general regulations of the Bank, not in contradiction to Islamic Shariah rules and principles.

(5-5) Settlement of disputes The parties hereto have agreed that if a dispute, disagreement or claim arises regarding this contract and the Parties fail to settle it amicably within two weeks after either Party gives notice to the other Parties regarding the dispute disagreement or claim, it shall be referred to the competent Court of XYZ, The submission to the jurisdiction of the courts referred in this clause shall not limit the right of the Bank to take proceedings against the Second Party in any other court of competent jurisdiction, nor shall the taking of proceedings in any one or more jurisdictions preclude the taking of proceedings in any other jurisdiction.	
(5-6) Headings The Headings of this contract are for convenience and reference only and they shall not be used in the interpretation or execution of any provision of the contract.	
7-3 Any matters not mentioned in this contracts shall be subject to laws and practiced commercial norms of XYZ in addition to not-contradicting Islamic shariah rules and the common terms and conditions of the bank,.	
	ره في هذا العقد يخضع لأحكام الشريعة الأساسي للبنك، وما لا يتعارض معهما من التجارية النافذة بدولة ا ب ج.
(5-7) Counterparts and appendices of Contract This Contract is made in Arabic and English. However, if there is discrepancy between Arabic and English texts, the Arabic text shall prevail. All the said appendices referred to herein shall form an integral part thereof this contract, and shall be read and construed in accordance with the provisions and conditions thereof. In witness whereof and with the intention of the parties to be bound legally by this contract, the representatives of the parties have signed this contract on the above date and an original copy is made available to the Second Party.	
(8-5) Appendices to this agreement are: 1. 2.	
(6) Signatures	
First Party	
Bank XYZ Name of authorized signor: Designation: Signature: Seal: Date:	

Second Party
Client: Name of authorized signor: Signature: Date:

Appendix 3: Musharaka Agreement

Musharaka Contract No. ()	
Musharaka Details	
Date	
Musharkah Asset descriptions	As the appendix attach with Annexure (2) in this agreement
Deal No.	
Musharaka Capital	
Musharaka share of First Party in the diminishing capital is % equivalent to () XYZi Dinars. Musharaka share of Second Party in the diminishing capital is % as per the following details: 1. Participation in cash: () XYZi Dinars 2. Participation in kind (),valued at () XYZi Dinars. 3. Or ALL	
Musharaka Beginning date (MM/DD)	
Musharaka Expiry date	
Securities	

Profit Distribution ratio (in case of Musharaka in business) First Party % Second Party %	
For official use of Bank XYZ only	
Checked by	Approved by
Posted by	

Appendix 4: Muzn Bank: Diminishing Musharaka agreements:

MASTER DIMINISHING MUSHARAKAH AGREEMENT
DATED: THIS AGREEMENT is made between the following parties: (1) ABC Islamic Banking ABC a banking company incorporated under the laws of the ABC Country (“Bank”) of the first part; AND (2) THE CUSTOMER whose name and particulars described in Item 1 of Schedule 1 hereto (“Customer”) of the second part.
RECITALS: (A) At the request of the Customer, the Bank has agreed pursuant to the Facility Letter dated the day and year as set out in Item 2 of Schedule 1 hereto (“Facility Letter”), to make available the Diminishing Musharakah Facility of up to the amount as set out in Item 3A of Schedule 1 of this Agreement (“Facility”) pursuant to the terms of the Facility Letter (as defined herein) and subject to the provisions of this Agreement. (B) The parties agree to execute this Agreement to regulate the provision of the Facility subject to the terms and conditions herein. NOW IT IS HEREBY AGREED as follows: 1. DEFINITION AND INTERPRETATION 1.1 Definition In this Agreement, each of the following expressions has, except where the context otherwise requires, the meaning shown opposite it:

“Acquisition Payment” being payment by the Customer towards acquiring the units representing Bank’s ownership shares in the Asset.

“Agreement” or “this Agreement” means this Diminishing Musharakah Agreement inclusive of any parts thereof.

“Asset” means the asset as set out in Item 10 of Schedule 1.

“Bank” means ABC Islamic Banking ABC a banking company incorporated under the laws of the ABC Country and having its registered office at [***] and includes its successors in title and assigns.

“Bank’s Initial Acquisition Payment” means the amount referred to in Item 3B of Schedule 1 hereto subject to the terms of this Agreement and includes any part thereof.

“Bank’s Initial Ownership Share” means the Bank’s initial percentage of ownership share in the Asset at the commencement of the Co-ownership Period as set out in Item 3A of Schedule 1 hereto.

“Business Day” means a day on which the banks and financial institutions are open for the transaction of businesses of the nature required under this Agreement.

“Buyout Amount” means the amount to be paid by the Customer to the Bank in order for the Customer to fully acquire the Bank’s ownership share in the Asset together with any other amount due to the Bank under the Facility and the Transaction Documents either pursuant to an early settlement or due to the Termination Event.

“Conditions Precedent” means the conditions precedent as set out in Schedule 2 of this Agreement.

“Co-ownership Period” means the tenure of the Facility (including the construction period) being the period as set out in Item 5A of Schedule 1.

“Customer” means the customer whose name and particulars as set out in Item 1 of Schedule 1 and includes its successors in title and permitted assigns.

“Customer’s Initial Acquisition Payment” means the amount referred to in Item 3C of Schedule 1 subject to the terms of this Agreement and includes any part thereof.

“Customer’s Initial Ownership Share” means the Customer’s initial percentage of ownership share in the Asset at the commencement of the Co-ownership Period, as set out in Item 3B of Schedule 1 hereto;

“Declaration of Trust” the declaration of trust in the form and substance as set out in ATTACHMENT C, duly executed.

“Facility” means the Diminishing Musharakah Facility of up to the amount as set out in Item 2A of Schedule 1 subject to the terms of this Agreement and includes any part thereof.

“Facility Letter” means the Facility Letter issued by the Bank and duly accepted by the Customer dated the day and year as set out in Item 2 of Schedule 1 of this Agreement and includes any supplemental thereto.

“Ijarah Contract” means the contract entered into between the Bank and the Customer for the lease of the portion of the Asset owned by the Bank to the Customer in the form and substance of ATTACHMENT B, duly completed.

“Ijarah Tenure” means the tenure of the Ijarah Contract as set out in Item 5B of Schedule 1.

“Installment Payments” means collectively, the aggregate of (a) Acquisition Payment; and (b) Rental Payment to be paid by the Customer under the terms of this Agreement as set out in Schedule 5 of this Agreement.

“Musharakah Contract” means the contract entered into between the Bank and the Customer for the co-ownership of the Asset in the form and substance of ATTACHMENT A, duly completed.

“Musharakah Partners” means the Bank and the Customer, collectively and reference to “Musharakah Partner” refers to any one of them.

“A Country Riyal” or “OMR” means the lawful currency of the ABC Country.

“Purchase Undertaking” means the purchase undertaking provided by the Customer in favour of the Bank as per Schedule 4 hereto, duly completed.

“Purpose” means the purpose of the Facility as set out in Item 7 of Schedule 1.

“Rental Payment” means the lease rental payment being part of the Installment Payment payable by the Customer to the Bank under the Ijarah Contract.

“Security Documents” means the security documents as described in Item 8 of Schedule 1 and includes such other document or instrument creating Security Interests in favour of the Bank.

“Security Interests” means any mortgage charge, pledge, lien, right of set off or any security interest whatsoever or howsoever created or arising.

“Security Party” means any party, other than the Customer, providing security or guarantee for the Facility and as set out in Item 9 of Schedule 1.

“Seller” means the supplier, seller or vendor of the Asset and where the Customer is already the owner of the Asset, the Seller shall, in that instance, means the Customer.

“Service Agency Contract” in relation to the Ijarah Contract, means the service agency contract entered into between the Bank and the Customer for the appointment of the Customer as service agent in the form and substance of ATTACHMENT D, duly completed.

“Termination Event” means any of the events as set out in Clause 12 of this Agreement.

“Total Loss” means the occurrence of the events upon which the proceeds from the Takaful are insufficient to completely restore or repair the Asset or a situation where the Bank is of the view that Asset is destroyed such that restoration work is not economically feasible.

“Transaction Documents” means collectively the following documents:

- (a) Facility Letter;
- (b) This Agreement;
- (c) Musharakah Contract;
- (d) Ijarah Contract;
- (e) Security Documents;

and such other documents designated as such by the Bank.

“Variable Element Payment” means the payment which shall be calculated at the agreed Ijarah rate as set out in the Facility Letter on the basis of actual number of days elapsed in a 365 day period.

1.2 Interpretation

The headings in this Agreement are inserted for convenience only and shall not be taken, read and construed as essential parts of this Agreement.

References to clauses or schedules are to be construed as references to the clauses or schedules of this Agreement.

All references to the provision of any legislation or statute or decree includes references to any amendments, any statutory modification and re-enactment thereof or regulations proclamations, by-laws, published rulings, statements of policy or guidelines issued under or in relation to that legislation, statute or decree.

References to this Agreement or any agreement or instruments shall include all amendments, variations and modifications to this Agreement as shall from time to time be in force.

Words importing the singular number shall include the plural number and vice versa.

Where two or more persons or parties are included or comprised in any expression, agreements, covenants, terms, stipulations and undertakings expressed to be made by or on the part of such persons or parties shall be deemed to be made by and be binding upon such persons or parties jointly and severally.

Words importing the masculine gender shall include the feminine and neuter gender and vice versa.

A reference to a document includes any amendment or supplement to, or replacement or novation of that document.

Any reference to “laws of A Country” shall be construed so as to include, without limitation, any statute, ordinance, decree, regulation, ruling, , or order enacted, issued or prevailing in the ABC Country or any bureau, minister, instrument, agency, court, regulatory body, authority, legislative body or department thereof (including, without limitation, Central Bank of A Country or any taxing, fiscal or other monetary authority thereof).

The “winding-up” of a person includes the amalgamation, reconstruction, re-organization, administration and presentation of a petition with a view to winding-up or cessation of business of that person and the dissolution, liquidation, merger or consolidation of that person.

Any reference to a ‘person’ includes any individual, company, corporation, firm, partnership, joint venture, association, organisation, trust, state or agency of a state and reference to a person or party includes that person’s or party’s successors in title and permitted assigns.

3. BRIEF DESCRIPTION OF FACILITY

(a) Under the Shariah concept of Musharakah Mutanaqisah, the Bank and the Customer jointly purchase an identified asset (“Asset”) whereby the Customer contributes a certain sum as the initial payment (“Customer’s Initial Acquisition Payment”) towards part purchase of the Asset and the Bank shall contribute a certain sum being the balance of the initial payment (“Bank’s Initial Acquisition Payment”) towards the purchase of the Asset.

(b) The Bank leases its share of Asset to the Customer based on the principle of IjarahMawsufah Fi Zimmah (Forward Leasing) during the period of construction the Asset and thereafter on the basis of Ijarah (Leasing) upon completion of Asset (whichever applicable). In case of the Asset is ready for use, the Bank leases its share of Asset to the Customer based on the principle of Ijarah (Leasing).

(c) The Bank then appoints the Customer as its service agent in relation to the Asset upon the terms as stated in the Service Agency Contract.

(d) The Customer shall pay to the Bank Installment Payment (“Installment Payment”) which comprises of (i) Acquisition Payment being payment towards acquiring the Bank’s ownership share in the Asset, and (ii) Rental Payment being payments for the lease of the Asset.

(e) As a result of the Installment Payment made under the Facility, the Customer’s ownership share in the Asset increases and the Bank’s ownership share decreases proportionately until the Customer wholly and fully owns the Asset.

(f) The Rental Payment ceases immediately upon the Customer having fully acquired the ownership share in the Asset from the Bank.

4. THE FACILITY

4.1 The Facility and Amount

At the request of the Customer, the Bank agrees to make available to the Customer the Facility pursuant to which the parties shall enter into Transaction Documents, subject to the terms and conditions of this Agreement.

4.2 Purpose

(a) The proceeds from the Facility shall be used by the Customer towards the Purpose as set out in this Agreement.

(b) The Customer shall not utilise the Facility for any purpose other than the purposes as stated in Clause 4.2(a) above.

(c) Notwithstanding anything to the contrary, the Bank shall not be under any obligation whatsoever to ensure that the Facility is utilised towards the purposes as set out herein.

4.3 Facility Tenure

The tenure of the Facility shall be in the period similar to the Co-ownership Period and Ijarah Tenure.

5. AVAILABILITY

5.1 Conditions Precedent

The Bank’s obligation to make available the Facility to the Customer shall subject to the full compliance by the Customer of the Conditions Precedent to the satisfaction of the Bank.

5.2 Waiver of Conditions Precedent

(a) The Conditions Precedent are inserted for the sole benefit of the Bank and may be waived at the sole and absolute discretion of the Bank in whole or in part with or without terms or conditions and shall be without prejudicing the right of the Bank for insisting on the Customer's compliance in whole or in part with any such waived conditions precedent at any subsequent time in respect of future availability of the Facility.

(b) PROVIDED ALWAYS that notwithstanding the non-fulfillment of any of the conditions precedent set out herein the Bank may, without prejudice to all its rights and remedies hereunder, at its discretion and subject to such conditions as the Bank may deem fit to impose, disburse the Facility or any part thereof.

6. UNDERTAKING TO PAY

The Customer shall pay the Installment Payment (which comprise of the Acquisition Payment and the Rental Payment) in the manner and at the time as set out in this Agreement. The Customer further undertakes to pay any other amount due and payable to the Bank under this Agreement and other Transaction Documents as and when it falls due.

If the Customer fails to pay any Installment Payment on the payment date, the Customer shall make a charitable donation equal to 10% per annum of such overdue Installment Payment. The Customer authorizes the Bank to debit the Customer's account and credit such funds into a charity and welfare account maintained by the Bank and withdrawals from this account shall be made only on the approval of the Bank's Shari'a Supervisory Board.

7. PAYMENT

7.1 Prepayment

The Customer may prepay the Installment Payment subject to the following conditions:

the Bank shall have received from the Customer not less than thirty (30) days prior written notice of its intention to prepay ("Prepayment Notice") specifying the relevant installment to be paid and the date of such payment;

the Prepayment shall only be done on an Installment Payment date;

the Customer has paid in full all other monies due and outstanding to the Bank;

any Prepayment Notice once given shall be irrevocable and the Customer shall pay such amount and, on the date, as specified in such Prepayment Notice;

any prepayment by the Customer must be in amounts equivalent to the Installment Payment due on the Installment Payment Date and Acquisition Payments in at least two (02) immediately following Installment Payments;

7.2 Early Settlement

The Customer may make early settlement to the Bank of the Installment Payment in full, subject to the following conditions:

the Bank shall have received from the Customer not less than thirty (30) Business Days or such other period as may be prescribed by the Bank from time to time, prior written notice of its intention to make early settlement ("Early Settlement Notice") specifying the relevant amount to be paid and the date of such payment. The Bank has the right to determine the Buyout Amount. Save for manifest error, the Bank's calculation of the Buyout Amount shall be final and binding;

the Customer has paid in full all other monies due and outstanding under this Agreement and any Security Documents; and

any Early Settlement Notice once given shall be irrevocable and the Customer shall pay the amount as determined by the Bank on the date specified in such Early Buyout Notice.

7.3 Advance Payment

The Customer may pay the Installment Payment in advance. Any extra payment by the Customer will be treated as advance payment and may be made without the Customer giving any prior notice. The advance payments shall not be utilized towards reducing the Acquisition Payment and no profit or income shall be paid by the Bank for any amount of advance payment received.

7.4 No Re-utilisation on Amount Prepaid

Unless permitted by the Facility Letter, no amount prepaid may be made available for re-drawing or re-utilisation.

8. SECURITY

8.1 Execution of Security Documents

Where applicable, as security for the obligation to pay and timely payment of the Installment Payment, the Customer shall execute or procure the execution of the Security Documents in favour of the Bank in the form and substance acceptable to the Bank.

9. REPRESENTATIONS AND WARRANTIES

9.1 Representations and Warranties of Customer

The Customer acknowledges that the Bank has entered into this Agreement in full reliance of the representations and warranties of the Customer in the following terms:

the Customer is duly incorporated with limited liability and validly existing under the laws of a Country;

(b) the Customer and where applicable, the Security Party each has the power or capacity to execute, deliver and perform the terms of the Transaction Documents;

(c) each of the Transaction Documents constitutes the legal, valid and binding obligations of the Customer and where applicable, the Security Party in accordance with their respective terms;

(d) the execution, delivery and performance of each of the Transaction Documents by the Customer and where applicable, by the Security Party do not and will not violate or contravene the provisions of:

any law, regulation, or any order, or decree of any government authority, agency or court to which any of them is subject; and

any contract of whatever nature, or other undertaking, to which any of them is a party or which are binding upon any of them or any of their assets;

(e) all consents, licenses, approvals, orders or exemptions from of any ministry, agency, department or authority in A Country which are required to be obtained in connection with the execution, delivery, performance, legality or enforceability of the Transaction Documents or any of them have been obtained and are in full force and effect and no further consent, licence, approval, order, exemption is required therefor;

no bankruptcy or winding up proceedings or order have been commenced or entered against the Customer and, where applicable any Security Party;

(g) the Customer and, where applicable, the Security Party is not in default in the payment or performance of any of each of their obligations for financing/borrowed money, or in respect of other liabilities;

(h) there is no material adverse change in the financial conditions of the Customer and, where applicable, each Security Party or other conditions which will materially affect the ability of the Customer and, where applicable, the Security Party to perform the obligations of the Customer or the Security Party under the Transaction Documents or any of them; and

(i) the information furnished by the Customer and, where applicable, each Security Party in connection with the Facility do not contain any untrue statement or omit to state any fact and all expressions of expectation, intention, belief and opinion and all projections contained therein were honestly reasonable grounds after due and careful enquiry.

9.2 Continuing Nature of Representations and Warranties

The representations and warranties set out herein will remain in force and complied with in all material respects so long as any sums remains available for utilization by the Customer or remains payable hereunder and each of the above representations and warranties will be correct and complied with in all material respect on each day on which the Facility is disbursed to or utilized by the Customer.

10. COVENANTS

10.1 Affirmative Covenants

The Customer hereby covenants, agrees and undertakes with the Bank that so long as the Facility and any other obligations under this Agreement remains outstanding:

(a) Authorisations:

maintain in full force and effect all relevant authorisations (governmental and otherwise) and will promptly obtain any further authorisation which may become necessary to enable it to own its assets, carry on its business and perform its obligations under, and any of the transactions contemplated by the Transaction Documents; and

(ii) promptly carry out any registration, filing or notarisation of the Transaction Documents, pay any duty or tax and take any action whatsoever which may be necessary or desirable to ensure the validity or enforceability in A Country of the liabilities and obligations of the Customer or the rights of the Bank under the Transaction Documents in accordance with their terms;

Shariah compliant purposes: utilise the Facility for purposes that are in compliance with Shariah;

(c) Information: furnish to the Bank all such information as the Bank shall reasonably request concerning the use of the Facility and the business, operations and financial condition of the Customer;

(d) Consent: obtain or make provisions satisfactory to the Bank to obtain the governmental, corporate, creditors or other necessary licenses, approvals and consents for the financing hereunder and the due observance and performance of all its obligation and covenants hereunder;

Performance of Obligations:
the Customer shall:

inform the Bank of any legal proceedings, claims, or litigation involving the Customer;

punctually pay all his indebtedness when due and owing;

perform all his other obligations under the Transaction Documents.

(f) Termination Event: forthwith notify the Bank if becomes aware of the occurrence of any Termination Event, and will provide the Bank with full details of any steps which the Customer is taking in order to remedy or mitigate the effect of such Termination Event;

(g) Ranking: ensure that its liabilities under the Security Documents to which it is a party rank at least equally and rateably (paripassu) in point of priority and security with all its other liabilities (both actual and contingent) except;

liabilities which are subject to liens or rights of set off arising in the normal course of trading and the aggregate amount of which is not material;

liabilities which are preferred solely by laws of A Country and not by reason of any security Interest; and

any security interest created which is disclosed to the Bank prior to the date hereof.

Adverse Changes: promptly notify
the Bank of:

any material event or adverse change in the condition (financial or otherwise) of the Customer;

any litigation or other proceedings of any nature whatsoever being threatened or initiated against the Customer before any court tribunal or administrative agency which may have a Material Adverse Effect;

any dispute between the Customer and any government or statutory body in respect of the subject matter of the Security Interests under the Security Documents; and

all such notification to be given to the Bank not later than ten (10) Business Days after the Customer has knowledge of the change or of the litigation or other proceedings or threat thereof or dispute and the amount of any contingent liability if such amount is ascertainable;

(i) No Default: ensure that no default under any agreement or arrangement expressly referred to in this Agreement shall have happened and be continuing and which might

adversely affect the Customer's ability from performing the obligations under this Agreement and the Transaction Documents;

(j) Satisfactory Account: operate an active and satisfactory account and observe the approved limits of the Facility at all times; and

Taxes and Outgoings: comply with all applicable laws and regulations and will punctually pay and discharge all taxes, rates, outgoings, assessments and governmental charges or levies imposed on it or on its income or profits or any of its assets or properties prior to or on the due dates and deliver certified true copies of the relevant receipts to the Bank promptly on receipt of such receipts, unless such obligations are being contested in good faith and by proper proceedings as provided by law;

10.2 Negative Covenants

The Customer hereby covenants, agrees and undertakes with the Bank that so long as the Facility or any obligation of the Customer under this Agreement remains outstanding, that the Customer shall not, without prior consent in writing from the Bank being first had and obtained:

(a) Indebtedness: incur, create, assume, guarantee or permit to exist or guarantee any indebtedness for financing/borrowed monies other than,

(i) the indebtedness created pursuant to this Agreement; or

(ii) any other indebtedness disclosed which has been disclosed by the Customer and approved by the Bank prior to the date of this Agreement;

Security Interests: create or permit to exist over all or any part of its business or assets or undertakings any Security Interest other than those permitted under the Transaction Documents;

(c) Termination: terminate or seek to terminate, commit or threaten to commit a breach, amend vary, modify, supplement, novate, restate or replace or grant any waiver in respect of any of the provision of:

the Transaction Documents; or

any other agreement or instruments and arrangements entered into in connection with or in pursuance of this Agreement.

11. CHANGES IN CIRCUMSTANCES

11.1 Illegality

(A) FOR ASSET UNDER CONSTRUCTION

Where any one or more of the following occur –

- (a) the introduction, imposition or variation of any law, order, rule, regulation or decree; or
- (b) any change in the interpretation or application any law, order, rule, regulation or decree; or
- (c) any compliance with any directive or guideline, from the Central Bank or other federal fiscal authority,

makes it unlawful or impractical without breaching any such law, order, rule, regulation or decree, for the Bank to fund or give effect to its obligations under this Agreement, then –

- (i) the Bank's obligation (if any) in respect of any future availability of the Facility shall forthwith be terminated and the Facility shall be cancelled to such extent;
- (ii) the Customer shall upon being so notified, be obliged to pay to the Bank the Buyout Amount on such date as the Bank shall certify to be necessary to comply with the relevant law; and
- (iii) the Bank shall have right to exercise the Purchase Undertaking in the manner therein contained.

(B) FOR COMPLETED ASSET

Where any one or more of the following occur –

the introduction, imposition or variation of any law, order, rule, regulation or decree; or

any change in the interpretation or application any law, order, rule, regulation or decree; or

any compliance with any directive or guideline from the Central Bank or other federal fiscal authority,

makes it unlawful or impractical without breaching any such law, order, rule, regulation or decree, for the Bank to fund or give effect to its obligations under this Agreement, then-

- (a) the Bank's obligation (if any) in respect of any future availability of the Facility shall forthwith be terminated and the Facility shall be cancelled to such extent;

(b) the Bank's obligation to continue to provide leasing over the Asset upon taking effect of such events described in sub-clauses (a), (b) or (c) above shall be extinguished;

the Customer shall upon being so notified, be obliged to pay to the Bank the Buyout Amount and includes any other amount due and payable under the Facility on such date as the Bank shall certify to be necessary to comply with the relevant law; and

(d) the Bank shall have right to exercise the Purchase Undertaking in the manner therein contained.

11.3 Notification

Any notification by the Bank concerning any of the matters referred to in Clause 11.1 above shall, save for any manifest error be conclusive and binding on the Customer.

12. TERMINATION EVENTS

12.1 Default

If any of the following events shall occur,

Non-payment: the Customer fails to pay the Installment Payment due from under this Agreement on its due date, whether formally demanded or not; or

Non-payment of other amounts under Facility: the Customer fails to pay any amount due under the Facility (other than such amount specified in Clause 12.1(a)) on the due date or, if so payable, on demand and such failure to pay is not remedied within fourteen (14) days from the date such amount is due or demanded; or

Breach of terms: the Customer fails to observe or perform its obligations under the Facility and the Transaction Documents related thereto other than an obligation of the type referred to in paragraphs (a) and (b) above and in the case of a failure which in the opinion of the Bank is capable of being remedied, the Customer does not remedy the failure within a period of thirty (30) days after the Customer became aware or having been notified by the Bank of the failure; or

Execution: an encumbrancer takes possession, or a trustee, receiver, receiver and manager or similar officer is appointed in respect of the Asset, or distress, legal processor any form of execution is levied or enforced against the Asset; or

Judgments entered: one or more judgements or decrees shall be entered or passed against the Customer by any court of competent jurisdiction and such judgements or decrees shall not have been discharged or stayed or no appeal against such judgment being filed in any

appropriate appellate court within the time prescribed by law or if appeal has been filed, such appeal being dismissed; or

Bankruptcy: any step is taken or a petition for bankruptcy or winding up is presented against the Customer and the Customer has not taken any action in good faith to set aside such petition within thirty (30) days (or within such time as permitted by law) from the date of service of such petition being made against the Customer; or

Incorrect representation and warranty: any representation or warranty made or deemed made by the Customer under this Agreement or which is contained in any certificate, document or financial or other statement furnished at any time pursuant to the terms of this Agreement prove to have been incorrect in any material respect on or as of the date made or deemed made; or

Notice to Comply: The Customer fails to comply with any notice given hereunder and under the other Security Documents requiring him to remedy any breach of the terms of this Agreement or the other Security Documents within the time stipulated therein; or

Indebtedness: any other indebtedness of the Customer becomes, or becomes capable in accordance with the relevant terms thereof of being declared due prematurely by reason of a default by the Customer in his obligations with respect to the same, or the Customer fails to make any payment in respect thereof on the due date for payment or upon the security for any such indebtedness becoming enforceable; or

Cross Default: the Customer commits a default of any provision of any agreement, or security documents, or both (as the case may be) or fails to pay any amount due to the Bank or to any institutions within the Bank's Group of Companies relating to other accounts or facilities granted by the Bank or any institutions within the Bank's Group of Companies to the Customer or the Customer commits a default of any provision of any agreement, or security documents in which the Customer is a guarantor or security provider; or

Validity of Security Documents: the Security Documents or any of them shall be challenged with regard to its validity by any person or if the Bank shall be of the opinion that the Security created pursuant to the Security Documents is in jeopardy; or

Failure related to Takaful: The Customer fails to effect, maintain or renew any Takaful cover as required to be effected, maintained or renewed by the Customer; or

Creditors: the Customer shall make an assignment for the benefit of the creditors of the Customer or enter into an arrangement for composition for the benefit of the creditors of the Customer or allows any judgement against the Customer to remain unsatisfied for a period of fourteen (14) days or more; or

Legal Proceedings: legal proceedings suit or action of any kind whatsoever (whether criminal or civil) be instituted or commenced or threatened to be commenced against the Customer:

then at once or at any time thereafter the Bank may at its sole discretion, by notice to the Customer declare that Termination Event shall have occurred whereupon notwithstanding anything to the contrary provided in this Agreement:

the Customer shall be obligated to pay the Buyout Amount or any part thereof remain outstanding; and

the Customer shall purchase the balance of the Bank's Initial Ownership Share pursuant to the Purchase Undertaking.

For the purpose of this clause, each of the above paragraphs is to be construed independently and no one Termination Event limits the generality of any other Termination Event.

12.2 Enforcement of Security

At any time after the declaration of the Termination Event, the Bank shall be entitled (but not obligated) to enforce its remedies under this Agreement and the Security Documents.

12.3 Concurrent Remedy

Notwithstanding any provision hereof, it is hereby expressly agreed that upon declaration of any Termination Event, the Bank shall thereafter have the right to exercise all or any of the remedies available under this Agreement and any security documents or by law statute or otherwise and shall be entitled to exercise such remedies concurrently, including pursuing all remedies available under and pursuant to the security documents and/or Transaction Documents and/or civil suit and/or pursuant to any statute or otherwise to recover amount due and owing by the Customer to the Bank. In the event the Bank does not wish to exercise such remedies concurrently the Bank shall be entitled at its discretion to institute civil suits against the Customer or any party providing security to recover all monies outstanding or to dispose of or realise any security herein provided.

13. PROCEEDS

13.1 Application of Proceeds

If after the security created hereunder becomes enforceable or upon a declaration of the Termination Event, all monies received by the Bank from any proceeding instituted or step taken under any of the Security Documents shall (subject to the payment of debts which by law have priority, if any), be applied by the Bank:

firstly, towards payment of all costs charges and expenses incurred and payments made by the Bank under the provisions of all or any of the Security Documents;

secondly, towards payment to the Bank of the Buyout Amount or any part thereof remaining unpaid including any late payment compensation charges;

thirdly, towards payment to the Bank of all other monies due and remaining unpaid under the Security Documents or any related documents; and

fourthly, any surplus shall be paid to such persons entitled thereto.

13.2 Deficiency in Proceeds

Without prejudice to the rights of the Bank under this Agreement, if the amount realised by the Bank on the sale or application of the properties or assets under the Security Interests to the Bank pursuant to Clause 13.1 hereof, after deduction and payment from such sale of all fees, costs, charges and other outgoing arising out of such realisation is less than the amount due to the Bank and whether at such sale the Bank is the purchaser thereof or otherwise, the Customer shall on demand pay to the Bank, the difference between the amount due to the Bank and the amount so realised. Until the payment of such differential amount is made, the Customer shall pay late payment compensation charges on the differential sum from the date it is due until the date of actual payment made. The late payment compensation charges will be channelled by the Bank to charity.

14. STATEMENT OF ACCOUNT

A statement of account in writing stating the amount payable by the Customer under the Facility and/or under the Transaction Documents and indication as to how such amount has been calculated and duly certified by any authorised officer of the Bank shall in the absence of manifest error be conclusive evidence that such amount is in fact due and payable by the Customer including for the purpose of legal proceedings.

15. PAYMENTS

15.1 Payment Clear From Deduction

All payments to be made under the respective Transaction Documents shall be calculated and be made without (and free and clear of any deduction for) set-off or counterclaim and in immediately available and transferable funds for value on the due date thereof.

15.2 Withholding

All payments by the Customer under the Transaction Documents shall be made in full without any deduction or withholding (whether in respect of set off, counterclaim, duties, taxes,

charges or otherwise whatsoever) unless the deduction or withholding is required by law, in which event the Customer shall:

(a) ensure that the deduction or withholding does not exceed the minimum amount legally required;

forthwith pay to the Bank such additional amount so that the net amount received by the Bank will equal the full amount which would have been received by it had no such deduction or withholding been made;

pay to the relevant taxation or other authorities within the period for payment permitted by applicable law the full amount of the deduction or withholding (including, but without prejudice to the generality of the foregoing, the full amount of any deduction or withholding from any additional amount paid pursuant to this clause); and

furnish to the Bank, within the period for payment permitted by the applicable law, either:

(i) an official receipt of the relevant taxation authorities in respect of all amounts so deducted or withheld as aforesaid; or

if such receipts are not issued by the relevant taxation authorities on payments to them of amounts so deducted or withheld, a certificate of deduction or equivalent evidence of the relevant deduction or withholding.

16. INDEMNITY

16.1 Indemnity

The Customer shall at all times fully indemnify and keep the Bank indemnified against all and any action, proceeding, claim, expense, loss, damage or liability which the Bank may incur as a consequence of or arising from or connected to the negligence in Customer's control, possession or use of the Asset, including but not limited to any damage or injury to persons or property and the costs and liabilities arising from such claims.

The Customer shall at all times fully indemnify and keep the Bank including any of its agents, employees or representatives indemnified against any action, proceeding, claim, expense, loss, damage or liability (as to the amount of which a certificate of the Bank, shall in the absence of manifest error, be conclusive and binding upon the Customer) which the Bank may incur as a consequence of any Termination Event or otherwise in connection with this Agreement or the Transaction Documents or other related documents unless such expense, loss, damage or liability is attributable to the default, negligence or fraud of the Bank.

Any certificate issued by the Bank in connection with the above shall, in the absence of manifest error, be conclusive.

Without prejudice to its generality, the foregoing indemnity shall extend to any expenses, fees (including legal fees on solicitors and client basis) or other sums whatsoever paid or payable in connection with the enforcement of any of the rights of the Bank under this Agreement and the Security Documents.

16.2 Indemnities Separate

The foregoing indemnities shall constitute obligations of the Customer, separate and independent from its other obligations under this Agreement, and shall give rise to separate and independent causes of action against the Customer.

17. EXPENSES

17.1 Expenses

In entering into this Agreement, the Customer agrees to pay:

to the Bank all expenses, in each case on the basis of a full indemnity, (including legal and out-of-pocket expenses) incurred by the Bank in connection with the negotiation, preparation or completion of the Transaction Documents and any related documents;

any expenses covenanted to be paid by the Customer under this Agreement which are paid by the Bank on behalf of the Customer and form part of the indebtedness herein; and

if any amount due under the Transaction Documents shall be required to be recovered through any process of law, or if such amount due or any part thereof shall be placed in the hands of solicitors for collection (in addition to the monies then due and payable hereunder) the Bank's solicitors' fees and any other fees and expenses incurred in respect of such collection and where applicable, the account of the Customer shall be debited accordingly.

17.2 Stamp duty

In entering into this Agreement, the Customer agrees to pay all stamp, documentary and other similar duties and taxes to which this Agreement, the Transaction Documents or any related documents may be subject.

18. ASSIGNMENT AND TRANSFER

18.1 Benefit of Agreement

The Bank shall be entitled after giving due notice to the Customer, to assign its rights under this Agreement or any part thereof and/or transfer its obligations under this Agreement or any part thereof, and

(i) for this purpose may disclose to a potential assignee or transferee or any other person who derives or may derive rights or obligations under or by reference to this Agreement such information about the Customer as shall have been made available to the Bank; and

(ii) where the Bank transfers its obligations or any part thereof, the Customer shall execute such documents as are reasonably necessary to release the Bank to the extent of the transfer and join the transferee as a party hereto.

All costs and expenses incurred by the Bank and/or the assignee/transferee pursuant to or incidental to such assignment/transfer which arises from breach by the Customer or the Security Party of the term of the Facility or upon occurrence of the Termination Events, shall be borne by the Customer.

All costs and expenses incurred by the Bank and/or the assignee/transferee pursuant to or incidental to such assignment/transfer which do not arise from breach by the Customer or the Security Party of the term of the Facility, shall be borne by the Bank.

18.2 No Assignment or Transfer by Customer

The Customer may not assign or transfer any of its rights and/or transfer any of its obligations under this Agreement and/or under the Transaction Documents to which it is a party or any part thereof without the prior written consent of the Bank.

19. FURTHER PROVISIONS

19.1 Reconstruction

The liabilities or obligations created under the Transaction Documents shall continue to be valid and binding for all purposes whatsoever notwithstanding any change by amalgamation reconstruction or otherwise which may be made in the constitution of the Bank and similarly the liabilities or obligations created by the Transaction Documents shall continue to be valid and binding for all purposes whatsoever notwithstanding any change by amalgamation reconstruction or otherwise howsoever in the constitution of the Customer or any party providing security and it is expressly declared that no change in any manner or of any sort whatsoever in relation to or affecting the Customer or the party providing security shall in any way affect the security liabilities or obligations created hereunder in relation to any transaction whatsoever whether past present or future.

19.2 Rights cumulative, waivers

(a) The rights of the Bank under this Agreement are cumulative, may be exercised as often as the Bank consider it reasonably appropriate and are in addition to the Bank's other rights under any applicable law.

(b) The rights of the Bank in relation to the Facility (whether arising under this Agreement or under any applicable law) shall not be capable of being waived or varied otherwise than by an express waiver or variation in writing.

No failure or delay in exercising nor any omission to exercise any rights power privilege or remedy accruing to the Bank under this Agreement or any Transaction Documents in favour of the Bank upon any breach of the Customer shall impair any such right power privilege or remedy or be construed as a waiver thereof or any acquiescence in any breach, nor shall any action by the Bank in respect of any default or any acquiescence in any breach, affect or impair any such right, power privilege or remedy of the Bank in respect of any other or subsequent breach.

19.3 Notices

Any notice or communication under or in connection with this Agreement shall be in writing and shall be delivered personally, or by post or facsimile to the addresses set out in this Agreement or at such other address as the recipient may have notified to the other Party hereto in writing. Proof of posting or despatch of any notice or communication shall be deemed to be proof of receipt:

if it is personally delivered, at the time of delivery and duly acknowledged;

in the case of a letter sent by post, on the third (3rd) Business Day after posting;

in the case of telex or cable, on the Business Day immediately after transmission;

in the case of a facsimile, on the Business Day immediately after transmission provided that the sender has received an answer back confirmation and has sent a copy by post confirming the facsimile transmission.

19.4 Severability

Any term, condition, stipulation, provision, covenant or undertaking contained herein which is illegal prohibited or unenforceable in any jurisdiction shall, as to such jurisdiction, be ineffective to the extent of such illegality, prohibition or unenforceability without invalidating the remaining provisions hereof and any such illegality, prohibition or unenforceability in any jurisdiction shall not invalidate or render illegal, void or unenforceable any such term, condition, stipulation or undertaking in any other jurisdiction.

19.5 Variation of terms

The provisions and terms of this Agreement may at any time be varied or amended by means of letters or such other means as the parties may mutually agree and thereupon such amendments and variations shall be deemed to have been amended or varied accordingly and shall be read and construed as if such amendments and variations have been incorporated in and had formed part of this Agreement at the time of execution hereof.

19.6 Disclosure of information

The Customer hereby agrees and permits the Bank to disclose any information relating to the Customer, the Facility and the Transaction Documents to:

the Central Bank or such other authority having jurisdiction over the Bank;

any party (including professional advisers and debt collection agent) pursuant to any enforcement, preservation and/or attempted enforcement or preservation of this Agreement;

any party providing security or any surety; or

any party or authority, if required by any law, regulation or by-law or pursuant to any order from any court of competent jurisdiction.

The Customer hereby expressly consents to such disclosure and hereby confirms and declares that no further consent from the Customer is necessary or required in relation thereto.

19.7 Central Bank

The Facility shall be at all times governed by such rules, regulations or directives issued or imposed upon the Bank from time to time by the Central Bank of A Country or any other authority having jurisdiction over the Bank.

19.8 Terms of Facility Letter Incorporated

All the terms and conditions stated in the Facility Letter are taken to be incorporated into this Agreement and shall form integral parts thereof.

(b) If there is any conflict or discrepancy between the provisions of this Agreement and the terms and conditions of the Facility Letter, the provisions of this Agreement shall prevail for the purposes of interpretation and enforcement of this Agreement.

19.9 Right of Set-Off

The Customer hereby agrees that the Bank may at anytimeafter the Termination Event, notwithstanding any settlement of account or other matter whatsoever, combine or consolidate all or any of the then existing accounts of the Customer in credit including accounts in the name of the Customer or of the Customer jointly with others (whether current, deposit,financing or any other nature whatsoever, and whether in A Countryi Riyal or in any other currency) and thereafter set-off or transfer any sum standing to the credit of any such accounts in or towards satisfaction of any monies obligations and liabilities of the Customer to the Bank hereunder. Where such combination, set-off or transfer requires the conversion of one currency into another such conversion shall be calculated at the then prevailing spot rate of exchange of the Bank (as conclusively determined by the Bank) for purchasing the currency for which the Customer is liable with the existing currency so converted.

19.10 Additional Terms and Conditions

The Facility hereby granted shall be further subject to additional terms and conditions as set out in Schedule 3 hereto (if any).

19.11 Time

Time shall be the essence of this Agreement.

19.12 Successors Bound

This Agreement binds the parties hereto and their respective successors in title and permitted assigns.

20. GOVERNING LAW

This Agreement is governed by and shall be construed in accordance with the laws of A Country and the parties hereto agree to submit to the jurisdiction of the Courts in the ABC Country.

[End of Clauses]

EXECUTION PAGE OFMASTER DIMINISHING MUSHARAKAH AGREEMENT:

IN WITNESS WHEREOF the Parties hereto have executed this Agreement on the day and year first above written.

For the Bank

Signed for and on behalf of)
ABC ISLAMIC
(ABC Bank)

by its lawful attorney in the presence of:

For the Customer

Signed by the authorised signatory
for and on behalf of the CUSTOMER
in the presence of:

ATTACHMENT A: MUSHARAKAH CONTRACT

DATED:

THIS MUSHARAKAH CONTRACT is made between the following parties:

(1) ABC Islamic Banking ABC a banking company incorporated under the laws of the ABC Country ("Bank") of the first part;

AND

(2) THE CUSTOMER whose name and particulars described in Item 1 of Schedule 1 hereto ("Customer") of the second part.

A-1. PURCHASE, ACQUISITION AND CONSTRUCTION OF ASSETS

(a) At the request of the Customer, the parties hereby agree as follows:

(i) If at the time of execution of this Agreement, the Customer has entered into a sale and purchase agreement to acquire the Asset from the Seller, the Bank agrees to jointly purchase rights, interests and benefits in the Asset with the Customer up to the Bank's Initial Acquisition Payment to facilitate the acquisition of the Asset from the Vendor; or

(ii) If at the time of execution of this Agreement, the Customer is the legal owner of the Asset and the Customer intends to get financing for the Purpose, the Bank agrees to acquire from the Customer the rights, interest and benefits in the Asset for the consideration of up to the Bank's Initial Acquisition Payment by executing a sale agreement with the Customer and making the payment as per the Customer's instructions.

(iii) If at the time of execution of this Agreement the Asset needs to be constructed, the Bank and the Customer agree to get the Asset constructed jointly in the agreed ownership shares.

(b) For the purpose of sub-clause (a)(i) above, the Customer hereby agrees and acknowledges that he has entered into the sale and purchase agreement as the nominee of the Bank in relation to the Bank's rights, interest and benefits in the Asset.

A-2. CO-OWNERSHIP

In case the Asset needs to be purchased:

(i) Subject to the terms of this Agreement, the Parties hereto agree to acquire the Asset as co-owners.

(ii) For the above purpose, the Customer contributes the Customer's Initial Acquisition Payment, which shall represent the Customer's Initial Ownership Share in the ownership share in the Asset.

(iii) The Bank contributes the remaining of the acquisition payment amount of up to the Bank's Initial Acquisition Payment, which shall represent such percentage in the Bank's Initial Ownership Share in the Asset.

(iv) The Customer shall execute the sale agreement with the seller on behalf of the Musharakah Partners and submit the same to the Bank immediately.

In case the Asset needs to be constructed:

(i) Subject to the terms of this Agreement, the Parties hereto agree to get the Asset(s) constructed jointly in the agreed Ownership Shares.

(ii) For the above purpose, the Customer shall contribute the Customer's Initial Acquisition Payment in stages on the dates and the amount mentioned in the Schedule 4 – The Schedule of Stage Payments, which shall represent the Customer's Initial Ownership Share in the ownership share in the Asset being constructed.

(iii) The Bank shall contribute the remaining of the acquisition payment amount of up to the Bank's Initial Acquisition Payment in stages on the dates and the amount mentioned in the Schedule 4 – The Schedule of Stage Payments, which shall represent the Bank's Initial Ownership Share in the ownership share in the Asset being constructed.

(c) In the case of the Asset needs to be constructed, the following provisions will apply:

- (i) The Musharakah Partners hereby appoint and the Customer hereby accepts the appointment to act as the agent on behalf of the Musharakah Partners with all powers and authority to enter into, execute and conclude any contract related to the construction or the Asset ("Construction Contract") with any third party contractor ("Contractor").
- (ii) The Customer as agent, agrees and undertakes to supervise and will exercise the highest standard of diligence and care in monitoring the punctual and due performance by the Contractor of its obligations under the Construction Contract with a view to ensuring that the Asset will be constructed in accordance with the specifications within the time and for the price stipulated in this the Construction Contract.
- (iii) Without prejudice to the generality of sub-clause (ii) above, the Customer shall be obliged to:
- (aa) advise the Bank, as soon as reasonably practicable, of any delay or anticipated delay in the completion of the construction of Asset with full details thereof;
- (bb) deal with all regulatory and administrative matters relating to the construction of Asset in accordance with the applicable laws;
- (cc) ensure that the works in the relevant stages have been executed by the Contractor in conformity with the Construction Contract.
- (iv) The Customer shall not, without the prior written consent of the Bank, make any amendments, alterations or modifications of the Construction Contract including but not limited to any amendments, alterations or modifications of the Construction Contract which may,
- (aa) result in an increase in the contract price payable thereunder; or
- (bd) result in an extension of the completion date of Asset; or
- (cc) result in a change of the specification of Asset; or
- (dd) not be in accordance with usual good practice.
- (v) If in breach of this Clause 5, the Customer gives instructions to the Contractor as a result of which there is an increase in the contract price or the Bank becomes liable to any party for any claim, loss, damage or expense then the Customer agrees to bear the increase in the contract price or, as the case may be, to indemnify the Bank for any such claim, loss, damage or expense.
- (vi) It is agreed that the Customer shall provide sufficient number of skilled and qualified personnel as would be necessary to carry out the duties under the Construction Contract.

(vii) The Customer shall take all reasonable actions to protect, preserve and enforce the terms of the Construction Contract including to initiate legal actions against the Contractor without having the need to make the Bank as a party in the said action or legal proceedings.

(viii) The Customer shall indemnify and keep the Bank fully indemnified from any costs, expenses, losses or damages that may arise from the breach of the Contractor under the Construction Contract or from the actions or legal proceedings that the Customer may initiate against the Contractor, if such costs, expenses, losses or damages are due to or arising from the Customer's action, misconduct or negligence.

A-3. UNDERTAKING TO ACQUIRE THE BANK'S OWNERSHIP SHARE

(a) Pursuant to the Purchase Undertaking, the Customer undertakes to acquire the Bank's ownership share in the Asset by making Acquisition Payments promptly during the Co-ownership Period upon the terms of this Agreement as set out herein.

(b) The ownership share in relation to each Acquisition Payment made by the Customer is transferred from the Bank into the Customer from time to time in proportion with each payment of the Acquisition Payment made by the Customer to the Bank.

A-4. RIGHTS IN ASSET

A-4.1 Rights of Customer

Except as otherwise agreed in the Agreement, the Parties agree that the Customer shall have the following rights in respect of the Asset;

(a) to occupy, use and quiet enjoyment of the Asset; and

to purchase the ownership rights of the Bank in the Asset at any time at the Buyout Amount subject to the terms of this Agreement.

A-4.2 Rights of Bank

Except as otherwise agreed in the Agreement, the Parties agree that, the Bank shall have the following rights in respect of the Asset,

(a) the right of entry or re-entry for the purpose of inspection of the Asset, upon proper and reasonable notice to the Customer;

- (b) the right to cure any defects affecting the Asset subject to the giving of reasonable notice to the Customer (but shall not at any time impose any obligation upon the Bank to cure or rectify such defects);
- (c) the right to receive notice and at its discretion, give (or refuse) consent to any further creation of Security Interests over the Asset (except for the creation of Security Interests to secure the Installment Payment under this Agreement which the Bank hereby expressly gives its consent);
- (d) the right to approve any significant improvements to the Asset (but such right shall not impose any obligation upon the Bank to make or pay for such improvements).

A-5. EARLY ACQUISITION

Save as otherwise provided in the Master Diminishing Musharakah Agreement, the Customer may on any Installment Payment date specified in Schedule 4 hereto and prior to maturity of the Co-ownership Tenure, make a prepayment by way of making an early acquisition payment to the Bank to acquire the Bank's ownership share in the Asset in whole or in part subject to the terms as set out in the Master Diminishing Musharakah Agreement and the terms and conditions as determined by the Bank.

A-6. CHANGE IN OWNERSHIP POSITION

- (a) The Parties acknowledge that as a result of the Acquisition Payment under the Installment Payment made or to be made by the Customer under this Agreement, the Customer's ownership share in the Asset will increase and the Bank's ownership share will decrease proportionately.
- (b) The Parties acknowledge that the ownership rights, interest and benefits of the Bank in the Asset shall at all times be governed and reflected by way of contract only pursuant to the terms of this Agreement.
- (c) As and from the date of this Agreement and pursuant to the terms of the Declaration of Trust, the Customer declares that the Customer shall at all times, hold that portion of rights and interest in the Asset in trust for the Bank in respect of the portion of rights and interest in the Asset that the Customer does not yet own at any time during the Co-Ownership Period.
- (d) Upon full and final payment of the Installment Payment, the Bank will notify the Customer that the Customer has become the sole owner of the Asset.

[End of clauses of this ATTACHMENT A]

EXECUTION PAGE OF MUSHARAKAH CONTRACT:

IN WITNESS WHEREOF the Parties hereto have executed this Musharakah Contract on the day and year first above written.

For the Bank

Signed for and on behalf of
ABC ISLAMIC
(ABC Bank)

by its lawful attorney in the presence of:

For the Customer

Signed by the authorized signatory
for and on behalf of the CUSTOMER
in the presence of:)
ATTACHMENT B: IJARAH CONTRACT
DATED:

THIS IJARAH CONTRACT is made between the following parties:

(1) ABC Islamic Banking ABC a banking company incorporated under the laws of the ABC Country (“Bank”) of the first part;

AND

(2) THE CUSTOMER whose name and particulars described in Item 1 of Schedule 1 hereto (“Customer”) of the second part.

B-1. LEASE OF ASSET

(a) At the request of the Customer, the Bank hereby leases and the Customer hereby takes on lease of the Asset (in such portion corresponding with the Bank’s Ownership Share) for consideration of Rental Payment subject to the terms of this IjarahContract.

(b) The Customer acknowledges that the lease of the Asset is on an “as is where is” basis and that the Bank does not make nor is deemed to have made any representation or warranties as to the title, value, condition or otherwise whatsoever (including without limitation, any statutory warranty or condition under the laws of the ABC Country).

(c) If at the time of execution, the Asset is not ready for use or occupation by the Customer, the parties agree that this IjarahContract, shall for all intent and purpose, be deemed as an agreement by the Customer to lease the Asset in advance from the Bank.

(d) Immediately upon the Asset is ready for use or occupation by the Customer, the parties agree that agreement to lease pursuant to Clause B-1(c) shall be replaced with and superseded by this Ijarah Contract.

B-2. RENTAL PAYMENT (IJARAH COMPONENT)

The Rental Payment shall consist of:

(i) the Variable Element Payment (as defined in Clause 1.1 of the Master Diminishing Musharakah Agreement); and

B-3. UNDERTAKING TO PAY RENTAL PAYMENT

The Customer hereby undertakes and agrees to promptly pay the Rental Payment in the manner as set out in the Agreement.

If Clause B-1(c) applies, the Rental Payment payable by the Customer under this Part D shall, for all intent and purpose, be considered as payment of advance rental based on the Shariah principle of IjarahMawsufah Fi Zimmah.

If the Asset cannot be occupied due to the construction of the Asset is abandoned which cannot be revived, the advance rental as referred to in Clause E-3(b) as duly paid by the Customer, will be refunded to the Customer in the manner as determined by the Bank.

B-4. COVENANT BY CUSTOMER

The Customer being lessee under this Ijarah Agreement hereby covenants that throughout the Ijarah Tenure:

(a) it shall observe and comply with and shall cause to be observed and complied with the provisions of any written law with which it may be required to comply for the operation and use of the leased Asset;

(b) it shall upon receipt of any notice, order or direction from any appropriate authority affecting or which may adversely affect the leased Asset or the use thereof, forthwith deliver to the Bank a copy of such notice, order or direction and shall forthwith comply with such order, notice or direction;

(c) it shall at its own expenses make any modifications, alterations or improvements to the leased Asset so long as such modifications do not adversely affect the useful life and value of

the leased Asset and are carried out in accordance with all applicable law, and shall also make such modifications that are required by any appropriate authority;

(d) upon the expiry of the Ijarah Tenure, it shall yield up possession of the Asset;

(e) it shall notify the Bank of the occurrence of any Ijarah Default or any event which with the giving of notice, lapse of time or fulfillment of any condition would be likely to become a Termination Event as soon as it becomes aware of it;

(f) it shall not create or attempt to create any Security Interests over the Asset or attempt to assign, sell, transfer or dispose of in any way, the legal and/or any other title to the Asset; and

keep the Asset free from distress or execution or any other legal process and shall inform the Bank immediately if the Asset is the subject matter of any litigation, legal execution, distress or lien by any person and shall bear all costs and expenses (including legal costs on a full indemnify basis) to have the Asset released therefrom.

B-5. TERMINATION EVENTS

The Customer hereby agrees and acknowledges that upon declaration of Termination Event by the Bank under the Master Diminishing Musharakah Agreement, the Bank shall have the right to exercise any or all of its rights under this Agreement and the Security Documents including but not limited to terminate the lease arrangement under this Ijarah Contract and to require the Customer to purchase the Asset pursuant to the terms of the Master Diminishing Musharakah Agreement.

B-6. SUB-LEASE

Subject to the terms of the Master Diminishing Musharakah Agreement and any other terms and conditions as imposed by the Bank from time to time, the Customer is permitted to sub-lease the Asset to any other party acceptable to the Bank. Any rental under the said sub-leasing may be received by the Customer so long the Customer is not in breach to any terms and conditions of the Master Diminishing Musharakah Agreement.

B-7. REVIEW AND VARIATION OF RENTAL PAYMENT

The Customer hereby agrees that the Bank shall have the right to review and/or vary the Rental Payment annually, or at such other interval as set out in the Facility Letter, in the manner as

determined by the Bank subject to a floor of 1% below the agreed rate in the Facility Letter and a ceiling of 10% above the agreed rate in the Facility Letter. Any variation to the Rental Payment shall be advised by the Bank by way of notification in writing and shall take effect from the effective date as set out in the said notification.

[End of clause of this ATTACHMENT B]

PAGE OF IJARAH CONTRACT:

IN WITNESS WHEREOF the Parties hereto have executed this Ijarah Contract on the day and year first above written.

For the Bank

Signed for and on behalf of
ABC ISLAMIC
(ABC Bank)

by its lawful attorney in the presence of:

For the Customer

Signed by the authorized signatory
for and on behalf of the CUSTOMER
in the presence of:
ATTACHMENT C: DECLARATION OF TRUST
DATED:

THIS DECLARATION OF TRUST is made between the following parties:

(1) ABC Islamic Banking ABC a banking company incorporated under the laws of the ABC Country (“Bank”) of the first part;

AND

(2) THE CUSTOMER whose name and particulars described in Item 1 of Schedule 1 hereto (“Customer”) of the second part.

C-1. DECLARATION OF TRUST

(a) The Customer hereby acknowledges the co-ownership arrangement with the Bank pursuant to the Shariah concept of Musharakah Mutanaqisah give rise to the Bank becoming the co-owner of the Asset together with the Customer.

(b) The Customer hereby declares that the Customer shall at all times holds the portion of the ownership share and rights in the Asset that the Customer does not own at any time during the Co-Ownership Period, in trust for the Bank subject to the terms of the Master Diminishing Musharakah Agreement and this Declaration of Trust.

ATTACHMENT D: SERVICE AGENCY CONTRACT

DATED:

THIS SERVICE AGENCY CONTRACT is made between the following parties:

(1) ABC Islamic Banking ABC a banking company incorporated under the laws of the ABC Country (“Bank”) of the first part;

AND

(2) THE CUSTOMER whose name and particulars described in Item 1 of Schedule 1 hereto (“Customer”) of the second part.

D-1. Appointment of Service Agent

The Bank as the co-owner of the Asset hereby appoints the Customer to be its service agent in respect of the Asset and the Customer hereby accepts such appointment on the terms and conditions set out herein.

D-2. Duties of Service Agent

In consideration of the Bank entering into the Ijarah Contract with the Customer, the Customer hereby agrees and undertakes with the Bank that throughout the Ijarah Tenure, the Customer shall carry out the following duties and functions for and on behalf of the Bank:

- (a) the Customer shall be responsible for and shall carry out all major maintenance and structural repairs whenever required on the Asset;
- (b) the Customer shall be responsible for and shall attend to pay all outgoing, quit rents, assessment bill, other bills issued from the relevant authority from time to time;
- (c) the Customer shall be responsible for insuring or causing to be covered/insured and at all times throughout the Ijarah Tenure keeping covered/insured or causing to be kept covered/insured the Asset under a Takaful policy taken out in the name of the Bank (and with the Bank named as beneficiary and loss payee) against any loss or damage to such Asset caused by such perils as are normally covered/insured against in accordance with prudent industry practice including the Takaful as stated under Clause D-9 below. The Customer shall if requested, immediately upon obtaining or renewing such Takaful, furnish the Bank with a copy of the relevant policy and contribution (premium) receipt. The proceeds from the said Takaful policy shall be applied in the manner as stated under Clause D-9.2 herein or any other manner acceptable to the Bank; and

(d) upon receipt of any notice, order or direction from any appropriate authority affecting or which may affect the Asset or the use thereof, the Customer shall forthwith deliver to the Bank a copy of such notice, order or direction or the statute, regulation or other instrument under or by virtue of which it is issued.

D-3. Ownership Expenses

D-3.1 Payment of Ownership Expenses

The Bank and the Customer agree that the expenses incurred or to be incurred pursuant to in Clause D-2(a), (b) and (c) shall, for the purpose of this Agreement be referred to as ownership expenses (“Ownership Expenses”) and shall be borne proportionately as between the Bank and the Customer based on their respective prevailing ownership share.

D-3.2 Advance and Set Off

(a) At all times during the tenure of this Service Agency Contract, the Customer shall pay his portion of Ownership Expenses as well as Bank’s portion of the Ownership Expenses.

(b) Subject always to sub-Clause (c) below, the Bank will reimburse the Customer (in his capacity as Service Agent), the Bank’s portion of Ownership Expenses amount on the final Installment Payment date.

(c) If the Customer fails to notify the Bank’s portion of the Ownership Expenses at least ten (10) Business Days prior to the final Installment Payment date or the early settlement date or on the date of termination notice issued to the Customer as the case may be, the Customer agrees and confirms that, and the Bank shall have the right to consider that the Customer is willing to bear the Bank’s portion of the Ownership Expenses and consequently, the obligation of the Bank to bear the Bank’s portion of the Ownership Expenses is extinguished.

(d) The Bank will reimburse by way of setting off the Bank’s portion of the Ownership Expenses from the last Acquisition Payment.

D-4. Ijarah Contract

The Customer hereby agrees and acknowledges that its obligations as service agent as set out under Clause D-2 above shall be in addition to and shall not in any way prejudice or derogate from its obligations as a lessee under the Ijarah Contract.

D-5. Retirement or Removal of Service Agent

(a) The Customer shall continue as service agent of the Bank for the entire duration of the Ijarah Contract and shall not be entitled to resign or retire as a service agent, save and except with the prior written consent of the Bank.

(b) Upon termination of the Ijarah Contract, this Service Agency Contract shall be deemed to have been terminated and the service agency of the Customer shall forthwith come to an end and neither party shall have any further rights or obligations in respect of each other save and except for antecedent breaches.

D-6. Covenant

The Customer hereby covenants to the Bank as follows:

(a) it shall carry out its duties under this Service Agency Contract with all due skill, care and attention and shall owe to the Bank all such fiduciary duties as the law or equity may impose upon an agent to his principal:

(b) notwithstanding the agency set out in this Service Agency Contract, the Customer shall not be entitled to, nor incur any liability on behalf of the Bank or bind the Bank to any obligation in respect of which it has not expressly consented to in writing; and

c) that it shall obtain and keep in force all consents, authorization, licences and exemptions required by it or the rendering of the services required of it under this Service Agency Contract and otherwise for the observance and performance of its obligations under this Service Agency Contract.

D-7. Indemnity

The Customer hereby agrees to indemnify and hold harmless the Bank from and against all losses, damage, costs, expenses and liabilities as may be incurred or suffered by the Bank as a result of any breach or non-performance by the Customer of its obligations hereunder.

D-8. Payment of Taxes

D-8.1 Obligation

(a) Since the Customer has or having the exclusive right to occupy, possess, use and enjoy the Asset, it is the intention of the Parties that the Customer shall solely have the tax benefits as well as obligations related to the Asset.

(b) Under the Musharakah Contract, the Customer hereby agrees to bear and pay any taxes related to or associated with the Asset and shall enjoy and be entitled to the right to claim any tax benefit, credit or deduction for the payment of such sums or other items related to or associated with the Asset. The Customer agrees that notwithstanding the Customer being the co-owner of the Asset until the end of the Co-ownership Period under this Agreement, the Customer shall pay the whole one hundred percent (100%) of the amount of all taxes due in relation to or associated with the Asset (including but not limited to any taxes on the gains upon disposal of the Asset).

D-9. Takaful

D-9.1 Obtaining and Maintaining Takaful

(a) In consideration of the Bank giving and/or agreeing to give to the Customer the exclusive right to occupy, possess, use and enjoy the Asset, the Customer shall obtain and maintain Takaful coverage of not less than the outstanding Bank's ownership share or financing amount or for such amount as may be acceptable to the Bank on the Asset against all insurable risks including but not limited to, loss or damage by fire, explosion, lightning, tempest, flood, riot, cyclones, civil commotion, strike and malicious acts and other risks as the Bank may require. The Customer shall, if permitted, name the Bank as an additional covered/insured in the Takaful policy and any renewals thereof or if not permitted, to include the Bank as financier and/or loss payee.

(b) The Bank shall have the right but not obligated to increase the Takaful coverage amount on the Asset. In the event that the Bank is of the view that the coverage taken by the Customer is insufficient, all cost and expenses incurred by the Bank in increasing the coverage including any payment of contribution (premium) shall be for the account of the Customer and shall on demand, reimbursed by the Customer to the Bank.

(c) Whenever required by the Bank, the Customer shall take and maintain a Takaful mortgage reducing term Takaful/life Takaful policy or a mortgage decreasing term policy as the Bank may in its absolute discretion decide or any other policy guaranteeing the payment of the Buyout Amount.

(d) The Customer may or if requested, shall provide the Bank with the original Takaful policies, all receipts of paid contribution (premium) and any renewal certificates.

D-9.2 Takaful Proceeds

(a) The Customer hereby agrees to assign and shall continue to assign all rights to the Takaful proceeds to the Bank.

(b) In the event of loss, any proceeds under the Takaful policy may at the Bank's discretion, be applied towards restoration or repair of the Asset to its original state, if such repair and restoration is, in the opinion of the Bank, economically feasible.

(c) If the repair and restoration is, in the opinion of the Bank not economically feasible, in the event of Total Loss, the Takaful proceeds may at the Bank's discretion, be distributed between the Bank and the Customer proportionately. Any deficiency shall be borne by the Bank and the Customer proportionately.

[End of clause of this PART D]

EXECUTION PAGE OF SERVICE AGENCY CONTRACT:

IN WITNESS WHEREOF the Parties hereto have executed this Service Agency Contract on the day and year first above written.

For the Bank

Signed for and on behalf of)
ABC ISLAMIC
(ABC Bank))

by its lawful attorney in the presence of:
For the Customer

Signed by the authorized signatory
for and on behalf of the CUSTOMER
in the presence of:

ATTACHMENT E: PURCHASE UNDERTAKING

DATED:

TO:

ABC Islamic Banking ABC
[ADDRESS]

RECITALS:

(A) Pursuant to the Master Diminishing Musharakah Agreement dated the day and year as set out in Item 2 of the Appendix hereto (“Master Diminishing Musharakah Agreement”) made between us particularly as stated in Item 1 of the Appendix hereto (“Customer”) and the Bank, the Bank has, at our the request, agreed to make available the Diminishing Musharakah Facility of up to the amount as set out in Item 3 of the Appendix hereto (“Facility”) subject to the terms and conditions therein contained.

(B) As a term of the Facility, we (in our capacity as the Customer) and the Bank have entered into the Musharakah Contract whereby the Bank has, at my/our request, contributed or shall contribute payment towards the co-ownership of the Asset with us, up to the Bank’s Initial Ownership Share upon the terms and conditions therein contained.

(C) As agreed by us under the Musharakah Contract, we have agreed to grant an undertaking within the terms and contents as herein contained.

NOW IT IS HEREBY AGREED as follows:

E-1. Incorporated Definition

In this Purchase Undertaking, terms defined in the Master Diminishing Musharakah Agreement shall, unless otherwise defined herein, have the same meaning when used herein.

E-2. Purchase Undertaking

In consideration of the Bank having agreed to grant the Facility to us, we hereby irrevocably undertake to acquire the units representing Bank's ownership share in the Asset on the Installment Dates and at the price equal to value of units mentioned in the Installment Schedule.

In case of last Installment Payment we undertake to purchase the Bank's remaining ownership share at the price equal to value mentioned in the Installment Schedule plus the Bank's share in Ownership Expenses that the Service Agent advises you ten (10) Business Days prior to the last Installment Date.

We also undertake to purchase the Bank's complete remaining outstanding ownership share if any of the following events shall occur:

- (i) upon maturity or early settlement of the Facility;
- (ii) upon occurrence of the Termination Event;
- (iii) upon the occurrence of matters set out in Clause 11.1 [Illegality] of the Master Diminishing Musharakah Agreement.

for the consideration of the Buyout Amount. The Buyout Amount shall be calculated as follows:

$$A + B + C + (A \times 1\%)$$

Where:

A = Value of Bank's outstanding share.

B = Value of Bank's share in Ownership Expenses

C = Any other amount payable by the Customer

E-3. Terms of Master Diminishing Musharakah Agreement Incorporated

All the terms and conditions stated in the Master Diminishing Musharakah Agreement are taken to be incorporated into this Purchase Undertaking and shall form integral parts thereof. In the event of any conflict or discrepancy between the provisions of this Purchase Undertaking and the terms and conditions of the Master Diminishing Musharakah Agreement, the provisions of this Purchase Undertaking shall prevail for the purposes of interpretation and enforcement of this Purchase Undertaking.

E-4. Governing law

This Purchase Undertaking is governed by and shall be construed in accordance with the laws of A Country and we hereby agree to submit to the jurisdiction of the Courts in the ABC Country.

E-5. Successors bound

This Purchase Undertaking shall be binding upon my/our successors-in-title and on the successors-in-title and assigns of the Bank.

[End of Clauses of ATTACHMENT E)

Appendix 5: Diminishing Musharaka Matrix Risk

	Stage	Risk matrix	Evaluation of risk	Stage of agreement.	Inherent risks
1	Pre-contract procedures	Ensure that the place of participation (real estate or land) is valued by an external valuer.	Medium	Initial oversight	Legality of the sequence, parties' independence, and contracts
2		Ensure that the sales contract includes the correct data: contract date, seller's name, sale value, sales description data and parties' signatures (bank and seller).	High	Procedures and Performance	Legality of the sequence, parties' independence and contracts
3	Conclusion of the participation contract	Ensure that the bank has calculated the administrative fees on the customer according to the fees approved by the Shariah supervisory body.	Hight	Automated system	Legality of revenue and expenses
		Ensure that the promise of purchasing shares from the bank before or by the date of the participating contract includes the following: the contract statements are correct; the project is	Medium	Procedures and Performance	The legality of the document

		accurately stated, with its total value and the value of the bank's share; the value of the sale is clear the number and dates of the payments are specified; and the signatures of the parties are taken			
		Ensure that the participation contract includes all the correct data: date; name and data of the partner; property data; duration of participation; value of the participating capital each party's shares; and the signatures of the parties (lessor and lessee).	High	Procedures and Performance	The legality of the document
		Verification of the bank's eligibility mechanism for participation quotas, whether by selling or leasing shares, and the bank deducts funds from the customer until after signing the sale or lease contract and that the premium is deducted in accordance with the dates stated in the contract.	High	Procedures and Performance	Legality of the sequence, parties' independence, and contracts
		Ensure that the quota lease is concluded at the same time or after the diminished participation contract; that the project description data is correct; and the number of instalments, the value	High	Procedures and Performance	Legality of the sequence, parties' independence and contracts

		of each instalment, and the date of the first and last instalment are all specified.			
		Ensure that the contract for the sale of shares is concluded at the end of the term or at early payment, and that the bank sells all shares.	High	Procedures and Performance	Legality of the sequence, parties' independence and contracts
		Ensure that the contract of sale of shares at the same time or after the contract of diminished participation, includes correct description data; that the value of the sale of shares is higher than the value of the bank's shares in the participation; and ascertain the number of instalments, the value of each instalment, and the date of the first and last instalment.	High	Procedures and Performance	Legality of the revenue and expense
		Ensure that the participant (customer) has not signed a sale contract and a lease of shares for the same participation on the same date in all shares.	High		Legality of the revenue and expense

		Ascertain the schedule of instalments by considering: the dates of maturity of the monthly instalment; the value of the instalment; its compatibility with the quota lease; the value of the monthly remuneration or the value of the monthly quota ownership; and the contract of sale of shares.	High		Legality of the document
		Ensure that the bank adheres to the timeline of the transaction according to the legitimate controls.	High	Procedures and Performance	Legality of the sequence, parties' independence, and contracts
		Ensure automation systems are designed to comply with Shariah	High	Procedures and Performance	Legality of the sequence, parties' independence, and contracts
		Ensure that the data and signatures in the forms and contracts are met and are approved by the Shari 'a Supervisory Board.	High	automated system	Legality of the document
4	Guarantees	Ensure that the bank has taken sufficient guarantees from the customer such as registration of the property, mortgage, deposit, etc.	Medium	Procedures and Performance	Legality of the guarantee

5	Avoidance/ modification of participation contract	In cases of dissolution of the participation, ensure that there is a letter signed by the customer requesting the avoidance, together with the signature of the bank	Medium	Procedures and Performance	Legality of the document
		If the contract of sale or lease of shares is amended to change the price or duration, it must be ascertained that there is an attachment to the contract of sale or lease signed by both parties, and a notice signed by the bank so stipulating.	High	Procedures and Performance	Legality of the document
6	Deferral of instalments	Ensure that the bank does not calculate an additional amount on the deferral fee of instalments approved by the Shari 'a watchdog, that the customer signed an application form of postponement, and the bank prints a new instalment schedule.	High	Procedures and Performance	Legality of revenue and expenses
7	Early settlement	Ensure that the bank deposits the customer's benefits from his or her insurance in a symbiotic manner in the event of early payment of the transaction, if the insurance is internal.	High	Procedures and Performance	Legality of revenue and expenses
		Ensure that the bank has not calculated additional fees or profits on schedule at early payment.	High	Procedures and Performance	Legality of revenue and expenses

Appendix 6: Interview guide

Dear Respondent,

*My name is Layla Dowaishan, and I'm a Master's student in Islamic banking and finance at the University of Bahrain. I need your support to perform my study in **Challenges in the Application of Partnership Contracts in Islamic Banks: A Theoretical Analytical Study**, and your insights are valuable to us. We'll be focusing on the challenges and reasons that limit the use of Musharaka contracts in Islamic banks, and your perspectives will help us to understand the main challenges of Musharaka contracts. The results and recommendations of this study will and should help us to find a possible solution to limit these challenges.*

Name:

Gender:

Position:

No. of years served in the Islamic Banking Industry:

1. Are you satisfied with the present position of Musharaka contract in Islamic Financing? هل أنت راضٍ عن الوضع الحالي لعقد المشاركة في إجمالي التمويل الإسلامي؟
2. What are the internal constraints that limit the size of financing by a partnership (Musharaka contract) in your opinion? ماهي العوامل الداخلية التي تعرقل من استخدام عقد المشاركة؟
3. What are the external constraints that limit the size of financing by a partnership (Musharaka contract) in your opinion? ماهي العوامل الخارجية التي تعرقل من استخدام عقد المشاركة؟
4. How do these challenges compare to those faced in assets-based contracts (debt contracts such as Murabaha/Tawarruq/Ijarah)? كيف تقارن هذه التحديات التي تواجه عقد (Murabaha/Tawarruq/Ijarah) مع تلك التي تواجه عقود الأصول؟

المشاركة بتلك التي تواجه العقود القائمة على الأصول (عقود الديون)
مثل المراجعة/الإجارة؟

5. How could Musharakah contracts be improved to better serve the interests of banks and customers? كيف يمكن تحسين عقود المشاركة لخدمة مصالح البنوك والعملاء بشكل أفضل؟

Maqasid Al-shariah

Q1: In your opinion does Islamic banks operate according to the principle of profit and loss sharing or on the principle of debt? في رأيك هل تعمل المصارف الإسلامية وفقاً لمبدأ تقاسم الأرباح والخسائر أو على أساس مبدأ الدين؟

Q2: Do existing contracts in Islamic banks already fulfill the purpose of Maqasid al Shariah? هل عقود المشاركة القائمة في المصارف الإسلامية تحقق الغرض من مقاصد الشريعة؟

Q3: In your opinion, which contract assists in achieving Maqasid al-shariah more: equity-based contracts such as Musharaka, Mudarabah, etc. (عقود المشاركات) or assets-based contracts such as Murabaha and Ijrah (عقود المداينات) And why? في رأيك، أي من العقود تساهم في تحقيق مقاصد الشريعة بقدر أكبر العقود القائمة على المشاركات ام العقود القائمة على المداينات ولماذا؟

خلاصة

الهدف: تهدف هذه الدراسة إلى بيان التحديات المرتبطة بتطبيق عقد المشاركة في البنوك الإسلامية في مملكة البحرين، وباستكشاف مدى تحقيق عقد المشاركة والبنوك الإسلامية بمقاصد الشريعة. كما عرضت هذه الدراسة تطبيقات عقد المشاركة في باكستان وفي سلطنة عمان.

الطرق: باستخدام البحث النوعي، تم إجراء مقابلات مع ١٠ أشخاص من الخبراء المختصين بالشريعة الإسلامية ومنهم موظفون البنوك الإسلامية الذين يخدمون في البنك أكثر من ١٥ سنة، كما أجريت مقابلات مع المختصين بالمخاطر الذين لديهم الإلمام الكافي بمعنى وهيكل عقد المشاركة. تم استخدام برنامج انفيو لتحليل البيانات التي تم جمعها.

النتائج: أظهرت النتائج بأن أسباب ندرة تطبيق العقد ترجع إلى - صعوبة العقد في التنفيذ لما يتطلبه من مراجعة دوريه وارتباطه بمخاطر عالية بالنسبة للعقود الأخرى، - القوانين والأنظمة، - قلة وعي الموظفين والأفراد في المجتمع بعقد المشاركة. وكما أظهرت النتائج بأن عقد المشاركة القائم على مبدأ الربح والخسارة يحقق الغرض ومبادئ مقاصد الشريعة بصورة أكبر من العقود الأخرى.

القيمة: تساهم النتائج الحالية صاحبين القرار والسياسات في النظر ومعرفة التحديات التي تؤول البنوك الإسلامية في مملكة البحرين إلى ندرة استخدام عقد المشاركة، وتسهل لوضعي القرارات والسياسات النظر إلى النتائج المقدمة في هذه الأطروحة.

الكلمات المفتاحية: البنوك الإسلامية، المشاركة، المشاركة المتناقصة، مقاصد الشريعة، تحديات عقد المشاركة.

جامعة البحرين



قسم الصيرفة الإسلامية

كلية ادارة الاعمال

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أطروحة مقدمة كجزء من متطلبات الحصول على درجة الماجستير في الصيرفة والتمويل الإسلامي

اعداد

ليلى عيسى دويشان

٢٠١٦٤٧١٦

اشراف

د. مهدي ميلي

أستاذ مشارك

جامعة البحرين

مملكة البحرين

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