

# Shariah Advisor's Report - 2013

الحمد لله رب العالمين، و الصلاة و السلام  
على خاتم الأنبياء والمرسلين، محمد المصطفى  
الأمين، وعلى آله وأصحابه أجمعين، وبعد:

By the Grace of Allah, the year under review was the twelfth year of Islamic commercial banking for Meezan Bank Limited. During this year, the Bank developed and executed a variety of new as well as established Islamic banking products and transactions after due approval from the Shariah Supervisory Board and/or Shariah Advisor. During the year, the Shariah Supervisory Board (SSB) of Meezan Bank held one meeting to review various products, concepts, transactions, processes and their Shariah-compliance, referred to them by the Shariah Advisor.

As part of the Shariah-compliance framework a full fledged Product Development & Shariah Compliance (PDSC) department is working under my supervision. The role of this function is facilitating new research & product development activities, refining existing products & procedures, providing Islamic banking training, conducting Shariah audit & compliance reviews of branches and departments, coordinating with the Bank's Shariah Supervisory Board and providing Islamic Financial Advisory services to both local and foreign institutions.

Following were the major developments that took place during the year:

## Research & New Product Development

Alhamdulillah, during the year, the Bank was able to develop and successfully launch various innovative products and structures, adding value to the Islamic financial products palette of the Bank.

An innovative Shariah compliant product, based on Wakalah for handling Foreign Currency Close out cases was developed. The product enables to provide Shariah compliant solution to a global problem being faced by Islamic financial industry.

As an alternate to the conventional 'repo' transactions, the Bank has developed and executed secured interbank placement transactions as a solution for managing liquidity.

Keeping in view the Bank's increasing focus on 'Shirkatul Aqd' based financing an exclusive short term Musharakah based product was developed for Al Meezan Investment Management Ltd (AMIM). Furthermore, 'Running Musharakah' product saw a continuous rise with several blue chip companies opting for financing through this mode.

In addition to the above, short term Musharakah Sukuk were developed by the Bank for the power producer LALPIR Power in addition to the previously developed Sukuk for the power generation sector for KAPCO and HUBCO.

A unique Wakalah pool based solution for Mudarabah

companies having Shariah-compliant investment was also developed. Apart from this, structured solutions were developed for different blue chip corporate clients.

It is pertinent to mention here that the Bank has also suggested several Shariah-compliant mechanisms for providing funding to deserving candidates under Prime Minister's Youth Financing Scheme. Alongside this, as members of the Steering committee for the promotion of Islamic banking and finance created by the Finance Minister, we are actively contributing the committee with our Vision of establishing Islamic banking as banking of first choice.

Meezan Kafalah is another addition to the innovative deposit products menu of Meezan Bank. The product is an alternative to conventional 'Banca assurance' and has initially been offered to internal customers and the roll out is expected in the first quarter of 2014, Insha,,Allah.

## Training & Development

During the year 114 Islamic banking training sessions were held in which 4,207 employees participated throughout Pakistan, as compared to 3,314 employees who participated in 109 Islamic banking trainings last year.

Meezan Bank conducted 39 seminars and workshops in 12 cities of the country and also in 3 different countries of the world which were attended by more than 2,500 participants representing customers, general public and professionals.

The Bank also launched the 7th batch of Islamic Banking Certification Course Level 1 and has also completed 2nd batch of Islamic Banking Certification Course Level 2; an advanced-level certification program designed to enhance the Islamic banking expertise of the Bank's employees. Besides this, the Bank also conducted comprehensive advanced-level 6-day Islamic banking courses for Branch Managers, Operation Managers and senior front-end employees at Islamabad, Karachi and Lahore Regions. Deposit Refreshers and new deposit product-specific training sessions were also held on regular basis throughout the year. In addition, 'Kafalah' trainings were also conducted during the year, at pan Pakistan level.

## Shariah Advisory

Alhamdulillah, on the Islamic financial advisory side the Bank continued its expansion both locally and internationally by sharing its expertise, knowledge, experience and the success story of Meezan Bank Limited with its clientele.

In the international arena, the Bank inked an agreement with Ethical Finance Ltd. (EFL) for establishing first retail Islamic bank in the Republic of Mauritius by providing Shariah Technical Services & Support in the areas of Islamic banking product development, Shariah controls, training and other related services. The Bank signed another milestone agreement with Temenos Headquarters SA, Switzerland, for providing Shariah Technical Services & Support including certification of banking software in compliance with recognized Shariah standards like AAOIFI etc.



In the area of Islamic capital markets, the Bank continued to advise all major Islamic mutual funds mainly comprising of those offered by Al-Meezan Investment Management Limited (AMIM) and NBP Fullerton Asset Management Limited (NAFA), regarding establishment & launch of various types of Shariah-compliant Mutual Funds. During the year, the Bank facilitated AMIM and NAFA for the launch of different funds under the category of Capital Preservation & Pension funds. Furthermore, the Bank facilitated AMIM in successful conversion of its Balanced Fund from closed-end to open-end.

During the year, the advisory team conducted a customized workshop on Islamic banking concepts for technical and business consultants of National Data Consultants (Pvt) Ltd., a local partner of Temenos headquarters. The Bank also continued to provide advisory services for Islamic consumer sales product to United Sales (Pvt.) Ltd. (USL), a subsidiary of Dawlance group under the umbrella of Diyanat financing.

As a learning, development and capacity building initiative, the Bank introduced an Islamic banking certification course from the platform of International Institute of Islamic Bankers.

Meezan Bank, being the major player in the establishment of KMI-30 Index (KSE Meezan Islamic Index) which is Pakistan's first ever Shariah-compliant Islamic Index, continued to advise Karachi Stock Exchange (KSE) regarding matters related to re-composition of the KMI-30 Index.

### Review of Assets

The Bank primarily used Murabaha, Ijarah, Diminishing Musharakah, Musawammah, Istisna, Tijarah, Musharakah and Salam for its financing activities during the year.

It is encouraging to note that the Bank has moved towards diversification in the usage of various financing products and has reduced the reliance on Murabaha, as is evident from the Bank's financing portfolio. In this context the share of Istisna increased to 20%, share of Musharakah & Running Musharakah has increased significantly to 8%, while the share of Diminishing Musharakah, Murabaha & Ijarah remained at 29%, 28% & 7% of the total financing portfolio. The Bank's total financing portfolio reached Rs. 133.5 billion (gross) as of December 31, 2013. All these transactions were executed using Shariah-compliant financing agreements.

Financing Modes	2012	2013	Growth/(Decline)
Diminishing M u s h a r a k a h	33%	29%	( 4 % )
<b>Murabaha</b>	31%	28%	( 3 % )
Istisna	18%	20%	2 %
<b>Musharakah &amp; Running</b>	1%	8%	7 % <b>Musharakah</b>
Ijarah	8%	7%	( 1 % )
<b>Salam</b>	1%	4%	3 %
Tijarah	4%	2%	( 2 % )

### Review of Liabilities

On the liability side, the Bank offered different Shariah-compliant deposit products based on the mode of 'Mudarabah' & 'Qard'. Total deposits of the Bank increased by 26% and reached a sum of Rs.289.8 billion as at December 31, 2013. During the year, the Bank accepted deposits on the mode of Musharakah for short-term liquidity management from inter-bank market and corporate clients.

Throughout the year, the process of allocation of assets and funds to various deposit pools; announcement of overall profit sharing ratios for Mudarabah-based deposits; monthly allocation of weightages and distribution of income to deposit accounts was monitored and reviewed in accordance with Shariah rules and principles.

### Shariah Audit & Compliance Reviews

The Shariah Audit function plays a vital role in achieving the objective of ensuring Shariah compliance by evaluating the adherence to Shariah guidelines in each and every activity undertaken by the Bank. The Shariah Audit function keeps a continuous check on all activities starting right from the time of opening of a branch and goes hand in hand at each step of product offering till the stage of final profit distribution to the customers.

Shariah Audit of 287 branches and departments was conducted as a part of the Bank's efforts to strengthen the internal Shariah controls mechanism. These audits not only cover the transactions that the branches/departments undertake but also include an evaluation of the Shariah knowledge of staff.

On the financing side, the Bank's PDSC team makes extra efforts to understand the customer's business model before approving or renewing any facility. Frequent customer meetings, factory visits and reviews of business processes and transactions are undertaken to ensure that the facility being offered to the customer is delivered through a process that ensures compliance with Islamic Shariah. Shariah Audit of the process of profit distribution to depositors is also conducted periodically to ensure adherence to Shariah guidelines.

During the year, credit approvals, restructuring of financing facilities, customer-specific transaction process flows, text of LGs and security documents were reviewed to ensure Shariah compliance while offering financing products to the customers.

As a part of its ongoing activities, the PDSC department approved more than 1000 product structures and process flows for its clients. Moreover, random physical inspections and concrete measures were taken to verify the purchase evidences and invoices of financing transactions, thus further improving the quality of internal controls. In Istisna and Tijarah transactions, existence of goods was ensured by conducting 100% physical inspections at the time of taking delivery of the goods.

It is a matter of concern that during the year 2013, direct payments for Murabaha financing to Corporate and



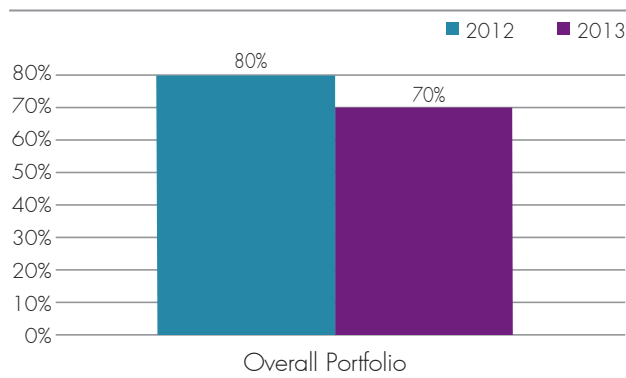
SME/commercial customers dropped from 80% to 70%, a decrease of 10%. It is highly recommended that concrete efforts should be made in order to increase the percentage of direct payment in Murabaha transactions. However, in terms of cases disbursed under Murabaha, the overall number of direct payment Murabaha transactions has increased.

#### Summary of Direct Payment in Murabaha Financing for Meezan Bank

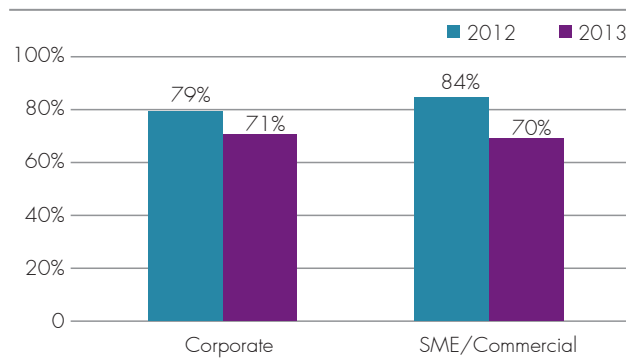
Murabaha Financing Direct Payment	2012	2013	Growth/Decline
Overall Portfolio	80%	70%	(10%)
Customer Wise Segregation			
Corporate	79%	71%	(8%)
SME/Commercial	84%	70%	(14%)

(The percentages above are rounded off)

#### Overall Direct Murabahah Financing Year-wise Trends in %



#### Customer-wise Segregation Year-wise Trends in %



In addition to the above-mentioned compliance measures, Shariah audit & compliance review of 287 branches and departments was conducted during the year to gain firsthand understanding of the activities being carried out at the branches and departments.

An exercise of gauging the basic understanding of the staff about the structures and concepts of Islamic banking & finance was also conducted by way of interviews and on the spot training sessions were conducted to address any shortcomings identified during the course of such reviews.

The audit covered overall Shariah-compliance of the Bank's operations and their alignment with the guidelines given by Shariah Advisor and the SSB. In the process, following areas were looked into:

- Suppliers' existence was confirmed by visiting the suppliers' premises on sample basis
- Cross verification of Murabaha transactions with customers' record was done to ensure that the transactional documents represented actual occurrence of events on ground
- Genuine purchase evidences were obtained to execute Murabaha transactions to ensure that Murabaha disbursements are not availed to set off previous balances with the supplier
- Agreements for Murabaha, Ijarah, Diminishing Musharakah, Istisna, Tijarah and Bai Salam were reviewed
- Declarations, description of assets, relevant purchase invoices, sequence and order of the documents and time difference between purchases and declaration in Murabaha were reviewed to obviate the possibility of fictitious transactions
- Murabaha Monitoring Sheets (MMS) and Delayed Declaration Reports (DDR)
- Purchase deeds, treatment of ownership related cost & recovery of rentals in Ijarah transactions
- Ownership ratio in Diminishing Musharakah for housing and issuance of timely unit sale receipts
- Investment made in stock with reference to the stock screening criteria
- Import finance transactions and related documentation
- Extensive reviews of client payment, purchase cycle and periodic assessment of client's processes
- Other related documents and procedures followed by different functional areas
- Profit-sharing ratio, profit weightages, pool working, asset & deposit allocation for deposit products

#### Murabaha Monitoring System

A system for continuous monitoring of Murabaha transactions is in place whereby the branches extending Murabaha financing are required to submit a monthly reporting sheet, after thorough review by the branch/departmental management, to PDSC for review and continuous monitoring of Murabaha transactions to avoid any mistakes/errors.

#### Charity

During the year, an amount of Rs. 57.4 million was transferred to the Charity Payable Account, this includes Rs. 30.08 million to eliminate the non-compliant income portion identified during Shariah audit, Rs 3.38 million to purify the dividend income earned from the investment made in the Shariah-compliant stocks by the Bank and Rs. 23.91 million transferred to charity payable account, in the normal course of business, on account of non-timely payments by customers in various financial transactions. Moreover, an amount of Rs. 98.3 million was disbursed from the Charity Account after approval of the Shariah Advisor. Details of Charity are available in note # 18.4.

#### Recommendation

Based on the review of various transactions and operations of the Bank, I recommend that:





- The Bank should evaluate the possibility of offering its products, services and network in the international market so as to make other people benefit from Islamic banking.
- The Bank's IT system must be strengthened to facilitate internal as well as external customers. In this regard, asset side product modules should be given immediate priority.
- With the expansion in size and reach, the Bank should explore the possibility of offering unconventional Islamic banking services which may include the development of warehouses and showrooms for trading purpose.
- The Bank should focus on new innovations and explore the possibility of entering into more specialized Shariah-compliant financing modes such as Microfinance, Shariah-compliant private equity and venture capital.
- Due care regarding the mindset and commitment towards the cause of Islamic banking should be taken during the process of hiring of new staff. Moreover, it is recommended to increase the scope of Islamic banking knowledge assessment process already implemented for new Branch and Operations Managers to Area Managers, department heads and new joiners at senior level.
- The Bank should continue its policy of expansion to spread Islamic banking and in this regard continue its focus on employees' training related to Islamic banking products and services offered by the Bank with specific focus on front line staff.

### Conclusion

As per the charter of the Bank, it is mandatory on the management and employees to ensure application of Shariah principles and guidelines issued by the Shariah Supervisory Board and Shariah Advisor and to ensure Shariah-compliance in all activities of the Bank. The prime responsibility for ensuring Shariah-compliance of the Bank's operations thus lies with the management.

Based on the extensive reviews of sample cases for each class of transaction, related documentation, processes, profit distribution mechanism for the depositors and management's representation made in this regard, in our opinion, the affairs, activities and transactions, performed by the Bank during the year comply with the rules & principles of Islamic Shariah in light of the guidelines and directives given by the Shariah Supervisory Board, Shariah Advisor of Meezan Bank and SBP guidelines related to Shariah-compliance. The non-compliant income identified during the review is being transferred to the Charity Account.

May Allah bless us with the best Tawfeeq to accomplish His cherished tasks, make us successful in this world and in the Hereafter, and forgive our mistakes.

Wassalam Alaikum Wa Rahmat Allah Wa Barakatuh.

**Dr. Muhammad Imran Usmani**  
Member Shariah Supervisory Board & Shariah Advisor

Dated: 26th Rabi ul Awal 1435 H/January 28, 2014

### تجاویز

متعدد و متنوعہ کا جائزہ لینے کی بنیاد پر ہمیں درج ذیل امور تجویز کرتا ہوں:

- بینک کو اپنی سروسز اور پروڈکٹس بین الاقوامی سطح پر کسٹمرز کی ترجیحات کو ملحوظ رکھتے ہوئے آفر کرنے کے لیے تجویز کرنا چاہیے۔
- بینک کے IT سسٹم میں مزید تقویت آجانی چاہئے، اس سلسلے میں اندرونی اور بیرونی کسٹمرز کی ضروریات کی تکمیل اور Assetside پر ہونے والی سرمایہ کاری کے طریقہ کار کی طرف خصوصی توجہ کی جائے۔
- بینک کی ترقی اور منڈی ورک کے پھیلاؤ کو دیکھتے ہوئے اب اس بات پر غور کرنا چاہیے کہ جو معاملات مروجہ سودی بینکاری میں رائج ہیں اور اب تک ان کا شرعی متبادل تیار نہیں کیا گیا ہے ان کا متبادل تیار کیا جائے اور تجارتی مقاصد کیلئے شروع یا گودام وغیرہ قائم کئے جائیں تاکہ تجارتی سرگرمیاں بڑھ سکیں۔
- بینک کو یہ چاہیے کہ نئی سہولیات پر مستقل غور کرتا رہے اور دیگر شرعی جائزہ موبلی طریقوں کو متعارف کرائے مثال کے طور پر ہانگرو فنانس، شریعہ کمپلائنس پرائیویٹ کیوبینی اور وی ٹیچر کمپنل۔
- نئے ملازمین کو ملازمت فراہم کرتے ہوئے ان میں اسلامی بینکاری کے مقاصد تک پہنچنے کے عزم و ہمت کو خصوصی طور پر مد نظر رکھنا ضروری ہے۔ نیز میزبان بینک میں رفتار کی اسلامی بینکاری سے متعلق معلومات کو جانچنے کے لئے جو نظام رائج ہے اس کے دائرہ کار میں مزید وسعت پیدا کی جائے اور برائے شہر سے لے کر ایریا فیجر اور شعبوں کے سربراہوں تک کی اسلامی بینکاری سے متعلق معلومات کو جانچنے کا ایک نظام ترتیب دیا جائے۔
- بینک کو چاہئے کہ اسلامی بینکاری کی توسیع کے مقصد سے اپنے آپ کو مسلسل وسعت دینے کی پالیسی جاری رکھے اور اس سلسلے میں وہ اپنے ملازمین کی تربیت کی طرف اپنی توجہ مبذول رکھے۔ اسلامی بینکاری کی پروڈکٹس اور بینک کی طرف سے پیش کردہ خدمات کے بارے میں ملازمین (اور خصوصاً فرنٹ آفس کے ملازمین) کا معیار معلومات مزید بڑھانا اور ان کی مزید تربیت کا انتظام کرنا نہایت اہم ہے، بینک کو چاہئے کہ اس جانب اپنی توجہ برقرار رکھے۔

### خلاصہ کلام

بینک کے چارٹر کے تحت تمام انتظامیہ اور ملازمین کے لیے ضروری ہے کہ وہ شریعہ سپروائزر اور شریعہ ایڈوائزر کی طرف سے جاری کردہ بینک کے تمام معاملات سے متعلق ہدایات پر عمل درآمد کو یقینی بنائیں۔ بینک کے معاملات کے شریعت کے مطابق ہونے کی بنیادی ذمہ داری بینک کی انتظامیہ پر عائد ہوتی ہے۔

بینک کی طرف سے انجام کردہ مختلف عقود، ان کے متعلقہ دستاویزات، اس کے طریقہ کار، ڈیپازیشنرز کو تقسیم ہونے والے نفع کا طریقہ کار، اور ان کے متعلق انتظامیہ کی دی گئی رائے کے جائزہ کی بنیاد پر ہماری رائے میں رواں سال میں بینک کی طرف سے کیے گئے عقود اسلامی شریعہ کے ان اصولوں اور ہدایات کے مطابق ہیں جو میزبان بینک کے شریعہ سپروائزر اور شریعہ ایڈوائزر اور اسٹیٹ بینک آف پاکستان کی طرف سے جاری کی گئی ہیں۔ اس جائزہ کے دوران جو غیر شرعی آمدنی پائی گئی وہ چیریٹی میں منتقل کی جا رہی ہے۔

اللہ تعالیٰ سے دعا ہے کہ وہ ہماری رہنمائی ان راہوں کی طرف کرے جو اس کی رضا کا باعث ہوں، ہمیں دنیا اور آخرت میں کامیابیوں سے نوازے اور ہماری غلطیوں اور خطاؤں سے درگزر فرمائے۔ آمین

والسلام علیکم ورحمتہ اللہ وبرکاتہ

ڈاکٹر محمد عمران عثمانی

ممبر شریعہ سپروائزر اور شریعہ ایڈوائزر  
موری ۲۶ ربیع الاول ۱۴۳۵ھ / ۲۸ جنوری ۲۰۱۴ء