Financing of Entrepreneurs in India: a New Dimension under Islamic Finance

Fayaz Ahmad Lone*

College of Business Administration, Prince Sattam Bin Abdulaziz University, Saudi Arabia

Abstract

Financing is one of the basic requirements of a project which Entrepreneur needs to start. Project financing is both for short term and long term. The sources from which the Entrepreneur can meet their financial needs for their project vary from country to country. In some countries, Institutions dealing in providing finance to Entrepreneurs share profits and losses and in some countries (like India) only profits are shared and losses are transferred to entrepreneurs. The former is called Mudarabah financing, which is currently working in more than 300 institutions in the world. Under this type of financing, risk is also shared and not transferred to entrepreneurs. This type of financing has shown tremendous success as far as entrepreneurship is concerned. While taking the pros and cons of this type of financing, the paper provides a comprehensive detail about its prospects and problems, as far as Indian entrepreneurship is concerned. It is explained in the paper how entrepreneurs can be through Islamic finance. As there are six ways for financing the entrepreneurs and all are explained in this paper.

Keywords: Islamic Finance, Entrepreneurship and Islamic Finance, Islamic Business, Indian Entrepreneurship.

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*Correspondence to: Fayaz Ahmad Lone, College of Business Administration, Prince Sattam Bin Abdulaziz University, Saudi Arabia
Email: f.lon@sau.edu.sa; www.wdibf.com
Introduction

Finance plays a key role in the entrepreneurship development. Some financial institutions not only provide finance to entrepreneurs but also extend professional and promotional assistance on an ongoing basis. The sources from which an entrepreneur gets finance in India (shown in figure 1) are usually State Financial Corporations (SFCs), National Small Industries Corporation (NSIC), State Small Industries Corporation (SSICs), State Industrial Development Corporations (CIDCs) in addition to commercial banks and other financial institutions. State Industrial and Investment Corporation of Maharashtra (SICOM), Gujarat Industrial Investment Corporation (GIIC), Cooperative Banks, Entrepreneurs need huge capital in the beginning stage of enterprise, and it is also needed throughout the life of a business. The new entrepreneurs face significant difficulties in acquiring capital at start-up. Before seeking outside financing, an entrepreneur should first explore all methods of internal financing, such as using profits, selling unused assets, reducing working capital, obtaining credit from suppliers, and collecting accounts receivable promptly. After all internal sources have been exhausted; the entrepreneur may find it necessary to seek additional funds through external financing. External financing can be in the form of debt or equity. When considering financing, the entrepreneur needs to consider the length of time, cost, and account of control of each alternative financial arrangement. There are different financing options to Indian entrepreneurs; some of the important options are below mentioned.

Objectives of the study

1. To explain which options of financing are available to entrepreneurs in India
2. To know how Islamic finance is an alternative to financing of entrepreneurs in India
3. To explain different options of Islamic finance for the entrepreneurship development
4. To suggest the measures for introducing this kind of finance in India

Research Methodology

The entire study is based on secondary data. To complete the present study, data has been collected from different sources like magazines, periodicals, journals in addition to number of websites and Islamic banks. Islamic banking and its principles have been thoroughly studied.

Institutions that help Entrepreneurs

(a) National Small Industries Corporation (NSIC), Small Industries Development Organization (SIDO), Khadi and Village Industries Commission (KVIC), Handloom Board, Silk
Board, Commodity Boards etc., have schemes to help SSI units in marketing their products. Some of them also help in promoting exports of goods manufactured by SSI units/Entrepreneurs.

(b) SIDO is one of the important agencies that help SSI units in marketing their products through consultancy, testing and marketing facilities. The SIDO functions as a model agency for formulating, coordinating and monitoring policies and programmes for promotion and development of small-scale industries in the country.

(c) SIDO also promotes ancillary units to public sector enterprises. Besides, many large industrial houses actively pursue the policy of promoting ancillary units for their purchases of stores. SSI units can take advantage of this facility and secure a regular market for their products.

(d) District Industries Centers (DICs) provide marketing and other assistance to SSI units under a single roof.

(e) State-level Small Industries Corporations (SICs) participate in tender programmes of government purchases and then sub-contract these tenders to SSI units.

(f) The Government of India has established trade centers at various places which disseminate information on market potentials and conditions. These centers also organize fairs and exhibitions where SSI units can exhibit and sell their products.

(g) Twenty-seven Small Industry Service Institutes (SISIs) have been set up by SIDO at various places for disseminating market information. Thirty-eight Exchange Centers have also been set up within some SISIs to help units in securing sub-contract jobs.

(h) The SIDO has already set up 31 branch Small Industries Service Institutes, 4 Regional Testing Centers, 3 Process-cum-Product Development Centers and 20 Field Testing Stations to provide a comprehensive range of facilities to small-scale units.


Although such development corporations like the Industrial Development Bank of India (IDBI), the Industrial Finance Corporation of India (IFCI), the Industrial Credit and Investment Corporation of India Ltd. (ICICI), and the Industrial Reconstruction Bank of India (IRBI), Small Industrial Development Bank of India (SIDBI), State Industrial Development Corporations (SIDCs) and State Financial Corporations are basically constituted to provide industrial finance, particularly to medium and large units, their role in assistance is by no means less important. These institutions, together with the Life Insurance Corporation of India (LIC), General Insurance Corporation of India (GIC) and the Unit Trust of India (UTI), play a significant role in the rapid growth of small-scale industry. The emergence of small-scale units on a sizeable scale in the last decade has given a real impetus to the industrialization of underdeveloped areas.

Among the term-lending institutions, financial assistance to small-scale industries is mainly provided by SFCs, SSIDCs, and SIDCs/SIICs and by the IDBI under its refinance of industrial loans and bills rediscounting schemes. Assistance sanctioned and disbursed by these institutions to projects ventured by entrepreneurs are discussed further.

The network of commercial banks, co-operative banks and regional rural banks, SFCs, State Industries Development Corporations (SIDCOs) and National Small Industries Corporation (NSIC) provide the framework for financial assistance to small-scale and medium-scale industries. The Industrial Development Bank-of India (IDBI) provides funds to commercial banks and SFCs through its scheme of refinance of industrial loans and rediscounting of machinery bills. The commercial banks are the main source of short-term loans/advances while SFCs provide long-term loan advances to entrepreneurs. A National Bank for Agriculture and Rural Development (NABARD) has been set up for the supply of credit to entrepreneurs.
in Agriculture and for Small Village and Cottage Industry sector in rural areas.

State Industrial Development Corporations (SIDCs) were set up in the 1960s and 1970s to act as catalytic agents in the industrialization of states. The SIDCs are established as wholly-owned undertakings of the State Governments under the Companies Act, 1956 or as autonomous corporations under specific State Acts. In addition to providing term assistance to industrial projects by way of loans, underwriting and guarantees, the activities of SIDCs also covered promotional functions such as formulation of project ideas through industrial potential surveys, preparation of feasibility reports and selection and training of potential entrepreneurs. Further, activities of SIDCs extended to setting up of industrial project in the medium and large sectors either in the joint sector, i.e., in partnership with private entrepreneurs or as wholly owned subsidiaries, administering incentive schemes of Central/State Governments and providing risk capital to new generation entrepreneurs.

Designed to assist in the development of entrepreneurship constitute an integral part of the national institutional network engaged in extending long-term finance to industrial sectors. Entrepreneur have been playing an effective role for more than three decades in the rapid growth of small and medium scale units and through them have contributed significantly in creating employment opportunities and in achieving wider regional dispersal of industrial development. Despite all these institutions which assist in the development of entrepreneurship, a new method of generating capital from commercial banks is Islamic banking or Islamic finance which works in profit and loss basis.

**Shift towards Islamic finance**

In world different products of Islamic finance are available in more than 75 countries and it is estimated that Islamic banking is USD 500 million as far its market is concerned. These banks provide capital for different types of businesses and thus encourage entrepreneurship to a large extent. Although more than 300 Islamic banks/financial institutions are presently in the competitive market but some countries like India had not started this type of banking due to one or other reasons. In India, this banking can be started only when Reserve Bank of India (RBI) will issue permission for this type of banking and necessary arrangements are being done for the same. There is a misconception among the general public that this banking is only for Muslims which is not true. Now what Islamic banking is and how it works, is briefly explained in this following.

**Principles of an Islamic financial system**

The basic framework for an Islamic financial system is a set of rules and laws, collectively referred to as shariah, governing economic, social, political, and cultural aspects of Islamic societies. Shariah originates from the rules dictated by the Quran (holy book of Islam) and its practices, and explanations rendered (more commonly known as Sunnah) by the Prophet Muhammad. Further elaboration of the rules is provided by scholars in Islamic jurisprudence within the framework of the Duran and Sunnah. The basic principles of an Islamic financial system can be summarized as follows:

**Prohibition of interest.** Prohibition of riba, a term literally meaning “an excess” and interpreted as “any unjustifiable increase of capital whether in loans or sales” is the central tenet of the system. More precisely, any positive, fixed, predetermined rate tied to the maturity and the amount of principal (i.e., guaranteed regardless of the performance of the investment) is considered riba and is prohibited. The general consensus among Islamic scholars is that riba covers not only usury but also the charging of “interest” as widely practiced.

This prohibition is based on arguments of social justice, equality, and property rights. Islam encourages the earning of profits but forbids the charging of interest because profits, determined ex post, symbolize successful entrepreneurship and creation of additional wealth whereas interest, determined ex ante, is a cost that is accrued irrespective of the outcome of business operations and may not create wealth if there are business losses. Social justice demands that borrowers and lenders share rewards as well as losses in an equitable fashion and that the process of wealth accumulation and distribution in the economy
be fair and representative of true productivity.

**Risk sharing.** Because interest is prohibited, suppliers of funds become investors instead of creditors. The provider of financial capital and the entrepreneur share business risks in return for shares of the profits.

**Money as “potential” capital.** Money is treated as “potential” capital—that is, it becomes actual capital only when it joins hands with other resources to undertake a productive activity. Islam recognizes the time value of money, but only when it acts as capital, not when it is “potential” capital.

**Prohibition of speculative behavior.** An Islamic financial system discourages hoarding and prohibits transactions featuring extreme uncertainties, gambling, and risks.

**Sanctity of contracts.** Islam upholds contractual obligations and the disclosure of information as a sacred duty. This feature is intended to reduce the risk of asymmetric information and moral hazard.

**Shariah-approved activities.** Only those business activities that do not violate the rules of shariah qualify for investment. For example, any investment in businesses dealing with alcohol, gambling, and casinos would be prohibited.

How this type of financing, could help to the entrepreneurs in getting easily finance is explained in detail in the following pages.

**Distribution of Profit between Entrepreneur and the Bank**

In studying the principle of division of profit, it should be borne in mind that the conditions of partnership may vary, for example:

1) The entrepreneur may transact the business with capital procured from the bank only, and with no other capital.
2) The entrepreneur may invest his own capital in the business in addition to capital procured from the bank.
3) The entrepreneur may invest personal capital loaned to him otherwise than by the bank.
4) The entrepreneur may invest additional capital from another party on the basis of mudarabah.
5) The entrepreneur may enter into (active) partnership with another entrepreneur whose capital is also invested in the business.
6) All the above conditions may apply at one time, namely, a business in which the personal capital of the entrepreneur, the capital provided by a partner, and the capital provided on the basis of mudarabah, are invested together.

In each of these cases, the capital of the bank has been procured on mudaraba and not on the basis of partnership. In the accounts following, it has been assumed that a sum of Rs. 100,000 has been acquired from the bank on condition that half of the profit earned from it will go to the bank and half to the entrepreneur

1. In situation (1), if there is a profit of Rs. 10,000 a sum of Rs.5,000 will be paid to the entrepreneur, and the remaining Rs.5,000 together with the capital of Rs. 100,000 will be refunded to the bank. If the business results in a loss of Rs. 10,000 the capital is reduced to Rs.90,000 and this amount will be refunded to the bank, which must sustain the loss of Rs. 10,000. The entrepreneur will neither receive nor pay anything. If the bank has fixed another ratio of profit division, for example, 40% for the bank, 60% for the entrepreneur, or vice versa, the profit will be accordingly divided. But in case of loss, the loss will be entirely sustained by the bank. In mudaraba a loss takes place only in the capital and as such is borne by the owner of the capital. This principle is not influenced by the ratio for profit division as laid down in the mudaraba agreement

2. In situation (2) the entrepreneur himself invests Rs. 100,000 in addition to the capital of Rs. 100,000 procured from the bank, and works the business with the joint capital of Rs.200,000. Supposing there is a profit amounting to Rs.20,000 in the business the same will be first spread over the total capital and then half of the profit earned from the bank's capital will be paid to the bank, the balance going to the entrepreneur. A sum of Rs. 15,000 will thus be the entrepreneur's share, and Rs.5,000 the bank's. The bank will get back its capital and the entrepreneur will get back his. From the profit of Rs. 15,000,
Rs. 10,000 is profit on his own capital and Rs. 5,000 is his share in the profit earned from the capital invested by the bank which is, of course, his reward for the successful operation of the business with the above capital. If the business results in a loss amounting to Rs. 20,000, the bank will bear one half, and the entrepreneur the other half. As explained earlier, loss is reduction in capita! and is borne by the owner thereof according to the ratio of his investment.

3. In situation (3), the entrepreneur invests a capital of Rs. 100,000, acquired on loan on his own responsibility, besides the Rs. 100,000 procured from the bank. The entrepreneur's private borrowing will be reckoned his private capital and he will get profit or make loss as described above for situation (2). If the business gains Rs. 20,000, Rs. 100,000 plus Rs. 5,000 will be hand back to the bank; and Rs. 100,000 plus Rs. 15,000 will remain with the entrepreneur who must of course return the Rs. 100,000 he borrowed privately. In case of a loss of Rs. 20,000 he will repay Rs. 90,000 to the bank, and must make up the Rs. 10,000 wanting in the Rs. 100,000 which he borrowed on his own responsibility. The bank does not share in responsibility for the loan he obtained privately.

4. In situation (4) Rs. 100,000 has been acquired on the basis of mudaraba from another party (the investor) in addition to the Rs. 1,00,000 from the bank and a third sum of Rs. 100,000 invested by the entrepreneur himself. Thus the business is run with a total capital of Rs. 300,000. Supposing that in this deal with the investor it has been decided that half of the profit earned from his investment will be paid to him and half goes to the entrepreneur, then, from an overall profit of Rs. 30,000, Rs. 20,000 will go to the entrepreneur and Rs. 5,000 each to the bank and to the investor. The bank, the entrepreneur, and the investor will also get back their capital. Thus, the principle of profit-sharing has remained unaffected: the whole profit is divided over the whole capital; the entrepreneur is paid for his services from this overall profit according to the terms and conditions settled between him and the bank, and between him and the investor. If the business results in a loss amounting to Rs. 30,000, that loss will be divided equally (or proportionally, as the case may be), over all three capitals. The bank, the entrepreneur and other investors will each suffer a loss of Rs. 10,000 and get back a sum of Rs. 90,000 only. No portion of the losses suffered by the bank and the investor will be borne by the entrepreneur.

5. In situation (5), the entrepreneur procures a sum of Rs. 100,000 from the bank on mudaraba, and with the bank's consent, enters into a partnership agreement with this capital with a second entrepreneur, who invests a capital of Rs. 100,000 in order to run the business on a total capital of Rs. 200,000. It has also been settled between the two entrepreneurs that they will share in the profit equally, and it has been agreed between the bank and the entrepreneur that the bank will receive half of the profit earned by the entrepreneur and half will go to him. Thus if the business makes a profit of Rs. 20,000, Rs. 10,000 will go to the second partner on his investment of Rs. 100,000 on the basis of partnership; Rs. 5,000 will go to the bank which provided a capital of Rs. 100,000 on the basis of mudaraba and Rs. 5,000 will go to the entrepreneur who put in the effort of setting up the business. If the business results in a loss of Rs. 20,000 the bank will sustain one half, the remainder to be sustained by the second partner who provided capital on the basis of partnership. The first entrepreneur who made no investment will not share the loss, nor will he receive any reward for his business efforts.

In the above situation it would be perfectly in order if, in spite of making equal investment it were settled that the first entrepreneur and his partner should get 60% and 40% respectively from the profit earned, or the first entrepreneur receive one-third and his partner two-thirds. Under all these circumstances the bank would receive an already fixed ratio as its share in the profit which the entrepreneur would get from his partner under their agreement deed. It would also be in order to carry out the agreement with the condition that from the total profit the second entrepreneur should get 50% and the bank 25%. The remaining 25% would go to the first entrepreneur who had procured capital from the bank. The exact figures in any of these examples may be varied in individual cases.

6. In situation (6), there are a great many possibilities, since it combines some of the principles presented in the preceding lines. It must suffice to understand the underlying principle of distribution: Suppose that the entrepreneur invests Rs. 100,000 in a business run by his partner A (who also invests Rs. 100,000), and on behalf of this joint venture, he acquires Rs. 100,000 from the bank on the basis of mudaraba, and a further Rs. 100,000 from another partner B. It is decided between the bank and B that half of the profit earned on their total capital will be paid to the bank and between the entrepreneur and A that they
will divide equally the total profit of their joint venture. This business is, therefore, run with a total capital of Rs.400,000. If it gains Rs.40,000, the bank would get Rs.5,000 and partner B would get Rs.5,000. Partner A and the entrepreneur would each get Rs.15,000. The principle of distribution of profit is that first of all the total profit will be spread over the total capital to give profit of Rs.10,000 per 100,000 invested. According to the agreement deed of *mudaraba*, partner B and the bank would receive half of the profit, i.e., Rs.5,000 each. The balance, Rs.30,000, of the total profit on the joint venture must be divided according to the agreement deed between the entrepreneur and partner A.

If the business results in a loss of Rs.40,000 it will be divided equally between the bank, partners A and B, and the entrepreneur, because their capital investments were equal.

From the bank's viewpoint the common factor in all these cases is the precondition that if the business results in a loss the loss is sustained in full by the bank according to its full share in the joint capital. If there is a profit the bank must pay to the entrepreneur a fixed ratio from its profit earned on its capital investment. We have illustrated in the examples above that the underlying principle is not influenced by the nature or the size of the entrepreneur's business into which the bank has put its capital on the basis of *mudaraba*. In other words, as regards profit-sharing or loss, it does not matter whether or not the other partners have also invested their capital in the enterprise.

We have not so far mentioned short-term loans taken out by the entrepreneur. Such loans will be repaid before accounting for overall profit and loss and may not be counted with the original capital investment. As explained above, the percentage loss and profit in the business will be determined only on the basis of the capital including long-term loans invested. The short-term loans are only the credit transactions of the business. Undoubtedly though, sales on credit do expand the business and enhance the opportunities for profit and, since the credit transactions are based upon the capital used to run the business, profit and loss will be accounted for on the basis of the invested capital. The same is the case with (short-term) loans of smaller amounts. These loans do expand and modernize the business and provide opportunities for earning profit but they are not included in the capital when accounting for loss and profit.

It is possible for the bank to enter into various forms of agreement with one or more entrepreneurs or business institutions, and it is also possible that they may invest further capital procured on *mudaraba* or an active partnership basis with yet other parties. In all the different possible permutations, the underlying principle of profit-sharing or loss-sharing remains unaffected. First of all, the share of investors on the basis of *mudaraba* should be paid out of the total profit to the business in which capital was invested on that same basis, and also some capital was procured through loans taken out with the consent of the partners in the business. The balance of profit should then be divided among the business partners according to a predetermined ratio and, in case of loss, the loan which was taken out on behalf of the joint business should be repaid in full. The balance of loss will be borne by the entrepreneurs and the partners proportionately according to their capital investment. In our opinion the bank will not invest in a business in which capital got on long-term loans is also being invested. But capital for investment, got on the basis of *mudaraba*, may be approved by the bank, as well as capital got on the basis of (active) partnership. The principle of division of profit and loss has been illustrated in the examples above. The same rules apply to short-term loans, taken out on behalf of the partnerships, which have been explained above in the context of *mudarabah* agreement.

**Investment in ongoing Business**

With a new enterprise, there is need only for a mutually agreed audit, and no theoretical problem arises in determining the profit or loss for the different parties who have invested along with the bank. But there is also the possibility that the entrepreneur may be running a factory, or some other agricultural, industrial or commercial enterprise, and approach the bank for a loan. The bank must ascertain what amount of capital is already invested in the business before investing its own capital. The bank should also work out fully the total assets of the business, for future profit or loss cannot be determined without this information. The most popular method of making such assessments is to determine what are the moveable properties
(machines, manufactured goods, raw materials, etc.) and all the immovable property (buildings, grounds, etc.) would fetch if put on the market for sale. After this, the immediately available and repayable amounts owed to the enterprise should be included in the valuation of its overall assets. The total thus accounted for will constitute the original capital over against the capital provided by the bank: the bank's profit or loss from any future transaction will be based upon the relation between the two. It is immaterial whether the owner of the business is the entrepreneur himself or whether there are also other partners providing further capital on the basis of mudaraba, prior to the procurement of capital from the bank.

The method of assessment of the value of the business should be one on which the bank and the entrepreneur both agree. The services of experts may be hired, where necessary, and where both parties can trust the experts' professionalism and integrity. Regarding monies owing to the enterprise at the time of execution of the agreement a workable alternative may be for the entrepreneur to undertake responsibility for them; in this case such monies will not be accounted for in the valuation of the assets of the enterprise.

A similar problem arises where the entrepreneur decides to procure additional capital from the bank on the basis of active partnership, to jointly run the business. Some scholars have considered it essential that both parties should join the enterprise with capital in cash — to avoid eventual dispute and disorder. It is, however, very tedious to do this — it is even detrimental to the interest of the business, slowing down the economic process while the running enterprise is converted into a joint one. We therefore consider it proper to adopt the above method in industrial enterprises. The capital investment of the entrepreneur may be reckoned in the total assets of the business and the bank should add its capital thereto, preferably in cash, the future account between the parties being maintained on the basis of the above two capitals. The method of valuation of the business's assets should be agreed to by both parties, thus preventing any possibility of dispute or misunderstanding at a later stage.

A question arises regarding the length of the term of agreement if the nature of the enterprise is such that after a fixed period it may be reckoned 'complete' and the capital invested converted into cash, the bank may wish to make the investment over the whole period. No problem arises in reckoning up profit or loss for, on completion of business, the entrepreneur will have the account audited and divide profit or loss accordingly. But seeing that, in modern times, industrial enterprises continue indefinitely, their time of completion can hardly be determined beforehand. Under such circumstances the bank may pursue either of two alternatives. Either it may provide the capital for a specific period, or make the investment for an indefinite period, in which case it should be able to withdraw its capital as and when it desires. In both cases the same method of valuation of the assets of the business will be employed as was explained above for refunding capital and auditing the account. One reason for this is that if the entrepreneur continues the business, even after refunding the bank's capital to the bank, it may not be possible to audit the account on conversion of the whole capital invested into cash — the more so as, in reality, the decision to sell goods, machines and raw materials put in order to clear the account, cannot be taken. It would be fatal for any industrial enterprise to convert all its assets into cash simply to settle up its account; such a step could have serious consequences, not only for the entrepreneur but for the whole economy. Ultimately this may mean that, in practice, industrial entrepreneurs would not get capital from the bank. In the light of this it seems to be vital that the final division of loss or profit and audit of the account are reckoned according to the above method of valuing the assets in the joint capital. The bank would eventually get back its capital in cash, and its legitimate profit in cash, according to the accounts maintained. The procurement of cash to make these payments to the bank will be the responsibility of the entrepreneur who, while wanting to continue the business, also wants to refund the bank's capital. (What methods he adopts to achieve this have no bearing on the present discussion.)

As has already been explained in the discussions on the Islamic principles of partnership, and mudaraba, it is, in the opinion of scholars, essential to convert the capital of the enterprise into cash for the sake of proper accounting and final division of profit or loss. This argument is aimed to avoid any possibility of fraud in the accounts, resulting in a misunderstanding or usurpation of the rights of any of the partners. Without doubt, conversion of the assets into capital would achieve that objective. But, while this is possible in agricultural and commercial enterprises, to do so in modern industrial enterprises may
entail many individual and social disadvantages. In our view if valuation of the assets of the enterprise is carried out in a way that both parties can agree to, no serious problem need arise, when profit or loss are worked out.

In order to make auditing of the account and study of the business transaction more convenient, it should be obligatory upon all the partners to prepare a statement at suitable intervals (e.g. annually or half-yearly) to determine the total financial assets of the enterprise according to modern accounting methods. The bank should also keep such intervals in mind when making investments — that is, fix a quarterly or yearly or some other period — and on completion of this period either partner should be empowered to terminate the agreement. In that circumstance, the bank's capital should be refunded and after accounting for profit or loss, its account cleared. If, however, the partners so wish it, the agreement may be continued for another quarter or year, as jointly agreed. In such cases division of profit or loss will be final and have no bearing upon succeeding extensions of the agreement obviously, with joint consent, the partners may keep the agreement running continuously and indefinitely. They may wish to postpone division of profit or loss to a future date, and regard any intermediate settlement of account as temporary. In case of fixed term agreement, the final settlement of account would only be possible before the end of the term if both (all) parties agree to this, or if one partner dies in a circumstance that may necessitate (early) termination of the agreement.

If an entrepreneur, who already has bank capital invested in his business, wants to make further investment with additional capital from either the bank or another entrepreneur, the financial state of the business must be assessed with a view to the proposed additional investment at the time of its proposal, and in the manner outlined above. Every partner, on introducing new capital, becomes a shareholder in the enterprise under a new agreement, and it is then necessary in theory to clear the account of those investors whose capital is already invested in the business, their current profit and loss having been determined. In practice, it is not necessary that either their capital actually be refunded or their share in the profit of the business. It may be sufficient to reckon up the value of such capital together with their profit and loss, and amend the agreement accordingly.

Even if the bank has provided the entrepreneur with capital for an unlimited period, the same method of accounting and division of profit or loss can be adopted after suitable intervals, quarterly or yearly, etc. As the bank would need to determine the total profit or loss after the completion of its clients' accounts, the fact of a long-term investment should not prevent the fixing of a time limit for the determination of quarterly profit or loss and continued payment to the bank of profit on its invested capital.

So far we have discussed the procedure of investment of capital on the basis of (active) partnership or mudaraba. But for future discussions we will assume that the bank makes investment on the basis of mudaraba only. This removes possible complications in the discussion while not significantly influencing its outcome. Keeping all aspects of the proposed banking system in view, it can be readily imagined, if the bank does offer partnership on the principles of Shirkai-e-Enan alongside loans on mudaraba, what influence this will exert on the overall banking system and what modifications will be needed in detailed implementation.

Conclusion

1) The bank would provide the entrepreneurs with its capital on the basis of mudaraba.
2) The whole of any loss incurred on the capital provided by the bank would be borne by itself.
3) The financial liability of the bank must not exceed its capital. (The highest loss to be suffered can thus be equal to the total capital invested.)
4) The distribution of profit may take place before the closing audit of the accounts.
5) On completion of business the bank may have its capital refunded along with any increase or decrease according to
profit or loss.

6) At the outset it is essential to determine the extent of capital already invested in the business or that which is being invested now in addition to capital provided by the bank on an earlier occasion.

7) It is necessary to draw up a fresh agreement for any additional investment in the business whether of capital from another source or from the bank itself.

8) In cases of both definite and indefinite term investment the bank may at any time withdraw its capital with the consent of the entrepreneur. The bank may, however, be required to wait for some time for the completion of its account which may extend to a quarter.

Suggestions

Educated youth having no financial background hesitate to borrow from conventional banks because of the risk in the entrepreneurship business. The Islamic finance can become a big opportunity for them to encourage them for entrepreneurship.

India is eyeing a stake in the booming Islamic banking industry with its proposed implementation being assessed with great interest by the Indian policymakers. But they have to substantially modify the legal framework which governs the Indian banking system prior to offering

Under the current Indian banking laws, it is almost impossible for Islamic banking to be carried out in India due to the mandatory requirement for interest payments on deposits. The concept of profit-loss sharing or partnership is alien to the conventional banking framework of India and thus not allowed under the law. The tax treatment of Islamic finance products, unless reviewed, would be the biggest hindrance to the implementation of Islamic banking in India.

Regulators are still in doubts about the scope of Islamic banking, having understood that from a mere religious perspective. A committee to analyse the impact of Islamic banking to the Indian communities not withstanding their religious faith was never established. Thus, the potentials of Islamic banking to resolve India’s real economic problems were not realized.

Indian entrepreneurs face the biggest challenge of financing the projects; Islamic banking is the biggest opportunity to overcome such problems.

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