

EXAMINING THE LEGALITY OF NIGERIA DEPOSIT INSURANCE CORPORATION AS THE INSURER OF CUSTOMERS' DEPOSITS FROM THE PERSPECTIVE OF SHARIA

Muhammad Kamaldeen Imam-Tamim, Khadijah Akorede Salawu
Faculty of Law, University of Ilorin, Ilorin, Nigeria
Email: imamtamim@unilorin.edu.ng

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Abstract

The establishment of NDIC was the government's major policy shift from saving the banks from collapsing to saving the deposits of the depositors, and the Corporation insures both conventional and Islamic banks. However, the establishment and operational framework of this Corporation is devoid of any Islamic bias. The research work examines the legality of NDIC as an insurer of customers' deposits within the provisions of Sharia by looking into the need for and the extent to which Islamic banks can participate in the scheme. The research is a normative research and uses a qualitative approach. This method is used to obtain the data from the sources in order to examine the legality of NDIC and its operation within Sharia as the insurer of Islamic bank deposits. The results showed that the major aim of the Corporation is in line with the Sharia but the operations enacted by some legislative frameworks are contrary to the provisions of Sharia. Some recommendations were prescribed to amend these lapses to further improve the standing of NDIC as an Insurer of the deposits of Islamic bank's customers; introduction of a mudarabah or musharakah arrangement where the parties involved would share the profit and loss in respect of the invested funds, and the adoption of an Islamic Deposit Insurance Scheme to ensure that Islamic Banks' participation in DIS is fully sharia-compliant.

Pembentukan NDIC merupakan perubahan kebijakan utama pemerintah untuk menyelamatkan bank dari keterpurukan. Kebijakan ini juga bertujuan menyelamatkan simpanan para deposan dan asuransi perusahaan di bank konvensional maupun

syariah. Penelitian ini mengkaji legalitas NDIC sebagai penjamin simpanan nasabah dalam ketentuan syariah dengan melihat kebutuhan dan partisipasi bank syariah dalam skema tersebut. Artikel ini merupakan penelitian normatif menggunakan pendekatan kualitatif. Metode tersebut digunakan untuk memperoleh data dari sumber dan menguji legalitas NDIC serta operasionalnya sebagai penjamin simpanan bank syariah. Hasil penelitian menunjukkan bahwa tujuan utama perusahaan sejalan dengan syariah, tetapi eksekusi yang dilakukan oleh beberapa kerangka legislatif bertentangan dengan ketentuan syariah. Beberapa rekomendasi ditentukan untuk mengubah penyimpangan ini, yakni (1) meningkatkan posisi NDIC sebagai penjamin simpanan nasabah bank syariah, (2) sosialisasi akad mudarabah atau musyarakah yang memberikan aturan pada pihak-pihak terlibat untuk berbagi keuntungan dan kerugian sesuai investasi dana, dan (3) penerapan Skema Asuransi Simpanan Syariah untuk memastikan bahwa partisipasi bank syariah dalam DIS sepenuhnya sesuai syariah.

Keywords: deposit insurances scheme, maqasid al-shariah, mudarabah, musharakah

Introduction

Customers patronize banks primarily for the security they provide for their deposits.¹ Ironically, recent happenings in both global and local scenes have revealed that this security is not ordinarily guaranteed when the financial institution encounters crisis.² The need for the mitigation of the dire consequences to customers, when this incidence occurs, warranted the establishment of deposit insurance.³ This has also contributed to the growth in the adoption of Islamic finance frameworks, which are considered as an alternative financial system following the global financial crisis that has seen the collapse of several giant conventional financial institutions.⁴ In spite of the benefits of the Islamic banking framework, both Sharia-compliant financial institutions and conventional banks require the extra financial security that is provided by deposit insurance for their customer's deposit. This financial security is meant to provide assistance and promote prudent risk taking to the depositors of bankrupt banks.⁵ The safety nets created by the

1 Asyraf Wajdi Dusuki and Nurdianawati Irwani Abdullah, "Why Do Malaysian Customers Patronise Islamic Banks?," *International Journal of Bank Marketing* 25, no. 3 (2007): 142–60, <https://doi.org/10.1108/02652320710739850>.

2 Joseph E Stiglitz, "Initiative for Policy Dialogue Working Paper Series THE FINANCIAL CRISIS OF 2007 / 2008 AND ITS MACRO- ECONOMIC CONSEQUENCES," no. April (2009).

3 Stiglitz.

4 Edib Smolo and Abbas Mirakhor, "The Global Financial Crisis and Its Implications for the Islamic Financial Industry," *International Journal of Islamic and Middle Eastern Finance and Management* 3, no. 4 (2010): 372–85, <https://doi.org/10.1108/17538391011093306>.

5 Jessica Hagen-zanker, Elisa Mosler Vidal, and Georgina Sturge, "DESIGNING FINANCIAL SAFETY NETS TO FIT Country," no. June (2017).

deposit insurance avoid disintermediation⁶ resulted in bank failures. Deposit insurance helps in maintaining confidence and soundness in the financial sector in countries implementing it.⁷

Nigeria Deposit Insurance Corporation (NDIC) was created for the protection of the banking industry and other related services that have to do with customers' deposits in Nigeria.⁸ This measure is put in place to promote financial stability and protect bank depositors, either fully or partly, from losses caused by the banks' inability to pay debts when due. Nigeria operates both conventional and Islamic banking systems and the Government has made it compulsory for operational banks to join the Depositor Protection Scheme as members and pay the required premium.⁹ The general importance of the NDIC is to protect the interest of the depositors of deposit-taking financial institutions. This enhances financial security and encourages economic participation.¹⁰ This overall importance suggests that a link exists between the concept of deposit insurance and *maqasid sharia* that is aimed at promoting benefits and repelling harms and *maslaha*,¹¹ which means utility, good, beneficial, or advantage.¹² However, the basic principle of all Islamic financial transactions is that they must be free from *riba* (Interest), *gharar* (Uncertainty), *maisir* (Gambling), and Sale/Purchase of unlawful Goods and Services.¹³ Although the goals of the scheme are beneficial

6 **Disintermediation** in finance, is the withdrawal of funds from intermediary financial institutions, such as banks and savings and loan associations, to invest in them directly. Generally, **disintermediation** is the process of removing the middleman or intermediary from future transactions www.investopedia.com/terms/d/disintermediation.asp accessed on March 15, 2019.

7 IADI, 'Core Principles for Effective Deposit Insurance Systems' p. 6, 2010.

8 By Olukotun et al., "Bank Distress in Nigeria and the Nigeria Deposit Insurance Corporation Intervention," *Type: Double Blind Peer Reviewed International Research Journal Publisher: Global Journals Inc* 13 (2013).

9 Salisu Hamisu and Rusni Hassan, "Depositors Protection Scheme : Appraisal of Islamic Banks' Participation in Deposit Insurance System Depositors Protection Scheme : Appraisal of Islamic Banks Participation In," no. October (2020), <https://doi.org/10.15640/jibf.v5n1a3>.

10 G A Ogunleye, "Deposit Insurance Scheme in Nigeria: Problems and Prospects By," 2002, 1–17, [http://proshareng.com/admin/upload/reports/NDICs Deposit Insurance Scheme in Nigeria - Problems Prospects \(2\).pdf](http://proshareng.com/admin/upload/reports/NDICs%20Deposit%20Insurance%20Scheme%20in%20Nigeria%20-%20Problems%20and%20Prospects%20(2).pdf).

11 Tawfiq Al-Mubarak and Noor Mohammad Osmani, "Applications of Maqasid Al- Shari ' Ah and Maslahah in Islamic Banking Practices : An Analysis Introduction : Maslahah : The Demand of Time," *An Analysis. In International Seminar on Islamic Finance in India*, no. October (2010): 17, <https://doi.org/10.13140/RG.2.1.3578.0644>.

12 "IADI | International Association of Deposit Insurers | Home.Html," accessed on December 2, 2021, <https://www.iadi.org/en/core-prin> Olukotun, Ademola G et al, 'Bank Distress in Nigeria and the Nigerian Deposit Insurance Corporation Intervention' ciples-and-guidance/core-principles/.

13 Buerhan Saiti and Adam Abdullah, "Prohibited Elements in Islamic Financial Transactions: A

to the Islamic Banking System of Nigeria, the problem of the permissibility of insurance and the methods used in fulfilling this scheme needs to be in line with the Sharia to ensure its legality under the Sharia. This poses a problem because all financial institutions in Nigeria (Islamic banks included) are expected to be insured by NDIC. There are possibilities of NDIC violating the basic principle of all Islamic financial transactions as it is not Islamic-oriented. There is no Islamic deposit insurance scheme in Nigeria to make a provision for the peculiarities of the Islamic Financial System, which ensures the provision of an ideal climate for Islamic banks to be insured.

Another study explains that NDIC has been successful in monitoring banks. It is proven by an increase in asset returns in 1990-2007, which is a cost-paid increase in insurance schemes, but there is a liquidation dividend due to the falling of banks and the temporary failure of bank insurance premiums. Therefore, it is hoped that NDIC will be able to start heavy surveillance on its authority by shipping their premiums when they are due and by ensuring that any loans taken from the bank can be traced by borrowers in real order to avoid certain loans resulted in the bank's failure.¹⁴ This study intends to look into the potential of deposit insurance (NDIC) in preventing the public from experiencing financial difficulties, instilling public confidence about the safety of deposits, promoting financial stability and maintaining competitiveness of Islamic deposits while keeping the activities of the insurer in line with the provisions of Sharia.

Research Methods

Normative research is also known as doctrinal research, a research on a law that is conceptualized and developed on the basis of the adopted and developed doctrine. In this study, the researcher seeks to analyze and study the NDIC's authority to provide guarantees for the Nigerian people for their deposit in financial institution. The research legal materials used are primary and secondary legal materials. Documentation techniques are used to extract the information from written sources, such as archives, records, official documents, and so on. The data obtained through the documentation study were then analyzed using qualitative descriptive methods.

Comprehensive Review," *Al-Shajarah* 21, no. Specialissue (2016): 139–59.

14 H Dennis and Okowa I Okowa, "NIGERIA DEPOSIT INSURANCE CORPORATION AND BANKS PERFORMANCE: TREND ANALYSIS," *International Journal of Advanced Academic Research | Social and Management Sciences* | 6, no. 5 (2020): 2488–9849, <https://doi.org/10.46654/ij.24889849>.

Islamic Banking System In Nigeria

The establishment of the Islamic banking system is central to the injunctions of Islamic commercial transaction, which prevents Muslims and the institutions that serve them from dealing in interests (*riba*) and transactions considered to be contrary to Sharia.¹⁵ It then shows that the fundamental aim of Islamic financial institutions is offering Sharia-compliant transactions and activities in all of their dealings. Islamic banking, also known as non interest banking, is defined as a banking system that is based on the principle of Islamic or Sharia law and guided by Islamic economics. Two fundamental principles of Islamic banking are the sharing of profit and loss, and the prohibition of the collection and payment of interest executed by the lenders and investors. Islamic banks make profit through equity participation, which requires the borrower to give the bank a share in their profits rather than paying interest. Islamic banking is guided in Islamic principles and all banks undertakings follow those Islamic morals. Islamic rules on transaction are called *Fiqh al-Muamalat*. According to Investopedia, there are over 300 Islamic banks in over 51 countries around the world, including the United States of America.¹⁶

Taking a cue from the part of the world where Islamic banking system was adopted with increasing success, there were desires and agitations in Nigeria as to the implementation of Islamic Banking System in its financial sector. The reasons of Nigeria having high Muslim population and taking the advantageous financial discipline are one of the characteristics of the Islamic Banking System, which is needed in the Nigerian economy. It is beneficial not only to the preservation of the Islamic principle among the country's Muslim population, but it also helps in stabilizing the financial sector of the nation as a whole.¹⁷

Concept of Interest in Sharia

The concept of interest occupies a significant position in the economic system of Sharia.¹⁸ Interest in Arabic is referred to as *riba*, which in classical Islamic

15 Nwaosala E.F & Kasie G.E, 'Islamic Banking in Nigeria: A Critical Appraisal of its Effect on The Nigerian Economy'.

16 Lim S, 'Islamic Banking',

<http://www.investopedia.com/terms/i/islamicbanking.asp> accessed on May 3, 2019.

17 Mustafa Daud, Ibrahim Mohd Yussof, and Adewale Abideen, "THE ESTABLISHMENT AND OPERATION OF ISLAMIC BANKS IN NIGERIA: PERCEPTION STUDY ON THE ROLE OF THE CENTRAL BANK OF NIGERIA," *Australian Journal of Business and Management Research* 1, no. 2 (2011).

18 Muhammad Zubair, Sadia Khattak Law Department, and Abdul Wali Khan University Mardan KPk Pakistan, "CONCEPT OF RIBA (INTEREST) IN ISLAMIC LAW: ITS IMPACT ON SOCIETY,"

Jurisprudence means surplus value without counterpart or to ensure equivalence in real value.¹⁹ Interest (*riba*) is strictly prohibited in Islam as dealing with interest-based transactions means declaring war with Allah and His Messenger (Muhammad, peace be upon him).²⁰ One of the moral principles behind the banning of interest is the need to forbid inflated interest, which is an instrument of injustice and this injustice stems from the fact that interest-based transaction encourages an imbalance in the share of power and wealth between the lender and the borrower.²¹ The result of this is that interest-based transaction gives the lender the capacity to exploit the needs of the borrower and to dictate the rate of return, leading to the potential of the lender for maximizing his profits to the detriment of the borrower and in some cases it is more impoverishing the borrower.²² Another reason for forbidding interest on a societal level is because it damages the spirit of cooperation among people, gives birth to enmity, hatred and is inherently a principal agent of class formation, which creates a class of people whose money increases without them making any effort.²³

Classical jurists opined that interest is out rightly prohibited and it includes both *riba an nasiyah* (interests on loans) and *riba al fadhl* (interest through unfair sales).²⁴ Interests on loans is practiced under the conventional banking system. It refers to the duration of time, which is given to the borrowers for the repayment of loans in return for extra amount over the principal amount.²⁵

Islamic banking is different from conventional banking because Islamic banks are not allowed to offer a fixed rate of return on deposits and are not allowed to charge interest on loans.²⁶ Based on this guiding principle in Islamic financing on the prohibition of interest, Muslims are not permitted to receive or pay interest

Sci.Int.(Labore) 27, no. 4 (2015): 3601–3, <http://www.1stethical.com/wp->

19 Abu Umar Faruq Ahmad and M Kabir Hassan, “RIBA AND ISLAMIC BANKING,” n.d.

20 Q.S. al-Baqarah [2]: 279.

21 Zubair, Khattak Law Department, and Wali Khan University Mardan KPk Pakistan, “CONCEPT OF RIBA (INTEREST) IN ISLAMIC LAW: IT’S IMPACT ON SOCIETY.”

22 Zubair, Khattak Law Department, and Wali Khan University Mardan KPk Pakistan.

23 *Dalam Menyelesaikan and Konflik Antarumat*, “Pascasarjana Universitas Islam Negeri (Uin)” 1963 (2017). “Deposits,” accessed on December 3, 2021, <http://www.financialislam.com/deposits.html>.

24 Intisar A. Rabb, *The Oxford Encyclopedia of the Islamic World, The Oxford Encyclopedia of the Islamic World* (Oxford: Oxford University Press, 2009), <https://doi.org/10.1093/acref/9780195305135.001.0001>.

25 Gabriele Badano and Matteo Bonotti, “Rescuing Public Reason Liberalism’s Accessibility Requirement,” *Law and Philosophy* 39, no. 1 (February 1, 2020): 35–65, <https://doi.org/10.1007/s10982-019-09360-8>.

26 Beng Soon Chong et al., “Islamic Banking: Interest-Free or Interest-Based?,” *Pacific-Basin Finance Journal* 17, no. 1 (2009): 125–44, <https://econpapers.repec.org/RePEc:eee:pacfin:v:17:y:2009:i:1:p:125-144>.

and are therefore barred from conducting business with conventional banks.²⁷

Customers' Deposits and its types in Islamic Banking

A customer deposit is a funding component of a banking institution.²⁸ Customer deposit or bank deposit consists of money placed into banking institution for safekeeping.²⁹ The account holder has the right to withdraw deposit funds, as stated in the terms and condition governing the account agreement. Customer deposit refers to the liability rather than the actual funds that has been deposited. When someone opens a bank account and makes a cash deposit, he surrenders legal title to the cash, and it becomes an asset of the bank. In turn, this makes customer's deposit a liability owed by the bank to the depositor.³⁰ Customers' deposits are important sources of financial strength for Islamic banks as these deposits are used to increase the capacity for financing operations which thereby increase the profit for shareholders.³¹ Basically, there are four types of customers' deposit in Islamic banking; they are Current deposits, Savings deposits, Term deposits and Investment deposits.

Current deposit permits its customers to deposit and withdraw their money at any time and does not require a minimum balance in the deposit account.³² It is based on the Sharia commercial principles of *Wadiyah*, *Amanah* or *Qard Hasan*.³³ Under the *Amanah* arrangement, the Islamic banks treat the funds as a trust and cannot use these deposits for its operations.³⁴ However, the Islamic banks does not guarantee the refund of deposits in case of loss resulted from the circumstances beyond its control.³⁵ In *Wadiyah*, the bank takes permission from the depositors to use the deposits and guarantees the return of the deposits whenever the depositors

27 "Ariff, M. 'Islamic Banking,' *Asian-Pacific Economic Literature*, 2 (2). 46-62. September. 1988.," accessed December 3, 2021, <http://www.sciepub.com/reference/22946>.

28 Chong et al., "Islamic Banking: Interest-Free or Interest-Based?"

29 "Bank Deposits Definition," accessed on December 3, 2021, <https://www.investopedia.com/terms/b/bank-deposits.asp>.

30 "Bank Deposits Definition."

31 "Deposits."

32 Akilu Aliyu Shinkafi and Nor Aini Ali, "Islamic Financing Products and Instruments: A Thematic Review," *Online Journal of Research in Islamic Studies* 5, no. 2 (2018): 35-60, <https://mjes.um.edu.my/index.php/RIS/article/view/15435>.

33 Issa Qaed and Mansour Qaed, "The Concept of Wadiyah and Its Application in Islamic Banking," *Quest Journals Journal of Research in Humanities and Social Science* 2, no. 11 (2014): 2321-9467, www.questjournals.org.

34 Shafi'i Abdul Azeez Bello and Rusni Bt Hassan, "Saving and Current Account in the Context of Shari'ah Contract," *Nigerian Chapter of Arabian Journal of Business and Management Review* 1, no. 12 (2014): 8-17, <https://doi.org/10.12816/0003711>.

35 "Deposits."

demand.³⁶ Current deposits based on the principle of *Qard Hasan* involves the act of the customer giving the bank the authority to use his/her account funds to invest in its operations, and this is considered as a non-interest loan by the depositor to the bank.³⁷ However, the bank is obligated to return the credit balance to the depositor who has no right to receive any profit on the balance.³⁸

Savings deposit is similar to current deposits as it also permits customers to deposit and withdraw money at any time they want; however, savings account operates in a different way. Deposits in savings accounts are accepted based on the principle of *Mudaraba*.³⁹ *Mudaraba* is an investment contract where one party (*Rabb-ul-mal*)⁴⁰ provides the capital and the other party, which is the bank (*Mudharib*), provides the skill and experience.⁴¹ In a deposit *Mudaraba*, the depositor acts as the capital supplier while the banks act as the investor. Term Deposit; Term deposit is a type of arrangement where the deposits of customers are held for a fixed period of time and these deposits are in turn used to invest in business activities in accordance with the Sharia.⁴² This type of deposit is commonly structured based on the commodity *Murabaha*, *Wakala* unrestricted investment and *Mudaraba* general investments.⁴³ Investment deposit; Investment deposit is based on the principle of partnership (*Mudaraba*) which entails profit sharing, and it covers all accounts where the client agrees to place deposits for a fixed term. In principle, the bank is not allowed to provide guarantee for the principal and fixed return except on voluntary basis.⁴⁴ However, banks can arrange a third-party guarantee.⁴⁵

36 "About Us | Trust Bank Ltd," accessed on December 3, 2021, <https://www.tblbd.com/about-us>.

37 Mohammad Omar Farooq, "Qard Hasan, Wadi'ah/Amānah and Bank Deposits: Applications and Misapplications of Some Concepts in Islamic Banking," *Arab Law Quarterly* 25, no. 2 (2011): 115–46, <https://doi.org/10.1163/157302511X553985>.

38 Farooq.

39 Ayub Muhammad Ayub, "UNDERSTANDING Islamic Finance," 2013, <https://books.google.co.id/books?id=WpBeDwAAQBAJ&printsec=frontcover&dq=WpBeDwAAQBAJ&hl=id&sa=X&ved=0ahUKEwiAn8KZ0fDnAhUN63MBHevGC0kQ6AEIKjAA#v=onepage&q&f=false>.

40 Rahama H, 'Guarantee of Investment Deposit in Islamic Banks: Fiqh Analysis'.

41 "IslamicMarkets.Com," accessed on December 3, 2021, <https://islamicmarkets.com/education/sources-funds-of-islamic-ban>.

42 'The Concept of Wadi'ah and Its application in Islamic Banking' P.71.

43 Trust bank, 'A Bank for Financial Inclusion', <http://www.tblbd.com/node/107> accessed on April 23, 2019.

44 "Islamic Finance | Rab-Ul Mal," accessed on December 3, 2021, <https://www.investment-and-finance.net/islamic-finance/r/rab-ul-mal.html>.

45 Habibur Rahman, "Guarantee of Investment Deposits In Islamic Banks : A Fiqhi Analysis," *Journal of Islam, Law and Judiciary* 1, no. 3 (2015): 37–53.

Deposit Insurance In The Nigerian Banking System

Nigeria operates a dual banking system of both conventional banking and Islamic /non-interest banking system. A bank DIS is a financial guarantee to, particularly, customers with smaller income and savings, in the event of a bank failure. Bank deposit insurance schemes are developed out of the need to protect depositors, especially the uninformed ones, from the risk of loss and to protect the banking system from instability occasioned by runs and loss of confidence. In this regard, Deposit Insurance becomes the tool through which such service can be rendered and they are established to perform some functions such as the following ones:⁴⁶

Insuring all deposit liabilities of all licensed banks and such other deposit-taking financial institutions, such as micro-finance banks operating in Nigeria so as to engender confidence in the Nigerian banking system. *First*, giving assistance in the interest of depositors in case of imminent or actual financial difficulties of banks occurred, particularly where the suspension of payments is threatened. *Second*, guaranteeing payments to depositors in case of imminent or actual suspension of payments is executed by the insured banks or financial institutions up to the maximum deposit insurance coverage.

The banking system has been singled out for the special protection because of the vital role banks play in an economy whether it is developed or is developing. For a DIS to be effective in achieving the objectives above, it must be properly designed, well implemented by the agency established to execute the scheme and well understood by the members of the public.⁴⁷ A well designed DIS contributes to the stability of a country's financial system by reducing the incentives for depositors to withdraw their insured deposits from banks following the rumors about the bank's financial crisis.⁴⁸

The establishment of the Nigeria Deposit Insurance Corporation (NDIC) brought about the introduction of an Explicit Deposit Insurance Scheme into the Nigerian banking sector. Along with the major function of NDIC, which is to insure the deposits of all banks and other deposit-taking financial institutions licensed by the CBN, the corporation is also fashioned to enhance the existing safety-net in the banking sector. The result of this is the boost in the confidence

46 "Role Of Deposit Insurance In Financial Inclusion The Nigerian Experience – Nigerian Observer," accessed on December 3, 2021, <https://nigerianobservernews.com/2015/06/role-of-deposit-insurance-in-financial-inclusion-the-nigerian-experience/>.

47 "GUIDANCE FOR DEVELOPING EFFECTIVE DEPOSIT INSURANCE SYSTEMS Financial Stability Forum Financial Stability Forum FSF FSF," 2001.

48 Ogunleye, "Deposit Insurance Scheme in Nigeria: Problems and Prospects By."

of the bank customers. It was also designed to serve as an additional framework and a substitute to the government's supporting policy (implicit insurance) that was used prior to the creation of Corporation.⁴⁹

Before NDIC was created, The Nigeria government had been trying to put in measure to forestall bank failure because of its adverse effects on citizenry. Because of this, underperforming banks were given the government's support. However, such direct supports (implicit insurance) could not be sustained under the Structural Adjustment Program introduced in 1986 which, among other implications, deregulated the economy towards market orientations. With the establishment of the NDIC, the negative impact of bank failure was minimized while moral hazard associated with direct government support was eliminated.⁵⁰

The Legal Framework Of The Nigerian Deposit Insurance Corporation

The Nigerian Deposit Insurance corporation is regulated by the Nigerian Deposit Insurance Corporation (NDIC) Act No. 16 of 2006. It empowered the corporation to insure all deposit liabilities of licensed banks and other financial institutions⁵¹ with the exception of insider deposits counterclaims and deposits held in the off-shore branches of local banks.⁵² Article 3 Section (1) of the mentioned Act states that, notwithstanding any provision contained in any other law, no person other than the corporation shall insure deposit liabilities or guarantee payment to depositors of insured institutions operating in Nigeria.

The corporation is empowered to come to the aid of an insured bank in case of imminent or actual financial difficulties, which may threaten payment of customer.⁵³ This may be in form of liquidity support to the banks on agreeable terms, giving guarantee for the bank's loans, or even taking over the management of a wobbling bank until its financial position improves.⁵⁴

In the event that the corporation exhausts all its protective alternatives and a failing bank still has to postpone payment, the corporation is obliged to pay every insured depositor up to the insurable limit, which is presently ₦500,000

49 "IADI | International Association of Deposit Insurers | Home.Html."

50 "Iganiga B. O. (2010). Evaluation of the Nigerian Financial Sector Reforms Using Behaviourial Model, *Journal of Economics* 1(2) 65-75.," accessed on December 3, 2021, <http://www.sciepub.com/reference/150048>.

51 Article (1) of the NDIC Act No. 16 of 2006

52 Article 2 (1) & Article 15 (1) of the NDIC Act No. 16 of 2006; Insider Deposit is the deposit of bank staffs while counter-claim is a deposit account used as collateral for a loan account in the same bank.

53 Article 2 (1b) and Article 37 (2) of the NDIC Act No. 16 of 2006.

54 Section 36 BOFIA (Banks and Other Financial Institutions Act) LFN 2004.

and ₦200,000 per depositor, for each account in Deposit Money Banks (DMBs) and Microfinance Banks (MFBs) respectively.⁵⁵ For this reason, adequate financial resources are required to meet the scheme's obligations and operational costs. In Nigeria, the Act establishing the NDIC recognizes four sources of funding the activities of the scheme. These are insurance premium contribution by participating in the institutions, capital contributions and periodic recapitalization provided by the owners of the scheme, borrowing facility from the CBN and special contributions or levies imposed on healthy member institutions as and when necessary.⁵⁶

In specific terms, Article 17 (1) of the NDIC Act No. 16 of 2006 states that the assessment rate for premium by insured bank is set as 15/16 of 1% of the total deposits of member institutions per annum that is about 0.94 percent. For other deposit-taking financial institution, the premium to be paid is set at 18/16 of 1% of total deposits per annum as at 31st December of the preceding year with the possibility of reduction in premium rate when the Deposit Insurance Fund (DIF) is more than 10 times the paid-up capital as provided in Section 12 (2) of the Act. Section 16(a-c) specifies the assessment base as the total deposits of insured institutions except the following deposits: insider deposits⁵⁷, counter claims from a person who maintains both a deposit and loan accounts, with the former serving as collateral for the loan; and such other deposits as may be specified from time to time by the Board. Also, Article 11(1) of the Act indicates the amount of initial capitalization shown by the government as 5 billion with the provision for periodic recapitalization in Article 11(3). Also, where the Deposit Insurance Fund (DIF) of the corporation is not sufficient for its insurance obligations, Article 17(5) provides that all participating institutions shall be obliged to pay to the corporation, a special contribution that is no more than 200% of the amount of an annual premium. Rules and regulations guiding distress resolution in Nigeria flows directly from the provisions written in the Bank and Other Financial Institutions Act No. 25 of 1991 (as amended).⁵⁸

Finally, the day-to-day administration of NDIC is also being funded⁵⁹ from the income earned from the investment of the Deposit Insurance Fund (DIF) in accordance with the Act. Article 13 (1-3) gives the corporation the power to invest money not immediately as required by the Federal Government securities and such other securities. The income of this investment is to be placed in the corporation

55 Article 20 (1) of the NDIC Act No. 16 of 2006.

56 Article 10(1) of the NDIC Act No. 16 of 2006.

57 These are the deposits of staff, including directors of the insured institutions.

58 Article 38 of the BOFIA (Banks and Other Financial Institutions Act) LFN 2004.

59 Article 10(1a-e) of the NDIC Act No. 16 of 2006.

account and be defrayed for administrative expenses of the Corporation. Article 52(1) also gives the NDIC the power to borrow such monies from the Central Bank of Nigeria as it may deem fit for the discharge of its statutory functions, which include⁶⁰ insuring deposit liabilities of licensed banks; provision of financial and technical assistance for the interest of the depositors to banks; also, rendering assistance to insured institutions in order to protect the interest of the depositors;⁶¹ guaranteeing payments to depositors in the financial or banking sector in the case of imminent or actual suspension of payments set by the insured institution; and ensuring orderly and efficient closure of failed institutions.

Requirement Of The Nigerian Deposit Insurance Corporation As The Insurer Of Customer's Deposit

There are several requirements of the Nigerian Deposit Insurance Corporation (NDIC) as the insurer of customer's deposit. The *first* is licensed banks. One of the requirements of the NDIC is that once a deposit-taking financial institution is licensed by the Central Bank of Nigeria (CBN), such as Universal Banks (deposit money banks), micro-finance Banks (MFB) and Primary Mortgage Institutions (PMIs), that licensed financial institution automatically becomes a member institution of the NDIC as membership is compulsory that is provided under the NDIC Act No. 16 of 2006.⁶² *Second*, insurance premium. All member institution of the NDIC are required to pay premium annually and the method employed in Nigeria is *Ex Ante*, which means that the payment is made annually by the members before the envisaged event happens and the payment is based on the formula that is stated as 15/16 of 1% of the total annual deposits of banks by virtue of the Section 1 of the NDIC Act No. 16 of 2006. *Third*, The maximum deposit insurance limit. Under the repealed NDIC Act, the maximum insurance limit was set at ₦50,000 per depositor in the event of a failure of an insured institution and that was applied to insured depositors of all the 33 closed banks up to year 2000 and this limit coverage lasted till 2005.⁶³

After the repeal of the Act in 2006, the maximum coverage increased to ₦200,000 per depositor. At the inception and up to recent past, the insurance of deposit service was limited to only conventional licensed banks, but that has

60 Article 2 of the NDIC Act No. 16 of 2006. <https://ndic.gov.ng/ndic-develops-framework-for-deposits-insurance-ndic-for-no-interest-bank-deposits/> accessed on July 28, 2019.

61 Ogunleye, "Deposit Insurance Scheme in Nigeria: Problems and Prospects By."

62 Section 15 of the NDIC Act No. 16 of 2006.

63 "THE LEGAL AND INSTITUTIONAL FRAMEWORK FOR THE OPERATION OF DEPOSIT INSURANCE SCHEME IN NIGERIA ~ Project Topics and Materials | Download Free Research Projects," accessed on December 3, 2021, <https://www.projectreserve.com/2017/06/the-legal-and-institutional-framework.html>.

been changed with the extension of coverage to other deposit-taking financial institutions, specifically Micro-Financed Banks (MFBs) and Primary Mortgage Institutions (PMIs) at a limit of ₦100,000. The reason deals with the will to encourage the small investors to improve on their banking habits since they are assured of the safety of the deposit at all times.⁶⁴ Currently, the corporation provides coverage to twenty-four (24) banks, 882 Micro-finance banks (MFBs) and 101 Primary Mortgage Institutions (PMIs) and the limit currently stands at N500,00 per depositor of Deposit Money Banks (DMBs) and N200,000 per depositor for MFBs and PMIs.⁶⁵

NDIC Framework for Non-Interest Deposit Insurance Scheme

In the beginning, Islamic banks (*Ja'iz* Bank) and conventional banks essentially ran non-interest packages (Stanbic IBTC and Sterling Banks), but it was not covered under the NDIC Deposit Insurance Scheme (DIS). Following the provision of Section 10(2) of the NDIC Act No. 16 of 2006⁶⁶, the corporation developed a framework for insuring their deposit liabilities. The Maximum Deposit Insurance Coverage (MDIC) for the Non-Interest banking Institutions is set to be the same as the conventional banks, which is ₦500,000 and ₦200,000 per depositor per account in Deposit Money Banks (DMBs) and Microfinance Banks (MFBs) respectively.⁶⁷ The following Non-Interest Deposits are covered under the scheme: Safe Keeping Deposit, Interest Free Deposit for Investment, Profit Sharing/Loss Bearing Deposit, Profit and Loss Sharing Deposit, and any other deposit type that is Non-Interest Based and approved by the Central Bank of Nigeria (CBN). The following financial products are, however, not covered under the Scheme: insider deposits; counter-claims from one person who maintains both a Deposit Account and a non-interest-bearing loan account and/or a loan based on *murabahah* financing where the deposit account serves as a collateral for either or both of the loan accounts and inter-bank takings.

64 'Value Creation in the Context of Deposit Insurance System' p. 36

65 Nigerian Deposit Insurance Corporation (NDIC), 'A brief on Nigeria Deposit Insurance Corporation (NDIC) to the House Committee on Banking and Currency', p. 2, 2011.

66 SS. 10(2) NDIC Act States that "The Corporation Shall have the power to establish a separate Deposit Insurance Fund (DIF) for each category of insured institution in which all assessed premium shall be deposited and which and which fund the cooperation will utilize for the respective insured institutions."

67 <https://ndic.gov.ng/ndic-framework-for-non-interest-deposit-insurance-scheme/> accessed on May 28, 2019.

Sharia Perspective Of Deposit Insurance

Insurance is a form of safeguard against uncertainties, and it provides some forms of financial recompense for losses suffered due to the incident of unanticipated events, insured within the policy of insurance.⁶⁸ In a practical definition, insurance is the equitable transfer of the risk of a potential loss, from one entity to another, in exchange for a premium and duty of care.⁶⁹ It is a form of risk management primarily used to hedge against the risk of catastrophic financial loss.⁷⁰ Globally, insurance corporation has grown into super profitable commercial enterprise through underwriting and investment of premium collected from the insured ones by the insurers.⁷¹ The insurer predicts the likelihood that a claim will be made against his policies and prices his products accordingly, using tools of statistics and probabilities.⁷²

On the ruling of the permissibility of commercial insurance in Sharia, Ibn Abiddin scrutinized maritime insurance practices that was prevalent in his time, which has the same characteristics as the contemporary commercial insurance and declared it impermissible under Sharia because it involved elements of uncertainty (*gharar*) and interest (*riba*).⁷³ Consequently, the same ruling is applied to commercial insurance that has a high level of uncertainty in that payment of the premium. It occurs when what is being bought is not well-defined and in most cases, the amount to be paid or received is not known from the beginning and these activities are also enshrined in the transactions based on interest.⁷⁴ Although deposit insurance is not fundamentally the same as conventional insurance, they have similar principle.⁷⁵

DIS is allowed in sharia based on the following authorities;

68 Insurance, 'Mathematics for commerce, Economics and Business', p140.

69 Banking and Insurance, <https://sol.du.ac.in/mod/book/view.php?id=1226> accessed on May 28, 2019.

70 Insurance, <https://www.investopedia.com/terms/i/insurance.asp> accessed on August 17, 2019.

71 Insurance Premium, www.businessdictionary.com/definition/insurance-premium.html accessed on August 17, 2019.

72 Hamisu and Hassan, "Depositors Protection Scheme : Appraisal of Islamic Banks Participation in Deposit Insurance System Depositors Protection Scheme : Appraisal of Islamic Banks Participation In."

73 Ibn Abiddin, '*Hashiyat Radd Al-Mukhtar Ala al-Durar Al mukhtar*', 2012.

74 Hamisu and Hassan, "Depositors Protection Scheme : Appraisal of Islamic Banks Participation in Deposit Insurance System Depositors Protection Scheme : Appraisal of Islamic Banks Participation In."

75 Yusuf Sani Abubakar et al., "Concept of Deposit Insurance : A Comparative Study between Conventional System and Shariah," *Journal of Business and Management* 18, no. November (2016): 90-97, <https://doi.org/10.9790/487X-1810069097>.

...help one another in righteousness and piety but do not help one another in sin...⁷⁶

An evidence is also found in the hadith narrated by Abu Hurayra that:

Once two women from the tribe of Huzail were fighting each other and one hit the other with a stone which killed her alongside the fetus in her womb. The Prophet (S.A.W) ruled that the compensation for the fetus was freeing a male or a female slave and the compensation for the woman's life was blood money (*Diyah*) to be paid by the former's clan (*Aqilah*).⁷⁷

The prophet's ruling that the clan should take the responsibility was relied upon by scholars as an evidence to support the group of people to secure themselves from financial problems in form of DIS.

Deposit insurance also shares a similarity with cooperative insurance (*takaful*), which is acceptable in Sharia.⁷⁸ *Takaful* is an arrangement in which a group of participants mutually agree to help the members in the scheme who suffer loss or damage arising from specified risks.⁷⁹ In such arrangement, the participants agree to make contributions (*tabarru'*) into a fund to assist members during incidence.⁸⁰ The *takaful* insurance has a similar basic principle as conventional deposit insurance because it provides protection for loss occasioned by the attachment of risk. However, *takaful* differentiates itself from conventional deposit insurance in a number of ways.⁸¹ *First*, risk protection provided by people who face exposure to the same type of risk through the system of *tabarru* (donation) into a common pool, which is used to provide indemnity on claims,⁸² unlike conventional Deposit Insurance where risk is transferred to the insurer who provides indemnity in exchange for premiums.⁸³ *Second*, the money paid by the insured ones to the conventional insurer in exchange for risk protection belongs to the insurer, but the money paid to pool as *tabarru* belongs to the contributors. *The last*, the conventional deposit insurance may make any kind of investment including interest-bearing ventures, but a *takaful* operator may only invest in sharia-compliant businesses and may not involve itself in interest-bearing investments.⁸⁴

In regard to this, it has been suggested that Islamic financial services being

76 Q.S. al-Maidah [5]:2.

77 Al Bukhari, '*Sahih Al Bukhari*' vol. 5, 1987 ed. 2172.

78 Abdulqadir I.A, 'The Legal Framework for Islamic Banking in Nigeria', Pp. 20-39,2012.

79 Md Khairuddin Hj Arshad, "Implementation of an Islamic Deposit Insurance System for the Islamic Financial Services Industry," *Fourth Islamic Financial Stability Forum*, 2011, 160.

80 "IADI | International Association of Deposit Insurers | Home.Html."

81 'Islamic Banks' Participation in Deposit Insurance Scheme: A Legal Appraisal', P. 17.

82 Maysami R.C & Williams J. J, 'Evidence on the relationship between Takaful Insurance and Fundamental Perception of Islamic Principles', 2006.

83 Archer A & Nienhaus, 'Takaful Islamic Insurance: Concepts and Regulatory Issues', 2009.

84 Maryam Dikko, "An Analysis of Issues in Takaful (Islamic Insurance)," *European Journal of Business and Management(Online)* 6, no. 15 (2014): 1-5.

inseparable from the general principles of the sharia must base their foundations on the *maqasid al-Sharia*, which is aimed at promoting benefits and repelling harm to ensure the distinction from conventional finance.⁸⁵ Thus, the Deposit Insurance Scheme employed by Islamic banks must be free from the elements that Islam strictly prohibits, which is why Muslim communities aspire for a deposit insurance system that meets Sharia requirements. This has led to the creation of Islamic Deposit Insurance Scheme in some Muslim-dominated countries for Islamic banks.⁸⁶

The Requirements of Sharia for a Deposit Insurance Corporation

The basic principle of all Islamic financial transactions is that they must be free from prohibited elements such as interest (*riba*), uncertainty (*gharar*), and gambling (*maisir*). Interest (Riba); Interest exists in any financial transaction when there is an unequal exchange of two interest-based commodities or an exchange of money for money with different quantities, different values and at different times. Interest obviously gives an advantage to people with a surplus of money, who receive a premium on their money lent out to people faced with a deficit of money.⁸⁷

In a DIS, where banks pay premium to the deposit insurer and are reimbursed when the need arises, the technicality of labelling the acts as an interest-based transaction has raised debates. DIS does involve the exchange of money for money, and it occurs with different values and at different times. Hence, some Sharia scholars would argue that it is an interest-based transaction and, therefore, non-permissible.⁸⁸ The interest element could also involve the deposit insurer when carrying out activities like protecting deposits, investing in the deposit insurance funds, lending given to troubled banks, and obtaining external funds (when in deficit), and carrying out such activities in an interest-based system.⁸⁹

Uncertainty (Gharar); Uncertainty exists when either the object or the subject matter of a transaction or activity is uncertain. It can occur either naturally or through a deliberate act performed by parties involved in the contract. All transactions and activities including deposit insurance may contain the element of uncertainty. Sharia scholars distinguish two categories of uncertainty: permitted and prohibited under

85 “MaqasidAlShariahinIslamicFinanceAnOverviewFINAL,” n.d.

86 “IADI | International Association of Deposit Insurers | Home.Html.”

87 “Sharia Compliance in Deposit Insurance - Opinion - The Jakarta Post,” accessed on December 3, 2021, <https://www.thejakartapost.com/academia/2016/08/02/sharia-compliance-in-deposit-insurance.html>.

88 Jocelyn Grira, M. Kabir Hassan, and Issouf Soumaré, “Pricing Beliefs: Empirical Evidence from the Implied Cost of Deposit Insurance for Islamic Banks,” *Economic Modelling* 55, no. January (2016): 152–68, <https://doi.org/10.1016/j.econmod.2016.01.026>.

89 Engku Rabiah Adawiah ENgku Ali Mohd Daus Bakar, *Essential Readings in Islamic Finance* (Kuala Lumpur : cert Publications sdn Bhd, 2008).

Sharia. Sharia prohibits uncertainty when, for example, its existence is excessive, which could lead to undue losses for one party or disagreement between the transacting parties.⁹⁰ The uncertainty element exists in a deposit insurance, in respect of the failure of a bank. Nevertheless, such uncertainty may not be prohibited as it is unavoidable and naturally embedded in deposit insurance. The setting-up of a deposit insurance system is in line with the government's strategy that it must always be ready to face the failure of a bank and to protect insured depositors. Some Sharia scholars have disapproved of the deposit insurance model arguing that it entails excessive uncertainty as the insured risk might not materialize.⁹¹

According to another argument, such uncertainty is not prohibited as it does not provide an avenue for one party to gain while another will suffer loss. There is no issue of uncertainty in deposit insurance with regard to, for example, the deposit products covered, the amount to be reimbursed to insured depositors, and when they would be reimbursed, as an explicit deposit insurance system would address these through government regulation.⁹²

Permissibility of NDIC As The Insurer Of Customer's Deposit From The Perspective Of Sharia

Islamic banks, like all other banks operating in Nigeria, are mandated to participate in the Deposit Insurance Scheme as stipulated by Section 15 of the NDIC Act and non-compliance amounts to criminal offence, which makes the erring bank liable to a fine of five hundred thousand naira (₦500, 000) on conviction for each day the offence continues.⁹³ The scheme aims at protecting the banking system and offering financial guarantee to the depositors.⁹⁴ Regarding the promotion and sustenance of public confidence in the banking system, the corporation is empowered to come to the aid of an insured bank in case of imminent or actual financial difficulties that may threaten payment.⁹⁵ This may be in form of liquidity support to the banks on agreeable terms, giving guarantee for the banks' loans, or even taking over the management of a wobbling bank until its financial position improves⁹⁶ all of elements that have bases in Sharia.

90 Marhaini W. and Ahmad W. (2008), Some Issues of *Gharar* (Uncertainty) in Insurance, Essential Readings in Islamic Finance. pp 247-268.

91 Ebrahim M, 'Risk management in Islamic financial institutions' 2011.

92 Wan Marhaini and Wan Ahmad, "Some Issues of Gharar (Uncertainty) in Insurance," *Jurnal Syariah*, 10:2 [2002] 61-80, 1972, 61-80.

93 Article 15 (1) (2) & (3) of the NDIC Act No. 16 of 2006

94 Umoh P. N, 'Bank Deposit Protection: The Nigerian experience', 2003.

95 "NDIC – Protecting Your Bank Deposits," accessed on December 3, 2021, <https://ndic.gov.ng/>.

96 Article 2(1) (b) and 37 (2) of the NDIC Act No. 16 of 2006.

Nigeria does not operate a standalone Islamic Deposit Insurance Scheme, but the provision of Section 10(2) of NDIC Act 2006,⁹⁷ empowers the Corporation to develop a standalone framework for insuring the deposit liabilities of Islamic Banks. With this in mind, Hamisu and Hassan argued that most of the basis of reference considered in justifying the permissibility of DIS has always been on the matter of public interest (*maslaha*).⁹⁸ However, they opined that in most countries practicing an explicit Islamic Deposit Insurance system like Malaysia and Nigeria (NDIC), it is in a form of a tripartite arrangement, where the depository institutions (banks) perpetually pay yearly premiums while the deposit insurers on behalf of the government insures the depositors.⁹⁹

This arrangement has been argued to breach the principle of *Al-Ta'awuni 'alal birri* (helping each other in good deeds) because of the fact that the participation in the scheme was made mandatory by an act or a legislation, and the financial institutions perpetually pay yearly premium, without any plan for a plough back of the premium or even a premium holiday at some point, even when the financial institution does not show any sign of weakness or failure.¹⁰⁰ Meanwhile, the depositor who is being insured shares no risk in the arrangement. In Islamic social relationship, both *ta'awun* (mutual help or cooperation) and *tabarru'at* (willingly relinquishing individual right for collective benefits) exist under willing and mutual agreement for cooperation towards achieving certain collective benefit.¹⁰¹

In another opinion, it has been argued that although the objectives of DIS is compatible with the *Maqasid al-Sharia*, some of the laws establishing it need amendments and, likewise, its operations need adjustment for Islamic banks to be fully integrated without going contrary to the Sharia principles.¹⁰² Related to this, the NDIC empowered by the Act has created a framework, which is the Non-Interest Deposit Insurance Scheme (NIDIS) that caters for non-interest banking in Nigeria, which takes the core nature and

97 Article 10(2) of the NDIC Act No. 16 of 2006: "The Corporation shall have the power to establish a separate Deposit Insurance Fund (DIF) for each category of insured institution in which all assessed premium shall be deposited and which fund the cooperation will utilize for the respective insured institutions".

98 Hamisu and Hassan, "Depositors Protection Scheme : Appraisal of Islamic Banks Participation in Deposit Insurance System Depositors Protection Scheme : Appraisal of Islamic Banks Participation In."

99 Hamisu and Hassan.

100 Mohammed Khnifer, "Towards a Universal Islamic Deposit Insurance System" 20, no. December (2010): 26–29.

101 Hairul Suhaimi Nahar, "Insurance vs Takaful : Identical Sides of a Coin?," *Journal of Financial Reporting and Accounting* 13, no. 2 (2015): 247–66, <https://doi.org/10.1108/jfra-02-2015-0029>.

102 Hamisu and Hassan, "Depositors Protection Scheme : Appraisal of Islamic Banks Participation in Deposit Insurance System Depositors Protection Scheme : Appraisal of Islamic Banks Participation In."

rules that guides their transaction into consideration.

Islamic Provisions for Deposit Insurance

Under the Government's Regulation approach, the government implements the deposit insurance system by giving priority to the socio-economic benefits of the system over the way it is conducted in the absence of a Sharia-compliant approach. Such a view is strengthened by the fact that there is hardly any alternative to deposit insurance as a means to satisfy the legitimate need for deposit protection. In this regard, the government regulation approach tolerates the existence of any forbidden elements that are inherent in the deposit insurance mechanism. Other approaches are used where the government, in consultation with Sharia scholars, believes that the public interest argument alone is insufficient to justify a Sharia-compliant deposit insurance system.¹⁰³

A contract is the best available means, be it in Islamic or conventional legal systems, to reflect the intention and consent of contracting parties.¹⁰⁴ In the *Quran*, there are over 40 verses on several types of commercial contracts. Among the contracts that have been applied to Islamic financing and deposit products are loan (*qard*), cost-plus (*murabahah*), profit-sharing (*mudharabah*), profit and loss sharing (*musharakah*), leasing (*ijarah*), safe custody (*wadi'ah*) and agency (*wakalah*).¹⁰⁵ For a DIS, which is in compliance with the sharia (Islamic Deposit Insurance Scheme), applicable contracts include "guarantee with fee" (*kafalah bil ujr*) and "donation" (*tabarru'*).¹⁰⁶

There is an ongoing debate about the adoption of the guarantee contract in any financial transaction, owing to the existence of the fee element in the contract.¹⁰⁷ On the one hand, a number of classical Sharia scholars are of the view that charging a fee for a guarantee is not allowed, based on the argument that the contract is voluntary in nature.¹⁰⁸ On the other hand, some Sharia scholars recognize the need to allow it, based on the current needs of the community. They argued that receiving a premium in the form of fee in deposit insurance is indeed necessary as it is used to fund the operations of the IDIS. Beside reimbursing insured depositors in the event of failure, the fund is also needed to cover the deposit insurer's operating and development costs. Another justification of the need to collect premiums is that it is not feasible to develop an IDIS that is solely

103 "IADI | International Association of Deposit Insurers | Home.Html."

104 Different Persons Definition of Contract, <https://www.lawteacher.net/free-law-essays/contract-law/different-persons-definition-of-contract-law-essay.php> accessed on August 18, 2019.

105 IADI, "Shariah Approaches for the Implementation of Islamic Deposit Insurance Systems," *IADI Discussion Paper*, no. November (2014).

106 Nahar, "Insurance vs Takaful : Identical Sides of a Coin? ."

107 Zamir Iqbal, "Challenges Facing Islamic Financial Industry," n.d.

108 Iqbal.

financed by the government or by private funds.¹⁰⁹ Deposit protection, through blanket guarantee, could be costly for the government, which in turn would place a direct or indirect financial burden on the public.¹¹⁰

Another approach that can be adopted is the Combination of both the Government regulation and Contract. Under this mixed approach, the deposit insurer will first find the most suitable contract, which is the contract whose conditions match some or most of the deposit insurance operations.¹¹¹ Any aspect of operations that is not in line with the conditions will be addressed by the government regulation. For instance, in Sudan, the government has assessed and decided to adopt a *takaful* contract for its IDIS. As a *takaful* contract involves voluntary contributions or premium payments from the IBIs, the government could issue a regulation making premium payments mandatory.¹¹²

The Lacunae In The Provisions Of Ndic Act From The Sharia Perspective

Some of the provisions of the 2006 NDIC Act run in contrast to the rules governing Islamic banking. Some of these sections of the Act and the consequences are mentioned below:

Encouragement of Interest based Investment by the NDIC Act

Section 13(1) of NDIC 2006 Act empowers the Corporation to invest its funds in Federal Government securities. 1). The Corporation shall have power to invest money not immediately required in Federal Government Securities or in such other securities as the Board may from time to time determine”.¹¹³

The NDIC protects the Deposit Insurance Fund in safe but liquid financial instruments such as Treasury Bills, Federal Government Bonds and instruments of similar nature.¹¹⁴ This type of transactions and investments by the Corporation is not allowed by the Sharia as the investment in the Federal Government securities introduce elements of interest that go against the principles of Islamic Banking.

Penal Interest of Section 15 of NDIC Act, 2006 for Membership Defaulter

This section states that: 1). All licensed banks and such other financial institutions in Nigeria engaged in the business of receiving deposits shall be

109 Mher Mushtaq Hussain and Ahmad Tisman Pasha, “Conceptual and Operational Differences Between General Takaful and Conventional Insurance,” *Australian Journal of Business and Management Research* 01, no. 08 (2012): 23–28, <https://doi.org/10.52283/nswrca.ajbmr.20110108a03>.

110 IADI, “Shariah Approaches for the Implementation of Islamic Deposit Insurance Systems.”

111 Hamisu and Hassan, “Depositors Protection Scheme : Appraisal of Islamic Banks Participation in Deposit Insurance System Depositors Protection Scheme : Appraisal of Islamic Banks Participation In.”

112 ‘An Analysis of Islamic Takaful Insurance- A Cooperative Insurance Mechanism’ Pp. 109-132.

113 Section 13(1) of NDIC 2006 Act

114 “Page Not Found – NDIC,” accessed on December 3, 2021, <https://ndic.gov.ng/ndic-develops-framework-for-deposits-insurance-nidis-for-no-interest-bank-deposits/>.

required to insure their deposit liabilities with the Corporation. 2). Any licensed bank or such other deposit-taking financial institution which contravenes the provisions of subsection (1) of this section shall be guilty of offence and be liable to a maximum fine of ₦500, 000.00 for each day the offence is committed. 3). All principal officers of such licensed bank or deposit-taking financial institution which contravenes subsection (1) of this section commits an offence and is liable on conviction to a term of imprisonment for 3 years or a fine of not more than ₦5,000,000 (five million naira) or to both¹¹⁵ such fine and imprisonment.

Membership is compulsory under the Act, and an Islamic bank desirous of operating in Nigeria has no choice but to be a participant in the insurance scheme, a failure of which attracts penalty. This arrangement has been argued to breach the principle of *Al-Taawuni alal birri* (helping each other in good deeds).¹¹⁶ Islamic social relationship of *ta'awun* (mutual help or cooperation) and *tabarru'at* (willingly relinquishing individual right for collective benefits) are existing under willing and mutual agreement for cooperation towards achieving certain collective benefit without compulsion that can lead to a potential strain on the participating institutions.

Interest Charged On The Default Of Payment Of Premium Section 17, Subsection 7 Of The NDIC Act. This subsection provides that (7). Any premium payable by an insured institutions and which remains unpaid for more than three months after a demand notice had been served on such institution shall attract interest at a rate equivalent to the prevailing Minimum Rediscount rate (MRR) of the Central Bank of Nigeria.

In a situation where a bank fails to pay its annual premium at the prescribed time, interest is to be paid on the premium for the default. Prohibition of Interest in Islam is not only in respect of receiving it. Muslims are enjoined to move away from both collection and payment of interest. However, since membership in the NDIC has been made compulsory, any bank (including Islamic Banks) that fails to comply with the time stipulated for payment of premium would be penalized by paying Interest which Islam abhors. The Prophet (PBUH) has been reported to have condemned: 'the one who consumes *riba* (interest), the one who gives it to others, the one who writes it down and the one who witnesses it'.¹¹⁷

115 Hamisu and Hassan, "Depositors Protection Scheme : Appraisal of Islamic Banks Participation in Deposit Insurance System Depositors Protection Scheme : Appraisal of Islamic Banks Participation In."

116 'Islamic Banks' Participation in Deposit Insurance Scheme: A Legal Appraisal', 2011.

117 Sahih al-Muslim, Kitab Musaqaah.

Interest-based financial assistance Article 37(2)

Grant loan on such terms as may be agreed upon by the Corporation and the failing insured institution; b) Give guarantee for a loan taken by the insured institutions; c) Accept an accommodation bill with interest for a period not exceeding 90-day maturity exclusive of days of grace and subject to the renewals of not more than seven times. Provided that interest rates applicable to facilities extended to the failing institution shall not exceed the minimum Rediscount Rate of the Central Bank of Nigeria.

The pumping of money into ailing banks (including Islamic banks) performed by the NDIC is interest based. The liquidity support provided by the Corporation for financial institutions is interest-based, at the prevailing Minimum Rediscount Rate of the CBN.¹¹⁸ This practice is in open contradiction with the prohibition of interest in transaction under Islamic Law and the basis of the prohibition is the commandment of the Law-Giver where He says; 'O you who believe! Be afraid of Allah and give up what remains (due to you) from *riba* (from now onward), if you are really believers.' Failure to heed to this commandment attracts a promise of war against the practitioners by Allah and His messenger.¹¹⁹

The Distribution Of Profit Obtained From The Investment Of The Premium

The profit obtained from the investments of the premium is shared between the Federal Government of Nigeria and the NDIC without any share given to the banks who pay the money, and this runs contrary to the Islamic principle stating that '*there should be no infliction or reciprocation of harm*.' This arrangement sidelines the banks, which are the most important entities in the transaction and their depositors. This arrangement can be termed unjust, especially at instances where the Corporation accrues a large profit.

Because of the nature of Deposit Insurance Scheme in Nigeria, which is *Ex-Ante* (premium paid periodically in anticipation of a future banks' failure), banks are mandated to pay, and this is a continuous payment, regardless whether or not the envisaged event occurs in years. This means that the banks keep losing a part of their money without a trace or account or possibility of recovery. The financial institutions enjoy no plan for a plough back of the premium or even a premium holiday at some point, even when the financial institution does not show any sign of weakness or failure. This also breaches the Islamic social relationship of mutual help or cooperation and exempt the banks from the profit and loss

118 Umoh P.N, 'Bank Deposit Protection: The Nigerian Experience', P. 57, 2003.

119 Q.S. al-Baqarah [2]: 278-279.

sharing in the transaction.¹²⁰

Conclusion

The fundamental objective of all Islamic financial institutions is to offer Sharia-compliant transactions and activities in all of their dealings. A central tenet of this demands that they must be free of interest-based transactions and all other activities considered by Sharia as unlawful. This injunction by inference also applies to all other institutions that take part in direct transaction with Islamic financial institutions, for an example, being an agency that insures their customers' deposits.

It has been established that the Scheme is in line with Sharia. There are links that exist between NDIC and *Maqasid al-Sharia*, which is aimed at promoting benefits and repelling harms and *Maslahah*, which refers to something good for the public. Deposit insurance protects the public from losing money that they place in a bank when the bank fails. Its implementation is a noble initiative as it prevents the public from facing financial difficulties, especially for those who have limited financial resources and, as a result, could be exposed to social problems. Islam urges its followers to avoid poverty as this could lead them to disobey Allah. Islam always wishes every creature to have a good and convenient life without having to face any difficulty. It also urges its followers to prepare themselves to face any possible disasters, which includes finding a means to protect their wealth. As such, the setting-up of a deposit insurance system represents the Muslims' response to the urge to protect their money when a bank fails. Muslims are also urged to help each other in good deeds. In line with this principle, the government introduced deposit insurance as an initiative to assist the public in protecting their wealth. Such arrangements may also be made privately with the same intention of helping the public. Nevertheless, the principle of Sharia states that all transactions of Islamic financial institutions must be free of interest, uncertainty, gambling, and sale/purchase of unlawful goods and services.

In this research work, attempts have been made in examining the importance, the features, the operations as well as the permissibility of the Deposit Insurance Schemes. Distinctions were made between DIS and conventional Insurance, and similarities between the former and cooperative Insurance permitted under the Islamic law were highlighted. The research has shown the effectiveness and importance of the Deposit Insurance Scheme in the protection of depositors in many countries. The establishment of the Nigerian Deposit Insurance Corporation

120 'Insurance vs Takaful: identical sides of a coin?' P. 247.

has gone a long way in ensuring that depositors in financial institution do not suffer any kind of loss resulting from the failure of a bank and helps regulating and supervising the activities of these financial institutions when the need arises. The Corporation insures both conventional and Islamic banks in Nigeria, and a framework for Non-Interest Deposit Insurance scheme (NIDIS) has been developed to cater for Islamic Banking. However, based on the findings of this research work, it is concluded that although the aim and objectives of the NDIC is in line with the Sharia and so is permissible, Sharia-compliance hurdles still exist within the operation of the NDIC, preventing the full participation of Islamic Banks, and these hurdles are in form of Interest based earnings, liquidity support and penalty. This research concludes that NDIC operation, as the insurer of Islamic banks, is both constitutional and legal. This happens because it is set up by a legitimate government for the prosperity of the general public and to the advantage of Islamic banks. An approach to insuring Islamic bank is made through the regulation arranged by the government where there is no suitable DIS using Islamic contracts or one is yet to be developed due to constraints. This is the case found in the Nigeria system. Islamic banks will be vulnerable to distress if they don't participate and will also discourage the intending customers. This study therefore proffers the listed solutions and recommendations below to ensure that the operations of the NDIC is sharia-compliant. The recommendations (1) The Nigerian Deposit Insurance Corporation (NDIC) should target a benchmark on the amount in which a premium must reach and once this benchmark is reached, the profit generated from the investments of the premium paid by the Islamic banks may be shared among the premium payers and the NDIC. Islamic banks, as corporate institutions, are bound by the Islamic jurisprudential principle: 'there shall be neither harm nor reciprocating harm'; also, as much as Corporation stands for an equitable distribution of wealth and resources, they are equally and legally restrained from allowing any injustice targeted their shareholders who paid the premium. (2) A type of a premium tax holiday where Islamic banks do not pay premium for a certain number of years, in a situation where they do not experience failure for a specific period of time (10 years), should exist. The reasons behind this suggestion are the times where the banking system enjoys stability for a considerable length of time, the Corporation's fund is not used for the object of its creation, and a continued withholding of excessive liquidity after a while will amount to hoarding, which negates the principle of equitable distribution and circulation of resources. (a) There should be a profit and loss-sharing arrangement to prevent Interest-based operations. The sharia prohibits the collection and payment of

interest in any transaction, but the principle of sharing profit and loss is allowed in Islam. This can be done by introducing a *Mudarabah* arrangement with the insured banks in respect of invested funds. In this case, the Corporation's share of the accruing profit would be pre-agreed percentage and in case of loss, it bears no further responsibility than forfeiture of its managerial efforts and where the Corporation's funds form part of the investment fund. A *Musharakah* arrangement would be appropriate where both the Corporation and insured banks would share both the profit and loss. The former will be based on pre-agreed ratio, which may not necessarily follow the ratio of contribution while the latter will be shared based on the percentage of the partners' contribution to the fund. (b) The amendment of some sections of the NDIC Act (penal and interest-based dealings) are in line with certain principles of Sharia. The following Sections of the 2006 NDIC Act need amendments. Section 13(1) should be amended in a way that will involve investment of the Non-Interest Deposit Insurance Funds (NIDIF) in *Sukuk* bonds instead of Government Treasury bills, which is suitable for Deposit Insurance Fund (DIF) only. Section 15 should be amended in such a way that it will only make membership voluntary and not mandatory. Section 17(7) should include a proviso that will exempt Islamic banks from paying interest on default for the premium payment and to prescribe some other penalties. This reform will help reducing, if it cannot completely eliminate, the hindrances restraining Islamic banks from the full enjoyment of the operations of the NDIC. (c) The Nigerian Government should adopt an Islamic Deposit Insurance Scheme (IDIS) and efforts should be made for the establishment of a common ground within the administration of an Islamic Deposit Insurance (IDI) to minimize and eliminate disagreements, so a point of consensus under Sharia is achieved.

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