

ISLAMIC FINANCE IN INDIA: THE MISSING OPPORTUNITY

On January 5, 2010, in response to a PIL filed by Dr. Subramaniam Swamy, the High Court of Kerala granted a stay on the proposed activities of the Islamic Non-Banking Finance Company, Al-Barakah Financial Services Ltd. The NBFC in question has been co-promoted by state-owned Kerala State Industrial Corporation (KSIDC) and some businessmen belonging to different religious communities, including Hindus and Christians. The entity was aimed at mobilising much needed financial resources for the infrastructure development of the state of Kerala, which is poor in mineral and other resources required to develop the state into an industrial one. The feasibility study was conducted by a reputed international consulting firm. The consultant in its report on the feasibility of the venture from the legal angle, has also mentioned the existence of several RBI approved Islamic NBFCs in India, including one in Kerala. The only novel aspect about the present venture was participation of a state-owned economic entity (KSIDC) in the company - with a 11% stake. The remaining 89% or Rs. 89 crore was to be brought in by private businessmen, all Indian.

The presumptions made by the litigant are that the organization was (1) to be a banking organization, (2) to exclude non-Muslims, (3) to abuse provisions of the Indian Constitution granting the right to practice a religion of one's choice and (4) to function under an extra constitutional *Shariah* authority with supra regulatory powers.

It is very clear that Islamic Banking is not possible in India at the moment, unless certain changes are made in the regulation. This is also the crux of the Anand Sinha Committee of RBI, which was formulated to look at Islamic banking products in the Indian milieu.

It is understood that the proposed company itself never sought to project itself as a banking organization. Whatever reports that appeared in certain sections of the media describing it as an Islamic bank can hence be put down to either poor awareness of the technical differences between an NBFC and a bank or the common tendency to hype any news item relating to “Islamic Banking” on the part of sections of the media.

The allegations made by the plaintiff are:

- a. Order of state of Kerala allowing setting up of the financial company by KSIDC is a clear instance of the state favoring a particular religion.

- b. KSIDC identifies with Islam to the exclusion of all other religions.
- c. The actions mentioned above amount to the State promoting a particular religion.
- d. The company by adhering to *Shariah* rules prohibiting certain activities such as charging of interest and trading in alcohol, pork, and entertainment including cinema and music, which are legally permissible in India is going against the constitution.

The Honorable High Court of Kerala is seized of the matter with regard to the above. Further, the Court in its stay order (dated January 5, 2010) opined that the matter needs deeper deliberation and therefore, it (the Court) decided to include the Union of India and RBI as additional respondents in the matter. The matter is *sub judice* and therefore, any comment on the above would not be appropriate at the moment.

Dr. Swamy has also written critically on the same subject in a recent issue of *Organiser* (Vol. LXI, No. 28, New Delhi, January 17, 2010). While refraining from commenting on any aspects of the order of the Court, one can certainly analyze in a dispassionate and objective manner the issues raised by Dr. Subramaniam Swamy in his usual strident fashion in the article. The author writes:

1. **“An Islamic bank cannot charge interest, but then what does it do to survive? By giving by one hand, and taking away twice as much or more by the other hand!”**

It is well understood now that the essence of Islamic finance is relating returns from a business to its results. It is in this respect that Islamic finance differs fundamentally from conventional finance, wherein the operations are basically debt-driven and the returns fixed in advance, as the RBI committee Report too very clearly acknowledges. So Islamic finance does not need any creative accounting or duplicity to survive, as Mr. Swamy insinuates. In fact a large number of non-Muslims participate (even in India) in *Shariah*-compliant schemes. Surprisingly, some of these schemes have also been found to be among the best performing schemes in the market.

2. **Again Dr. Swamy writes: “...an Islamic bank is like a boiled ice cream; it cannot exist in real life without tricking our confidence”.**

It is amazing that he can make such a claim when one finds Islamic finance in operation in 75 countries across the globe, including many non-Islamic and secular countries. In secular countries with small Muslim minorities, such as UK, US, France, Germany, South Africa and India or Muslim countries with large non-Muslim minorities, such as Malaysia, one finds substantial non-Muslim

participation in Islamic finance institutions and schemes. Are the authorities in all these countries willing participants in a giant con operation being perpetrated on their gullible non-Muslim and Muslim citizens in the name of an alien religion. Dr. Swamy needs to answer that.

- 3. Mr. Swamy also asserts: “It is clear that Islamic bank or NBFC cannot be started in India without violating numerous laws and regulations”.**

As we have noted, Islamic banking is not possible in the current Indian regulation and that is the reason there is no Islamic bank functioning in India as yet. This does not however mean that the present situation needs necessarily to continue for all time in the future or that there is something in Islamic finance that is fundamentally against the Indian constitution. It is really a question of pragmatic economic policy of the country at a point in time. Till less than two decades ago private banks, private mutual funds, private insurance companies were all prohibited. There are however already many Islamic NBFCs working with full approval of RBI.

- 4. “Islamic banks will not be permitted by Sharia to give loans for liquor manufacture, cinema, hotel, entertainment industry, etc. These however are under current laws of India legitimate and legal activities.”**

When one refers to an Islamic NBFC (whether in the Indian context or anywhere else), it should be understood that the primary mandate the institution operates under is derived from the law of the land and not from Islam or the *Shariah*. It is also “Islamic” in the sense that it voluntarily binds itself to adhere to certain additional restrictions in its business operations, which Islam prescribes. Nor are the doors of such “Islamic finance” institutions closed to adherents of religions other than Islam or to atheists too for that matter. It can be no one’s case that a business has to necessarily enter all spheres of business to be in compliance with the constitution. Similarly, we need to make a difference between permissible and compulsory. Certain activities are no doubt permissible in the Indian legal system, but it is not compulsory that everyone must be engaged in these to adhere to the Indian Constitution. There are many states in India where alcohol is banned; it does not mean they are violating the Constitution. Secondly, many of the activities that the *Shariah* prohibits are accepted as harmful to society by a fairly sizable segment of secular civil society too.

- 5. Then we have Dr. Swamy spewing the usual BJP vitriol against the government for ‘appeasing’ Muslims. “Dr Manmohan Singh believes that Muslims must get first charge on our resources, they**

**are keeping silence, much as Bhisma and Drona kept quiet when Draupadi was disrobed”.
“...now patriots in Kerala must rise and protest to save Kerala from fast-creeping Islamisation. And
rest of India must help”.**

Arguments like the above put forth by the maverick politician are motivated and highly instigating in nature. The less said about them the better. It may perhaps be in the interest of KSIDC to adduce some of these writings of Dr. Swamy before the honorable court to put in perspective his motivations for filing the case.

It is unfortunate that an imaginative measure designed to draw funds into productive investment for the common good, from adherents of an excluded section of society (while keeping the measure equally accessible to other sections as well) is sought to be subtly and insidiously transformed and falsely portrayed by the plaintiff in the case as a question of favoritism to a particular faith.

Respondent	State of Kerala	R1
Respondent	Principle Secretary to Government (Kerala)	R2
Respondent	Kerala State Industrial Corporation (KSIDC)	R3
Respondent	Union of India (Through Ministry of Finance)	R4
Respondent	Reserve Bank of India	R5

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