



# Experience of Iran in Islamic Banking



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# Brief History of Banking in Iran



**Imperial Bank of Persia was established in 1888**

**Bank Sepah as the first Iranian bank was established in 1925**

**Bank Melli Iran (National Bank of Iran) was established in 1928 and functioned as Central Bank until 1960**

**Central Bank of Iran(CBI) was established in 1960 according to the Banking and Monetary Law**

**Total of 36 Banks (24 Commercial and 12 Specialized) with 8,275 branches operated until 1979 of which 4 were state owned and 32 were private banks**

**Nationalization of banking system after Islamic Revolution and amalgamation of banking system reduced the number of banks to 9 ( 6 commercial and 3 specialized) with 6,581 branches**



# Brief History of Banking in Iran



**Liberalization of Banking sector commenced in 2001**

**Currently Iranian banking system consists of Central Bank of Iran , 39 Banks and Non Bank Credit Institutions in 2019**

**All Iranian Banks listed on Tehran Stock Exchange (TSE) are also complying with the Securities Market Law of Iran and the regulations issued by Securities and Exchange Organization (SEO)**

**Financial Intelligence Unit (FIU) at Ministry of Economic Affairs and Finance to combat money laundering and financing of terrorism activities**



# Islamic Banking in Iran



**According to article 4 of Iran's Constitution, the Conventional Banking System had to be changed and transformed to comply with Islamic Sharia criteria.**



**Law for Usury (Interest) Free Banking was legislated by Iran's Parliament and approved by Foqaha (Islamic Scholars) of the Guardian Council responsible for checking the compatibility of all regulations and laws with Islamic criteria in 1983 and came to effect on March 1984.**

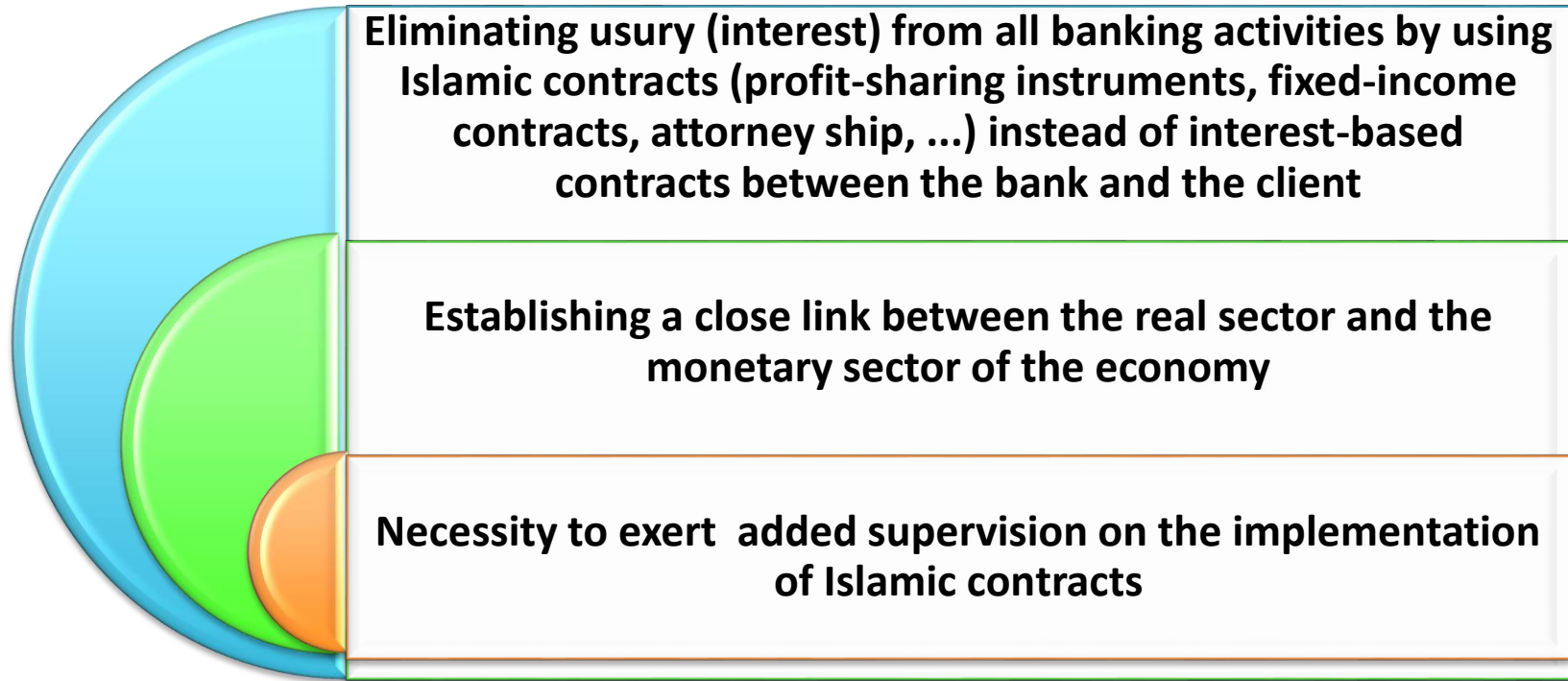
**For the first time in the world, Iran introduced a comprehensive and unified Interest Free Banking system and replaced the conventional banking practice in Iran.**



# Islamic Banking in Iran



The main characteristics of Iran's Usury-free Banking System are:





# Mobilization of Resources and Modes of Financing based on Usury Free Banking Act of Iran

## Mobilization of Resources:

### Gharz-al-hasaneh Deposits :

The relationship between the depositor and the bank is based on **Interest Free lending and borrowing**

- **Current Account**
- **Saving Account**

### Investment Deposits :

The relationship between the depositor and the bank is based on **Attorney Ship**

- **Short Term Deposit similar to a regular saving account in the conventional banking system, but without fixing the interest rate**
- **Long term Deposits ranging from 3 months to 5 years**
- **Special Purpose Deposits in terms of Profit Sharing Securities**



## Mobilization of Resources and Modes of Financing based on Usury Free Banking Act of Iran

**The main distinction between Iranian Islamic Banking and Conventional Banking is that the Rate of Return on Investment is not fixed :**

- **Applying Forecasted Rate of Return as Advance Rate**
- **Settlement of ultimate rate of return by applying the difference between real rate of return based on performance of the bank and the Advance Rate calculated on annual basis**



# Mobilization of Resources and Modes of Financing based on Usury Free Banking Act of Iran

## Modes of Financing based on Islamic contracts

- **Interest-Free Loans (Gharz-al-hasaneh)**
- **Fixed Income Contracts based on forecasted Rate of Return on underlying transactions**
  - Murabaha (installment sale)
  - Hire-purchase
  - Istisna
- **Profit/loss sharing modes of financing**
  - Civil partnership
  - Legal Partnership (equity participation)
  - Mudarabah
- **Direct Investment by banks**





## Calculation of the bank total Revenue and sharing it between Bank and Depositors

### ➤ Total revenue of the bank consists of:

- Fees and commissions (Non-joint income)
- Income from credit facilities granted (Joint income)

### ➤ Method of allocating income to the bank and depositors

- Dividing the joint income between the bank and depositors in proportion to the bank's own funds and the depositors' resources,
- Calculating the difference between ultimate and on account payment of interest to depositors and allocating the underpayment to them,
- The bank's share of joint income,
- Allocating 2.5% - 3% of the depositors' share of income to the bank,



## Challenges



**Difficulties in determination of the Fixed Income Contracts due to the current high rate of inflation in the Iranian economy**



**Supervision on execution and assuring timely repayment of projects which are financed by the bank on the basis of Partnership and Mudarabah**



**Interaction with other Islamic Banking systems around the world**



**Complicated Accounting System for calculation of real rate of return (ROR) on term deposits for the difference between ultimate and advance rate of return**



**Training of employees and educating clients**



**Thank you for your  
attention**