

Appendix -III

Framework of Rate of Return

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Bangladesh Bank

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1. Introduction

Islamic bank accepts Mudaraba deposits under the principle of Mudaraba in which the bank plays the role of entrepreneur (Mudarib) and the depositors as fund provider (Rabb al -Maal). Under this principle, profit accrued from investment and financing are shared between the Mudaraba depositors and the bank based on pre-agreed profit ratio. Losses, if any, will be borne by the depositors unless the loss is due to the negligence by the bank in managing the depositors' funds.

Given this unique relationship where the depositors would have a direct financial interest over the bank's income, a standard framework for calculation of rate of return is essential that depositors will receive their portion of the investment profits in a fair and equitable manner. The framework of rate of return should also be transparent, perceivable and address all necessary information. Towards these, Bangladesh Bank has prepared a framework of rate of return to standardize the method on the calculation of rate of return for the full-fledged Islamic Banks, Islamic Bank Subsidiaries and Islamic Branches of the Conventional Banks.

2. Objective

The objective of introducing the framework of rate of return is:

- i. To enable the banks under Islamic Shariah to follow the uniform standard in calculating the rate of return on Mudaraba deposits.
- ii. To clarify the different issues of profit calculation yardstick that often creates ambiguity amongst the Islamic banks.
- iii. To ensure the Mudaraba Depositors' interest that they are getting their portion of investment income in a fair and equitable manner.
- iv. To provide a basis for the new Islamic bank that could not yet develop such rate of return framework.
- v. To enable the Islamic bank to follow the Mudaraba principles on profit calculation for Mudaraba depositors as per Shariah requirement.

- vi. To ensure the better level of transparency as well as to disclose the Islamic banking operations.

3. Scope

This framework of rate of return on Mudaraba deposit is applicable to full-fledged Islamic Banks and Islamic Branches of the Conventional Banks licensed under Bank Companies Act 1991.

4. Principles

The following principles should be followed by the Islamic banks of all categories in distributing investment income to the Mudaraba depositors:

- i. Mudaraba depositors of the bank will share income derived from investment activities deploying the Mudaraba funds. Income Under this category will mean and include Profit, Dividend, Capital Gain, Rent, Exchange Gain and any other income derived from the deployment of fund.
- ii. Profit sharing ratio (PSR) between the Mudaraba deposits and the bank (Mudarib) should be declared before the starting of accounting year/at the time of Mudaraba contract and to be duly disclosed to the Mudaraba depositors.
- iii. The bank may reduce or raise the Profit Sharing Ratio before the starting of any accounting year/at the time of Mudaraba contract but cannot be reduced after the declaration is done for any accounting year.
- iv. The Gross Income derived from investments during the accounting year will, at first, be allocated to Mudaraba deposits, as per ratio of participating fund in the outstanding investment. If the Mudaraba deposits is higher than total outstanding investment, then participating ratio of Mudaraba deposits (as per Annexure-1) to be considered as 100 %. Profit on investment income to be distributed amongst the Mudaraba depositors as per pre-agreed ratio taking 100% as the participating fund in the total outstanding investment.
- v. Management fee and Investment Loss Off-Setting Reserve, if any, may be deducted from Mudaraba depositors' share of investment income subject to