

# **Islamic Financing Facility for Storage of Agricultural Produce (IFFSAP)**

## List of Abbreviations

<b>C&amp;F</b>	Cost and Freight
<b>IB</b>	Islamic Bank
<b>IBB</b>	Islamic Banking Branch
<b>IBI</b>	Islamic Banking Institution
<b>LC</b>	Letter of Credit
<b>SBP</b>	State Bank of Pakistan
<b>PIFI</b>	Participating Islamic Financial Institution
<b>SBP BSC</b>	State Bank of Pakistan Banking, Services Corporation
<b>SME</b>	Small and Medium Enterprises

## Key Terms and Definitions

**Customer:** The entity or person seeking or availing financing facility from the PIFI under the Islamic Financing Facility for Storage of Agricultural Produce.

**Facility:** Finance / mudarabah investment(s) provided by State Bank of Pakistan (SBP) under the scheme.

**General Pool:** General Pool means the Mudarabah-based pool of funds managed by the PIFI where funds of the majority of the depositors are invested /deployed.

**Grace Period:** A period at the beginning of the Mudarabah investment/financing during which only profit/rentals will be paid by customer. During this period SBP will not take back its investment from PIFIs.

**Islamic Bank (IB):** Full fledged Islamic commercial banks including Islamic banking subsidiaries of conventional banks.

**Islamic Banking Branches (IBB):** Designated Islamic banking branches of conventional banks established under IBD Circular No.02 of 2004.

**Islamic Banking Institutions (IBIs):** Full fledged Islamic commercial banks, Islamic banking subsidiaries of conventional banks and Islamic banking branches of conventional banks.

**Mudarabah Investment:** An investment made on the basis of mudarabah by SBP in the general pool of PIFI for the purpose of this scheme.

**Scheme:** Scheme will be a combined reference to the facility along with the regulatory instructions issued hereunder.

**SME Customers:** Refer to SME customers as defined in SBP Prudential Regulations for SME financing.

## **Islamic Financing Facility for Storage of Agricultural Produce (IFFSAP)**

The Islamic Financing Facility for Storage of Agricultural Produce (IFFSAP) is being offered to Islamic Banking Institutions (IBIs) and Islamic DFIs (collectively referred to as Participating Islamic Financial Institutions (PIFIs)). State Bank of Pakistan (SBP) shall make mudarabah investment with PIFIs under section 17 (6B) of the SBP Act, 1956 (the “SBP Act”). SBP will act as *Rab-ul-Maal* by providing mudarabah investment facility to the PIFIs, in the form of investment in the PIFI’s general pool, and the PIFI shall act as the *Mudarib* of general pool. The exposure of SBP under the scheme shall be on all assets of the PIFI’s general pool to the extent of SBP’s investment in general pool, and therefore shall not be limited to the assets financed under the scheme.

This document comprises of the following two main sections:

- 1) The Facility which is further divided into the following:
  - 1.1: Salient features containing details of the scheme pertaining to scope of the scheme, assigning financing limits to PIFIs, period of investment and payments, disbursement of funds from PIFI to customers and disclosure in annual audited accounts.
  - 1.2: Shari’ah structure of the facility discusses the disbursement of funds from SBP to PIFI under mudarabah, investments being part of the general pool of assets of PIFI, expected return on financing under the scheme and profit/loss allocation and distribution
- 2) Regulatory instructions which contain instructions of the State Bank of Pakistan for PIFI to follow under this scheme such as risk assessment, penalties and general terms & conditions

### **1. THE FACILITY:**

#### **1.1. Salient Features:**

##### **1.1.1. Scope of the Scheme:**

- i) The local currency financing shall be available on long-term basis for establishment, expansion and balancing, modernization & replacement (BMR) of Steel/ Metal / Concrete Silos, Warehouses & Cold Storage facilities for storing agricultural produce.
- ii) Financing facilities shall be available for:-
  - (a) Purchase of new imported & locally manufactured plant & machinery, equipments and accessories thereof, to be used in Steel/Metal/Concrete

Silos, Warehouses and Cold Storages. Detail of machinery is given in Annexure –I.

- (b) Purchase of new generators. The capacity of generator shall, however, not be in excess of in-house energy requirements of the Silos/Warehouses / Cold Storages.
  - (c) Up-to 65% cost of entire civil works.
- iii) Financing shall be available to the extent of C&F value/ex-factory/ showroom price of the new imported or locally manufactured plant, machinery, equipments and accessories thereof.

**1.1.2. Participating Islamic Financial Institutions (PIFIs):**

- i. All Islamic Banking Institutions (IBIs) including full-fledged Islamic banks, Islamic banking subsidiaries and Islamic banking branches of conventional banks and all DFIs having authorized Islamic financing operations (IDFIs) under permission of SBP (collectively referred to as PIFIs) may participate in the scheme by submitting an application to the concerned department of SBP.
- ii. Islamic banking branches of conventional banks / DFIs may participate in the scheme by applying to SBP for allocation of sub-limit, subject to a maximum of 20% of the parent bank's limit under the Financing Facility for Storage of Agriculture Produce, for utilization by Islamic banking branches under this scheme. SBP may consider request for enhancement of the ceiling of 20% on case-to-case basis depending upon the merit of each request and keeping in view size and operations of the Islamic banking business of the PIFIs.

**1.1.3. Assigning Financing Limits to PIFIs.**

- i) Yearly limits shall be allocated to individual PIFIs under the scheme.
- ii) The limits shall be allocated for each fiscal year from 1<sup>st</sup> July to 30<sup>th</sup> June, the utilization of which will be periodically reviewed. SBP may cancel the unutilized limit for reallocation to other PIFIs. No PIFI shall be authorized to sanction financing with a view to merely utilize the limit under the scheme.
- iii) Applications for sanction of limits for each fiscal year (July-June basis) shall be sent by the interested PIFIs to the concerned Department of SBP each year on such date and in such manner as may be advised by SBP from time to time.
- iv) After the sanction of limit by SBP, the PIFIs shall submit a duly executed agreement for availing the facility (as per prescribed format IFFSAP - 1), along with the names of the Offices of SBP BSC from where it intends to avail the facility.

- v) The funds made available under the scheme to PIFIs shall be provided by the designated offices of SBP BSC under the limits conveyed by the concerned department of SBP, Karachi in favor of each PIFI, on yearly basis.

#### **1.1.4. Period of Investment and Payments**

- i) Financing shall be available for a maximum period of seven years including a maximum grace period of up-to six months.
- ii) For SME customers (as defined in Prudential Regulations for SME financing) the financing shall be available for maximum period of ten years including grace period of up-to six months.
- iii) In case financing is provided on staggered basis, maximum period of financing shall start from the date of disbursement of 1<sup>st</sup> installment.
- iv) The retirement of financial obligations/redemption under the scheme shall be made by the customers in equal half yearly/quarterly installments depending upon the underlying mode of Islamic finance used by PIFI. PIFIs, however, shall not be permitted to require their customers to pay the profit/return/rental amounts at a frequency of less than three (03) months except at the time of early-payments/liquidation of financing.
- v) The Mudarabah Investment made with the PIFIs shall mature on the due date agreed with SBP, and SBP is authorized to deduct outstanding balance of its investment in the general pool as per "Instructions for Profit & Loss Distribution and Pool Management" for Islamic banking Institutions issued vide IBD circular No. 3 dated November 19, 2012, as amended from time to time.
- vi) In case a customer pays the financing amount or its installment, in part or in full, on or before the due date(s), SBP's share in the general pool will be redeemed equal to the payments received from customer. PIFIs shall adjust the financing amount so received from the customer by purchasing the SBP's proportionate share in the general pool immediately, but not later than three (03) working days, from the concerned Office of SBP BSC, failing which the SBP shall also be given the profit, as per the actual profit of the general pool, for the number of days this proportionate share is not purchased by the PIFI. However, no penalty shall be charged either from PIFI or its customer in case of payment of financing amount or installment, in part or in full, before due date.

#### **1.1.5. Disbursement of funds from PIFI to Customers:**

- i) The facilities shall be allowed against a single or multiple underlying transaction(s), designed on the basis of Islamic modes of financing, approved by the Shari'ah Board of the concerned PIFI. The modes of finance will include all those modes listed in Section E of Annexure I of IBD Circular No.02 of 2008, as amended from time to time; including combination of those Islamic modes of financing (Hybrid arrangements). In case of consortium/syndication, the whole process, starting

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from the structuring of the transaction till its completion, should be duly approved and monitored by Shari'ah Board/Shari'ah Committee formed for consortium/syndication.

- ii) PIFIs shall provide financing facilities to the prospective customers as per their financing policies duly approved by their Board of Directors and vetted by the Shariah Board of concerned PIFI. Further financing shall be subject to compliance with all rules and regulations including Prudential Regulations as prescribed by the State Bank from time to time.
- iii) PIFIs shall ensure that proceeds of financing are used exclusively for the intended purpose. They shall also ensure that customers have fulfilled pre-disbursement formalities, through due diligence as per their own internal arrangements to avoid malpractices and mis-utilization of funds under the scheme.
- iv) An entity being financed under the scheme should have minimum rating of 4 as per "SBP's Guidelines on Internal Credit Risk Rating Systems in Banks/DFIs" issued vide BSD Circular No.8, 2007. However, PIFI may relax this condition only for SME customers having clean e-CIB record, keeping in view PIFIs' own risk assessment policy duly approved by their Board of Directors and SBP Prudential Regulations for SME financing.
- v) PIFIs shall at all times remain within the limits assigned to them for disbursements / financing under the scheme in a given financial year. Facilities should not be sanctioned in favor of customers in anticipation of sanction of limits by the SBP.
- vi) Entire financing shall be subject to the adherence of all rules & regulations issued by SBP from time to time.
- vii) Disbursements by PIFIs should not be made to the customer directly; instead payments shall be made to the manufacturers / suppliers of plant & machinery.
- viii) PIFIs shall not take more than six weeks in evaluating an application for financing under the scheme from the date of receipt of complete information from the customer. Where the request is declined, the PIFI will explicitly apprise the prospective customers in writing, the reasons for rejecting the application.
- ix) Advance payment to the extent of 20% of the C&F value/ex-factory/ showroom price of imported or locally manufactured machinery can be made in terms of related underlying agreement by securing the PIFI's interest. In case of imported machinery, advance payment will be subject to compliance with the terms & conditions prescribed in FE Manual and instructions issued from time to time by SBP's Exchange Policy Department in this regard.
- x) The PIFI undertakes to intimate SBP promptly of any change in the position of any customer provided with finances by the PIFI under the scheme.

**1.1.6. Disclosure in Annual Audited Accounts:**

- i) The external auditors of the PIFI shall, during the course of annual audit, verify compliance of the PIFI with the terms and conditions of the scheme, specially relating to SBP's share in mudarabah investment, profit calculations and payments

made on SBP's mudarabah investment. A 'Certificate of Compliance' shall be issued to the PIFI and a copy thereof should be sent by PIFI to the concerned Department of SBP.

- ii) These facts shall be disclosed separately under appropriate heads, in the annual audited financial statements of the PIFI, the aggregate amount of mudarabah investment made by SBP in such PIFI, as may be outstanding and payable by it, on the date of the preparation of its financial statements.

## **1.2. Shari'ah Structure of the Facility:**

### **1.2.1. Disbursement of Funds from SBP to PIFI under Mudarabah:**

- i) After making disbursement(s) on account of the facility to the customer, the PIFI shall approach the concerned Office of SBP BSC for obtaining Mudarabah Investment to the extent of the amount disbursed/financed to the customer.
- ii) The SBP BSC office shall provide mudarabah investment on submission of duly filled in prescribed documents i.e. (a) Mudarabah Investment Request Form (IFFSAP – 2) (b) Debit Authority (IFFSAP – 3) (c) Copy of Demand Promissory Note by PIFI's customer (IFFSAP 4) (d) Financing Agreement between PIFI and customer (inclusive of redemption schedule) (e) Undertaking of the customer on the format (IFFSAP 5), (f) A copy of Internal Audit Certificate as per Para 2.3. (x) of the scheme, and (g) Any other document(s), as advised by SBP, from time to time.

### **1.2.2. Investments being Part of the General Pool of Assets of PIFI:**

The funds obtained from SBP shall be part of the PIFI's general pool and thus shall be subject to the risks and rewards of the pool's assets like other depositors of the pool.

### **1.2.3. Expected Return on Financing under the Scheme:**

- i) The expected rate of return on financing provided by the PIFI to its customer under the scheme may not exceed rates announced by SBP on similar refinance facilities. Further, SBP expects profit rates/return on its investment close to its return on such type of refinance facilities.
- ii) The expected rate of return on financing once fixed shall remain locked-in for the entire duration of the financing, provided that the customers continue to pay all scheduled amounts at the respective due dates.
- iii) In case the customer(s) fails to make payment of the amount of installment as per the original payment schedule, provisions of the late payments as stipulated in the underlying financing agreement with the customer shall apply for the overdue period besides taking other actions to recover the same as per PIFI's approved policies for recovery in similar cases.



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- iv) Where financing to a project is provided on staggered basis, each installment shall attract the expected rate of return applicable on the date of disbursement of installment by the PIFI.

#### **1.2.4. Profit/Loss Allocation and Distribution:**

- i) The SBP's investment in the general pool will be assigned profit sharing ratio and weightage keeping in view SBP's expected rate of return as well as PIFI's policy and practice for such type of depositors in the general pool; the weightage shall be used to calculate profits on the SBP investment.
- ii) At the end of every month, but not later than the 7<sup>th</sup> working day of the following month, after calculating the actual profit of the general pool by the PIFI, SBP's share of profit will be appropriated for credit into a separate non-remunerative account held with the PIFI. The profit accumulated in this account shall be transferred to SBP within 7 working days from the close of a calendar quarter. No profit shall accrue or be applicable on the amount standing to the credit of this non-remunerative account.
- iii) The determination of profit will be made in line with section 2 of "Instructions for Profit & Loss Distribution and Pool Management" for Islamic Banking Institutions (PIFIs) issued vide IBD Circular No.3 dated November 19, 2012, as amended from time to time.
- iv) **IFFSAP Reserve Fund – (RF-IFFSAP):** SBP shall create a Reserve Fund (RF) at SBP BSC from its share in profits of the scheme. If in any month, SBP's share in profit is more than the expected return; such excess profit shall be transferred to the RF-IFFSAP. The PIFIs shall advise the SBP BSC offices accordingly, within 7 working days of close of quarter, by issuing separate advices for transfer of profit amount into 'Profit Account', and for transfer of excess amount into 'IFFSAP Reserve Fund.'
- v) **Loss Sharing:** If at any time, the general pool of an PIFI suffers a loss, it shall be borne by all the depositors of the general pool, including SBP, to the extent of their respective ratios of investments in the general pool.

## **2. REGULATORY INSTRUCTIONS:**

### **2.1. Risk Assessment:**

- i) Each PIFI shall be required to have:
  - (a) Well defined policies and established procedures for appraisal of projects to be financed under the scheme, particularly with regard to their technical and financial viability.
  - (b) Robust internal controls to protect depositors'/rab-ul-maals' and PIFI's interest and to fulfill all requirements/conditions of project financing including collateral requirements to mitigate the risk of customers' failure to honor their commitments. The risk assessment policy should cover varying business

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requirements and provide well-defined methodologies for assessing the financial fitness of prospective customers.

- ii) PIFIs shall undertake necessary due diligence process as per their financing policies before sanctioning the financing facility under the scheme and ensure compliance with all applicable prudential regulations and SBP instructions. Further, in case of imported plant & machinery / raw material, PIFIs shall obtain satisfactory credit reports on suppliers & manufacturers of plant and machinery etc. as required under chapter XIII of Foreign Exchange Manual. Furthermore, the sanction/approval of the financing shall be linked to the risk profile of the potential customers as per PIFI's risk measurement / assessment policies.

## **2.2. Penalties:**

- i) SBP, in its capacity as the regulator, shall have the right to appoint an independent consultant to verify that the conditions of the scheme are properly fulfilled/complied with by PIFI. In case the report of the consultant points out irregularities on the part of the financing PIFI or the customer, SBP reserves the right to redeem the amount of mudarabah investment made with the PIFI along with penalty at the rate prescribed in sub Para (v) below including the cost of such verification.
- ii) It will be the responsibility of the PIFIs to secure their interest and the interest of depositors/investors in this regard, however, in no case fine imposed on PIFI due to PIFI's negligence shall be passed on to the customer. In case, any PIFI passes on the fine to the customer, the PIFI shall be under obligation to justify the same to ensure that the fine is not passed on to the customer merely on the strength of the action of SBP.
- iii) In case of delay in payment by the customer, the delay would trigger the collection of charity amount from the customer as per the undertaking given by the customer. Any charity amount collected by the PIFI from customers relating to the delay in payment of financing will be given by the PIFI to charity. Similarly, in case of delay, the PIFI shall also have the right to recourse to the security of the customer, where such risk management provisions have been adopted to recover the amounts due. In some mode of financing, the PIFI has a right to take additional amount in cases of delays and defaults as rent on un-purchased share in underlying asset. The same shall be approved by Shari'ah Board of PIFI.
- iv) The customers shall continue to remain liable for payment of fines / penalties on account of their non-compliance to the requirements of the scheme. Such fines/penalties as and when recovered, from the customers shall invariably be passed on to SBP by the concerned PIFI. The failure of the PIFIs on this account shall be construed as their non-compliance of the scheme, and would attract punitive measures as prescribed by SBP.
- v) In case of violation of the terms & conditions laid down in the scheme, the SBP shall reserve the right to impose & recover the fine/penalty at the rate of paisa 60 per day per Rs. 1,000/- or part thereof

**2.3. General Terms & Conditions:-**

- i) The PIFIs shall submit their operations/process manual of the scheme duly vetted by the Shariah Board of concerned PIFI, to the concerned department of SBP for information and review before launching the scheme and seeking of limits and shall also reasonably address the observations if any raised by the department.
- ii) The cost of takaful/ insurance, transit insurance/transit takaful shall not be financed under the facility.
- iii) The PIFIs shall ensure the correctness / evaluation of feasibility & cost estimates either through expertise available in-house or through an outside reputable consultant (either an individual or a firm) & place it on record.
- iv) Maximum financing of PIFIs to a single project shall not exceed Rs 500 million under the scheme. However, PIFIs may provide financing facilities over and above the said maximum limit from their own sources, keeping in view their internal policies.
- v) In case of financing requirements exceeding Rs 200 million, PIFIs are encouraged to provide finance under consortium arrangements.
- vi) In case SBP announces new rates on similar refinance facilities which are lower than the expected rate of return fixed by the PIFI for its existing customers, in terms of Para 1.2.3 (ii) of the scheme, then benefit will be passed on to the customers while keeping in view "Instructions for Profit & Loss Distribution and Pool Management" for Islamic banking Institutions issued vide IBD circular No. 3 dated November 19, 2012, as amended from time to time.
- vii) In case of financing for civil works, the PIFI concerned shall monitor as per its own mechanism that the funds are utilized strictly for the construction purpose as per approved plan. PIFIs may open an escrow account where customer's share is deposited for making matching disbursements for civil works.
- viii) Financing shall be available only against LCs in case of financing against imported plant & machinery / raw material to be used for construction of the Silos/Cold Storage.
- ix) In case of the import of plant & machinery/raw material for construction of the Silos/Cold Storage, the foreign currency required for making payment against LC, shall be purchased by the PIFI of the customer from the inter-bank market at prevailing rates. In case the machinery/raw material is to be imported under usance LC, both the customer and its PIFI(s) would ensure that they have made necessary arrangements to hedge their position against adverse exchange rate movements as per the Shariah compliant structure. The quantum of the financing amount in equivalent Pak rupees shall be determined on the basis of the rupee resources required for purchase of the foreign currency on the actual date of retirement of LC and shall be released in accordance with the payment terms.

- x) Mudarabah Investment shall be provided on the basis of certification by the Internal Audit of financing PIFI with regard to confirmation that the financing is within the terms and conditions laid down in the scheme. A copy of the said Internal Audit Certificate shall also be submitted to the concerned office of SBP BSC at the time of obtaining Mudaraba Investment.
- xi) Financing under the scheme shall be checked/verified by SBP's Banking Inspection Department (BID) during regular inspection of the PIFIs to ensure that the same has been allowed as per the terms and conditions of the scheme.
- xii) Financing shall not be available for the purpose of acquisition of land.
- xiii) Second-hand plant, machinery and equipment shall not be eligible under the scheme.
- xiv) All LCs (sight as well usance) established after announcement of the scheme shall be eligible for financing.

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**Annexure – I**

**List of Plant & Machinery used in Silos**

Plants & machinery for Silos also includes Loaders & Un-loaders, Portal Cranes, Conveyors (Belt and Chain), Elevators, In-line weighing machines, Dryers, Grain/Rice Cleaning and Sorting Equipment, Bagging Machines, Weighbridges, temperature control equipments.