



Islamic SME Asaan Finance (I-SAAF) Scheme

Infrastructure, Housing & SME Finance Department

STATE BANK OF PAKISTAN

List of Abbreviations

IB	Islamic Bank
IBB	Islamic Banking Branch of Conventional Bank
IBI	Islamic Banking Institution
PIBI	Participating Islamic Banking Institution
SBP	State Bank of Pakistan
SBP BSC	State Bank of Pakistan Banking Services Corporation
SME	Small and Medium Enterprise
I-SAAF	Islamic SME Asaan Finance

Key Terms and Definitions

Customer: The entity or person seeking or availing financing facility from the Participating Islamic Banking Institution (PIBI) under the Islamic SME Asaan Finance (I-SAAF) Scheme.

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 Participating Islamic Banking Institution (PIBI) where funds of the majority of the depositors are invested/ deployed.

Islamic Banks (IBs): Full-fledged Islamic commercial banks including Islamic banking subsidiaries of conventional banks.

Islamic Banking Branches (IBBs): Designated Islamic banking branches of conventional banks.

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 IBIs for the purpose of this scheme.

Participating Islamic Banking Institution (PIBI): PIBIs (IBs and IBBs) approved by SBP to participate in the scheme.

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

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

Islamic SME Asaan Finance (I-SAAF) Scheme

Access to finance can play an important role in development of Small and Medium Enterprises (SMEs) sector. In order to overcome the inherent structural deficiencies in SME lending like asymmetry of information, lack of collateral, high delivery costs etc., State Bank of Pakistan (SBP) is offering a SME Asaan Finance (SAAF) scheme. Moreover, the Shariah compliant alternate i.e. Islamic SME Asaan Finance (I-SAAF) scheme has also been offered to Islamic Banking Institutions (IBIs) and referred to as Participating Islamic Banking Institutions (PIBIs) under the scheme. SBP shall make Mudarabah investment in IBIs 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 PIBIs, in the form of investment in IBI's general pool, and the IBI shall act as the Mudarib of general pool. The exposure of SBP under the scheme shall be on all assets of an IBI'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** contains details of the scheme viz. scope and eligibility criteria, period of investment and payments, assigning financing limits for PIBIs, disbursement of funds from PIBIs to customers and disclosure in annual audited accounts.
This section also covers the Shariah structure of the facility which discusses the disbursement of funds from SBP to PIBIs under Mudarabah, investments being part of the general pool of assets of PIBIs, expected rate of return on financing under the scheme and profit/ loss allocation & distribution.
- 2. Regulatory instructions**, which contain instructions of the SBP for PIBIs to follow under this scheme such as risk assessment, penalties and general terms and conditions.

1. The Facility

1.1. Scope and Eligibility

- i. All SMEs (new businesses as well as operative businesses) that are new borrowers of a PIBI will be eligible; an SME can avail this facility from only one bank.
- ii. The PIBIs shall provide local currency finance for all types of financing i.e. term financing as well as working capital/running finance.
- iii. Maximum financing limit for single SME is capped at Rs 10 million.
- iv. Maximum tenor of financing extended to the customer will be as per terms & conditions of financing facility approved by the PIBI. The financing will be repaid on due dates agreed between the PIBI and the customer

- v. The PIBIs will approve the borrowing limits of eligible customers (SMEs) keeping in view their credit requirements, cash flows, repayment capacity and risk profile.

1.2. Participating Islamic Banking Institutions (PIBIs)

All PIBIs including full-fledged Islamic banks and Islamic banking subsidiaries under permission of SBP (collectively referred to as PIBIs) may participate in the scheme by submitting an Expression of Interest (EOI) as announced by SBP for granting the status of PIBI. However, in case a conventional bank also having IBBs is selected under the scheme then it can disburse available refinance limit, as per its discretion, through its conventional and IBB network.

1.3. Assigning Financing Limits for PIBIs

- i. SBP will allocate refinance limits to the selected PIBIs equal to the bids quoted by them under the scheme.
- ii. After the allocation of limit by SBP, PIBI shall submit application along with duly executed agreement for availing the facility (as per prescribed format I-SAAF -1) and I-SAAF 1 - Annex) from SBP BSC Karachi Office.

1.4. Period of Investment and Payments

- i. The retirement of financial obligations/ redemption under the scheme shall be made by the customers from the date depending upon the tenure for which the facility is availed and underlying mode of Islamic finance used by PIBIs.
- ii. The Mudarabah investment made with the PIBIs 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.

1.5. Disbursement of Funds from PIBIs to Customers

- i. The financing shall be allowed against a single or multiple underlying transaction(s), designed on the basis of Islamic modes of financing, approved by the Shariah Board of the concerned PIBI. 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).
- ii. The PIBIs shall undertake due diligence process in accordance with their respective financing policies before sanctioning the facility subject to Prudential Regulations for SME financing.
- iii. The PIBIs shall reasonably ensure fulfillment of the pre-disbursement formalities by the customers through due diligence in accordance with their own internal arrangements to avoid mis-utilization of the facility through over invoicing, etc. while extending financing facilities to the customers.

- iv. In case of purchase of plant and machinery under term financing, disbursement by PIBI will not be made to the customers directly. In such cases, payments will be made to the suppliers of the plant and machinery to the customers.

1.6. Disclosure in Annual Audited Accounts

- i. The external auditors of the PIBIs shall, during the course of annual audit, verify compliance of the PIBIs with the terms and conditions of the scheme, especially 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 concerned PIBI and a copy thereof should be sent by PIBIs to the SBP (concerned department).
- ii. The above facts shall be disclosed separately under appropriate heads, in the annual audited financial statements of the PIBIs.

1.7. Shariah Structure of the Facility

1.7.1. Disbursement of Funds from SBP to PIBIs under Mudarabah

- i. After making disbursement(s) on account of the facility to the customer, the PIBI shall approach SBP BSC Karachi Office for obtaining Mudarabah investment to the extent of the amount disbursed/ financed to the customer. Section 2.2 may be referred for details.
- ii. The SBP BSC Karachi Office shall provide Mudarabah investment to PIBI on submission of following duly filled in prescribed documents
 - a. Mudarabah Investment Request Form (I-SAAF –2)
 - b. Debit Authority (I-SAAF –3)
 - c. Copy of Demand Promissory Note by PIBI (I-SAAF –4)
 - d. Undertaking of the SME customer on the format (I-SAAF-5)
 - e. Any other document(s), advised by SBP, from time to time.

1.7.2. Investments being Part of the General Pool of Assets of PIBIs

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

1.7.3. Expected Return on Financing under the scheme

- i. The expected rate of return on financing provided by the PIBI 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. 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 its approved policies for recovery in similar cases.

1.7.4. Allocation and Distribution of Profit / Loss

- 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 PIBI's policy and practice for such type of depositors in the general pool. Such weightages shall be used to calculate profits on SBP investments.
- ii. At the end of every month, but not later than the 7th working day of the following month, after calculation of the actual profit of the general pool by the PIBI, SBP's share of profit will be appropriated for credit into a separate non-remunerative account held with the PIBI. The profit accumulated in this account shall be transferred to SBP within 7 working days from the close of each calendar quarter. No profit shall accrue or be applicable on the amount standing to the credit of reserve 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 (IBIs)" issued vide IBD Circular No. 3 dated November 19, 2012, as amended from time to time.

1.7.5. I-SAAF Reserve Fund (RF- I-SAAF)

- i. SBP shall create a Reserve Fund (RF) at SBP BSC Karachi Office 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- I-SAAF. The PIBIs shall advise SBP BSC Karachi Office 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 'RF- I-SAAF'.

1.7.6. Loss Sharing

- i. If at any time the general pool of a PIBI 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.
- ii. The PIBI will be responsible for any loss incurred to SBP under this facility, if the said loss is subsequently proven to have been caused on account of negligence/mis-statement and/or misrepresentation, on the part of PIBI, as determined by internal auditor, external auditor and/or SBP onsite inspection team.

2. Regulatory Instructions

2.1. Risk Assessment

- i. Each PIBI 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-maal' and PIBI's interest and to fulfill all requirements/ conditions of project financing. The risk assessment policy should cover varying business requirements and provide well-defined methodologies for assessing the financial fitness of prospective customers.
- ii. PIBIs 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.
- iii. Financing under the scheme shall be checked/ verified by onsite inspection teams of SBP during inspection of the PIBIs to ensure that the same have been allowed as per the terms and conditions of the scheme.

2.2. Methodology of Refinancing and Repayment

2.2.1. Allocation of Refinance Limits

SBP will allocate refinance limits to the selected PIBIs equal to the bids quoted by them under the scheme.

2.2.2. Grant of Refinance

- i. SBP will provide refinance for three years from the launch date of the scheme to the PIBIs selected through a transparent bidding process.
- ii. Refinance shall be provided to PIBIs by SBP BSC, Karachi Office on submission of refinance documents. SBP BSC, Karachi will provide refinance within two working days of receipt of complete information as required.
- iii. PIBIs will submit, on each Tuesday of the week, to SBP BSC, Karachi Office, average weekly portfolio outstanding position, in preceding week, calculated on daily product basis.
- iv. SBP BSC, Karachi Office, based on average weekly portfolio outstanding position, submitted by each PIBI, will provide refinance to PIBI on weekly basis within two working days after receiving refinance request, provided the portfolio has increased on week-on-week basis. Whereas, the PIBI will be required to repay, within two working days of each Tuesday, any excess outstanding refinance availed, provided the portfolio has decreased, on week-on-week basis.
- v. Any delays, exceeding two weeks, in disbursement of refinance amount to the PIBIs due to administrative reasons, will be compensated vide extension of corresponding number of days in repayment of such refinanced amount.

2.2.3. Repayment of Refinance

- i. The refinance granted by SBP BSC, Karachi Office to the participating banks will be recovered on due dates as reported to the Karachi office from the accounts of the banks maintained with SBP BSC, Karachi Office.
- ii. After 3 years, the refinance will be repayable by banks in 10 equal yearly instalments.
- iii. The PIBIs, in subsequent ten years available for repayment of the refinanced amount, will be permitted to retain the amount arising due to early repayments made by the borrowers, subject to condition that such PIBI disburses incremental finance to existing SME borrowers or to new SME borrowers. The incremental finance should be at least equivalent to an amount such that aggregate portfolio in relevant year, on daily product basis, continues to remain at least equal to expected portfolio outstanding amount for that year end. An illustrative example is placed at **Appendix-I**.

2.3. Guarantee/Risk Coverage

- i. Under the scheme, the Government of Pakistan will provide first loss portfolio level risk coverage of 40% to 60% on following portfolio categories:

Portfolio Category	Risk Coverage
Financing facility of up to Rs 4 million	60 percent
Financing facility exceeding Rs 4 million and up to Rs 7 million	50 percent
Financing facility exceeding Rs 7 million and up to Rs 10 million	40 percent

- ii. The risk sharing will be synchronized with the classification and provisioning criteria of SBP prescribed under Prudential Regulations for Small & Medium Enterprise Financing to ensure that the profit & loss account of PIBI is not affected as far as infections remain below risk coverage levels.
- iii. The guarantee/risk sharing will be applicable on financing disbursed under this scheme during the first three years. The validity of the guarantee/risk sharing facility will, however, come to an end after four years of the initiation of the scheme. The last payment under the risk sharing facility will be made for infections recognized at the end of last quarter of fourth year.
- iv. The risk coverage, at prescribed percentages, will be available separately for each portfolio category and appropriation of residual risk coverage from one portfolio category to another will not be permissible.
- v. Placement of each financing facility in respective category of risk coverage will be determined on the basis of approved limit of the borrower. Therefore, disbursement amount below approved limit or any subsequent reduction in the outstanding amount

of the financing facility would not result in movement of financing from one portfolio category to another portfolio category.

- vi. The PIBI, at each quarter end, will lodge their claims with Development Finance Support Department (DFSD), SBP BSC Karachi within 15 working days at the end of each quarter. The submitted claim should be equivalent to an amount of their financing loss provision against financing classified as non-performing on objective basis in terms of Prudential Regulations for Small & Medium Enterprise Financing. The reimbursement against lodged claims will be made by DFSD within 15 working days from available government funds to ensure that there is no adverse impact on the profit & loss statement of the bank due to portfolio losses guaranteed under the scheme.
- vii. All claims, prior to submission to the DFSD, should be duly vetted by internal audit department of participating bank. DFSD will release payment against the audited lodged claim. SBP may conduct inspection of lodged claims on sampling basis.
- viii. The PIBIs will not write-off any financing for a period of seven years from receipt of claim against such financing under risk coverage facility. The PIBIs will undertake to make all reasonable efforts to continue recovery efforts against the non- performing financing.

2.4. Penalties

- i. Financing under the scheme may be checked by SBP during onsite inspection of the bank to ensure that the same has been allowed as per the terms and conditions of the scheme.
- ii. 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 PIBI.
- iii. In case the report of the consultant points out the irregularities (such as over invoicing, ineligible sectors (other than SME or non Shariah compliant sectors) on the part of the financing PIBI or the customer, SBP reserves the right to redeem the amount of Mudarabah investment made with the PIBI along with penalty at the rate prescribed in sub clause 2.4 (vi) below including the cost of such verification.
- iv. It will be the responsibility of the PIBIs to secure their interest and the interest of depositors/ investors in this regard. However, in no case fine imposed on PIBI due to its negligence shall be passed on to the customer. In case, any PIBI passes on the fine to the customer, the PIBI 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.
- v. Notwithstanding anything contained in clauses 2.4 (i, ii & iii) above, 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 PIBIs from customers relating to the delay in payment of financing will be given by the PIBIs to charity. In some modes of financing, the PIBIs have 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 Shariah Boards of PIBIs.

- vi. The customers shall continue to remain liable for payment of fines/ penalties on account of their non-performance/ 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 PIBI. The failure of the PIBIs on this account shall be construed as their non-compliance of the scheme, and would attract punitive measures as prescribed by SBP.
- vii. 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. 1000/- or part thereof including the cost of verification as stated in sub-clauses 2.4 (i & ii) above.

2.5. General Terms and Conditions

- i. PIBIs shall ensure that financing under the scheme is extended only to meet the business needs of the customers.
- ii. PIBIs shall submit their operations/ process manual of the scheme to the concerned department of SBP for information and review before launching the scheme and shall reasonably address the observations, if any, raised by the department.
- iii. The cost of takaful/ insurance, transit insurance/ transit takaful and other incidentals shall not be financed under the scheme.
- iv. Financing under the scheme may be checked by SBP during onsite inspection of the PIBI to ensure that the same has been allowed as per the terms and conditions of the scheme.
- v. PIBIs shall ensure to immediately pay back any amount disbursed by SBP under guarantee / risk coverage, if SBP subsequently concludes that such claim made under guarantee / risk coverage was wrongfully claimed. PIBI will also pay fine on such amount as may be announced by the SBP from time to time, for the period for which such amount is availed by the PIBIs.
- vi. If any question arises with regard to interpretation of any instructions of the scheme, the decision of SBP shall be final.

APPENDIX-I

Illustrative Example

The refinance will be provided for the financing disbursed during first three years of the scheme. After three years, the banks will repay the refinance in ten equal yearly instalments. The banks, in

subsequent ten years, will be permitted to retain the amount arising due to early repayments made by the SME customers, subject to condition that such bank disburses incremental financing to existing SME customers or to new SME customers. The incremental financing should be at least equivalent to an amount such that aggregate portfolio in relevant year, on daily product basis, continues to remain at least equal to expected portfolio outstanding amount for that year end.

Example: Bank 'A' launches the scheme on January 01, 2021 and builds a portfolio of PKR 50 billion up to expiry of the scheme after three years on December 31, 2023. The amount of PKR 50 billion will be locked for repayment in ten equal annual installments for the bank 'A'. Therefore, bank 'A' will make first repayment of PKR 5 billion on December 31, 2024 and thereafter it will make repayment of remaining annual installments of PKR 5 billion on December 31 (or last working day) of each subsequent nine years. The last installment will be repaid on December, 2033.

Particulars	1	2	3	4	5	6	7	8	9	10
	Dec-24	Dec-25	Dec-26	Dec-27	Dec-28	Dec-29	Dec-30	Dec-31	Dec-32	Dec-33
Repayment	(5)	(5)	(5)	(5)	(5)	(5)	(5)	(5)	(5)	(5)
O/s portfolio	45	40	35	30	25	20	15	10	5	-

Accelerated Repayment Due to Early Repayments in Portfolio - The bank 'A', in 2025, witnesses early repayments in the portfolio build under the scheme and at December 31, 2025 the aggregate portfolio, on daily product basis, drops to PKR 34 billion; moreover, bank 'A' was also unable to make incremental financing to existing SME customers of portfolio or new SME customers. In such case, bank 'A' will be required to make repayment of PKR 11 billion on December 31, 2025 vis-à-vis scheduled repayment of annual installment of PKR 5 billion [i.e. scheduled repayment of PKR 5 billion plus accelerated repayment of PKR 6 billion due to early repayments in the portfolio].

Standard Repayments Due to Incremental financing to SME Customers - Whereas, in the event portfolio although witnesses early repayments during 2025; however, bank 'A' disburses additional financing to existing SME customers of the portfolio or to new SME customers and resultantly the aggregate portfolio of 2025, on daily product basis, continues to remain in excess of PKR 40 billion [i.e. minimum expected outstanding amount for December 31, 2025]; in case such Bank 'A' will continue to make repayment of scheduled annual installment of PKR 5 billion.
