DEVELOPMENTS OF NEW INTEREST – FREE BANKING INSTRUMENTS IN TURKISH PARTICIPATION BANKING SECTOR

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SOSYAL BİLİMLER ENSTİTÜSÜ
BANKACILIK VE FİNANS YÜKSEK LİSANS PROGRAMI

TEZ DANIŞMANI: SELAHATTİN SERBEST
2013

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TÜRK KATILIM BANKACILIĞI SEKTÖRÜNDE YENİ FAİZSİZ BANKACILIK ÜRÜNLERİNİN GELİŞİMİ

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Toplam Sayfa Sayısı:

Anahtar Kelimeler (Türkçe)	Anahtar Kelimeler (İngilizce)
1) Katılım Bankası	1) Participation Bank
2) İslami Bankacılık	2) Islamic Banking
3) Faizsiz Bankacılık	3) Interest – Free Banking
4) Sukuk	4) Sukuk

ÖZET

Bu tez genel olarak Türkiyede faizsiz bankacılık sisteminin Türk bankacılık sektörüne girişi ve sistemin kendi içerisindeki ihtiyaçları ve büyüme potansiyeli doğrultusunda geçmişten günümüze bu sisteme dahil olan yeni faizsiz bankacılık ürünlerinin gelişimi ve bu ürünlerin içeriği ile ilgili bilgiler vermektedir. Çalışmam da öncelikle Dünyada faizsiz bankacılık sisteminin doğuşu ile ilgili bilgiler verdim ve küreselleşen ekonomi doğrultusunda bu sistemin Türkiye ye gelişini ve Türkiye deki gelişimini aktarmaya çalıştım. Bu çalışmada hangi yeni faizsiz bankacılık ürünlerinin sisteme dahil olduğunu ve faizsiz bankacılık sisteminin ürettiği yeni faizsiz bankacılık ürünleri ile müşterilerinin hangi ihtiyaçlarına, nasıl cevap verdiğini aktarmaya çalışacağız. Son yıllarda yeni bir faizsiz bankacılık ürünü olarak sisteme katılan ve faizsiz bankacılık sisteminin geliştirdiği en önemli ve yeni enstrümanlarından biri diyebileceğimiz. Sukuk' un Dünya ve Türkiyede ki işleyişi üzerinde detaylı bir şekilde duracağız. Sonuç olarak Türkiyede faizsiz bankacılık sisteminin - üretilen ve sektöre dahil olan yeni bankacılık enstrumanlarının da etkisi ile- büyüme rakamlarından bahsedeceğiz.

ABSTRACT

This thesis contains information about inclusion of interest free banking system into Turkish banking system in Turkey and development of the needs of the system and the new interest free banking products that have been included into this system from past to present in accordance with the development potential and scope of these products. In my study, initially I give information about the birth of interest free banking system in the world and try to present the entrance and development of the system in Turkey according to the globalizing economy. In this study, we try to explain interest free banking products that are included into the system and how and what kind of customers needs are met through the new interest free banking products of interest free banking system. We emphasize in details the world and Turkey applications of Sukuk which can be assumed as one of the most important and new instrument that interest free banking system developed and which is included in the system recently as a new interest free banking product. In conclusion, we present growth figures of interest free banking system in Turkey under the influence of new banking instruments that are produced and included into the system.

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1. INTRUDUCTION

With its root getting at the beginning of the human history, borrowing at first stage occurred among people and afterwards it was fully institutionalized and turned to a function –a very important function- of the banks. At first, banks were helping for the borrowing action of people then they developed and diversified their function. Banks laid hands on many different fields; they stepped in not only fund collecting and allocating activities but also mediating for payments, insurance, keeping various goods and carrying out the statistical policies activities that can be considered as typical activities of banks.

When the subject is bank, it is the interest that is remembered at first place. For typical description, bank is the corporation that collects deposit and gives interest, in return grants loan and charges interest. Interest free banking and interest free banks that we hear much about lately have eliminated the close relationship between banks and interest. Rapidly developing and globalizing world has quickly improved itself, -as it always has- in the field of interest free banking system as well and made great steps in integrating the financial products and interest free systems for the financial needs of those who are sensitive.

While the banks that apply interest free banking system are on the one hand trying to present the common products with interest as interest free, on the other hand to get a slice of the cake conventional banks whose function is interest has created their interest free banking departments and with the certificates they obtained they provided interest free banking service and varied the customer groups.

At our study, we emphasize the birth of the interest free banking system, the processes it has gone though from its birth up today, within this process, the progress of the various new interest free banking products and their participation to the system and functioning of these products.

2. LITERATURE REVIEW

We benefited from various sources about the birth of participation banking and its history, the functioning of the participation banking in Turkey and the progress of the participation banking products. Besides, this study generally shows us that the products of conventional banking system can be adapted to the participation banking and interest free banking systems and they can also be practiced within the interest free system.

For general comprehension of the topic, Doç. Dr. Mustafa Uçar's ' " Türkiye de – Dünyada Faizsiz Bankacılık ve Hesap Sistemleri ", Yrd. Doc. Dr. Halil İbrahim Bulut, Reseach Assisstant Bünyamin Er's "Finansal yenilik ve Açılımları ile Katılım Bankacılığı " , Sabri Ulus "Katılım Bankaları ve Enstrümanları Yurt Dışı Uygulamaları " and various other books and internet sources are used in order to have a comprehensive view about the topic.

Participation banking documents of the Participation Banks Association of Turkey, articles regarding the participation banking at the archive of the Participation Banks Association of Turkey, information and documents regarding the participation banking products of the participation banks on their own web sites constituted great sources to our study. We also benefited from the current documents of participation banking department of Kuveyt Türk Participation Bank about the syndication transactions of the participation banks, Bahrain credits, Saudi Export Program (SEP) credits and structured finance studies.

While presenting 'Sukuk' which is a new product of participation banking and which we think will be very popular for many years, we benefited from the website information of Fitch Ratings and the study of Orhan Ozaydın named “ Bir Finans Enstrümanı olarak Sukuk’ un Uluslararası Piyasalardaki Yeri ve Türkiye ye kazandıracağı katma değer “ .

3. INTEREST FREE BANKING (PARTICIPATION BANKING) CONCEPT, THE BIRT OF THE SYSTEM AND ITS HYSTORICAL PROGRESS

3.1. Interest Free Banking (Participation Banking) Concept

Participation banking is called as 'Islamic Banking' worldwide. But 'interest free banking' is one of the other general term for the system. The term of 'Interest free banking' contains and refers to a wider range of definition when compare to the terms of Islamic Banking or Islam Banking. The term called as 'Islamic Banking' worldwide is defined as Participation Banking in Turkey.

The core of the interest free or Participation banking system is the meeting point of labor and capital. The system on the one hand collects the deposits of the labor owners and on the other hand gives these funds as capitals to the real sector in order to be used as the finance of real trades and the profit of this business partnership is shared among the bank and equivalents. The originate of the term 'Partnership' comes from the principle of bank's participation to the 'profit' or 'deficit'. The principle of interest free banking is partnership so in the system the results and amount of the profit is not certain for equivalents as it is for conventional banking system. Even it was certain the name of it would not be profit but interest. In this system, certain profit of the performed trade is not promised as it is promised in conventional banking system, the result may be loss as well. According to Saudi Arabian Monetary Agency(SAMA) definition for interest free banking; the corporation that performs the bank administration within the scope of the principles that Islamism lays down and confirms.(Islamic Conference Held in Riyad, 1980)

3.2. The Reasons for the Birth of Interest Free Banking System

Many economic and social corporation results from the obligation and direction of the society. One of the main factors that enabled to birth of the economic and social corporation of interest free banking is the needs of the society. We can group the needs that brought out the Interest Free Banking system in 3 main heading; religious, social and economical reasons.

Human being is made of not only body he also has spiritual part. Throughout history, religious believes of people made them turn to many different activities in their behavior and attitude and for their believes people went towards the pursuit and integration of any system. Islamism objects to interest and it led the Islamic geography and the people that live in this geography to a thought to establish a new system in accordance with Islamism. And this is the religious aspect of the birth of interest free banking system.

Society consists of individuals. And individuals are not equal but they have many different classes. Some of them are poor, some of them are provincial and some of them are rural. To establish a social peace in a society, good relationship among these classes is necessary. And the very first thing that must be applied to establish good relationship among these classes is to eliminate the gap between poor and rich classes. Within this concept, interest free banking or interest free system is a corporation that eliminates the rich to become richer owing to interest. As partnership is the dominant factor of interest free banking system there is no philosophy as ‘you work I get’ and this leads society one step forward to the social peace. (Uçar, 1987)

Thanks to its unique project based studies, interest free banking system helps to presents new employment opportunities and it plays a systematic role in the society.

When we look at another reason as economic reasons for the birth of interest free banking system we can say that interest free banking fills a very important gap in terms of economy. Interest free banking system plays a really important role in terms of including the under-the-mattress savings of those who are sensitive to interest system. It is greatly important to integrate these idle savings to the financial system through interest free banking system for economic growth and development.

3.3. Historical Progress of Interest Free Banking

The history of interest free crediting gets at the beginning of human history. Because people give and lend money to each other on condition that the

money is paid back. These debt were the same things in the beginning but with the invention of money debts turned to be cash money. When historical progress of banking is examined, it can be understood that almost all credit corporations worked interest free or aimed at working interest free when they first established.

The history of interest free banking goes to the years 2123-2081B.C. the reign of Hammurabi. The first written text about the subject was stated on Hammurabi laws. Chapters 100 and 107 states how the borrowing operations were performed and these texts are known as the first example for interest free texts in history. It was believed that the most powerful god of all ‘’Smash’’ the god of sun transmitted the fair decisions to Hammurabi and made him to rub these decision on a dichroite block of 2,25 meter high. Those decisions were about borrowing and collecting money.

The provisions of Hammurabi laws included lending, deposit of goods and commission contracts. On some of the clay plaques of Babel civilization, there were note payables regarding silver borrowing with interest. These plaques were written on several copies and after cooking, one copy was kept in temple, one copy was kept in archive and the others were given to the related parts. During these dates as legal corporations, territory hypothecs and lending in returns for guaranty operations were performed.

During first ages it was mainly the temple that took the responsibility of the banking operations. It was recorded that temples were first performed this duty with interest free and then they started to lend money with interest. It was determined after the excavations that the they first opened tangible(real) credits –in order that the peasants can buy the equipments and raw materials as seeds etc. and pay back during harvesting period- and later on they opened monetary credits. The documents that were found during the excavations clearly states that the main subject of the temples were borrowing and deposit acceptance, transfer from one account to another, confirmation and delivery orders, property voucher orders and these were organized very well on the models.

During loaning operations one third of the original capital was determined as one fifth for cash money export. On the other hand, it was stated that no interest were to be applied during the years without harvest because of the force majeure and no debt collection would be applied. It was also stated that any king of moveable property and real property, especially field hypothec or even guaranty of the prestigious people would be pledged asset in return for the debt.

During the following years it can be seen that banking operations were no longer monopolized by the temples but by some of the rich Jewish families dealing with trade. The most famous of those families were ‘Egibi’ and ‘Murashu’, living by Euphrates river B.C. 600-645. It was recorded that the Jews that were banished from Israel gave interest free credits on a large scale. Despite the ban in Torah, generally operations with interests were easily applied by the Jews in any time of history so It can be concluded that the ban of interest in Bible was harmed through this way. The most horrified obstacles that were laid down in order to protect and develop the religious ban were useful only for the Jews to invent much more various indirect ways to hide themselves to be seen as indifferent for the interest ban.(Akın, 1986)

The base of interest free banking ‘community of interest’ and ‘special form of partnership’ agreements were used with the names comenda and societa in medieval Europe. It was seen that interests increased so much that the society were overwhelmed with the heavy burden of those interests and the churches started to fight against the heavy interests. As a result of unsuccessful fight methods, churches turned to fight with the moneylenders with their own methods and established interest free corporations. Those corporations were able to survive for short time.

The first examples of interest free investments were seen B.C. 1000 in Egyptian civilization. There were laws banning loan sharking and interest. There were evidences that during B.C. 1600, bank notes were circulated and there were check like receipt of deposit in Egypt. In ancient Egypt, it was the formality to accept the treasury and storages as safe custody and the individuals consigned their gold, jewelers and grains to these places to be kept and the individuals were given a receipt with the value of the goods consigned. The individual with this kind of receipt would take the goods with the stated type and amount at any time he wants. The ones dealing with trade would accept this kind of receipt as goods and money. Those documents were accepted as currency tool in Phoenicia and Mesopotamia.(Döndüren, 1984)

Though it is not certain how it was operated, a corporation performing hypothec equivalent loaning was built in Bavyera and Freisingen in 1198. In XIV Salin Bourgeois established a fund that loans its members with capital in return for hypothec. Likewise, with the capital allocated to Saint Paul Church, London Cardinal Michel established a fund that performed interest free loaning to the public in 1361.(Ulutan, 1957)

It was also recorded that established by P. Michel and Milan in 1462, famous credit corporation Mondöpiyete was first loaning with interest free but later on when the expenses increased it turned to apply interest. Templiers that are the members of the Temple that was established to provide security of life and property of the Christian pilgrims gave the donations and safe custodies as interest free at first step.

As an interest free finance corporation, it is possible to see companionship communities and charitable communities that loan mostly to their own members. At present time, it is also pointed that investment funds that work on the basis of English profit sharing principle are pretty similar to interest free banking system. (Unit Trust Year Book 1980, The Financial Times Business Publishing Ltd., May 1981)

It is observed that crediting is performed mostly among the individuals, credit advances and deposit collecting is not allowed. Many strict measures were taken against interest after the Islamism and great care was given in order not to include any interest to the operations performed. But when the Islamic States fell into a decline measures against the interest got weak and it was seen that those times were abused by the Jews.

In time, Islamic geography widened and financial corporations that took banking task widened with trading. There was a need for corporations that would track the income and expenses of the state, fix the amount and fineness of coins with different methods, set the monetary systems. After Islamism those duties were performed by Treasury of Islamic State, bankers, provident funds, monetary foundations and community of interests.

When history of Islam is examined it will be seen that safe deposit boxes where subscriptions, various penalty fines, donations and consigned money are collected from the members of Ahi community which was the most important and effective tradesman community in the field of social and economic life of Ottoman Empire from the very beginning was an important interest free banking corporation. Those boxes were a capital source for the last years of Ottoman Empire. This capital is used by the members of community and those in need and no interest were claimed from the capital. But during the last years of Ottoman Empire, this community was damaged as well and started to give debt with interest.

In the second half of our age, there has been intensive progress in the field of interest free banking. The idea was first came out from a prestigious

Pakistani intellectual Muhammed UZAIR’s study of “ An Outline of Interestless Banking “ in 1955.

3.4. First Islam Bank and Modern Islam Banking

First Islam bank was established in Egypt in 1963 with the name of “Myt-Ğamr” and it was local and small scaled savings bank. It was established with the leadership of the King of Egypt Faysal in order to finance the textile industry accordingly into Islam Economy system. First established in “Myt-Ğamr”, the bank had 9 branch offices soon. (En-Neccar;1978) as a result of banks having a great favor and showing that any bank can work interest free in the kingdom, led the bank to be objected and closed in 1977.

Actual need for interest free banking occurred with the industrialization movement seen in Islamic countries in 20. Century and with the rapid increase of oil prices. Savings of the individuals were evaluated as profit and loss partnership for tradesmen. But with industrialization, there were a need for interest free corporations that would gather all those individual savings in order to finance big investment projects.

At the present time with its 56 Islamic Country membership, Organization of Islamic Conference (OIC) has contributed to the progress and practice of Islamic Banking system.

Islam Countries foreign affairs ministers were gathered in Jeddah in 1970. They called all Islam countries to promote and strengthen the economic partnership, mutual contribution in the fields of science and culture within the scope of Islamic principles. At the next conference that was held in Karachi, Egypt and Pakistan set forward that it would be suitable to establish an international Islam bank.

The idea of help for poor Islam countries from rich Islam countries became stronger after the great increase of oil-dollars as a result of the oil increase in 70s. So Islamic Development Bank was established after Islam Conference.

A committee was gathered in Cairo, in 1973 with the participation of Saudi Arabia, Labia, Jordan, Sudan, Morocco, Yemen, Iran, Afghanistan, Pakistan, Indonesia, Malaysia, Turkey and Mali representatives. The subject that was discussed was development of Islam economy and making Islamic world to benefit from the capital surplus. Committee took and announced very important recommendations. And the basis of Islam banking was established after the gathering of this committee. Following the recommendation, it is seen that Islam banks started to be established one by one.

Islamic Development Bank (IDB) is another important bank that was established with the basis of interest free system. The bank is decided to be established in the meeting that was held in Jeddah at 15 December 1973 with the participation of Islam countries finance ministers, which was recorded in good will document. Agreement contract was prepared in 1974 and accepted by Islam countries finance ministers committee in June 1975. The bank is established as an international finance corporation with the participation of 29 founder Islam country on 20 October 1975. It is a common opinion that Dubai Islamic Development Bank established in Dubai in 1975 is the first example of Islam Banks that finance very important fields as industry, agriculture and estates. (AIB, Islamic Bank; Special Issue, 1981)

The great reputation of Islam Banking DAR alMaal(DMI) was established in 1977. DMI carried on a business with the aim of helping those who wants interest free credits, who have enough experience but in a difficult financial situation to gain legal income and be beneficial to their nations. Another Islam Bank, Kuwait Finance House- KFH was built at the date of 23 March 1977.

Head of Pakistan state Ziya ül-Hak nationalized the banking system in Pakistan in 1979 and announced a declaration in order to make the banking system interest free throughout the country. The declaration was soon took its effect.(UZAIR, 1978) The banks in Pakistan started to receive deposits on profit and loss partnership basis from the date of 1 July 1979. This application carried on until 1983. After this date in order to work with interest free system, banks started their operations with a complete whole deposit changes.

In 1980s, another regulation in the field of interest free banking was carried out by Iran. Now, banking system is performed as interest free in Iran. It is observed that the main two corporations of Islam banking DMI and Al-Baraka groups became very active in 1980s and established their banks or branches in various countries.

4. THE BIRTH OF INTEREST FREE BANKING IN TURKEY

Not until 1970s when interest free finance tools were developed, the field started to experience some effort. But as a result of the close relationship with Islam countries in 1984, with the enactment of Commission of Banks, it was allowed to establish two corporations in 1984, named Private Finance Corporation that carried out bank functions and worked with interest free system. Turkey had the right to embody continuous member at the executive board of Islamic Development Bank in 1984. Since then Turkey has reached to a position that would play very effective role in Islamic world's biggest financial corporation that gathered fifty six states.

It can be said that State's Industry Worker Investment Bank that was established in 1975 with the aim of serving small and medium enterprises and the individuals who wants to evaluate their savings in accordance with interest free system brought very important experiences to our country. The bank continued its works in accordance with this aim until 1978. Correspondingly the scientific studies as well as national and international economic and politic developments, initial step to place interest free banking in Turkey was started to be taken.

Turkey followed import substitution policy until 1980s and afterwards stated to follow export-oriented growth strategy that aimed to globalization. This globalization strategy enabled the current financial innovations of the world to be penetrated our country. During this time, it was aimed to get economic stabilization with the thought of outward oriented economy strategy and reconstruction.

With these strategy and expansions the current financial innovations of the world was aimed to penetrate our country through the pass to free market economy. Within the lights of those thoughts, Turkish financial system started the reformation process and carried out very important reforms that provide liberty in financial markets in corporational and legal base.

As a result of those developments and reforms it was allowed to establish foreign banks. And 13 foreign banks opened branches in Turkey and the same opportunity was enabled to the citizens who want to evaluate their savings in interest free based.

Capital Market Law no 2499 was accepted on 28.07.1981 and Istanbul Stock Exchange (IMKB) was established. All the capital market tools started to be carried out with exchange-market's opening. Besides, money market within the body of Central Bank of Turkish Republic was opened, many new systems as Interbank market, with the liberalization on foreign currency exchange offices, leasing, factoring companies, intermediary of capital market were included to the system.

Because of the currency crisis that was experienced during those times, the need for foreign capital and to awaken the depressed economy, it was allowed foreign banks to be established in Turkey. During this outward oriented times, interest free banking application that had been carried out worldwide successfully was brought out to the agenda in Turkey by Bülent ULUSU. And with the enactment no 83/7505 dating 16.12.1983 approved by the president Kenan Evren and prepared by Turgut Özal, this opportunity was enabled to our citizens who want to evaluate their savings in accordance with interest free basis. Private finance corporations were included to Banking Law concept with the some amendments on the articles of Banking Law no 4389 with the law no 4491 regarding the amendment of Banking Law on 19 December 1999.

The aim with private corporation application was to promote private savings that was in low number in Turkey and to include under-the-mattress savings that were out of economy transferred to the fields as gold, foreign currency or estate. According to the Banking research of PIAR at that time, the rate of the people that do not invest deposit on banks because of their believes was 15%. (Kuwait Turk Participation Bank, History of Interest-Free Banking, http://www.kuveytturk.com.tr)

Another reason for the establishment of Private Finance Corporations was to provide foreign source to our country from gulf countries such as Arabia and Kuwait.

Private finance corporations that were adopted in a short time by Turkish public showed a rapid growth in terms of the funds they collected, work load and project capacities. 7 Private Finance Corporations have been established in Turkey since 1985. They got into practice and took their places in Turkish financial system respectively in 1985 Albaraka Türk Private Finance Corporation Inc., in 1985 Faisal Finace Corporation Inc., in 1989 Kuvety Türk Pious Foundations Finance Corporation Inc., in 1995 İhlas Finance Corporation Inc., 1995 Anadolu Finance Corporation Inc., in 1996 Asya Finance Corporation Inc.

Anadolu Finance and Family Finance merged under the name of Turkey Finance Participation Bank(Turkiye Finans Katılım Bankası) in 2001 and the bank still carries out its participation banking operations with this name. Currently, there are 4 participation banks that operates actively in Turkey.

İhlas Finance was damaged a lot after the crisis in 2001 and closed by leaving hundred thousands of sufferers behind. And this led to a great confidence crisis inside the private finance corporations. İhlas finance used to give more profit share to deposits when compared with the other finance corporations of the time and in 1999, the increase rate of profit share expenses was extremely increased when compared to profit incomes and the gap between those reached to maximum. The instability between income and expense ended with the bankruptcy of İhlas Finance.

Participation Banks are established in Turkey with reference to the decision of Cabinet. They carry out their applications in accordance with Banking Law and take on important tasks to include under-the-mattress savings to economy. In one sense, participation Banks with Venture Capital characteristic have great contributions to economy of the country through using the idle funds they collect in providing raw material, fabricated materials and investment goods that Turkish businessmen and entrepreneurs need.

Participation banks have continuously grown since the year they started their operations in 1985. The reasons such as; differentiation of striking of customer’s fancy and increasing competition made these banks to look for the ways to develop themselves rapidly and constantly. as the products when the operations started were not sufficient for the customers and the need for meeting interest free needs of interest sensitive individuals in various different fields as well led interest free banks to ask how to integrate the products of conventional bank that have very ancient roots in accordance with religious laws.

5. OPERATION OF INTEREST FREE BANKING, TURKISH PARTICIPATION BANKING PRODUCTS AND THE DEVELOPMENT OF NEW INTEREST FREE BANKING PRODUCTS

5.1 Operation of Interest Free Banking

The most important function of Islam banks is to collect money from the public and transfer it to production area, as it is for current banks. That means the main function of interest free banking system is credits and deposits (fund collecting), the same function as conventional banking. Today, banks perform these functions by collecting low interested deposits from public and transferring it to the producers with high interests. The gap between the interest they pay (deposit interest) and the interest they receive(credit interest) is the real income of the current banks. As the base of interest free banking system, all the transactions grounded deposit collecting and crediting are only performed in return for a service or goods. In other words the base of the banking system is buying and selling plus the profit gained from buying and selling.

Deposers are creditors; banks are debtors in current bank and deposer relationships. For the relationship between producers, banks are creditors and producers are debtors. And debtor party pays the interest to the creditor in return for the credit it received. There is no interest application in Islamic banking and it is also not possible to give money with interest as debt. For this reason, there is no debtor and creditor relationship between fund owners or producers.

On contrast, interest free banks have partnership relationship between both fund owners and creditors. The only condition that the bank is the creditor party is ‘loan in Islam’ (interest free debt) which is the debt given with no thought of gain. The individual that takes on debt from the bank with the aim of consumption or setting up a business pay the debt back with more than he takes. Except for these two conditions, there is another aspect that distinguishes interest free banks from conventional banks; they deal with buying and selling and leasing.

Within this general frame, in an integrated way interest free banks perform most of the other modern and traditional banking operations that the other banks perform.

5.2. Inspection of Participation Banking

Participation banks were inspected by Undersecretariat of Treasury until 2005, and since 2005 they have been subjected to the inspection Banking Regulation and Supervision Agency as all the other conventional banks.

Private finance corporation regulation was laid out in 2006 and since then participation banks have been subjected to the same inspection basis as all the other conventional banks with the banking law no 5411.

5.3. The Products of Turkish Participation Banking

Participation banks in Turkey started to carry out their operations with 7 to 8 products such as collecting, goods based fund using, EFT and money order that are characterized as the basic banking products. It is also possible to examine available interest free banking products and new interest free banking products that were produced in accordance with interest free banking system.

5.3.1. Account Types

Participation banks generally accept the accounts in three main types. These are current accounts, savings accounts and investment accounts.

5.3.1.1. Current Accounts

Drawing accounts that enable the money to be withdrawn at any time. The account is opened by their owner to meet the needs about trading or consumption when they are in need and ready for circulation. These kind of accounts can be withdrawn at any time. Drawing accounts of the banks enables cheque-book opportunities. These accounts enable liquidity and ease the transactions.

No profit share is paid to these accounts. Bank gets the authorization of using the amount that the account owners invested, for the other operations of the bank. But these accounts are guaranteed by the bank. In other words, when there is a loss in other operations of the bank, drawing account owners are not affected by the loss. Loan in Islam principle is valid for these accounts.

5.3.1.2. Saving Accounts

Interest free banks usually open these accounts to those who have small amount of savings and want to keep these savings in a safe place because of need and future concerns. These accounts accept the ones who save the residuals of consumption and want to use these savings in times of need. The money can be withdrawn at any time which is the same as current accounts in a way.

Bank pays money to savings owner as well but it can enable special privileges to fund owners such as financing small projects and installment sale of consumption goods. Those privileges can be thought as encouraging for the saving owners. With the aim of encouraging individuals for saving and investing their savings to the banks minimum degree that can be invested to the banks are arranged in minimum levels. The account is opened to;

- Either leave the saving account to investment account in order to participate in profit or loss,
- Or leave some part of the saving accounts to investment account and leave the rest to saving account in order to withdraw when in need,
- Or keep in owners saving account under the guarantee of the bank and without any profit aim.

On first condition deposit is transferred to the saving account. Depositor participates the profit or possible loss that the deposit can bring. The amount that remains in saving account is under the guarantee of the bank.

With the permission of interest free banking saving account owners, it can transfer some part of the funds of the account to investment. But in order to meet the amounts that the owners of the funds would withdraw, it is necessary for the bank to keep some part of the funds available. On condition that the bank obtains permission from the owners, bank can sometimes share the profits of owners of the saving accounts that it encouraged for investment. Those profits are evaluated as bonus for account owners and incentive. But possible loss belongs to the bank. The share that fund owner would receive is the amount that remains from his fund at the end of the year.

Saving accounts are characterized as consignment in Malaysia Islam Bank and loan in Islam in the other banks. It is possible to evaluate profits that are given to the saving owner with no guarantee as good manner. (Payment of the debt with no condition. A manner that is advised by the Prophet Mohammed)

5.3.1.3. Investment Accounts-Participation Accounts

They are the accounts that are opened by interest free banks to gain income for those who cannot invest their savings because of interest’s being forbidden by religion and cannot administer the money themselves. The ones who open investment account in the bank participate in the investment operations of the bank and gets the profit of loss of the bank according to the amount and time of the money they invested.

Investment accounts are opened in accordance with mudaraba principle of Islamic Law. It means, labor partnership is the principle. The profit that would occur with the partnership of capital and labor is shared in accordance with the percentage that is determined among the partners earlier. Labor owner is the assignee of the capital owner and the person that the goods is consigned. On condition of loss, fund owners with their capitalist position pay the loss. Bank does not participate the loss.

Periods of investment accounts starts from 30 days and goes to various times as 360 days and more than 360 days. Net profit to be shared to participant is not certain. Depositors receive the last profit share that was transferred to the accounts according to previous week's data. Instead of profit, loss can be shared. Corporation can determine the share of profit or loss it would receive as a result of transaction of these accounts as 20% or less with the permission of Central Bank. The funds that are saved in these accounts are under the guarantee of Saving Deposit Insurance Fund up to 50,000TL.

If participation accounts are not closed within 5 working days after expry dates, they are renewed with the same conditions. When profit shares given to participation accounts are calculated daily unit value calculation is applied. Profit share pools show increase or decrease according to the deposit amount of deposit owner. High deposits are transferred to high profit share pools and deposit owner gets higher profit share.

DAILY UNIT VALUE CALCULATION TABLE						
		Type of currency	TL			Total
		Account owner's participation rate for profit	75%	80%	90%	
		Account owner's participation rate for loss	87,5%	90%	95%	
1		Total Amount of Participation Accounts	177.025	718.780	114.201	1.010.006
2		Amount of Participation Accounts that do not Receive Share Profit/Loss	2.934	2	7.070	10.006
3		Amount of Participation Accounts that Receive Share Profit/Loss (1-2)	174.091	718.778	107.131	1.000.000
4		Account values	1.707	3.234	511,7	
5		Unit value	102,38	223,6	210,57	
6		Unit calculation value (4*5)	174.806	723.346	107.763	1.005.917
7		General Reserves				12.745
8		The Reserves that are saved to be shared with Participation Accounts				8.255
9		Required reserves (6* Required reserve rate)				55.325
10		Participation Accounts Encaisse Rate				84.661
11		Available Fund (6+7+8)-(9+10)				886.930
12		Credits made used				880.590
13		Idle Fund (11-12)				6.340
14		Fund Surplus that is made used (12-11)				0
15		Incomes of Participation Account (a+b+c+d)	44	194	32	271
	a	Participation rate of Income Shares	36,39	160,25	26,87	223,51
	a.1.	Profit Share Income obtained from Credits made use as Participation Account Oriented				278,69
	a.2.	Used Fund Surplus Profit Hit				0
	b	Collection made from Cancelled Credits	1,69	7,18	1,13	10
	c	Private Reserve Cancelation	2,54	10,77	1,69	15
	d	General Reserve Cancellations	0,85	3,59	0,56	5
	e	Reserved Cancellations Saved from the Profits to be Shared with Participation Accounts	3,04	12,92	2,03	18
16		Participation Account Expenses (a+b+c+d+e)	8,12	34,46	5,42	48
	a	Private Reserve Expenses	1,69	7,18	1,13	10
	b	General Reserve Expenses	1.01	4,31	0,68	6
	c	Saving Deposit Insurance Fund Premium Expenses	0,34	1,44	0,23	2
	d	Cautionary Reserve	5,07	21,54	3,39	30
17		Profit/Loss to be shared (15-16)	36,39	160,25	26,87	223,51
18		The amount that is Saved from the Income to be Distributed to Participation Accounts	1,82	8,01	1,34	11,18
19		Shared Profit/Loss (17-18)	34,57	152,24	25,53	212,34
20		New Unit Account Value (6+19)	174.841	723.499	107.789	1.006.129
21		New Unit Value (20:4)	102,4	223,6	210,6	
22		Undue Account Profit Shares (Expense Rediscounts) (20-3)	750	4.721	658	6.129

Table 1 : Daily Unit Value Calculation Table

(Kuveyt Turkish Participation Bank, Retail Banking Department)

According to the accounts included in Notice about Uniform Accounting Planning and Prospectus to be applied by Participation Banks, through the way of funds collected in participation accounts, credits being used with the source of participation accounts, interest share incomes gained from these and returns regarding participation shares and losses, Daily Unit value are determined in accordance with below stated table and its explanation.

5.3.1.4. Explanation of Daily Unit Value Calculation Table

Type of currency: TP, YP

Account owner's participation rate for profit: It is the rate to be considered when determining the share that account owners would receive as the profit as a result of transaction processes of funds collected in participation accounts.

Account owner's participation rate for loss: it is the rate to be considered when determining the share that account owners would receive as loss or deficit as a result of transaction processes of funds collected in participation accounts(private returns, general returns, Saving Deposit Insurance Fund).

1- Total Amount of Participation Accounts: It means the funds invested to participation accounts.

2- Amount of Participation Accounts that do not Receive Share Profit/Loss: the funds that are not included in calculations as profit sharing process is not initiated yet because of value date application of funds invested in Participation accounts.

3- Amount of Participation Accounts that Receive Share Profit/Loss: The amount that is calculated by subtracting participation accounts that do not receive share profit/loss from the total amount of participation accounts.

4- Account values: The total of account values are on the basis of unit value the total of account values that are identified on article 3 of this regulation,

5- Unit Values: The amount of unit price valid for current day, as identified on article 3 of this regulation.

6- Unit Calculation Value: the amount of unit account value valid for current day, as identified on article 3 of this regulation. This amount must be equal to the amount that is received when and if there is any on current day, the amount of participation accounts that do not get share from received profit/loss is subtracted from the total of the funds that are collected in participation funds and rediscount expenses of these funds. (4#5)

7- General Reserves: According to the Regulation regarding procedures and principles concerning determination of Credits and the Other Debts characteristics by the Banks through the Credits of participation account sourcing and the Reserves saved for them, the part of general reserves that are saved in participation accounts for the ones that are followed between Credits with Standard Characterization and the Other Debts and Credits with Close Observation and the Other Debts.

8- The Reserves that are saved to be shared with Participation Accounts: within the scope of article 14 no 3 of the Regulation regarding procedures and principles concerning Determination of Credits and the Other Debts Characteristics by Banks and the Returns saved for them; the reserves that are saved to be used in returning the private and general reserves and the part of Saving Deposit Insurance Fund premium in participation accounts.

9- Required reserves: It is the amount that is created by freezing in Turkish Republic Central Bank within the frame of Notice Provisions regarding Required Reserves. This amount is calculated by multiplying unit calculation value and the rate that is stated in the Notice.(6-required reserve rate)

10- Participation Accounts Encaisse Rate: It is the amount that is obtained by dividing participation fund total to the amount that they make available in liberal drawing account of safe boxes and correspondent in order to carry out their responsibilities and multiplying the rate obtained with the total amount of participation account in the event of Participation bank's being have to make a payment for participation accounts before the due date or when due.

11- Available Fund: The amount that is obtained by subtracting the total of required reserves and participation encaisse rate from the amount that is saved from unit account values, general reserves and participation account profits. [(6 + 7 + 8) – (9 + 10)]

12- Credits made used: Participation account oriented:

a) Credits with Standard Characterization and the Other Debts and Credits with Close Observation and the Other Debts(I. and II Group Credits)
b) Tracked Debts Net(III., IV. And V. Group Credits)
c) The total of Credit Profit Share Accrued Revenue and Rediscounts

13- Idle Fund: the amount that is obtained by subtracting credits made used from useable fund amount. (11-12)

14- Fund Surplus that is made used: it is the amount that is obtained by subtracting useable fund amount from the credits made used.(12-11)

15- Incomes of Participation Account (a+b+c+d+e)

a) Participation rate of Income Shares: profit share amount that is equal to usable fund surplus is subtracted from profit share income that is obtained from the credits that are made used participation account oriented. The amount obtained is separated according to its gravity among the total participation accounts basing currency type. The amount separated is multiplied by the participation rate of the account owner for the profit, and the amount obtained is the share that is saved from profit share incomes for participation account shares.

1- Profit Share Income obtained from Credits made use as Participation Account Oriented: currency type based profit share obtained from the funds made use participation account oriented. It is stated in Participation Account Agreement whether default interest of these overdue funds or profit share that is devoided of and incomes that are taken from Required Reserves are considered as profit share income in participation accounts share unit calculation.

2- Used Fund Surplus Profit Hit: It is the amount that the rate calculated by dividing used fund total to profit share income obtained from currency type participation account oriented used credits is multiplied by used fund surplus.

b) Collection made from Cancelled Credits: the amount that is saved for share of participation accounts from the collections made from cancelled credits used as participation account oriented.

c) Private Reserve Cancelation: It is the part relating participation accounts of cancelled amounts of saved private reserves for participation account oriented credits characterized as illiquid claim according to the regulation regarding procedures and principles concerning Determination of Credits and the Other Debts Characteristics by Banks and the Returns saved for them.

d) General Reserve Cancellations: It is the part relating participation accounts of cancelled amounts of saved general reserves for participation account oriented credits according to the regulation regarding procedures and principles concerning Determination of Credits and the Other Debts Characteristics by Banks and the Returns saved for them.

e) Reserved Cancellations Saved from the Profits to be Shared with Participation Accounts: The amount that is cancelled in order to compare Saving Deposit Insurance Fund premium partnership accounts and private and general reserves of observed reserves in the 3700 account of Amounts Saved from the Profits to be Shared with Participation Accounts.

16- Participation Account Expenses(a+b+c+d+e):

a) Private Reserve Expenses: It is the part that is shared for participation accounts as amounts of saved private reserves for participation account oriented credits characterized as illiquid claim according to the regulation regarding procedures and principles concerning Determination of Credits and the Other Debts Characteristics by Banks and the Returns saved for them.

b) General Reserve Expenses: It is the part that is shared for participation accounts as amounts of saved private reserves for participation account oriented credits according to the regulation regarding procedures and principles concerning Determination of Credits and the Other Debts Characteristics by Banks and the Returns saved for them.

c) Saving Deposit Insurance Fund Premium Expenses: Saving Deposit Insurance Funds share per participation accounts.

d) Cautionary Reserve: It is the Cautionary Reserve that is saved in order to be used in comparison of private and general reserves and Saving Deposit Insurance Funds share per participation parts and total amount of income items stated in explanation number 15 articles (b), (c)and (d). These reserves that are saved are recorded in 3700 account of Amounts Saved from the Profits to be Shared with Participation Accounts stated in Notice about Uniform Accounting Planning and Prospectus.

17- Profit/Loss to be shared: the amount that is obtained by subtracting participation account expenses from participation account incomes.

18- The amount that is Saved from the Income to be Distributed to Participation Accounts: Within the scope of article 14 no 3 of the Regulation regarding procedures and principles concerning Determination of Credits and the Other Debts Characteristics by Banks and the Returns saved for them reserved amount that is shared from the profit amount to be distributed to participation accounts from the date when unit price is calculated.

19- Shared Profit/Loss: it is obtained by subtracting saved from the profits to be distributed to participation accounts from profit/loss to be shared and it is the net income amount that is distributed to participation accounts on unit base.(17+18

20- New Unit Account Value: it is the amount that is obtained by adding the distributed profit/loss to the total unit account value.(6+19)

21- New Unit Value: it is the rate that is obtained by dividing new unit account value to the total account values.(20:4)

22- Undue Account Profit Shares (Expense Rediscounts): Profit share of undue participation accounts . This profit share starts to operate by the opening/renewal of the account but as it is not fall due no assessment is applied. The amount that is obtained by subtracting new unit account vale from participation account amount that would take share from profit/loss.(20-3)

By using above stated calculations, daily unit vale number is obtained and gross profit share rate is obtained according to the following formula.

$$\frac{\text{Last daily unit value calculation}}{\text{Unit Value of pool equal to due date long - 1}} = \text{Gross Profit Share Rate}$$

5.3.2. Fund Application Methods

5.3.2.1. Application of Funds Accrued in Current Accounts

While it was an obligation for Participation Banks to keep in cash minimum 10% of funds accrued in current accounts money either in safe boxes or in trade banks, there is no such obligation at the moment. 11% of current accounts must be kept in Central Bank in cash or liquid stocks that Central Bank determines. These rates can be changed by Central Bank.

Funds accrued in current accounts can be applied to natural and legal person without and due date restriction. It is free to use in Participation Bank foreign currency, Turkish Banks or International currency and in trade market.

5.3.2.2. Application of Funds Accrued in Participation Accounts

As it is the same for Conventional Banks, funds accrued in Participation accounts are applied to blockage by Central Bank first. In accordance with Central Bank Notice as conventional banks, Participation banks are to save 11% of Turkish Liras participation accounts with 3 months due time, 8% of participation accounts with 3 months due time, 6% of participation accounts with 1 year due time and 5% of participation accounts with 1 year and over due time to Central bank as reserve and it can use the rest of the amount as fund to real sector and individual users. For foreign currency these rates are 11% for participation accounts reaching up to 1 year, 9%for participation accounts over 1 year.

5.3.3. Mudaraba (Profit-Loss Sharing)

Mudaraba takes part in literature as Profit-Loss sharing, Sleeping Partnership. Mudaraba is a contract where by one side the investor or Rabb ul Mal contributes money and the other side work, being the manager or Mudarib. The Rabb ul Mal bears all losses, and the Mudarib earns a profit share:

Mudaraba is a concept to provide capital to somebody undertaking the work. It could be understood as being similar to the function of an asset manager or employed manager of a company.

Legally this concept is established as permissible by the consensus of the scholars and not based on primary sources of the Shariah.

As the profits are shared with the manager (Mudarib) and the capital provider (Rabb ul Mal) but the losses are beared only by the capital provider this mode is also named profit sharing – loss bearing. Before the manager gets his share, the losses, however, if any, needs to be recovered. A wage could be negotiated.

5.3.3.1. Restricted Versus Unrestricted Mudaraba

Capital can be provided as being unrestricted for any purpose the manager deems fitting or it is possible to grant it upon conditions what has to be made with it; the latter is technically called restricted Mudaraba (Mudaraba al Muqayyadah), e.g. all investment funds. An unrestricted Mudaraba is called a Mudaraba al Mutlaqah.

5.3.3.2. Two-Tier Mudaraba

Two-Tier Mudaraba was the initial concept for Islamic banking. The structure is set up so the Islamic bank is engaged in two different Mudaraba transactions, one with depositors and one with those who provides financing. The first Mudaraba is between the bank and the client with surplus capital (depositors) and the second one is between the bank and the clients who require financing.

The first tier Mudaraba between depositors and the Islamic Bank has those depositors acting as Rabb ul Mal and the bank acting as the Mudarib. The depositors place their funds with the bank with no guarantee of principal and a return based on the profitability of the investments made by the bank on their behalf. As with other Mudaraba, the depositors bear any losses and share profits with the Islamic bank according to a pre-agreed ratio.

The second tier Mudaraba between the Islamic bank and those receiving financing has the bank acting as Rabb ul Mal and the customers acting as Mudarib. The bank bears all losses except in cases of fraud by the Mudarib and share profits with the customer according to a pre-agreed ratio.

The concept was developed by Islamic economists as credible alternative to saving accounts. In a two-tier Mudaraba, the bank provides an intermediation role between depositors and customers needing financing and is expected to be able to achieve sufficient diversification and use its greater resources to more adequately protect depositors from risks associated with each individual second tier Mudaraba agreement. However, because the Islamic bank retains liability for all losses, which are then passed along to depositors, it suffers from an informational asymmetry that has limited its use in practice.

Another problem with the two-tier Mudaraba model is that not only do depositors have their principal at risk, they are also likely to see significant swings in the profits paid on their deposits. One solution to the latter problem is to smooth profits across time using a profit reserve, which could lower the volatility for the depositors.

5.3.3.3. Mudaraba for Insurance

As discussed under Takaful a Mudaraba contract is recommended regarding the funds of the Insurance contract, while the Agency (Wakala) is suggested for the insurance pool regarding the claims to be made.

Although Mudaraba is not actively applied today, Albarak Turk Participation Bank applies some mudaraba applications. These applications are construction projects and shared as 50%-50%. Following examples are about this mudaraba concept.

Yorum Istanbul Project

Investor is Yorum Construction Company in this project and Albaraka Türk participated to the project by giving only capital not labor. Project consists 558 houses.

Batı Şehir Project

Investor of the project is Emlak Konut Real Estate Partnership – Ege Yapı Limited Company. Albaraka Türk Participation Bank participated to the project with mudaraba method by investing capital and excluding labor. There are 3150 houses in the project concept. First step of the project is planned to end in 24 months and the project is planned to be completed in 36 months. The territory is 167 decare and situated right behind Doğan Media Center and Dünya Newspaper and right besides İstoç Oto Center. The project has 800 meters frontal to TEM autobahn and 450 meters frontal to third bridge linking road.

İstWest Project

Investor of the project is Fer Real Estate Development and Construction Corp. Company. Albaraka Türk Participation Bank participated to the project with mudaraba method by investing capital and excluding labor. The area of the project is 68.735m2. There are 14 blocks. The owner of the area is Boyner Holding. There are 931 pieces of houses with types studio flat, 1+1, 2+1, 3+1, 4+1. Besides the houses, there are 73 work places.

5.3.4. Musaraka (Special Form of Partnership)

While mudaraba has a passive capitalist that is not included in the job and an active enterpriser that enables labor to the job, Musaraka has a complete partnership with the active inclusion of both capital and labor. By the agreement that the parties sign, they do not lay any condition to prevent other parties' works. Financial loss belongs to the capitalist in Mudaraba, the capital is shared according to the share percentage.

a) Provisions of Musaraka

- Subject and its duration: there is no limitation for occupied area. There might be a private lot or the aim may be general trading. As it is constructed on stand for proxy, it may remain temporary or permanent.
- Partners: the scope of partnership is wider as there is no guarantee in this company. It can be constructed with any class of people, even with non-Muslims.
- Principles: Capital and profit. The capital that is invested does not have to be equal. Profit rate is determined by parties with an agreement, it is not bound to capital rate. If profit rate is not assigned, the company collapses.
- Profit: as profit is gained both by capital and labor, active and ingenious partner is proposed to be given more amount of profit than stated in the agreement. In case of loss, P/L is shared in accordance with the capitals of the partners.

- Loss: Loss and damage is shared in accordance with the capitals of the partners even the contrast is stated. New partners are subject to a limited based responsibility principle.

While today, mudaraba applications are performed in Participation Banks, musaraka operations with investment of both capital and labor are not performed. It is because investing labor besides capital is another specific area and needs different kind of proficiency. Banks transfer the collected deposits to real sector and individual users basically through production backing (murabaha) system.

5.3.5. Direct Collection System (DCS) / Direct Borrowing System(DBS)

Called as DCS and ABC in short the system is the total progress enabling firms with branch system to operate their cash flow with their affiliate branches safely through automatic file transfer method. The system is applied in conventional banks and added to participation banking system with the thought of its being suitable for interest free system.

The base of the system is collection of receipt value when it is on due according to the receipt information of the main company sends to the bank through electronic environment. When branch account is not enough, due payment is applied through goods finance within DBS limits opened to the branch.

5.3.5.1. Advantages of DCS&DBS to the Main Company

- Main company can collect costs safely with no risk and on due date from its branches.
- Brach account can be examined during the option due that is determined after the receipt due date for collection. Company can report DBS limitations, receipt result information entered in the system, collection information of its branches.

5.3.5.2. Advantages of DCS&DBS to the Branches

- Primarily, braches can collect their costs on their current accounts, in case of insufficient balance of their accounts, they can provide goods transfer.
- They can only use finance management for the collection of costs.
- Costs can be collected only from current account.
- Besides Tl, USD and EUR indexed finance can be used.
- Payments and finance performed are recorded in the system.

5.3.6. Finance with Credit Guarantee Fund Warranty

Credit guarantee Fund supports development and progress of Middle and Small Enterprises. It eliminates the lack of warranty obstacle of good business idea and enables source for the investments and trade needs of the enterprises.

Small businesses cannot receive the finance opportunities of banks as easy as big businesses. This warranty problem is eliminated by credit guarantee fund. According to Credit Guarantee Fund, businesses with the number of employees less than 250 are accepted as SME, this kind of businesses of all around Turkey can apply Participation Bank for Credit Guarantee Fund.

The firms applying for Credit Guarantee Fund can be evaluated with a fixed evaluation price. In case that the application is approved and the credit is used with the warranty of Credit Guarantee Fund, a commission is taken around the rates 1% and 2% out of warranty balance every year of credit due time in cash according to warranty in cash and noncash or the other characteristics of warranty. Warranty maximum limit for a company is 1.000.000TL for Credit Guarantee Fund. Warranty maximum limit for the businesses that the company has direct or indirect risk group is 1.500.000TL. According to the risk sharing principle, credit guarantee fund at work can go warranty up to 80% of the credit.

5.3.7. Murabaha (Production Backing)

Murabaha is a sale type in Islamic Law. Vendor announces the cost and adds the profit share of the cost when agreeing with the customer. For example vendor can say: ‘ I bought the good for 100 and want 10 profit’. If customer agrees with the vendor’s want, this kind of buying-selling application is called as murabaha. Cost, margin of profit and final sales price is explicitly announced. The method is practical and has great premium rate. It can be used especially for the times when partnership types in interest environment get less application opportunities. It is the method that Participation Banks in Turkey applies mostly. When Participation

Banks determines investment pricing, they base many factors and determine credit profit share. For investment pricing that is done with no specific formula; the price is determined on the basis of cost of the fund (profit share given to fund), expenses, data in market, liquidity of the bank, the implementations that were not be able to performed because of the profit share rate are to known how far would not performed and the other factors that affect the rate. We can write participation bank investment profit share as followed;

Investment price = cost of the fund + net profit margin

When we looked at net profit margin more; Net profit margin = expenses + data in market +liquidity of the bank + the rate of the missing implementations not performed + other determining factors. Net profit margin of the first quarter of 2012 is 5 in average.

5.3.7.1. Murabaha Sale with Purchase Order

A customer that needs goods and could not find the source, asks bank to buy the goods. Murabaha has both the purchase order of the customer and the promise of the customer about buying the goods that the bank would buy.

Following this order and promise of the customer, bank buys the goods on condition that it sells the goods to the customer over its cost, with the rate and amount that it agrees with the customer. Customer buys the goods that the bank buys on behalf of the customer. The customer pays it in installments and on the conditions agreed with the bank. For example; if a construction company that starts to a new construction has not enough savings to buy iron, cement etc. material for the construction of the building, it applies the Participation Bank to buy and sell these materials to the Construction Company. Participation Bank buys those materials for the customer and sells to the customer with addition of agreed rates and amounts. Construction Company pays back its debt in installments with agreed profit. Participation bank here works as a wealthy trader. Murabaha system is mostly used for the finance of foreign trade, provision of raw and semi finished materials.

5.3.7.2. Foreign Trade Finance with Muharaba Method

As for the domestic market murabaha method, financing of the goods with agreed rates and amounts is the matter. The customer that does not have cash money and wants to buy the goods suitable for Islamic finance from other country applies the Participation Bank to buy and sell this goods for the customer with agreed profit and payment terms. Participation Bank buys the goods in cash money from the exporter and sells these goods to the customer with agreed profit and payment terms. Participation banks enable their corporate customers to finance with credit card.

5.3.7.3. Murabaha System Progresses

Participation Banks not only bring new products to rapidly growing and developing finance sector but also develop their available products in themselves and within this scope they distinguished the characteristic of using an available finance product in different businesses, they applied murabaha operations in many different goods and formed their customers alternative finance method.

5.3.7.3.1. XYZ Commodity Murabaha

a. Definition of Investment

XYZ Commodity Murabaha is a fixed payment investment type and based on the profit that is gained from buying and subsequently selling the goods processed in London Metal Stock. In XYZ goods murabaha, customer buys a certain amount of goods in cash money from goods company in London through XYZ and immediately after sells the same goods to XYZ in a fixed term. As the customer buys the goods in cash money and sells in fixed time with a fix profit, at expiry date of XYZ investment it needs to pay the capital and fix profit to the customer.(Ulus, 2012)

b. Investor Profile

- Investor demanding the protection of the profit until expiry date
- Investor eliminating long term investments and wanting to be always flexible about the expiry date
- The only condition; customer signs a new murabaha agreement in addition to the typical agreements it always signs and assigns XYZ the representative for tracking its operations.

Advantages

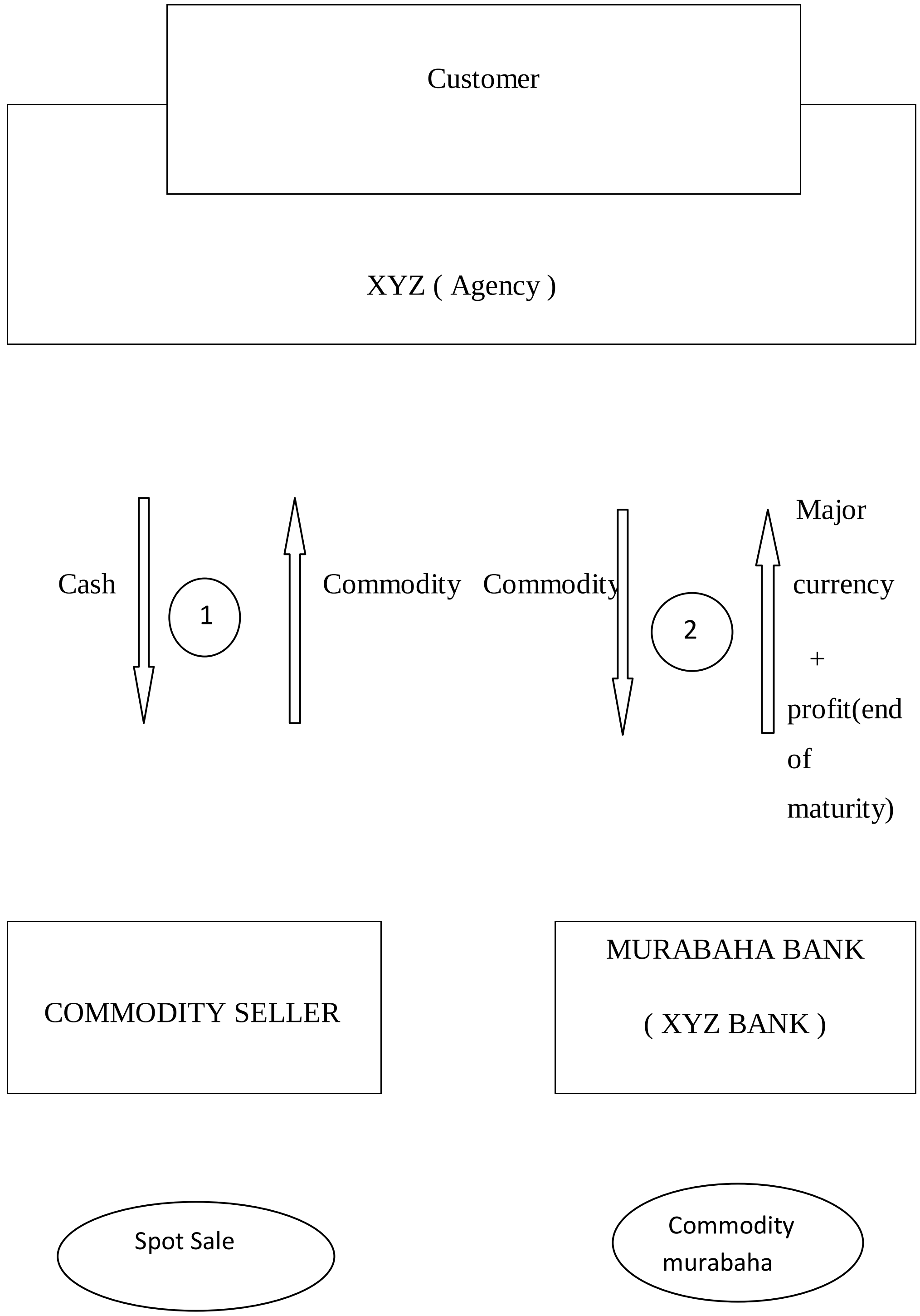
- Capital and profit is taken under protection at expiry date
- Flexibility at investment expiry date and in currency type in accordance with customer options.

Risks

- Capital is always under protection at expiry date
- As investment income is fixed on the first day and as it is short term, there is no high profit potential.

c. Investment Parameters

- XYZ Commodity(Murabaha) Agreement
- Currency units(TL, USD and EUR)
- Investment time (from 1 week to 30 days)
- Investment amount (5 Million TL/USD/EUR at least)
- Fixed profit rate



Customer
XYZ (Agency)
Cash
1
Commodity
Commodity
2
Major currency + profit(end of maturity)
COMMODITY SELLER
MURABAHA BANK
(XYZ BANK)
Spot Sale
Commodity murabaha

Figure 1: XYZ Goods Murabaha – Process Plan

(Ulus, S. 2011, Katılım Bankaları Enstrümanları Yurt Dışı Uygulamaları, TKKB, İstanbul)

- Customer chooses XYZ as an agency to buy and sell goods and signs the necessary legal agreement.
- Through XYZ, the customer buys the goods it needs for the investment from goods vendor and again through XYZ, sells the same goods with fixed profit and expiry date to murabaha bank.
- At expiry date murabaha bank pays both the capital and fixed profit to the customer through XYZ.
- XVZ takes only commission of those operations.

5.3.7.3.2. XYZ Twin Currency Unit Murabaha

Definition of Investment

- XYZ twin currency unit murabaha consist of two different but simultaneously happening operations and promises XYZ goods murabaha and withdrawal right of XYZ given by the customer. Promise is customer's acceptance of paying the capital and profit that comes from XYZ goods murahaba investment on expiry date with a fixed another currency determined on the operation date.
- With respect to the pre-chosen fixed currency it pays to XYZ alternatively in this was or pays the capital and its profit to the customer with the same currency type.

Investor Profile

- Wants to get more profit from XYZ goods murabaha investments
- Accepts to do the payment with another currency type alternatively
- Wants to minimize the rate risk that may occur as a result of import and export of the investment
- As an only condition, signs agency and promise agreements.

Advantages and Risks

- More profit is gained from XYZ goods murabaha
- Flexibility of currency types, rates and expiry dates and profit rate determination. The closer currency that is chosen on the operation day to the spot is, the higher the profit is.
- Capital is not guaranteed.
- Repayment may be performed with another currency.
- Limited profitability possibility

Investment Parameters

- Capital unit
- Second currency unit
- Expiry date choice
- Currency choice for expiry date
- Investment amount (100 thousand TL/USD/EUR at least)
- Opportunity to choose profit rate according to the rate

Forward Rate Expectation of the Customer:

- Expectation of EUR/USD currency to be close to the operation rate or the expectation of EUR/USD currency to slightly exceed at expiry date.

5.3.3.7.3.3. XYZ Tavarruk

- XYZ tavarruk short term fixed payment finance type and its finance is based on profit shares that are gained from buying and subsequently forward selling of the goods traded at London Metal stock. In short term murabaha finance, XYZ buys certain amount of goods from goods companies in London and sells the same goods immediately to the customer with terms. As XYZ buys the goods with cash price on the date of finance and sells with a fixed cost and forward price, customer must pay the fixed cost with the capital to XYZ at the end of finance.

Advantages

- Capital and fixed cost are under guarantee at the end of the expiry date.
- Flexibility of currency type and finance duration in accordance with the need of the customer

Risks

- Capital is always under protection at expiry date.
- As cost of finance is fixed on the first day and as it is short term, there is no high profit potential.

Customer Profile

- Want the capital and cost to be under protection until expiry date
- Eliminates long term finances and always wants to be flexible about expiry dates
- The only condition; customer signs a new murabaha finance agreement in addition to the typical agreements it always signs.

Finance Parameters

- XYZ short term murabaha finance agreement
- Currency units (TL, USD and EUR)
- Investment time (from 1 week to 30 days)
- Investment amount (depends on customer's credit condition)
- Fixed cost rate

5.3.8. İcare (Leasing)

Leasing system is brought out by the idea of meeting the middle term finance needs in USA in 1950s but the system has been used for ages in Islamic communities.

Participation Banks has the authority to apply leasing. In contrast to the conventional trade banks in our Country, Participation Banks apply their leasing applications in their own structure without establishing a separate leasing company.

Leasing is structured on an agreement between lesser and lessee. The time and cost of the lease must be stated on the agreement.Property of leased goods belongs to the participation bank, owner of the goods. Lessee customer benefits from the goods, pays a lease cost in return. Leasing time can change according to disposability of the goods.

There is another operation called as 'sell and back' though it is not the basic operation subject of finance leasing companies. Financial leasing company buys in cash the machinery, equipments of facility of the investor that needs cash money and simultaneously lease the goods to the investor. Customer gets the cash it is in need and pays back in installments. As can be seen, financial leasing company actually acts as a bank. Sell and back is named as 'Lyne Sale' in Islamic literature and it is totally cash credit with simulation for participation banks. Besides, leasing operation is subject to Turkish financial leasing law and executed within the scope of this law.

5.3.9. Hire-purchase

A customer that hires property from Participation Bank can apply to hire-purchase application when the customer wants to buy the hired property. As long as the customer's income raises and financial possibilities are widened, the customer can apply for hire-purchase application and get the property of the production tool that is hired. For a certain time the customer pays the value of the property in installments and gets the total ownership of the property in the end. As the customer pays the installment, the hire cost that the bank gets decreases in inverse proportion with the payment. In the end customer owns the property. The system is not used widely in Turkey.

5.3.10. Individual Finance Backing System

Participation Banks enable individual real estates and vehicles within the scope of murabaha system. The operation is as followed; the cost of goods or service that natural person vendee buys directly from vendors for individual needs as individual finance system, vehicle or real estate is paid back by Participation Bank to the vendor on behalf of the customer, in return the vendee is debit. Participation Banks does not have the same strategy with deposit banks in terms of individual consumer credit. Banks can make their individual customers to use the credits in cash, participation banks does not make any payment to its customer at any case. Besides, individual customer must be prudent man about individual credits. For example, if a customer wants to buy 4 fridges and 3 televisions and wants credit for those needs, the credit demand of the customer will most probably be rejected by the participation bank.

5.3.11. Bai Salam

Bai salam means a contract in which advance payment is made for goods to be delivered later on. The seller undertakes to supply some specific goods to the buyer at a future date in exchange of an advance price fully paid at the time of contract. It is necessary that the quality of the commodity intended to be purchased is fully specified leaving no ambiguity leading to dispute. The objects of this sale are goods and cannot be gold, silver, or currencies based on these metals. Barring this, Bai Salam covers almost everything that is capable of being definitely described as to quantity, quality, and workmanship.

5.3.11.1. Basic features and conditions of Salam

1. The transaction is considered Salam if the buyer has paid the purchase price to the seller in full at the time of sale. This is necessary so that the buyer can show that they are not entering into debt with a second party in order to eliminate the debt with the first party, an act prohibited under Sharia. The idea of Salam is normally different from the other either in its quality or in its size or weight and their exact specification is not generally possible.

2. Salam cannot be affected on a particular commodity or on a product of a particular field or farm. For example, if the seller undertakes to supply the wheat of a particular field, or the fruit of a particular tree, the salam will not be valid, because there is a possibility that the crop of that particular field or the fruit of that tree is destroyed before delivery, and, given such possibility, the delivery remains uncertain. The same rule is applicable to every commodity the supply of which is not certain.

3. It is necessary that the quality of the commodity (intended to be purchased through salam) is fully specified leaving no ambiguity which may lead to a dispute. All the possible details in this respect must be expressly mentioned.

4. It is also necessary that the quantity of the commodity is agreed upon in unequivocal terms. If the commodity is quantified in weights according to the usage of its traders, its weight must be determined, and if it is quantified through measures, its exact measure should be known. What is normally weighed cannot be quantified in measures and vice versa.

5. The exact date and place of delivery must be specified in the contract.

6. Salam cannot be affected in respect of things which must be delivered at spot. For example, if gold is purchased in exchange of silver, it is necessary, according to Shari'ah, that the delivery of both be simultaneous. Here, salam cannot work. Similarly, if wheat is bartered for barley, the simultaneous delivery of both is necessary for the validity of sale. Therefore the contract of salam in this case is not allowed.

7. This is the most preferred financing structure and carries higher order Shariah compliance.

5.3.12. Credit Cards in Participation Banking

Participation Banking credit card system applications are generally the same as conventional banks. In Participation Banking credit card system depends on the inter banks card center and the same system applications, which is the same as the other conventional banks. Purchase and sell of goods is the base of Participation Banking credit card system as murabaha applications but purchase of the products that is not suitable for interest free banking system such as alcoholic drinks etc. with credit card is limited by participation banking. Some participation banks apply installments with only late interest in credit card applications and when selling the product, they make installment with cash price equivalent. Bank Asya, Türkiye Finans and Albaraka Türk participation banks make installments with cash price equivalent, Kuveyt Türk Participation Bank makes installment with late interest conditioning. Before buying the goods with credit card, the customer is informed by text massaging about installment number, late interest inclusion and the customer prefers or denies making installment accordingly. This application can be done from any pos machine.

Credit card fees are credit responsibility of participation banks and some of the banks do not take annual card fees. Minimum payment is applied in conventional banks but participation banks do not have the same manner for the subject. KuvetyTurk and Albarak Turk participation banks do not have minimum payment application but Bank Asya and Turkiye Finanace take minimum payment. Credit card default interest rate is determined by

Banking Regulation and Supervision Agency as 2,83% and this default interest rate is transferred to a separate pool by participation banks and do not used as funds. According to the last data, 2,10,000 pieces of credit card is available at participation banks. With 1,500,000 pieces of credit card sell, Bank Asya is leading of all participation banks.

5.3.13. Bahreyn Credits

Bahreyn credits are formed on the basis of enabling financial support to the bank customers from sellted off-shore branches in Bahreyn by some of the participation banks in Turkey. Within this scope Bahrey branch of the participation bank plays the financier role and finance itself from local and international inter banks money market. In brief, Bahreyn muharaba credit is a mutual operation that is used to meet capital needs of small and medium enterprises.

Bahrey credits have 1 year 1 week time (between 372-385 days) and they are external credits. Credits have 1 year 1 week time because of taxation advantages of the time. Bahrey muharaba credits are project based. The goods that the customer buys or the finance the customer demands within Islamic Banking frame is recorded as credit in customer's account and participation bank customer transfers the money in return for a receipt to the party that the goods is purchased.

Bahreyn Muharaba application has three main steps. First step is 'Forming-marketing'. During this process, details of offered application is negotiated and completed. Second step is 'configuration and documentation'. During this step, murabaha application is performed and application agreements are negotiated. This step ends with signatures. Third and the last step is ‘Operation step’ and credit application continuous.

Bahreyn murabaha credit policy regulates the general rule and frame in application of activities regarding murabaha operations according to International market application of investment banking department of participation bank. Bahreyn murabaha application is a credit operation that is constituted in accordance with participation banking working principles and Participation Bank’s Bahreyn Brach gives murabaha credit within general conditions and principles of “Master Agency and Promise to Buy Agreement “agreement.(excluding commission).

5.3.14 Islam Development Bank Credits

5.3.14.1. Sep Credits

Saudi Fond for Development (SFD) is established as an official export credit corporation in 1999 and Saudi Export Credit Program of the corporation provides finance, insurance and guarantee services to its Saudi exporters and foreign customers of Saudi goods (importers).

5.3.14.2. Objective

Saudi Export Program was established to increase Saudi Arabia’s goods other than crude oil. The program enables finance and insurance means to foreign companies that import Saudi Arabia originated goods, which brings out financial agreement cooperation opportunity between mentioned company and participation banks. Within this scope, participation banks could give low cost finance (murabaha) to its customers dealing with import in Saudi Arabia.

5.3.14.3. Target Market

Apart from crude oil, all the goods that are subject to import are included to SEP concept and financed by it. The target market of the credit is import companies with potential and high credibility and morality.

5.3.14.4. Time and Period of the Credit

Minimum amount of the credit is 133.000 USD and maximum amount is 1,500,000 USD for all the customers. Date of redemption is 13 months later the beginning date of the credit.(active payment date of SFD). Credit period starts on the date that SFD makes payment to the import company on behalf of importer after importer receives the goods and credit period continuous until the repayments of the importer to the bank is completed.

5.3.14.5. General Specifications and Advantages of Credit

- Participation bank is allocated a certain limit within the program concept by SFD.

- It serves as a proxy of SFD in term of financing the goods and services apart from crude oil that Participation Bank's importer customers would buy from Saudi Arabia and it is responsible of repayment of the credit as the debtor part of SFD and carries credit risk of the importer.
- By force of finance agreement, local (Saudi) value added rate of subjected goods to be credited must not be less than 25%.
- Importer Company uses the credit with fix profit share application in accordance with interest free banking. Credit pricing is made on the basis of LIBOR + 1% (SFD) + 3% (Bank commission – depends on banks). Corporate marketing administration holds the amendment authority on behalf of commission. Labor is considered as an indicator to determine a profit share rate according to market conditions. Credit contains a funding relying on the commercial product and buying –selling agreement between buyer and seller. So determined final rate is the rate that becomes clear with credit period and excludes interest. Credit interest rates of conventional banks in sector is one of the indicators used to determine interest share rates constituted for murabaha funding of participation banks.
- Allocated commission is shared between related branch in terms of performance and participation bank.
- Banking and Insurance Tax of the commission amount must be collected. Profit share of the credit is collected on expiry date together with the capital according to repayment plan (unless otherwise stated).
- There are no financial responsibilities such as Banking and Insurance Transaction Tax of profit share.
- In terms of exported company the credit enables competitiveness; guarantee to collect goods value, quick collection and new markets finding opportunities. And this can enable Importer Company pricing and goods supplying advantages.
- In terms of Importer Company, credit enables medium and long term finance, low cost borrowing, easy cash flow planning and competitiveness.

- Participation Bank advantages in terms of SEP are opportunity to present alternative products, more effective credit limit usage of corresponding banks and higher foreign trade figures and competitiveness.

5.3.14.6. Work Flow

Credit Use

- Importer Company applies to a participation bank branch and states its finance demand. If application of the customer with assigned credit limit approved, SEP application form is filled and transmitted to participation banking.
- Customer of the bank must have an agreement with the Export Company about the payment through SEP credit. Pro forma invoice can be amended in accordance with this when necessary.
- Resale agreement is applied between Import Company and Bank (as SFD agency) about the operations approved by investment banking administration.
- Investment Bank administration sends authorization demand document to SFD. After checking this demand and all the other documents relating import, SFD send the authorization certificate showing that the transaction is approved to investment bank.
- After obtaining the authorization certificate, participation bank gives instruction to accredit in favor of exporter (through related branch). After the accreditation, exporter performs loading. After the documents that the bank received are checked, foreign trade and treasury operations unit of

SDF gives instruction about payment of cost of the goods to corresponding bank.

- Related branch enters the project to the system in order to collection of given long term credit references to make foreign sourced credits be informed with statistical aims to Central Bank of Turkey.
- SFD forwards profit rate about the operation, repayment table of the capital and its amounts to participation bank through payment instructions. These documents are sent to the related branch and foreign trade and treasury operations unit.

Credit Repayment

- Import Company pays the capital and profit rate to participation bank when operation period is over. Bank transfer this payment to SFD accounts and finishes credit operation.
- Participation bank takes the commission in cash. But within customer effectiveness and profitability, collection method of the commission depends on the evaluation of marketing unit.

Points to Consider

- Credit amount is determined by considering the tolerance rates of cost of goods on letters of credit.
- SEP makes payments only through Saudi Arabian Riyal and American Dollar currency types. This must be considered while negotiating with the customers.
- In order not to breach the relationship between SDF and participation bank and to maintain the mutual trust repayments must be

made on due times and branches must endeavor to inform the company in advanced.

- It is suitable to be informed at least one week earlier about the customs entry of the goods subjected to import. Credit demands, operations on process and Saudi Arabian holidays(Thursday – Friday) must be considered as well.
- It is a principle not to take risk without proper credit guarantee form.
- During SEP credit operations, participation bank customers must be directed to take the advantage of the other operations of the bank. Thanks to this credit use, positive working environment is established with the customer and through cross selling and marketing, maximum productivity of the customer must be gained.

5.3.14.7. Elements of IDB Group Partnership Strategy

5.3.14.7.1. Past Interventions by the IDB Group in Turkey

IDB Group total financing approvals for Turkey has reached US$4.6 billion. Total cumulative approvals of IDB project finance and technical assistance operations for Turkey since inception now exceeds US$ 1.1 billion. Since inception, IDB has approved 85 ordinary operations (net of cancellations) including special assistance. The transport sector has received the largest share of financing, around 34% of total approvals by value, while financial institutions, social services and industry received 22%, 18% and 15%, respectively. Distribution of the operations by mode wise has been balanced. Installment sale, leasing and istisna's modes has each had a share around one fourth of the total approvals while other modes, mainly equity and loans, account for the remainder. Turkey has been one of the major beneficiaries of IDB Group's trade financing programs.

A cumulative total of US$3.5 billion in (gross) trade finance operations has been approved for Turkey since the establishment of IDB. This figure represents about 10% of total gross trade financing approved by the IDB Group. Following the establishment of ITFC, the annual approval level for trade financing in favor of Turkish companies and banks rose from $50 million to US$200 million. Clients of ITFC are representing a wide range of sectors including food, agriculture, textile, automotive, petrochemicals, and electronics. The main financial institutional partners of ITFC in Turkey are Turk Exim bank and four Participation Banks. ICIEC has been supporting Turkish exports since inception of its operations.
The total amount of business insured by ICIEC for the exports from Turkey reached US$ 674 million while business insured regarding the imports to Turkey amounted to US$ 201 million. Regarding the investment insurance, ICIEC has not issued a policy so far, however, there are some applications received from Turkish investors about investments/projects in some of ICIEC member countries, which are under review, by ICIEC. Concerning investment promotion and capacity building activities, ITAP organized familiarization and capacity building programs in Turkey, in coordination with TOBB for the officials from other IDB Member Countries. (Islamic Develeopment Bank Group, Maint Report, Member Country Partnership Strategy of the IDB Group for Turkey)

Islamic Development bank extended in total 50 million USD credit with 13 months period repayment for the use of SME in Turkey in 2008. 40 million USD credit with 10 years period repayment was enabled for the use of MSE in 2009. Kuveyt Türk Participation Bank gained 25 million USD credit with 13 months period repayment from Islamic Participation Bank. Undersecreteriat of Treasury and Islamic Development Bank signed a credit agreement of 554 million USD amount for the finance of Seismic Risk Elimination and Emergency Preparedness Project in 2012. 110,070,000USD amount of the credit is 3 years nonrefundable in total 18 years period.

158,930,000 EUR amount of the credit is 5 years nonrefundable in total 15 years. 174,350,000 EUR amount of the credit is 3 years nonrefundable in 15,5 years.

5.3.15. Structured Finance Operations

5.3.15.1. Syndication operations in Participation Banking

Through only finance of operations suitable for interest free banking principles, participation banks take part in the operations that suits these conditions. So, before dealing with structured finance operations following principles are considered.

- The company that is to take part in syndication must operate in the field that is not prohibited according to interest free banking principles.
- Syndication operation structure must be in accordance with interest free banking principles.
- Participation banks must take part in short/medium and long term structured finance operations regarding finance of business capital and customer investment projects.

Syndication operation has three main steps. First step ‘ Pre-Authorization Step’ details of the offered operation is negotiated and completed. Second step is ‘Post Authorization Period’. Syndication operation is performed and agreement of the operation is negotiated in this period. This steps ends with signing ceremony. Third step is ‘Post Signature Step’. It is applied all syndication credit period long.

5.3.15.2. Participation Banking Murabaha Syndication Examples

Turkiye Finance Participation Bank signed murabaha credit agreement of 75 million USD with Bank Islam Brunei Darussalam in November 2011. Before this, Turkey Finance signed murabaha syndication credit of 300 million dollars with consortium consisting internationally 20 banks on CitiBank’s leadership in March 2011. Turkiye Finance signed the project finance credit agreement for 5 year period 75 million dollars credit that is nonrefundable for 2 years. And this is the credit with the longest period of all Participation banks. With the last murabaha syndication, the credits that Turkiye Finance received from abroad reached to 800 million dollars.

Bank Asya gained murabaha syndication over 300 million dollars with participation of 26 banks from 19 countries, in Turkey November 2011. Repayment of 1year period credit is LIBOR/EURIBOR+1,5 profit rate on condition. Bank Asya got murabaha syndication over 324 million dollars with participation of 28 banks from 17 countries in total and with the leadership of ABC Islamic Bank, Emirates NBD Bank, National Bank of

Abu Dhabi, Noor Islamic Bank ve Standard Chartered Bank in April 2012. Profit rate of 1year period murabaha operation is determined as LIBOR/EURIBOR+ %2.

In 2009, Kuveyt Türk enabled 115 million dollars syndication credit got as 1 year period and priced labor+%2,5 through Bahreyn branch. The other mediating banks of murabaha syndication that Kuveyt Türk was the regulatories are Liquidity Management House For Investment Company K.S.C.C Türkiye Halk Bankası A.Ş, İslam Kalkınma Bankası, City Bank N.A, Garanti Bank, İntenetional N.V, Gatehouse Bank, Plc National Bank Of Kuwait (International), Plc ve Standart Chartered Bank. Kuveyt Türk got Bahreyn credit of 150 million USD for 1 year period in April 2012.

Albaraka Türk got murabaha syndication credit of 240 million in 2010 and another murabaha syndication credit of 350 million dollars in September 2011. Period of murabaha syndication credit that was enabled with the participation of 25 banks – with leadership of Noor Islamic Bank, ABC Islamic Bank, Standart Chartered Bank and Emirates NBD and financial corporations -including abroad participations of Denizbank, Halkbank, Ziraat Bankası, Vakıfbank ve Yapı Kredi- from 17 countries is determined as 1 year. 202, 5 million dollars of the credit is LIBOR+1,50% cost, 103,3 million euro costs EURBOR+1,50.

5.3.16. Takaful (Islamic Insurance)

Participation Banks in Turkey recently incorporated Islamic insurance system to give a quick reply to the rapid development of banking system and needs of customers widely.

Takaful is an alternative form of cover that a Muslim can avail himself against the risk of loss due to misfortunes. Takaful is based on the idea that what is uncertain with respect to an individual may cease to be uncertain with respect to a very large number of similar individuals. Insurance by combining the risks of many people enables each individual to enjoy the advantage provided by the law of large numbers.

Islamic insurance system operates on this basis; the ones who wants to insure their goods goes to insurance company and becomes member they pay a price for a certain period of time (monthly, annual). This price is recorded on their behalf. Certain amount of the collected money is saved to pay damages. The rest is used for trading and investment. All the members participate in the investment and trade.

Insurance companies operate the premiums of their members in various pools and start to pay retirement pension to these members. Customers that pay premium is generally not interested in use of this money and the way of making profit. Takaful or Islamic Insurance system is based on questioning the use of these premium and the areas they are used. For non Islamic banking Insurance, the operations that are performed with invested premiums are questioned as being halal-forbidden principle of Islamism. The subject is not a matter of sensitivity.

Income of the trade sometimes meets the damage of the insurance owners and the rest is transferred to fund as income. The expenses of the company are met from the fund and trade incomes.

In interest free insurance system, the money collected is evaluated out of interest banks or finance system, in goods trade and precious metal market that does not have interest, in a buying-selling based finance operation that has no interest.

Participation Banks in Turkey established insurance companies that are their own associations and started to take share from insurance sector. Besides their own works participation banks address to all of the customers that needs insurance and they make progress in insurance sector as well.

An individual who needs takaful system and interest free insurance system and growing and developing interest free banking system of companies needs are met as well.

5.3.17. Forward in Participation Banking

Forward operation has been performed for many years in conventional banking system and for the last 5 years the system has been used in participation banking as well. Forward is an operation that bounds to an agreement and determines by parties the period, amount and price of any goods (currency, agricultural product etc.) to be delivered on postdate. Characteristic of the operation is that buying and selling agreement is made as today and delivery and return payment is made on post date with agreed price. Forward operations of participation banking include only timed currency buying-selling operations. . Forward operations of participation banking system is performed as participation account blockage or forward limited. The aim of forward is to protect from the future rate and price risks.

5.3.17.1. Participation Account Blockage Forward

A forward limit is formed by considering the financial data and affordability of the customer. No block is applied to the forward operation formed by opening a limit. Here, depending on the decision of credit committee forward limit can be a signature, cheque or hypothec. Guarantee decision is credit committee. Forward operation is applied to the customer providing guarantee in limited forward operation and on forward date the customer pays money to the account and operation ends.

In both forward operations, necessary forward agreement is made. In both operation period is minimum 1, maximum 365 days. Forward operations can be breach maturity and amount gap is minimum 5,000USD maximum 5,000,000 USD (amounts are parametric and can be changed if wanted). There is no turn in forward operation but if wants; participation Bank can perform adverse event and closes customer's position. 10% of withholding deduction from customer profit is applied in forward operations.

5.3.17.2. Forward limited Forward

A forward limit is formed according to customer's financial data and ability to pay. Blockage is not applied to the forward operation performed by opening a limit. According to the decision to be taken by credit committee forward limit may be in numeration for a signature, chaque or hypothec. Guarantee decision belongs to credit committee. In limited forward operation, forward operation is applied to the customer that guarantee is enabled and on forward date customer invests money on the account and operation is closed.

Related forward agreement is taken for both forward operations. Term is minimum 1 maximum 365 days for both operations. Forward operations may be breach maturity. Amount gap can be minimum 5,000USD maximum 5,000,000USD. (Amounts are parametric and can be changed if necessary). Forward operations are irreversible but in need of participation bank, it can close the customer position by applying reverse operation. 10% stoppage deduction of customer profit in forward operation.

5.3.18. Swap in Participating Banking

Swap is a product used to be protected from risks as forward.

- Among currency types in Swap, there is spot on one part and forward on the other part.
- Spot is suitable with expenditure contract Islamic principles.
- Promise is used on forward products(single sided)
- Product can be used in one day period.

5.3.18.1. Sway among Currency Units

Swap is a product that is used in order to be protected from risks as it is for forward operations.

- For swap products in currency units, there are spots on one part and forward contracts on the other part.
- Spot (expense contract is in accordance with the Islamic rules)
- Promise(one sided promise) is applied in forward products.
- Products can be used in one day time line.

5.3.18.2. Profit-Rate Swap

Profit-Rate Swap is a mutual agreement regarding the exchange of the payments of floating profit cost and fixed profit cost calculated by depending on the capital the parties agreed. The exchange is made on the same currency type. Capital amount is the same as the related goods value or the money borrowed. In short, one party becomes indebted with fixed profit and the other party with floating profit and then profit payments are exchanged.

In many profit rate swap, floating profit payments are stated with the reference of LIBOR. As can be understood, one of the main aim of profit swap is to eliminate high profit payments by changing a floating profit debt to a fixed profit debt or vise verse.

5.3.19. Mudaraba – Risk Capital Investment Partnerships

Mudaraba – Risk Capital Investment Partnerships is lately developing and is not completely started to be performed for participation banking. Mudaraba – Risk Capital Investment Partnerships (MRCIP) is open to public anonym partnerships that aim to participate venture firms. Participation shares of MRCIP –as of the other open to public firms- are sold to the investors with primary and secondary market operations. MRCIP is one of the common investment partnerships and has the same general features of the investment partnerships. Along with this, MRCIP cannot benefit from leverage factor as bank credit and/or bond issuing. MRCIP is in real a risk capital company and working conditions are completely similar to risk capital companies. Financial mediators of MRCIP are mainly interest free banks but trade banks and investment banks can be mediator as well.

There may be different MRCIP founded according to different investment aims and strategies. The aim and strategy of the partnership will be stated on partnership agreement. Similar to risk capital companies some MRCIPs use specialization strategies on enterprise and development base and on sector base while others applies diversification.

MRCIP with specialization strategies will have less on enterprise development stage and on sector enterprises. MRCIP with diversification strategies will have two or more on enterprise development stage and more on sector enterprises.

Four types of MRCIP are identified in model.

5.3.19.1. A Type Mudaraba-Risk Capital Investment Partnership

The enterprises of these partnerships on investment portfolio will be based completely on similar companies that are on core of inception stage.

5.3.19.2. B Type Mudaraba-Risk Capital Investment Partnership

The enterprises of these partnerships on investment portfolio will be based completely on similar companies that are on enlargement or company reformation stage.

5.3.19.3. C Type Mudaraba-Risk Capital Investment Partnership

The enterprises of these partnerships on investment portfolio will be based completely on similar companies that are on takeover stage.

5.3.19.4. D Type Mudaraba-Risk Capital Investment Partnership

The enterprises of these partnerships on investment portfolio will be based completely on similar and/or different companies that are on two or more stages of ‘core, inception, enlargement, company reformation and takeover’ stages.

A,B and C type Mudaraba-Risk Capital Investment Partnership follows significant conciliation strategies; mixed investment partnership type D

Mudaraba-Risk Capital Investment Partnership follows diversification strategies.

5.3.20. Mudaraba-Risk Capital Investment Funds

Another participation banking product of recent tears that has not started to be applied yet is Mudaraba-Risk Capital Investment Funds (MRCIF). Mudaraba-risk capital investment funds are financial mediators that form portfolio from participation shares of MRCIP and risk capital companies and manage – in accordance with fund agreement- the income taken from account owners in return for participation document. Fund does not have legal entity. Participation document owners do not have right to participate in the management of the fund. The responsibility of fund owner is to manage the fund on behalf of participation document on the basis of risk elimination and fiduciary ownership. MRCIF is a common investment fund and holds general features of investment funds. Along with this, investment area of MRCIP and risk capital companies is limited as participation shares.

Different MRCIFs will be established with different investment aims. Investment aims will be stated on agreements. Partnership shares that will be included to portfolio will be determent according to MRCIF investment aims. Portfolio of some of MRCIFs is formed completely of partnership shares of investment capital companies and MRCIPs that invested in specific enterprise development stages while portfolio of some others is formed of partnership shares of risk capital companies and MRCIFs that have investment on both enterprise and development and sectoral base.

Intermediately firms that would evaluate MRCIF and risk capital companies in determining partnership shares to be taken to fund must be included to the system in order to make MRCIP system gain functionality. Mentioned evaluation firms will at the same time give consultancy service for MRCIFs that will invest.

Four types of MRCIF are identified in model.

5.3.20.1. A Type Mudaraba-Risk Capital Investment Funds

Investment portfolio of these funds is based completely on MRCIPs and risk companies that invested in core and/or inceptive stage enterprises.

5.3.20.2. B Type Mudaraba-Risk Capital Investment Funds

Investment portfolio of these funds is based completely on MRCIPs and risk companies that invested in enlargement and/or company reformation stage enterprises.

5.3.20.3. C Type Mudaraba-Risk Capital Investment Funds

Investment portfolio of these funds is based completely on MRCIPs and risk companies that invested in takeover stage enterprises.

5.3.20.4. D Type Mudaraba-Risk Capital Investment Funds

This is a mixed fund. Investment portfolio of these funds is based completely on MRCIPs and risk companies that invested in similar or different enterprises that are on any of the two or more following stages as ‘core, inceptive, enlargement, company reformation ,takeover’.

For both model offer, when investors decide on the type of the partnership and partnership fund they need to make investment by considering risk capital investment types and risk premiums of profiles of these investments. For example, in risk capital finance investments with high risk groups are core stage investments that are defined as cash trap. On the other hand, though having high risk level, it brings the highest premium. So, an investor with the aim of getting high premium will prefer to invest in investment partnerships and investment funds that include core stage investments.(Bulut, 2009)

5.3.21. Participation Index

Participation Index is a stock market index that is traded at Istabul Stock Exchange and consists of participation shares in accordance with Participation Banking principles. Index is now actively used. Participation share choice is performed on the basis of Index Rules prepared by Participation Bank principles. So, index has companies that excludes finance, trade, service, mediation(banking, insurance, financial leasing, factoring and the other interest based types) on interest based business areas, alcoholic drinks, gamble, game of chance, foods like pork meat etc., press, publication, advertisement, tourism, amusement, tobacco products, weapon, forward gold, silver and currency trade. Besides, the companies that would like to participate into index must meet some financial rates. The company rate of total interested credits to market value must be less than 30%, the company rate of cash and security to market value must be less than 30%

and incomes that the company gets through above mentioned activity areas must be less than 5%. First 30 companies -open to public through its partnership shares- with highest market value in accordance with these rules forms index companies.

With progresses on buying-selling of partnership shares that are suitable for interest free investments and Participation Banking in the last decade, standardization of the area becomes obvious. Actually, we can see that these kind of similar investments have been performed by interest sensitive investors for long time. In reality principles are the same but as there is no standardization in sector wide there can be complexities. Participation index is an important step taken to fill the gap in this field and to construct standardization sector wide.

Another aim of the indexes characterized as indicators is comparison. It is thanks to index that investors can compare incomes of their investments with market incomes. There are sector indexes to compare the investments different sectors. But there was not any index that investors who invest in accordance with interest free and participation bank can compare. Comparison of different indexes was meaningless. Participation index is a useful tool to serve to this aim.

Depending on the amendments in regulations and developments in our market in recent years, we can see that new capital market tools become current issue. As the markets grow, alternative goods continue to be in need, in order to strike investor's interest. Index are one of the most important instruments of product developing finance corporations. Investment funds, stock investment funds, individual retirement funds and other investment tools can be developed through index. Participation index is based on goods addressing its own investment group and goods that can be used with the aim of product developing.

As alternative investments are rapidly growing worldwide and as these investments are one of the most developing areas, structuring a participation index to strike investor’s interest is very important. There is a great lack of addressing to this investor group in our country as we do not have any standardization in this field. As Participation Index Rules takes international applications into account, Participation Index and all the products and services of this index will also address to foreign investors. Participation index which is to meet the needs of investors that invest in accordance with Participation Banking principles and constitutions giving this service is the first step that is taken in this field- and in the fields of evaluation of partnership shares that would be accepted as credit guarantee, usability of derivative applications and partnership shares and in many other fields-, which brings it another value.

5.3.21.1. Starting to Calculate Index

Starting date of index is 31.12.2008 and it is calculated as price and premium index of simultaneous data from the date of 06.01.2011. the value of the index on the starting date of 31.12.2008 is 19.781,26 value which is the close value of Istanbul stock Exchange industrial index dating 31.12.2008. When index is calculated only with close prices between the dates 02.01.2009-05.01.2011 and with simultaneous data on the date 06.01.2011, it is calculated by the companies current on the index. Participation index exchange investment fund is put into operation on 16.05.2012.

5.3.21.2. Examination According to the Operation Area

The companies to be placed on the main list, main operation area,

- Finance, trade, mediation with interest(it contains banking, insurance, financial renting, factoring and other areas with interest)
- Alcoholic drinking
- Gambling, game of chance
- Pork meat etc. foods
- Tourism, entertainment
- Tobacco products
- Weapons
- Dated gold, silver and currency trading

5.3.21.3. Examination for Financial Rates

a) Companies on the main list are subjected an elimination according to their financial rates. In order to enter index;

i) Total interest credits/market value < %30

ii) Cash and security with interest premium/market value < %30

iii) Incomes of the applications stated article no 5.12.20.5.2 / total income< %5 rates crosscheck is needed. Income means all incomes of the company. These incomes include sales incomes, interest incomes, incomes of other activities and incomes of the activities out of main areas. Companies that cannot meet these criteria are eliminated from the list. If there is a provision that the company will have activities in accordance with Participation Banking principles, rate meeting of the company is not a must.

b) Although not stated on master agreement of the company, if open public company's finance tables, announcements and company's activity area according to other sources consist of the activities stated in article no 5.12.20.5.1. then the rates in article no 5.12.20.5.1. is taken into account. If the company does not meet these rates, it is eliminated from the list.

c) If company's direct or indirect- through partnership and participation- activities out of main areas activities include one or more of the above mentioned activities, the incomes of these activities are considered by means of participation rates. The average rates of the companies in index scope calculated according to articles no 5.12.20.5.2. a) iii) is announced by Rating Period.

d) If a company is known as having an activity relating above mentioned articles but its revenue search could not be made through official sources, a value or value range is found depending on the information gained from best effort underwriting open to public and/or from the company itself. If the company does not meet the rates stated on article no 5.12.20.5.2. a) with the value or value range gained, or no data is obtained about its meeting the rates, the company is eliminated from the list.

5.3.21.4. Index Companies 30

Adana Çimento (A), Afyon Çimento, Akçansa, Albaraka Türk, Aygaz, Bagfaş, Bank Asya, Bim Mağazalar, Bizim Toplu Tüketim, Borusan Mannesmann, Bursa Çimento, Çimsa, Enka İnşaat, Ford Otosan, Good-Year, İzmir Demir Çelik, Kardemir (D), Kartonsan, Koza Altın, Mardin, Çimento, , Nuh Çimento, Petkim, Pınar Süt, Sinpaş GMYO, Soda Sanayii, Trakya Cam, Tüpraş, Türk Telekom, Türk Traktör.

5.3.22. New Product in Participation Banking: Gold Accounts

It is an account type that is current and enables the savings to be evaluated through gold. Buying and selling activities in TL or USD can be managed by gold accounts. Without having low grade of fineness or carriage, one can buy and sell gold as currency even with 1 TL. Whenever wanted, physical equivalent of gold can be withdrawn from Participation Banks.

a) Characteristics

- 1 gr gold is processed at 1000/995 fineness net.
- Minimum process value limit is 0.01 gram.

- For natural entities, gold account up to 50,000TL is under guarantee of Savings Deposits Insurance Fund in other words under the guarantee of the government.
- Regular gold buying and selling process can be applies. With the instruction of customers, gold is bought to the account automatically from the branches on determined dates and regular gold saving can be achieved by this way.
- Without the need for price tracking, participation banks can instruct their branches about buying and selling on a specific rate. For example; customer can instruct as ‘when gold rate is 75TL; transfer the gold in my account to my TL account’.
- Customer can make a remittance between gold accounts or to another person’s gold account from participation bank branches of from internet branch.
- Customer can take the gold in the account as 1,2.5,5,10,20,50,100 and 1000 gram bullions. At this point bullion gold and delivery expenses must be paid.
- Gold cheques can be arrange by gold accounts or the gold can be withdrawn from branches or can be withdrawn from specific ATM, adding gold to gold account can be opened.

5.3.23. Adding Gold to Gold Account

Adding gold to gold account enables to make a profit and savings. Each gold gram is evaluated in real sector and the profit made returns to customer’s gold account.

a) Characteristics

- Account can be opened with minimum 10 gram.
- Income accrued on due date is shared 50/50 per cent between participation bank and customer.
- The account can be opened as 3 months, 6 months and 1 year time periods.
- As long as balance is not below 10 gram gold in the middle of period, gold can be sold from the account, no period change is applied; profit share is taken from the rest of the balance.

b) Advantages

In enables both gold investment and gaining profit share from it. Safe buying and selling is applied with no carriage and storage concerns. No labor cost is paid for gold buying selling processes. Profit is gained with even 10 gram; there is no need for billions of gold.

5.3.24. Gold Gram

It enables alternative investment opportunity for account owners who want to invest in physical gold instead of bank account or who want to evaluate his gold in bank 1,2.5,5,10,20,50 and 100 gold gram options are minted by Istanbul Gold Refinery(IAR) and sold to participation banks.

Certified gold grams can be converted to IAR certified gold grams by jewelers. This gold is evaluated in adding gold to gold accounts in participation banks.

a) Characteristics

- Pure physical gold with 24 fineness buying and selling processes can be performed without a need for an account or it can be performed easily from TL, USD or Gold accounts in the branch.
- Gold bought from participation bank or other gold with Istanbul Gold Refinery certificate are retaken as long as the packing is not deformed and can be changed at jewelers at any time.
- As gold gram has Istanbul Gold Refinery mark can be changed at not only branches but also jewelers. When gold grams are taken from Gold, TL, USD accounts or from the safe, certain amount of commission is taken.

b) Advantages

- Gold grams can be invested in bank accounts. Gold gram can be invested or withdrawn through Gold storage and adding gold to gold account.
- Labor cost is in minimum level when compared with the other physical investment types.
- It can be chanced in bank or in jewelers.

5.3.25. Gold Cheque

- Gold cheque substitutes for gold. It is formed on paper as a cheque and can be processed as gold. Gold cheques have various grams and they can be given to other individuals by customers. They can be used as presents as well.
- Customers can buy gold cheque through TL, USD or EUR accounts.

a) Advantages

- There is no need to be the customer of the bank to buy gold cheque from the bank.
- The owner of the present can receive the value of the cheque as TL, USD or certified gold gram or can open adding gold to gold account and start saving account.
- It is safe. No one but the person whose name is on the cheque can use it.

5.3.26. Silver Investment Accounts

It is an account type that is current and enables the savings to be invested in silver for the ones who wants. Buying and selling activities in TL or USD can be managed through silver accounts. The purity of the silver bought to the account is 1000(thousand) fineness. Silver can be bought even by 1TL.

a) **Characteristics**

- Remittance can be made between silver accounts. Buying instruction can be given at regular basis or at a specific rate of silver.
- For natural entity accounts, silver account up to 50,000TL is under guarantee of Savings Deposits Insurance Fund in other words under the guarantee of the government.
- Physical delivery is also applied in silver accounts.

5.3.27. Platinum Investment Accounts

It is an account type that is current and enables the savings to be invested in platinum for the ones who wants. Buying and selling activities in TL or USD can be managed through platinum accounts. The purity of the platinum bought to the account is 1000(thousand) fineness. Platinum can be bought even by 1TL.

a) **Characteristics**

- Remittance can be made between platinum accounts. Buying instruction can be given at regular basis or at a specific rate of platinum.
- For natural entity accounts, platinum account up to 50,000TL is under guarantee of Savings Deposits Insurance Fund in other words under the guarantee of the government.
- Physical delivery is also applied in platinum accounts.

5.3.28. Remittance of Gold

It is another new product that participation banking developed in recent years. Through gold remittance, customers can make remittance of gold from their accounts. The gold on the accounts can be transferred as gram or bullion. And receiver of the remittance can get it as gram or bullion from a branch on the same day of the transaction. In this way, gold can easily and safely reach at the targeted place.

a) Advantages

- The greatest advantage is, it is cost free.
- Gold can be transferred risk free with no security problem.
- There is no stealing or carriage risk.
- As bank does not demands storage cost, when gold prices get low more gold can be bought and saved in the bank.
- It enables great easiness to jewelers and manufacturers that transfer gold as part of their jobs.(for example; an individual who wants to send rough gold billion from Istanbul to manufacturers in Anatolia.)

5.3.29. Physical Gold Collection

Participation banking presents another new product to individuals with under-the-mattress gold savings. Now everybody can bring his gold (quarter gold coin, half gold coin, gold coin, gold bracelet, necklace etc., fine or white gold at any fineness) to participation bank branches and invest to their accounts as 24 fineness pure gold. And premium is taken from the gold invested to the account.

5.3.30. Gold Backing Operations

5.3.30.1. What is gold backing?

Gold backing is a credit system that participation banks sell the gold below its market value to jewelers and exchangers and on determined expiry date recalling the gold with the same price. Guarantee with margin is taken from the customers when the gold is sold with discount. On expiry date, the gold that is given as physical is recalled again as physical or customer pays it debt by buying bullion gold with the same value from the bank.

5.3.30.2. To Whom Applied?

Gold backing product can be given to jewelers, exchangers and enterprise banking dealing with golg business. According to the related regulation it is not suitable to be applied to the individuals not dealing with gold business.

5.3.30.3. How is its Application?

On TL basis, 50% of the amount demanded, on foreign currency basis 75% of the amount demanded is blocked from customers. Following example can explain this as;

Customer wants to buy 1kg gold.

If the customer wants to buy gold on TL basis;

Gold rate is assumed as 60TL. So current market value of 1 kg gold is 59.700TL (60x1.000x0,995). 1/2 part of it is 29850 and it is demanded from the customer in cash. The rest is 29.580TL (59.700-29.850=29.850). 1,5 times more of the rest, which is 44,775TL (29.850x1,5) is guaranteed.

If the customer wants to buy gold on USD basis;

Gold rate is assumed as 30TL. So current market value of gold is 29.850 USD. 3/4 (75%) part of it is 22.387, 50USD (29.850x3/4) and it is demanded from the customer in cash. The rest is 7.462, 50USD (29.850x3/4). 1, 5 times more of the rest, 11.193,75 (7.462,50 x1,5) is guaranteed.

The gold is given to the customer. Then, on expiry date the customer brings the gold back and the part taken as cash is given back to the customer.

- Gold backing operations are performed maximum for 1 year. With the agreement of the parties after 1 year, period can be extended.
- The amount of guarantee and cash to be collected can vary according to the features of the customer and decision of fund allocation. It can be as guarantee hypothec, cash blocking, partial guarantee.
- Forward Period Buying Selling Agreement is signed with the customer.

- Bank does not get any commission for the operation. Delivery and carriage expenses of gold are customer's responsibility.
- Operation does not end before due date.

5.3.31. Gold ATM Activities

Participation banks reformed in gold field and presented ATM that can give gold in return for money. Kuveyt Türk Participation Bank presented the first gold gram withdrawal machine and led the way. Thanks to this new product, customers inserts the amount of the money equal to gold gram value they would like to withdraw and receive pure gold with various options as 1,5,10 gram from ATM.

5.3.32. Individual Retirement in Participation Banking

When the obligation of government bonds and treasury bills on at least 30% rate inclusion to individual retirement funds was abolished with 12.01.2008 dating official gazettee issue, participation banks started to take necessary actions to include individual retirement system into the system as a new product of participation banking.

Within this scope, by considering the needs of individuals who want to make investment for retirement through individual retirement system but who want to benefit from the savings through interest free financial product; retirement investment fund is structured with financial investment tools conforming totally to Islamic rules and with a total protected collection structure including collection of savings and transferring to investment stages. Entry fee deduction is not group planning based, it is applied as deferred in individual planning. Executive deduction is 1% at group planning, monthly paid contribution rate in individual planning is between 1% and 4%. Fund operation expense deduction is 5, 02 in hundred thousand. It is 42TL in Minimum Contribution Rate Group Planning and 81TL in individual planning.

The fees that the customers give in individual retirement scope are evaluated in interest free instruments by participation banks. Collected fees can be evaluated as making a bundle of interest free products as fees, gold, platinum and if necessary index documents.

5.3.32.1. Fund Asset Evaluation

- Retirement Investment Funds are separate assets of participation banks. Instruments in these fund assets are saved independently from bank assets at competent body responsible for saving the asset in accordance with the regulation.
- Cash asset of the fund is saved in the participation accounts opened in participation banks.

5.3.32.2. Investment Strategies of Fund

KIND OF ASSETS	MIN.%	MAX.%

capital market instruments based on gold and precious metals which were exported in Turkey or out of Turkey	0	100
The shares which were exported in Turkey or out of Turkey	0	100
Debt instruments which were exported inTurkey or out of Turkey	0	100
Participation or current accaounts which will be opened at participation banks in Turkey or out of Turkey	0	20
Investement Fund Participation Document	0	20

Table 2: Investment Strategies of Fund

(http://www.kuveytturk.com.tr/pages/genel_bilgi.aspx)

5.3.33. A New Instrument in Turkish Participation Banking: Sukuk

5.3.33.1. Definition and History of Sukuk

Singular form of sukuk is sakk in Arabic; it means certificate, attestation, and instrument. Plural form sukuk means certificates. Named as interest free bond with its long past history sukuk was first used B.C. 2123-2081 during the reign of Hammurabi in Babel. 100-107 parts of Hammurabi Law states borrowing system regulation terms. Assumed as applied on the basis of godly sources are especially considered as the first example of interest free investment. Mudaraba(P/L Partnership) and musaraka(capital investment) are two of the important agreement types that understructure sukuk. The legal understructure is completed by Hanafi jurists in 8.century. Venetian traders transferred this legal system to Europe. Mudaraba agreement was first used among Italians and then Spanish people.

Starting from above stated agreement application methods, sukuk with its ancient roots has become a modern finance model today. Need for sukuk increased in the last decade. The reason is Islamic rules states that money cannot be earned through money and this is called as interest, which means interest cannot be accrued on debt. Islamic rules stated that money is not an evaluation tool and connot be assumed as an asset. On this condition, debt based assets instruments as security and bond are forbidden by Islamism. In the last century, Middle East and Gulf Islamic Arabian part that became wealthy by oil wanted to evaluate their fund surplus through a fixed income financial tool according to their believes. Demand was dominating in these parties, which led financial tool sukuk applied in our age again with its legal understructure and legal regulations. Sukuk is not a debt based document as security it is an agreement based on an asset. Instead of making income through debt it holds ownership right of an asset and tries to take benefits of its incomes. Sukuk is a fixed income instrument and this distinguishes sukuk from other traditional instruments. When a saving owner makes a sukuk agreement –when he owns a sukuk instrument- , he owns the instrument and cash flow as much as on his own rate of asset. The claim in sukuk is not only about cash flow but also about ownership. In other words, customer receives the shares of income obtained from sukuk instrument besides the earnings of sukuk instrument sales. Sukuk is middle-long term investment and can be fixed or floating. During his investment period, sukuk enables its customer a regular income flow. It is a liquid instrument that is placed in secondary market. Financial reliability evaluation and ranking of sukuk is performed by international ranking institutes, which helps and guides investors to analyze risk/income of sukuk instrument. (Orhan, 2011)

ISSUES (7 of 7)				
Latest Rating Date *	Issuer	Issue Name	CUSIP / ISIN	LT Rating
25-May-2011	SIB Sukuk Company II Limited	senior unsecured		BBB+
21-Apr-2011	TDIC Sukuk Limited	senior unsecured	XS0457216124	AA
21-Apr-2011	TDIC Sukuk Limited	senior unsecured		AA
23-May-2011	HBME Sukuk Company Limited	senior unsecured		AA-(EXP)
08-Oct-2010	PETRONAS Global Sukuk Ltd	senior unsecured	USY68856AG17	A
08-Oct-2010	PETRONAS Global Sukuk Ltd	senior unsecured	716743AC3 US716743AC33	A
15-Apr-2010	Qatar Alagaria Sukuk Company (QREIC)	senior unsecured	XS0313358508	BBB+

Table 3: Evaluation of Sukuk by Rating Institutions

(http://www.fitchratings.com/jsp/general/islamic_fin/Overview.faces?listingName=IslamicFinance)

5.3.33.2. Application Area of Sukuk

Sukuk is mainly used in three application areas: Project based sukuk, asset based sukuk and balance sheet indexed sukuk. Among these areas, project based and asset based are mainly used ones.

5.3.33.2.1. Project Based Sukuk

The money collected through sukuk funds are invested in a private project. The income and owner of this project is the investor that holds sukuk funds. Qatar Global Sukuk(QSC) exported by Qatar Government in 2003 is a good example of project based sukuk. Qatar Global Sukuk is established as special purpose vehicle (SPV). This SPV have the ownership of the land that a hospital to be constructed registered on its name. Qatar Government exported 2010October expiry dating 700M USD sukuk for Hamad Hospital in Doha. Annual income is LIBOR+ 0.45.

5.3.33.2.2. Asset Based Sukuk

In this category, saving owners holding sukuk funds holds right of ownership and right of income of asset that sukuk is based as well. In other words, it sells the right of income of asset that exports sukuk to sukuk fund owner. For example, there is sukuk guarantee certificate for the rent of 600mUSD that Malaysia Government prepared in 2002.in this agreement; Malaysia Government sold an area to a SPV institute. Customer sold his right that comes through this income to investors through SVP guarantee. SPV holding the ownership right exported floating income sukuk to fund owners for 5 years.

5.3.33.3. Sukuk Types

5.3.33.3.1. Mudaraba Sukuk

The meaning of mudaraba agreement between the parties is as followed; it is a partnership type that one party gives capital and the orther party gives labor and administration knowledge as capital. Capital owner gives his capital to a party that would give his labor and administration knowledge in order to progress and gain profit from capital owners capital. In this agreement type, mudaraba is labor and business owner that exports sukuk and sukuk share holders are investors. Mudaraba sukuk is a type of sukuk that symbolizes equal ownership of instruments, which has complete instrument, where sukuk customer's names are recorded and where income is shared according to the rate of shares that sukuk owners have. This kind of sukuk customers are asset owners. Mudaraba sukuk is applied in big investment projects with participation of wide population.

a) Characteristics of Mudaraba Sukuk is as followed:

I. Mudaraba sukuk means common ownership

II. Sukuk exporter gives share right to the customer on projects.

III. Mudaraba sukuk agreement is based on

i. Type of capital regarding export
ii. Income rate
iii. Legal announcement that states in the definition of export all the information showing that the other conditions are in accordance with Islamic rules.

IV. Customer of mudaraba sukuk has a right to sell his sukuk agreement on stock market and transfer his right. So, mudaraba sukuk is progressed on secondary markets.

V. SPV that collect funds from sukuk customers can invest its own savings to this formation. In addition to its share in profit it receives income according to its own capital that contributes to SPV.

VI. In this sukuk type, no guarantee is assured by exporter or the manager of the fund about the capital, fixed income or any income according to capital rate. Promotion brochure, the brochure that consist investment information about sukuk to be exported or Mudaraba sukuk exported as its continue do not guarantee that sukuk customer is to be made any fixed or floating payment. Income gained from the project is shared in accordance with Islamic rules. Profit and Loss of the project must be announced and the profit share that sukuk owners have must be distributed through SPV.

VII. In mudaraba sukuk reserve can be formed for unusual conditions as capital loss. It is formed by income deductions.

VIII. On condition that promotion brochure is independent from mudaraba agreement, in may include grant promise of third parties in order to meet any loss that can occur without any legal or illegal income of the project. When determined time of membership ends, sukuk customer with his own will can sell the sukuk he holds on secondary capital markets, can transfer his right to others.

Operation steps of mudaraba sukuk can be arranged as followed:

Investor agrees with project owner about project assignment.

SPV export sukuk to enable fund.

Investor receives regular income and final capital revenue that comes from project activities.

Investor submits the project to its owner when the project is completed.

5.3.33.3.2. Musaraka Sukuk

Musaraka is an investment sukuk that represents its entity. There is no difference between musaraka sukuk and mudaraba sukuk except the administrative commission that is formed between sukuk exporters and sukuk customers. Sukuk holders have voice on the project or activities according to their rates, they become owners of the project. This type of Musaraka sukuk is progressed on secondary market and it is an instrument that can receive turnover. It is equally exported certificate to finance an activity based on form a new project, develop an available project or any partnership agreement.

Application of Musaraka sukuk is as followed:

A Company and SPV make an agreement on agreed revenue at a specific time. In this agreement, the company promises to buy SPV's musaraka shares at certain periods.

Company becomes a participant by giving assets about the activity.

SVP becomes a participant by tha cash it gains from sukuk it exports.

Revenue is distributed to sukuk shareholders.

Company guarantees to buy musaraka shares from the price agreed earlier and at the end of predetermined time, SPV does not have any shares.

5.3.33.3.3. Icara Sukuk

Icara Sukuk is about asset/property leasing. Islamic leasing sukuk holders accord a right to get ownership, rent and income rights of property, The right to sell sukuk without effecting the rights of sukuk lessor. Maintenance expenses of property subjected to sukuk is met by leasing sukuk owners. Available and known assets have leasing contract and leasing sukuk holders have the ownership right of this assest. Leasing expenses are met by sukuk holders.

a) Characteristics of Icara Sukuk is as followed:

Leasing amount must be known before leasing sukuk of subjected property or asset. By protecting lessee's usufructary right, lesser can sell the property. In this case, new holder of the property has the right to receive lease.

Lease amount can be determined at first stage or can be renewed at other periods. Lease amount can be based on a certain variable and can be increased or decreased. According to Islam law, sukuk holders are responsible for finance and payments of main property structure. Lessee is responsible for meeting maintenance expenses resulting from the usage of the property. SPV buys and leases the property and shares the lease income among sukuk owners. Icara sukuk has turnover and progress on secondary market.

b) Leasing Sukuk operation system is as followed:

Source holder transfers related asset to SPV with a price that was agreed earlier.

SPV divides the price equally and exports sukuk certificates and a finance gained from investment owners is obtained. This fund is transferred to source holder.

In order to lease related asset again, source holder and SPV signs a leasing agreement for a certain period. Source holder becomes lessee.

SPV collects lease from lessee. Lease amount is distributed to sukuk holders in equal shares.

On expirty date of sukuk or in case of sukuk separation, asset is sold to source holder by SPV through a determined amount. This amount may not be equal to the whole debt of leasing sukuk provisions.

5.3.33.3.4. Murabaha Sukuk

Murabaha is cah buying of a property and seling it in terms to a needer. In this type of sukuk, property seller exports sukuk. Property buyer –or sukuk holder- enables fund. Then, sukuk holder have final sale right in the resale of the property.

Murabaha Sukuk operation system is as followed:

Debtor and SPV holder sign an agreement.

SPV exports sukuk and takes sukuk income from investors.

With its money, SPV buys property in cash from the seller of the property.

SPV adds profit margin to property and sells this property to the debtor in installments.

Debtor sells the property he bought in cash to any property buyer to gain finance.

Sukuk holders get their installment shares gained.

This sukuk type is widely used in Malaysia. It is also argued about its being suitable for Islamic world. Secondary market of it is considered as suitable according to Islamism.

5.3.33.3.5. Salam Sukuk

Salam sukuk is exported by SPV and it enables fund to saving owners. The funds bought are paid to SPV Company with a promise that certain asset will be delivered on forward date. SPV can market stated amount of asset with a higher price on delivery price. The spread between bought and sold is profit and it is distributed among sukuk customers.

5.3.33.3.6. Exemption Sukuk

Exemption sukuk is a certificate that has the equal value and is exported to enable required finance for manufacturing of goods that sukuk holder has. While savings received from membership are cost of the goods, sukuk exporters (seller/supplier) and members are buyers of planned goods. Certificate buyers own the product and they gain the right of sales value of certificate or sales value of product sold through parallel exemption. Exemption sukuk is useful in terms of financing big understructure projects. Exemption is appropriate for finance in terms of its allowing contractor in exemption to make parallel exemption agreement with sub-contractor. Because of this, financial corporation can take charge of profit oriented construction operation and it can transfer the construction operation to a professional company through sub-contractor agreement.

5.3.33.3.7. Hybrid Sukuk

Tabreed Istısna' / Leasing Sukuk[1]	
The Issuer	Tabreed Finance Company (Cayman Islands)

Renter	National Central Cooling Co. PJSC
Price Date	10 July 2006
Date of Organizing	20 July 2006
Period	5 years
Maturity Date	20 July 2011
Quantity	200 mn US$
Sukuk Type	Istısna' / Leasing
Leader Company	CIMB-Dredner HSBC
Project Establisher	BSC, Bahreyn
Margin	Libor that has 125 min. point one time in six months
Coupon Payment	Six months
Export Target	Building construction
Export List	London Stock Market
Rating	BBB- (S&P's)

As sukuk buying and selling is an important investment tool and as it considers different demands of investors, more comprehensive sukuk type 'Hybrid or mixed sukuk' staeted to operate in market. In Hybrid sukuk, related asset pool consist consist of Murabaha and leasing. Having an asset pool with different instruments enables higher movement capability of funds.

Table 4: A Sukuk Example

(http://www.riskcenter.com.tr/kredirisk/kredifiles/TS/sukuk.pdf)

5.3.33.4. International Sukuk Market

Sukuk market is young but accelerated increasing market in word wide. In sukuk market where Arabic and Gulf countries progress widely, there has been 51,2 billion dollar sukuk export in 2012. Global sukuk export was 16 billion dollars for two months in February 2011, which is an indication of accelerated increase for sukuk finance tool in world’s market.

5.3.33.4.1. London Sukuk Market

London stock is an important capital market of the world. It does the honors of the oldest market of the world and has 400 out of 500 companies in Fortune. The stock has 2,7 trillion dollars value. Market riggers tried hard to develop sukuk instrument and make sukuk to progress on their market in Christianity dominating land. And the numbers gained supported their idea.

Market plays role in export of two new sukuk certificates and so far has achieved 33 sukuk exports. London market sukuk volume increased to 19,5 billion dollars through 400million dollars SIB sukuk and 750 million dollars IDB sukuk recently exported. When we considered only London capital market, this amount may correspond to one per cent. England is ranked number nine globally in Islamic finance.

England organizes Sukuk Fairs every year and gathers many participants. State administrative, market riggers and Islamic law scientists are among the speakers.

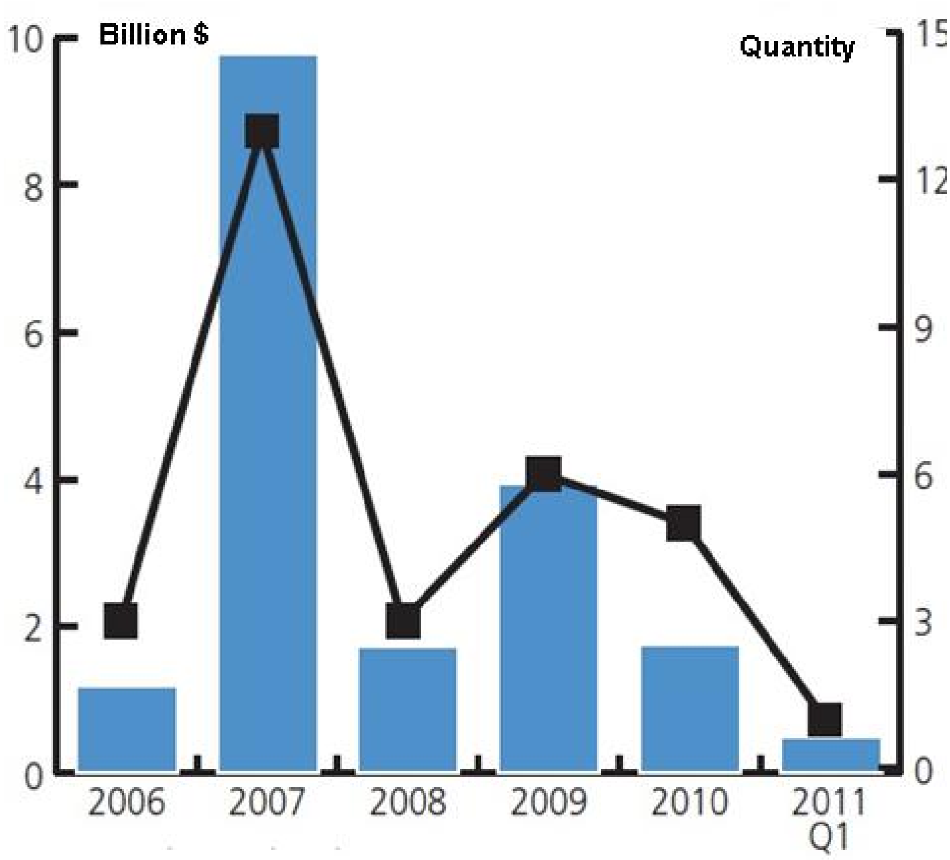


Figure 2: Sukuk Exports by year on London Stock List (http://www.londonstockexchange.com/specialist-issuers/islamic/base-propectuses/base-prospectuses.htm)

5.3.33.4.2. Malaysia Sukuk Market

Malaysia is heading in sukuk export as in the other Islamic finance tools. 61% of global sukuk export has been progressed in this country.Malaysia market became bond market leader of Asia by 213billion dollars in December 2009 and the market works at serious volumes in sukuk market when compared with global markets. It made 47% of world sukuk export in 2009 with 10 billion dollars sukuk export in 2009.

5.3.33.5. World wide Applications

Mudaraba Sukuk Application Shamil Bank gained investment capital of 360Suudi Riyal through territory development project with a real estate company that is active in Saudi Arabia. The aim of mudaraba is to bring income to investors because of their participation into territory finance.

Emirates performed sukuk of 550 million dollars with 7 years' time period through Musaraka agreement. Musaraka or joint venture is formed for construction of the general directorate building and engineering center that are stated near Dubai Airport and would be leased to Emirates later. Lease income and gained profit of Musaraka is used for making periodic payment in assurance certificate. Sitara Chamical Industries Ltd. Exported periodical sukuk based on profit loss share of 360 million Riyal in June 2002. Sukuk was fixed for 5 years and profit/loss share of the company was indexed to profit/loss of Chemistry department.

As authorized main regulatoriess; Kuwait Finance House (KFH), Liquidity Management Center(LMC) and Al Muthanna Investment Company(MIC) exported Lagoon City Musaraka sukuk of 125 million dollars to support Lagon City Residance and trade estate project that is part of Kheiran Pearl City.

Bahrain originated investment company Arcapita Bank Bayerische Hypo- und Vereinsbank AG, Standard Bank Plc and WestLB AG, London Branch (together as authorized regulatoriess) exported various foreign currency based(usdi eur and gbp) murabaha sukuk. Due time of sukuk is five years and offered price for 3 months LIBOR+175pips.

On Bahrain Government Salam Sgreement, Salam sukuk base asset is determined as aluminum. On agreement, in return for cash payment to the customer, customer is committed to sell aluminum on determined forward date. Bahrain Islam Bank (BIB) is assigned to represent the other banks demanding to participate in Salam Agreement.

BIB is authorized to sign the agreements and all the other documents on behalf of other banks. Besides, customer authorizes Bahrain Government as agency to market Salam based assets through distribution channels. Bahrain Government enables aluminum marketing with a price that would enable equal income with the other traditional short term money market instruments for Salam holders.

First sukuk was exported by Islamic Participation Bank and its content was as 68% Leasing sukuk, 30.73% murabaha and 3,4 exemption sukuk. This released sukuk was assigned as guarantor by IDB to enable international marketability. Sukuk of 400million dollars was exported by an incorporate corporation active in Jersey gulf islands, Solidarity Trust Services. Organization of Islamic Cooperation played a mediator role in buying these assets on consolidated net asset value from DIB and selling to Solidarity Trust Services.

5.3.33.6. Sukuk in Turkey

Turkey met sukuk officially through 100.000.000 USD with 2013 due time sukuk export of Kuvetturk. It was not surprising that this kind of enterprise came from Arabic partnered participation bank. Beyond this, sukuk was not that much matter of concern for Turkey. Though not on expected level, in order to get share from the cake Turkey has rapidly take into progress of sukuk legal inspections and legal regulations. In this part, new legal understructure of sukuk in Turkey and only sukuk example; Kuveyt Türk sukuk export will be discussed.

5.3.33.6.1. Legal and Administrative Understructure of Sukuk in Turkey

With a notice of Capital Market Board(CMB) issued on official gazette in 1April 2010 about principles regarding lease certificates and asset leasing companies (ALC), Turkey met sukuk officially. This notice determines principles regarding aim, objective, backing, identifications, ALC and record of leasing certificates.

The aim of the notice is stated as record of leasing certificate on CMB, export and sales of leasing certificates and regulation of principles regarding establishment and activities of ALC.

Establishment of ALC is defined as followed:

ALC is established by founders with the aim of gaining leasing income, exporting leasing certificate basing leasing incomes and transferring related asset to source corporation thereby leasing takeover assets to source corporation again. ALC can take assets belonging to the same source. ALC principles stated on the notice of ALC core agreement must be met and approved by CMB. Banking Regulation and Supervision Agency is consulted in Banks allowance to establish ALC.

According to the core agreement of asset leasing companies, an ALC exports leasing certificate (sukuk). It takes over and leases any asset for the name of itself and sukuk holders. Then it distributes the income collected through leasing of takeover assets to sukuk holders according to their share rates. At the end of leasing agreement, ALC takes over source asset back to Source Corporation on predetermined conditions. During property registration in other words during takeover of assets to ALC, forward buying provision in favor of source corporation must be stated in agreement.

The notice blocks some ALC activities. ALC does not deal with any activity or commercial activity except the ones stated in agreement, ALC does not draws credit, get debted and does not use its assets apart from sukuk activities stated above. ALC does not constitute any tangible right in favor of third parties through assets it holds. It cannot transfers the asset apart from the source corporation that carries out all the responsibilities of leasing contract. Besides, ALC transfers asset subjected to sukuk and distributes the gained income to sukuk holders according to holder’s share rates in case commitments given to sukuk holders are not carried out. This article must be stated as a provision in the agreement.

Administration of asset leasing company is stated on the notice. ALC board signs an agreement with Source Corporation that will take over its assets. The agreement consists of subjected asset's take over, leasing of these assets to Source Corporation and takeover of the same assets to source corporation at the end of lease. No real right is instituted in favor of third parties for assets subjected to turnover. ALC board is responsible for making payments of income gained through leasing and turnover of subjected assets to sukuk holders on behalf of ALC and sukuk owners. ALC administrative board distributes the gained income to sukuk holders according to holder's share rates through takeover of asset subjected to sukuk in case commitments given to sukuk holders are not carried out. Administrative expenses of ALC are stated in the core agreement. These expenses are announced to the public through registration statement or announcement to be made to qualified investors.

On press release of CMB regarding the note, three stages are defined about sukuk export; government, leasing-takeover methods.

5.3.33.6.2. Application of Sukuk in Turkey and Its Market

Sukuk application style in Turkey is as followed steps:

I. The first step is establishment of ALC in accordance with the notice prepared by CMB. Source Corporation is the corporation that wants to get finance through lease certificates to be exported by means of assets it owns (or leases). In this concepts it establishes ALC, or makes an ALC to be established and transfers subjected assets to ALC. Source Company is incorporate company. ALC that has sukuk export authority is an incorporate company. On press release of CMB regarding the note, activity area of ALC is limited to activities to be performed in sukuk export scope. In other words, it is a venture company that is established to perform only activities stated on the note.

II. In this step, takeover of subjected asset to ALC by the company is applied. ALC exports sukuk in order to collect ALC fund holders' demands, in this way finance is gained in return for the takeover. At the end of sukuk export operation – which means when saving holders take their sukuk- the money collected is paid to Source Company as the value of takeover asset.

III. In this step ALC leases subjected takeover asset to source corporation and receives lease income. With the lease income, ALC meets the periodical paybacks of sukuk exported by itself.

IV. On due date of sukuk, asset that ALC leased to source corporation is taken over to the source corporation. No asset remains in ALC assets. ALC's responsibility for investors through sukuk ends.

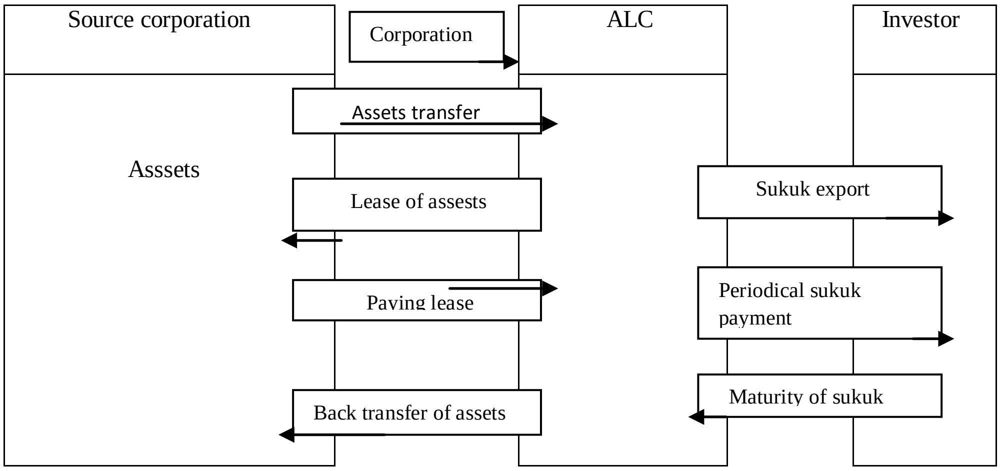


Figure 3: Sukuk Application Style in Turkey

(Konca, A. ,2011, Kira Sertifikları ve Vergisel Boyutu,Yaklaşım Dergisi, İstanbul)

5.3.33.6.3. The First And Only Sukuk Application In Tukey: KT Turkey Sukuk

Sukuk of 100.000.000 USD with 2013 due time is exported by FT Turkey and first sukuk application is performed in this way. Liquidity Management House(LMH) and Citibank were common regulatories. KT Turkey sukuk application received 1,5 times export sum demand. This operation was applies as 5.25. of final income.

Kuveyt Türk Participation Bank, participation banking unit manager Fatih Bey(1 June 2011) is informed about KT Turkey Sukuk exported by Kuveyt Türk as followed.

KT Turkey Sukuk is a hybrid sukuk. It is formed as 51 leasing, 49% Murabaha. KT Turkey sukuk is established as ALC. Kuveyt Turk Participation Bank Corp. (Kuveytturk) transferred right of lease and right of murabaha to ALC. ALC and sukuk holders declared trust to each other. ALC exported sukuk and collected fund to saving holders. Kuveytturk guaranteed selling and buying of assets. Kuveyt Türk, was guarantor for ALC. ALC assigned Kuveyt Türk as agency to operate its assets. ALC in other words KT Turkey Sukuk would pay sales income gained on expiry date from assets and from sukuk holder’s regular paybacks.

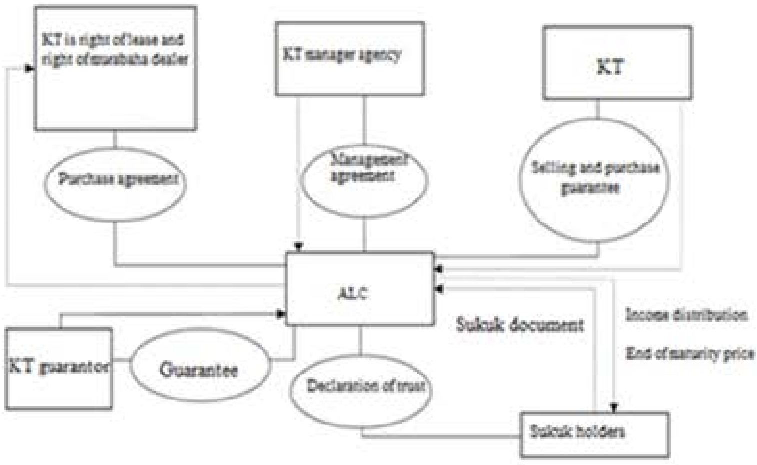


Figure 4: KT Turkey Sukuk Operation Table
(Kuveyt Türk Participation Bank, Investment Banking Department)

5.3.33.6.4. Sukuk's Worldwide Potential Market and Importance for Turkey

The only sukuk export of Turkey is 100.000.000 USD while sukuk market is of 51.000.000.000 USD. Turkey is at the very beginning of sukuk applications. Arabian Gulf Capital is widely rated on London and New York stocks. These stocks are very reliable and professional about financial tool use. Although belief and geography of them are so far away, a rational Arabian investor naturally makes his savings progressed on these stocks. But in the last eight years Turkey has become an increasing value in terms of economy and this strikes the attention of countries around Turkey. This is realized by the countries sharing the same belief and this led Turkey to start gaining more value and trust. Our investors that still suffer from capital scarcity look for finding fund to invest. In this scope, through sukuk financial tool, capital of Gulf countries can enter in our country. Potential market of Turkey is not only Gulf countries, Turk countries that share the same belief and sensitivity can be counted as well. Turk countries, which are getting wealthier thanks to their natural sources, would like to rate their funds in Turkey. In case Turkey becomes regional power, it will become center of attraction and draw investments of the neighbors. Sukuk will get its own place among these investments.

Kuveyt Türk Participation Bank applied its second sukuk export et the end of 2011. Sukuk export of 350million USD is arranged by Abu Dhabi Islamic Bank, Commerzbank, HSBC, Liquidity Management House and Standart Chartered Bank.

Albara Türk Partcipation Bank, planned 200 million USD sukuk export with 5 years period during the first quarter of 2012 and then declared the cancellation of this export. Asya Participation Bank is planning to export sukuk of 300 million USD with 5 years period on the second half of 2012. Turkiye Finance Participation Bank does not have any sukuk related application at the moment.

Tayland and some of old Soviet republics announced to start sukuk applications in 2012. Countries like Egypt, Senegal and Nigeria has started to sukuk applications. Countries like France, Japan and Hong Kong stated to have regulatory preparations for their future exports.

5.4. Partnership Structure of Participation Banks

Asya Participation Bank

Partnership name, surname / title	**Rate (%)**
Ortadoğu Tekstil Tic. San. A.Ş.	4,89
Forum İnşaat Dekorasyon Turizm San. ve Tic. A.Ş.	3,85
Osman Can Pehlivan	3,33
Birim Birleşik İnşaatçılık Mümessillik San. ve Tic. A.Ş.	2,40
BJ Tekstil Ticaret Ve Sanayi A.Ş.	2,26
Other Partners	30,39
Public	52,88

Table 5: Asya Participation Bank Corp. Partnership Structure

(Katılım Bankaları 2011, TKBB)

Albaraka Türk Participation Bank

Partnership name, surname / title	**Rate (%)**
Foreign Partnership	**66,16**
Albaraka Banking group	54,06
IDB	7,84
Alharthy Family	3,46
Other	0,80
Local partners	**11,06**
Public	**22,78**

Table 6: Albaraka Turk Participation Bank Corp. Partnership Structure

(Katılım Bankaları 2011, TKBB)

Kuveyt Türk Participation Bank

Partnership name, surname / title	**Rate (%)**
(%) Kuwait Finance House	%62
General Directorate for Foundations, Turkey	%19
IDB	%9
The Public Institution for Social Security	%9
Other	% 1

Table 7: Kuveyt Türk Participation Bank Corp. Partnership Structure

(Katılım Bankaları 2011, TKBB)

Türkiye Finans Participation Bank

Partnership name, surname / title	**Rate (%)**
NCB	%64,68
Boydak Group	%13,69
Ülker Group	%13,69
Other Partners	% 7,94

Table 8: Turkiye Finans Participation Bank Corp. Partnership Structure

(Katılım Bankaları 2011, TKBB)

Only Asya Paritcipation Bank has 100% domestic capital while other participation banks have foreign capitals.

6. FUTURE PROJECTION OF TURKEY PARTICIPATION BANKING

Interest free banking system is rapidly growing worldwide. As bank unions and acquisitions continue because of new market search, profitability and productivity, important agents of banks tries to present interest free products persistently.

Constitutions dealing with international banking such as Citigroup, USB, Deutsche Bank, HSBC,ANZ Grindlays, Lloyds TSB, BNP Paribas, Commerzbank, Sociate Generale try to get a slice from interest free banking by presenting interest free banking products to customers. Islamic Banking has been widened in England and France and it is detected by Federal Finance Detection Institution(BaFin) in Germany. First Islamic Insurance Company was opened in 2010 in Russia. Besides, Islamic Investment Fund operated actively in Germany was put into practice for the first time by Meridio Company in Germany. Among global banks in USA, only HSBC has interest free banking frame. Bombay stock in India is greatly demanded by interest free instrument index investors. Another development in the field of interest free banking happened in Australia. Australia made the necessary law amendments to prepare a base for interest free banking system.

While interest free banking is rapidly growing around the world, participation banks in Turkey has grown 10 times in 8 years. Participation banks are planning to increase their active size from 5% to 15% as their 2013 aim. Participation banks will maintain their capital partnership structure in the future as well. Asya Participation Bank has 100% domestic capital and is not looking for a foreign partner, the bank think to continue its activities with domestic capital. Kuveyt Türk is planning to increase its branch number to 650 until 2018. In June 2012, Bank Asya is the first participation bank opened on 'representative' base in India where no participation banking license is given.

4 participation banks actively operate in Turkey now. The number is estimated to increase in future. Following the sales period completion of Adabank, it received participation banking license. It is also stated that if authoritarian government establishes a participation bank, it will have positive reflects on stocks. Especially sukuk that greatly develops in recent years and interest free banking that is an increasing trend, will take Islamic finance industry much further.

In 2012, some of the participation banks has taken their rank to upper steps in banking field. Kuveyt Türk Participation bank aims to be in the first 7 bank in banking field of Turkey in 2018. Other banks estimate themselves as well to be at the higher ranks in the next 10 year as Turk banking system participation banking products are improved and as awareness increases.

7. MAIN FINANCIAL SIZES OF PARTICIPATION BANKS AND BANKING SECTOR(Mio TL- December 2011)

FINANCAL HEADLINES		PARTICIPATION BANKS			BANKING SECTOR		
		Dec. 11	Dec. 10	2011-2010 (change %)	Dec.11	Dec.10	2011-2010 (change %)
COLLECTED FUNDS **	Turkish Currency	24.041	22.235	8,1 %	466.912	440.163	6,1 %
	Foreing Currency	11.735	10.429	12,5 %	226.215	183.591	23,2 %
	FC-MINE	3.743	612	511,6 %	14.589	2.387	511,2 %
	TOTAL	39.519	33.276	18,8 %	707.716	626.141	13,0 %
FUNDS MADE USED ***		41.140	32.168	27,9 %	708.257	551.622	28,4 %
CREDITS THAT WİLL BE PURİFİCAİTON		430	327	31,5 %	3.903	3.240	20,5 %
TOTAL ASSETS		56.153	43.339	29,6 %	1.217.711	1.006.671	21,0 %
EQUITY		6.193	5.457	13,5 %	144.650	134.545	7,5 %
NET PROFIT ****		803	759	5,8 %	19.849	22.116	-10, 3%
PERSONNEL NUMBER		13,851	12.677	9,3 %	195.292	191.180	2,2 %
BRANCH NUMBER		685	607	12,9 %	10.518	10.066	4,5 %

Table 9: Main Financial Sizes Of Participation Banks And Banking Sector

(Katılım Bankaları 2011, TKBB)

* Prepared according to Banking Regulation and Supervision agency

** Funds collected from banks are excluded.

*** Credits on trace and foreign murabaha are excluded.

**** Net profit figure is compared with the same month of previous year

Sector share of participation banks is seen in December 2011 as followed;

COLLECTED FUNDS**	5,6 %	⇧ 5,3 %
FUNDS MADE USED***	5,8 %	⟺ 5,8 %
TOTAL ASSETS	4,6 %	⇧ 4,3 %
EQUITY	4,3 %	⇧ 4,1 %
NET PROFIT****	4,0 %	⇧ 3,4 %

Credits that will be purification (gross)	
Participation Banks	Banking Sector
3,0 % * ⇧	2,9 % ** ⇩

Table 10: Sector Share of Participation Banks December

(Katılım Bankaları 2011, TKBB)

* November 2011 % 2,9

** November 2011 % 2,9

Banking Sector Assets Development (thousand TL)

YEARS	PARTICIPATION BANKS	GROWTH(%)	BANKING SECTOR	SHARE (%)
2000	2.266.000		106.540.000	2,13 %
2001	2.365.000	4,37 %	218.873.000	1,08 %
2002	3.962.000	67,53 %	216.637.000	1,83 %
2003	5.112.934	29,05 %	254.863.000	2,01 %
2004	7.298.601	42,75 %	313.751.000	2,33 %
2005	9.945.431	36,26 %	406.915.000	2,44 %
2006	13.729.720	38,05 %	498.587.000	2,75 %
2007	19.435.082	41,55 %	580.607.000	3,35 %
2008	25.769.427	32,59 %	731.640.000	3,52 %
2009	33.628.038	30,50 %	833.968.000	4,03 %
2010	43.339.000	28,89 %	1.006.672.000	4,31 %

Table 11: Banking Sector Assets development

(Katılım Bankaları 2011, TKBB)

Assets Share of Participation Banks in Banking Field

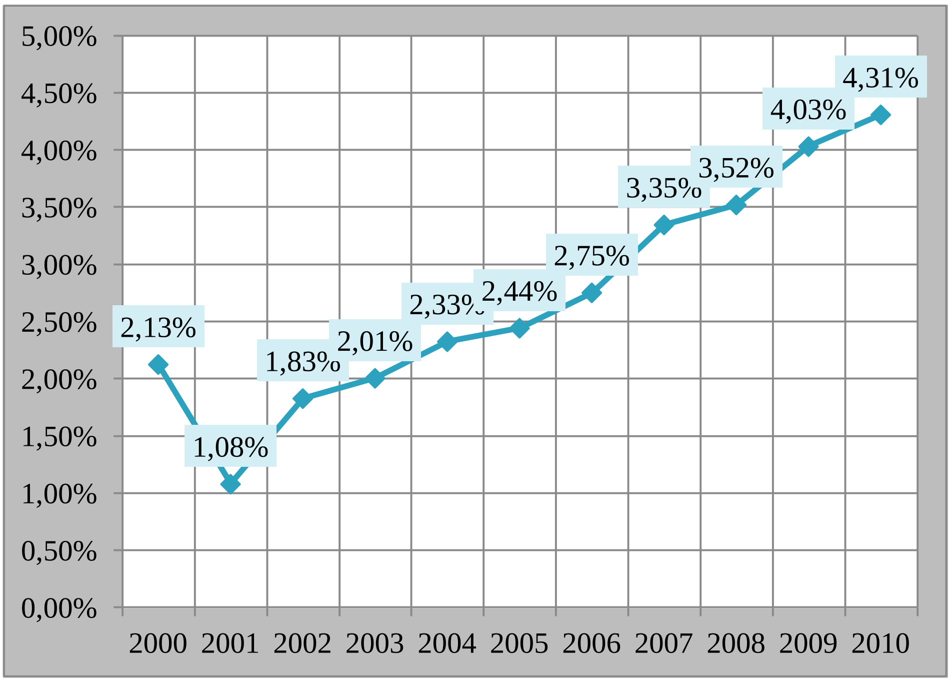


Figure 5: Assets Share of Participation Banks in Banking Field

(Katılım Bankaları 2011, TKBB)

YEARS	BRANCHES	GROWTH (%)	PERSONNEL	GROWTH (%)
2000	**110**		**2,182**	
2003	**188**	71%	**3,520**	61%
2004	**255**	36%	**4,789**	36%
2005	**290**	14%	**5,740**	20%
2006	**355**	22%	**7,114**	24%
2007	**422**	19%	**9,215**	30%
2008	**530**	26%	**11,022**	20%
2009	**560**	6%	**11,802**	7%
2010	**607**	8%	**12,677**	7%

Table 12: Branch and Personel Change of Participation Banks by year

(Katılım Bankaları 2011, TKBB)

NON-CONSOLIDATED NET PROFIT					
Bank	**2010/12 total profit 1.000 TL**	**2011/12 total profit 1.000 TL**	**Increase/ Decrease**	**2011/12 profit for per branch**	**2011/12 Profit for per personnel**
Albaraka	134,044	160,155	19%	1,312,746	61,503
Türkiye Finans	205,529	231,587	13%	1,272,456	68,476
Kuveyt Türk	159,648	195,042	22%	1,083,567	58,624
Bank Asya	259,962	216,090	-17%	1,080,450	47,503

Table 13: Participation Banks Net Profit Change

(Kuveyt Türk Participation Bank, Marketing Department)

Bank	Assets Size, thousand TL		
	2010/12	**2011/12**	**Increase/ Decrease**
Bank Asya	14,513,419	17,190,099	18.4%
Kuveyt Türk	9,690,553	14,897,592	53.7%
TürkiyeFinans	10,691,860	13,528,353	26.5%
Albaraka	8,406,301	10,460,885	24.4%

Table 14: Participation Banks Assets Size Change

(Kuveyt Türk Participation Bank, Marketing Department)

Gold amount, for 1.000 TL (31/12/2011 share serial)					
	2010/12	**2011/09**	**2011/12**	**Increase/Decrease**	**Share**
Kuveyt Türk	452,114	1,827,371	1,932,587	5.8%	13.5%
Bank Asya	123,372	849,885	951,984	12.0%	6.6%
TürkiyeFinans	375	466,088	521,400	11.9%	3.6%
Albaraka	47,659	293,786	324,813	10.6%	2.3%

Table 15: Participation Banks Gold Amounts

(Kuveyt Türk Participation Bank, Marketing Department)

THE SUM OF ACTIVITY INCOME (1.000 TL)			
	2010/12	**2011/12**	**Increase/Decrease**
Kuveyt Türk	604,866	786,847	30.1%
TürkiyeFinans	691,456	820,953	18.7%
Albaraka	472,253	552,664	17.0%
Bank Asya	1,022,072	1,060,697	3.8%

Table 16: Participation Banks Activity Incomes

(Kuveyt Türk Participation Bank, Marketing Department)

Participation Bank	Branch Number	Personnel Number
Albaraka	129 (may 2012)	2763 (may 2012)
Bank asya	200 (march 2012)	4542 (march 2012)
Kuveyt türk	185 (march 2012)	3326 (march 2012)
T.Finans	182 (march 2012)	3382 (march 2012)

Table 17 : *Participation Banks Branch and Personnel Number* (2012)

(Katılım Bankaları 2011, TKBB)

It is estimated that participation banks will develop the rapid growth and increase their shares in banking system to higher levels through increasing branch, personnel and customer number with their new banking products they develop.

8. CONCLUSION

In conclusion it is clear that participation banking is developing and getting accessible to more individuals in Turkey as participation banking makes progress every year and integrates conventional banking products that could be adapted to interest free banking system.

While participation banks started their activities in Turkey they had only 7-8 interest free banking products which made them reach to very narrow customer groups, they have made progress every year, developed interest free banking products and has started to strike their customer's need within interest free system in every aspect. Today their product number is over 30 and they access to wide customer groups. They have started to reach up to date conventional banking system customer groups as well.

When participation banking progress is examined from 2000, rapid development and change can be observed. While participation banks had only 110 branches and 2,182 personnel in 2000, they reached to 685 branches and 13,851 personnel at the end of 2011 and it is expected that the numbers will be increased to 800 in branches and to 15,000 in personnel at the end of 2012.

When we compare participation banking and conventional banking between 2010 and 2011 in Turkey, we can see that participation banks show more progress. When compared with 2011, conventional banks decreased their profit 10,3% in 2011 and participation banks increased their profit 5,8%. Besides, while asset volume of conventional banks increased 20%, asset volume of participation banks increased 30%. When the other values are examined, it can be observed that participation banks have developed much more than conventional banks.

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