

# Prepayment of Shariah: Compliant Direct Investment Deposits in Kuwait

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Many Islamic financial institutions and investment companies in Kuwait have used and continue to use Shariah compliant financing methods including murabaha, bay bithamanajil, ijarah, musharaka and istisna. The previously mentioned instruments ensure that those seeking alternatives to conventional financing have an opportunity to use these Shariah compliant methods, allowing them to avoid exposure to riba (interest). As many already know, any form of riba is prohibited under the principles of Islamic Shariah.

More recently, customers now have the opportunity, using the global commodity markets, to open direct investment deposits ("DI Deposit") with Shariah compliant banks. When completing a DI Deposit, the following procedures are followed:

- The customer informs the bank of the customer's specific investment objectives and appoints the bank as an agent to purchase commodities on the customer's behalf for the value of his or her investment amount (i.e. the deposit).
- The bank will thereafter complete a spot purchase of the commodities, paying a broker by debiting the customer's account and thereafter confirming the transaction to the client with legal title of the commodities being transferred to the customer. The entire transaction is executed through preapproved forms specifying the type of commodities, the date of purchase and a deferred payment date.
- The deferred payment date will correspond to the investment term as agreed between the parties and the deferred price will exceed the total purchase price by a specific profit margin to be paid to the Shariah compliant bank.
- Under the Shariah compliant DI Deposit, the bank will undertake all aspects of the commodity transaction on behalf of the customer through the execution of various sale contracts.

Unfortunately, there have been instances where DI Deposit agreements do not provide proper instructions on prepayment methods for its customers. The direct investment must outline how prepayment should be distributed in the event the customer or the bank wants to terminate the underlying arrangement.

Some direct investment agreements include language identifying the rights and responsibilities of the parties in the event of prepayment. Nonetheless, the best method to employ in early prepayment is by having the executing customer fill out a prepayment request form with the bank responding with an offer and acceptance form. The prepayment request form must outline the transaction date, the description of commodities, the total price paid and the deferred payment date. The latter form should also reference the original direct deposit agreement and the current request to make payment of the total price on an earlier date subject to a discounted price, while factoring in early payment, and calculate a reduction in the profit amount owed to the Bank. The offer and acceptance form must also provide specific details to identify the underlying transaction.

While Shariah compliant direct deposits can be attractive form of investment, potential investors should seek legal advice prior to undertaking any commitments so as to ensure, amongst other things, they have adequate prepayment options.