

PIDM's Islamic Protection Systems

Part 2: Shariah Arrangement for PIDM's Islamic Deposit Insurance System (IDIS)

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In Part 1, we gave a general view of the protection of Islamic deposits in relation to PIDM's role. In this article, we will share how PIDM administers the Shariah compliant deposit insurance system within the financial safety net system.

A Shariah concept is necessary for an IDIS to, among others, govern and set out the deposit insurance terms such as the relationship between PIDM and its Islamic member banks (IMBs), the roles of each party and how the protection of Islamic deposits is to be carried out.

As a comparison, a Shariah concept is also used by Islamic financial institutions such as Islamic banks and takaful operators to set out the contractual relationship and terms for their products and services.

PIDM adopts the Shariah concept of "guarantee with fee" (or *kafalah bi al ujr* in Arabic) in respect of its protection of Islamic deposits under the IDIS.

The suitability of this concept was resolved by the Shariah Advisory Council of Bank Negara Malaysia (SAC), the highest Shariah authority that provides rulings on Islamic banking and takaful in Malaysia. Under this concept, IDIS functions as follows:

- ◆ PIDM is the guarantor. The IMB is the guaranteed party since it has a financial obligation towards its depositors in respect of the monies of the depositors which are being held by the IMB. Depositors are the beneficiaries as their deposits are protected by PIDM.
- ◆ When an IMB fails, or in other words, becomes bankrupt, PIDM will protect eligible deposits. If the failed IMB is to be wound up, PIDM's deposit protection will be in the form of reimbursement to protected depositors. Pursuant to this reimbursement, PIDM can recover its losses due to the reimbursement from the liquidation of the assets of the failed IMB.

- ◆ For PIDM to guarantee an IMB's financial obligation towards its depositors, each IMB is required to pay a fee for PIDM's guarantee commitment in the form of annual premiums. The premiums that are collected from all IMBs are maintained in the Islamic Deposit Insurance Fund (IDIF) and segregated from the Conventional Deposit Insurance Fund, which is owned by PIDM.

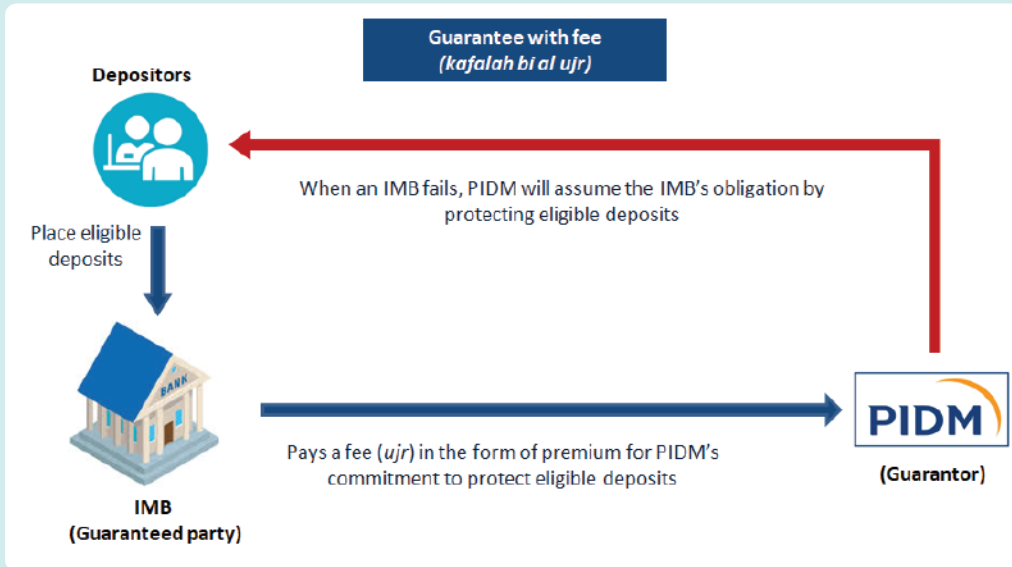


Diagram 1: The IDIS mechanism, which is based on the *kafalah bi al ujr* (guarantee with fee) concept

The IDIS is evolving due to the continuous development of the Islamic financial system and this may result in changes in the IDIS design features. Nevertheless, despite any changes that it needs to make to its IDIS design features, PIDM will ensure such changes will be consistent with the Shariah arrangement that it has adopted.

In Part 3, we shall set forth the types of Islamic deposits that are protected by PIDM.