

ON THE ROAD TO FAIRNESS FOR ALL – A REVIEW ON MALAYSIAN ISLAMIC BANKING CASES

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Abstract: *Equitable economic development is an essential element in order to achieve justice and equality in a multi-ethnic society. The reality of Malaysia, which is a country of multi-ethnicity, multi-religion and multi-cultural societies, demands a concept of justice and equality that is different from other countries, particularly the ones with homogenous societies. The highest law of the land places Islam, the religion associated with one of the main ethnicity, as the official religion of the nation and allowed the duality of economic system, in particular banking system, whereby conventional banking system exists side-by-side with the Shariah-compliant, Islamic one. By reviewing the pertinent literature on the development of Islamic banking, the reviewed cases on Islamic banking and its contributions to Malaysian society regardless of ethnicity and religion. The discussion in this paper therefore will be directed towards highlighting the laws and cases on Islamic banking and its implication to enhance the application of Islamic banking laws to consumers regardless of ethnicity and religion, in order to maintaining fairness and justice in a multi-ethnic society.*

Keyword: *Islamic bank, Shariah Law, Shariah Advisory Council, Multi-ethnicity, Justice.*

1.0 INTRODUCTION

In a multi-ethnic, multi-religion and multi-cultural country like Malaysia, there bound to have multiple problem occurs within the society. An effective dispute resolution mechanism are needed to avoid any imbalance or disadvantages, be they social or economic, to any particular ethnicity or religion. Law that is enacted by the Legislative is therefore posited as one of the main mechanisms which is able to satisfy those needs and creates harmonious relation among various ethnics across the nation. In light of this, this paper seeks to review pertinent literature with the view of highlighting the principles of justice and just practices in Islamic banking activities that are fair to all Islamic banking consumers regardless of ethnicity or religion.

The discussion in this paper is divided into four sections. Section 2 explains about the official position accorded to the religion of Islam by the Federal Constitution. Section 3 discusses the status of Islam and Shariah law in Malaysia. Section 4 is dedicated to describing the evolution on civil law and Shariah law in dealing with Islamic banking transactions and the conclusion for this paper will be in section 5.

2.0 Islam: The Official Religion of The Nation

Islam is accorded a formal status in the Federal Constitution of Malaysia where the Constitution declares that Islam is the official religion of the Federation (Article 3 Federal Constitution). Other provisions in the Federal Constitution strengthen this formal status of

Islam within the framework of the Constitution. For example, the Constitution provides that the King is under the duty to protect Islam (Fourth schedule, Federal Constitution), and laws can be enacted to prohibit the propagation of other religions among Muslims (Article 11 (4) Federal Constitution). Moreover, the constitutional position of Islam and Malay customs are guaranteed even during a period in which the Proclamation of Emergency is in force in that the broad legislative power conferred to the Federal government of Malaysia during such time does not extend to any matter of Islamic law or the customs of the Malays, among others (Article 150 (6A) Federal Constitution).

All these provisions are consistent with the historical position of Islam and Islamic law in Malaysia where Islamic law has always been the law of the land since the time of the Malacca Sultanate as evidenced from the existence of a written code of law known as *Undang-Undang Melaka* from the era of that Sultanate. Furthermore, there were several agreements between the British and the independent Malay sultanates in the Malayan peninsula that recognized matters relating to Islam as falling outside the scope of the British administration in those Malay states.

The special position of Islam as the religion of the land was also entrenched in the Johore's state constitution of 1911, long before the Federal Constitution declares the same as the official religion for the Federation of Malaysia. The constitutional promulgation of Islam as the official religion of the Federation paved the way for the establishment of special administration of Islamic law in the Malaysian legal system. The special status of Islamic law, or also known as Shariah law, in Malaysia's constitution and the history of continuous application of Islamic law in the Malay states before the coming of British colonial powers in the 18th century had proven the existence of a separate court system for trying cases according to the principles of Islamic law (Aziz 2006)[1].

Yet, based on the decision of the Supreme Court in *Che Omar bin Che Soh* [2] on the status of Shariah law under the Federal Constitution, some quarters argue that Malaysia is a secular state. The oft-quoted basis for their view is the part of Supreme Court's decision in that case which hold that even though Islam is the official religion of the Federation, it does not mean that all laws will be consistent with Shariah law. Piecemeal quotation of Supreme Court's decision in the above case has led to misconception that religion has no place in the administration of the country, when in fact, a closer scrutiny of the Supreme Court's decision shows otherwise. According to the Supreme Court, the colonial British had managed to replace the authority of God with that of the ruling institutions as the source of legal validity in the pre-Malaysia Malay States. This severance had effectively turned the ruling institutions in those states into secular ones. Since legality of law emanated from the ruling institutions, all laws, including administration of Islamic laws, in order to be valid, had to receive their validity through these secular, ruling institutions. This is the legal-historical legacy inherited by the Federation of Malaysia and is entrenched in the Federal Constitution. In the final analysis, the Supreme Court's decision shows that Shariah law is still a part of the law of the land, although now, to be valid, it must get the approval of a secular institution.

The Federal Constitution had created civil courts and authorized each state in the Federation to establish a Shariah court system and a native court system (Article 74, Federal Constitution). This is in line with the Federation's constitutional framework which is based on Federalism system of government whereby powers of government are distributed among the national (federal) level government and state level governments. Matters relating to the

religion of Islam are thus effectively placed under the purview of the Malay Sultans who head their respective states.

According to the High Court decision in the case of *Dato Kahar*, since Shariah courts are not created by the Federal Constitution, the status of the Shariah courts are lower than that of the civil courts [3]. However, this is contrary to the decisions made by Federal Courts on *Sukma Dermawan* and on *Kamariah Ali* which state that the power of the Shariah courts is concurrent with that of the civil courts [4]. Based on these two decisions, civil courts are barred from usurping the jurisdiction of Shariah courts even where lacunae exist in the administration of civil justice. In this regard, the Federal Court had concluded, in the case of *Latifah v Rosmawati*, that ‘it is the function of the Legislature, not the court, to try to remedy inadequacies in the law (as aforesaid). However, until the problem is solved, it appears that the only way out is - if in a case in a civil court, an Islamic law issue arises, which is within the jurisdiction of the Shariah court, the party raising the issue should file a case in the Shariah court solely for the determination of that issue and the decision of the Shariah court on that issue should then be applied by the civil court in the determination of a case. Similarly, if in a case in the Shariah court, a civil law issue arises, the party raising it should file a case in the civil court for the determination of that issue which decision should be applied by the Shariah court in deciding the case. This, however, is only possible if both parties are Muslims. In case an application to the Shariah court is resisted on the ground that the shariah court is bound, then the answer thereto is simply that interpretation of the Federal Constitution is a matter for the civil court, not the Shariah court. When this court says that the Shariah court has jurisdiction. Therefore, the Shariah court has the jurisdiction’.

3.0 The Status of Islam And Shariah Law In Malaysia.

Even though Islam is the official religion of the Federation, Shariah courts only have jurisdiction in matters of personal law and family law of Muslims and a limited criminal jurisdiction to try Shariah offences. Administration of Shariah legal system is placed under the jurisdiction of the state where each state Islamic Religious Department will administer Shariah law, as embodied in the relevant Shariah law enactments, as interpreted based on the Quranic precepts, prevalent School of Islamic Law (*Mazhab*) in the country and Shariah law of evidence enacted by the respective state.

Article 121 (1A) of the Federal Constitution provides a safeguard against usurpation by the civil courts of Shariah court’s jurisdiction. Based on Article 121 (1A), courts such as the High Court and subordinate courts shall not have jurisdiction with respect to any matter that lies within the jurisdiction of the Shariah courts. The second safeguard against usurpation of Shariah court’s jurisdiction can be found in paragraph 1, List II of the Ninth Schedule of the Federal Constitution i.e. the State List. List II or the State List, which lists down matters that fall under the jurisdiction of the state, provides in paragraph 1, among others, that the state shall have jurisdiction over all matters relating to Islamic law and personal and family law of persons professing the religion of Islam. Paragraph 1, List II also provides that the state has a limited jurisdiction to legislate in respect of the creation and punishment of Shariah offences committed by persons professing the religion of Islam insofar as such offences are not included in the Federal List.

Despite the generous provisions of the Federal Constitution, Shariah court appears to have a very limited jurisdiction. Shariah court acquire jurisdiction only with the express provisions of enacted laws and not by implication. As decided by the court of appeal for *Latifah Bte Mat*

Zin v Rosmawati binti Sharibun case, it was very clear that the determination whether the assets in question had been given as a valid 'hibah' by the deceased to the appellant was a matter that falls within the jurisdiction of the syariah court. However, when involve with the determination on the 'Hibah' issue and the beneficiary or beneficiaries entitled to it and in what proportion, if relevant, is within the jurisdiction of the syariah court. Then the civil court shall give effect to it in the grant of a letter of administration, and subsequently, in distributing the estate.

Shariah court does not have automatic jurisdiction over all matters referred to in paragraph 1, List II. As stated in Paragraph 1, list II;

Except with respect to the Federal Territories of Kuala Lumpur, Labuan and Putrajaya, Islamic law and personal and family law of persons professing the religion of Islam, including the Islamic law relating to succession, testate and intestate, betrothal, marriage, divorce, dower, maintenance, adoption, legitimacy, guardianship, gifts, partitions and non-charitable trusts; Wakafs and the definition and regulation of charitable and religious trusts, the appointment of trustees and the incorporation of persons in respect of Islamic religious and charitable endowments, institutions, trusts, charities and charitable institutions operating wholly within the State; Malay customs; Zakat, Fitrah and Baitulmal or similar Islamic religious revenue; mosques or any Islamic public places of worship, creation and punishment of offences by persons professing the religion of Islam against precepts of that religion, EXCEPT IN REGARD TO MATTERS INCLUDED IN THE FEDERAL LIST; the constitution, organization and procedure of Syariah courts which shall have jurisdiction only over persons professing the religion of Islam and in respect only of any of the matters included in this paragraph, but shall not have jurisdiction in respect of offences except in so far as conferred by federal law, the control of propagating doctrines and beliefs among persons professing the religion of Islam; the determination of matters of Islamic law and doctrine and Malay custom.

Instead, state legislature may only legislate on this matter in the absence of Federal law having jurisdiction over the same issue such as 'Hibah' as decided in the previous case. Despite this constitutional safeguard to prevent competing Federal-State jurisdictions over matters in the State List, incidents of clash of jurisdiction do occur. For example, disputes arising out of Islamic banking transactions are under the jurisdiction of the civil courts and trials are conducted according to the civil law procedural and evidential laws. However, reference to Part IV on Shariah Requirement, under Division 1, para 28(2) of the Islamic Financial Services Act 2013 which provides that, "For the purposes of this Act, a compliance with any ruling of the Shariah Advisory Council in respect of any particular aim and operation, business, affair or activity shall be deemed to be a compliance with Shariah in respect of that aims and operations, business, affair or activity."

When this Part IV is read together with Sections 3 and 6 of the Civil Law Act 1956, which continue to emphasize the use of common law and equity if there is any lacuna in the law, particularly in commercial matters (Section 6, Civil Law Act 1956), it becomes clear that there are exceptions to the strict, literal application of civil law by the civil court to Islamic banking transactions.

A review of the legislations on commercial matters in Malaysia shows that several laws which are in force such as the Contracts Act 1950, the Companies Act 1965 and the Takaful Act 1984 contain provisions which support the application of Section 3 and 6 of the Civil Law Act 1956. On this authority granted by Section 3 and 6 of the Civil Law Act 1956, the application of the provisions of the existing laws by the civil court shall be adjusted accordingly to accommodate the peculiarities of Islamic banking business (Ayub 2007) [5].

Clash of Shariah and civil courts jurisdictions has given rise to a number of problems, especially when it comes to litigation procedures. According to Zainal Amin Ayub (2007) [6], there should be harmonization of aspects of civil litigation, especially the discovery and appeal procedures, with the procedures currently in use in the Shariah courts, which are based on the precepts of Islamic law. There are also opinions that the presence of Shariah experts in the civil High Court is necessary. In relation to Islamic banking cases, this would create a hybrid legal system whereby there would be two courts – the civil court and the Shariah court - which have parallel jurisdictions in the field of Islamic banking (Shariff, Mohamed Ismail, 1998) [7]. Previously, Court cases involving Islamic banking issues had often brought to the limelight the issue of clash of jurisdiction of civil court and Shariah court. Among the number of cases wherein this issue was raised are *Tinta Press Sdn Bhd v Bank Islam (M) Bhd (1987)*, *Bank Islam Malaysia Berhad v. Adnan Omar (1994)*, *Dato 'Nik Mahmud Bin Daud v Bank Islam Malaysia Berhad (1996)*, *Bank Malaysia Bhd v Emcee Corporation Sdn Bhd (2003)*, *Bank Islam Malaysia Bhd v. Pasar raya Peladang Sdn Bhd. (2004)*, *Arab Malaysian Merchant Bank Bhd v Silver Concept Sdn Bhd (2005)*, *Malayan Banking Bhd v Ya'kub Oje & Anor (2007)*.

In the case of *Tinta Press Sdn Bhd v Bank Islam (M) Bhd (1987)*, the Islamic contract that involved in this case is Ijarah. The court pointed out that this is leasing contract and not loan. As such, the court upheld the decision of the courts below that the equipment are owned by the respondent (as lessor). The appellants do not have the right to the equipment until full payment of the lease rentals to the respondents. As for the case of *Bank Islam Malaysia Berhad v. Adnan Omar (1994)*, the issue is concerning Bai Bithaman Ajil (BBA). The court took the approach that the defendant when signing the agreements was fully aware of the nature and consequences, and he is now estopped from denying that the plaintiff has the right to claim from him the total sale price indicated in the property sale agreement. It will be inequitable to allow the defendant's claim where he himself has willingly entered into the contract in the first place.

Next case that relates to BBA is *Dato 'Nik Mahmud Bin Daud v Bank Islam Malaysia Berhad (1996)*. The court took the approach that the defendant when signing the agreements was fully aware of the nature and consequences, and he is now estopped from denying that the plaintiff has the right to claim from him the total sale price indicated in the property sale agreement. It will be inequitable to allow the defendant's claim where he himself has willingly entered into the contract in the first place. Initially, there was no intention for real transfer of the property from the defendant to the plaintiff vice versa, as signing the Property Sale Agreement (PSA) and the Property Purchase Agreement (PPA) are part of the whole process for the Islamic financing called BBA. Hence no issue arises as to the Malay reserved land, and whether the plaintiff is a Malay or not.

The following cases that also related to BBA are the case of *Bank Malaysia Bhd v Emcee Corporation Sdn Bhd (2003)*, *Bank Islam Malaysia Bhd v. Pasar raya Peladang Sdn Bhd. (2004)*, *Arab Malaysian Merchant Bank Bhd v Silver Concept Sdn Bhd (2005)* and

Malayan Banking Bhd v Ya'kub Oje & Anor. The issues in cases such as *Bank Malaysia Bhd v Emcee Corporation Sdn Bhd* (2003), *Bank Islam Malaysia Bhd v. Pasar raya Peladang Sdn Bhd*. (2004) are very much administrative and do not involve the substance or working mechanism of BBA. Because all the requirements in the NLC and RHC are fulfilled, the court granted the application for order for sale by the plaintiff.

Meanwhile as for *Arab Malaysian Merchant Bank Bhd v Silver Concept Sdn Bhd* (2005), the court took the approach that the defendant when signing the agreements was fully aware of the nature and consequences, and he is now estopped from denying that the plaintiff has the right to claim from him the total sale price indicated in the property sale agreement. It will be inequitable to allow the defendant's claim where he himself has willingly entered into the contract in the first place. Lastly, in the case of *Malayan Banking Bhd v Ya'kub Oje & Anor* (2007), The court took the approach to do justice to both plaintiff and the defendant, allowing the full claim by the bank, on the condition that the bank will give rebate and to specify the rebate amount.

However, the current ongoing harmonization of civil procedural and substantive laws to accommodate the Shariah peculiarities of Islamic banking principles and practices implies that instances of clashes of jurisdictions between the civil and Shariah courts will be a thing of the past in the nearest future. This harmonization process has addressed the concern of Islamic banking consumers that they are being denied the full measure of justice they deserve (Markom 2012) [8].

The harmonization exercise can be traced back to 2010, when Bank Negara established the Law Harmonisation Committee (LHC) which consists of the Central Bank, the Securities Commission, Attorney General, lawyers, International Shari'ah Research Academic for Islamic Finance (ISRA), and the Association of Islamic Banking Institutions Malaysia (AIBIM). LHC was established to coordinate and monitor the development of the legal system of the Islamic financial industry in Malaysia. Among the main objectives of the LHC, is providing financial *muamalat* contract that will bring about uniformity in financial *muamalat* contracts documentation in Malaysia (Tun Abdul Hamid Mohamad 2011) [9].

Nonetheless, the issue of homogenization of Islamic banking products offered by all financial institutions in Malaysia is however far from being resolved. Commonly all the legal documents are in English (Civil Procedurals) and common law lawyers who draft those documents could not appear in the Shariah courts. The law is in English not Shariah. In conclusion, it is evident that Islamic banking law and practice are currently undergoing a transformation process which will make them compatible with the civil law. However, the challenge is to ensure that the transformed Islamic banking law and practice meet the needs of the market demands and the way of life, if it is to achieve equality for all races and religions.

4.0 The Evolution on Civil Law and Islamic Law in Dealing Islamic Banking Transactions.

According to Al-Ghazali (1937) [10], Islamic banking institution is a financial institution that operates with the objective of carrying out transactions based on Islamic principles. The definition of Islamic banking institution however varies across countries and organizations. Based on section 2 of the Islamic Banking Act 1983, Islamic banking business is a banking business whose aims and operations do not involve any element which is not approved by the Religion of Islam. While according to section 2 of the Islamic Financial Services Act 2013, the term of "Islamic banking business" means the business of accepting Islamic deposits on current account, deposit account, savings account or other similar accounts, with or without

the business of paying or collecting cheques drawn by or paid in by customers; or accepting money under an investment account; and provision of finance; and such other business.

The practice of Islamic banking is based on Shariah principles. Shariah Principles are referring to the principles in the Quran (Surah An-Nisa 4). In which it reflects the human interpretation of Shariah, or in other words, it is known as the principles of Fiqh. Principles of Fiqh is an understanding of the principles of Islamic jurisprudence in general. Technically, Fiqh means practical knowledge of the Shariah position on a particular issue. However, Shariah principles is much broader than the principles of Fiqh. Shariah principles cover *aqad*, *ibadat*, *akhlak* (moral) and *muamalat* whereas the principles of Fiqh covers only matters of *ibadat* and *muamalat*. Shariah principles are considered as written legislations and principles of fiqh are derived from an understanding of the principles of Shariah law and are made by expert jurists (Ahmad Hassan, 1994) [11].

Islamic banking is built on the principle which bans the acceptance of interest (*riba*). It reflects the concept of fairness manifested through the concept of profit and loss sharing and banning of the practice of *riba*. According to Obaidullah (2005) [12] emphasized that in the Islamic financial system, all transactions will be applied based on the norms of Islamic ethics as implemented in Shariah law. In essence, the foundation of the Islamic financial system can be described as "fair" and in accordance with Shariah law. The Islamic financial system allows the freedom to make such transactions. But this does not mean that there is no restriction of freedom, prohibition of *riba* and *gharar* because the risk (uncertainty) is still controlled and banned any practitioner in the practice of Islamic financial system.

Since the year of 1986 until 2012, there are 29 reported court cases shows that this concept of fairness is reiterated over and over again i.e. any business or commercial activity must be fair and equitable [13]. In the case of *Dato Hj. Nik Mahmud Daud v BIMB* [14] the plaintiff had executed two agreements, namely the 'property purchase agreement' and the 'property sale agreement with the defendant under the defendant's BBA property financing facility. There was a purchase by the defendant through the former agreement of properties ('the said lands') for a price of RM520,000 which were then resold through the latter agreement to the plaintiff for RM629,200. Both the agreements were signed contemporaneously. On 8 May 1984, the plaintiff's attorney executed two charges of the said lands in favour of the defendant as securities for a loan of RM629,200, which loan was purportedly granted under the Islamic banking concept of *Al Bai Bithaman Ajil*.

In this action, the plaintiff applied for an order that the charges dated 8 May 1984, the property purchase agreement and the property sale agreement be declared null and void and of no effect. It was contended by the plaintiff that the execution of the property purchase agreement, the property sale agreement and the charge documents would clearly tantamount to an exercise to defeat the very purpose and intention of the Kelantan Malay Reservations Enactment 1930 ('the Enactment') and the National Land Code 1965 ('the Code'). Counsel for the defendant raised various issues to resist the motion, inter alia, the indefeasibility of the charges under section 340 of the Code and the interpretation of the Enactment, vis-a-vis *Al Bai Bithaman Ajil* transactions. The motion was dismissed with costs and the appellant appealed.

Meanwhile in *Bank Islam Malaysia Berhad v Pasaraya Peladang Sdn. Bhd.* [15], the court allowed the plaintiff's application which involved *Bai Bithamin Ajil*, a common Islamic banking lending facility. In *Bai Bithamin Ajil transaction*, there are two separate agreements

and a security document involved. In the first agreement, the bank would purchase the property concerned from the charger (the purchaser of the property who charges the property to the bank as collateral). In the second agreement, the bank would sell the property back to the chargor. Lastly, a security document that is a charge given by the charger to the bank to enable the bank to sell the property in the event of default by the charger. The chargor's defence that the transaction should be nullified due to existence of element of fraud was rejected by the court – the rationale being that based on the principle of Shariah law, all transactions that have been agreed and signed by all parties to the agreement will be deemed to be understood by the parties and that the parties have accepted the agreement voluntarily. Therefore, it cannot be said by any party to the agreement that there is an element of fraud in this Shariah oriented agreement [16].

According to Abdul Ghafar Ismail (2011) [17], basic contracts based on the principles of Shariah can be divided into three categories namely commercial contracts, participatory contract and support contract. Commercial contract is a contract of sale and purchase or exchange involving profit such as *murabahah* contract, *Bai Bithamin Ajil*, *salam*, *istisna*, and hire agreement such as *Ijarah*. Participatory contract is a contract that involves capital investment to create a profit-sharing relationship such as *musyarakah*, and *mudharabah*. The last category, the support contract, is a contract to fund and facilitate trade coupled with profit-sharing such as *rahn*, *kafala*, *wadiah* and *ibraa*.

In the case of *Bank Islam Malaysia Bhd v Rhea Zadani Corp Sdn Bhd* [18], The plaintiff had approved several *Istisna* facility for the first defendant. The purpose of the facility was to finance the cost of the building of housing project/shophouses. In order to enforce the facility, the plaintiff executed the *Istisna*' purchase agreement and the *Istisna*' sale agreement. The second to sixth defendants had signed the guarantee letter to guarantee the facility. The defendants failed to repay the facilities and the plaintiff filed this action to claim for the amount payable under the facilities. The plaintiff subsequently filed this application to record a summary judgment against the defendants under Ordinance 14 of the Rules of the High Court 1980 ('RHC'). The defendants contended that the plaintiff's application had to be dismissed based on, inter alia, the grounds that: (i) the *Istisna*' agreements were not based on the true *Istisna*' principles; (ii) there was defence, dismissal and counterclaim which outweighed the plaintiff's claim; and (iii) the plaintiff had wrongfully disturbed the operation of the first defendant's housing development account (HDA) whereby the plaintiff assumed the money in the HDA account to be a security.

The high court decided to allow the plaintiff's application with costs. The defendants' contention that the *Istisna*' agreements were not valid in Shariah without adducing any strong grounds in Shariah, was a lawyer's constructive defence which was purported to merely discharge the defendants' obligations under the agreements and ought to be dismissed. There was no evidence that showed that the plaintiff assumed the money in the HDA account as security on the first defendant's indebtedness. The plaintiff had the right to apply and withdraw the money from the HDA account which was the plaintiff's uncollected redemption based on the redemption letter/undertaking which had been withdrawn by the plaintiff to the end-financer since 2007-2010. Also, there was no issue of dismissal in this case. In which the defendant did not adduce any detailed evidence to support their contention that the related statement of account was wrong, not correct and/or inaccurate.

Next case is the case of *Cimb Islamic Bank Bhd v Lcl Corp Bhd & Anor* [19], The plaintiff, an Islamic bank, had to carry Islamic banking business and operations in a manner

that did not involve any element disapproved by Islam. Thus, when the first defendant, a customer of the plaintiff bank, applied for a term-financing facility, the plaintiff granted him the loan amount of RM48,450,000 under the concept of *bai bithman ajil* ('the BBA facility'), a sale and purchase transaction for the financing of an asset on a deferred and instalment basis with a pre-agreed payment period. In the present BBA facility, the first defendant agreed to sell to the plaintiff bank 16,000,000 units of the second defendant's shares in the first defendant's company ('the asset'). However, the first defendant was not the owner of the asset. The second defendant, director of the first defendant company was the owner of the asset. Thus, by way of a unilateral benevolent contract ('the letter of hibah') the second defendant voluntarily gave the asset to the first defendant, who in turn executed the asset purchase agreement to sell the asset to the plaintiff at RM12,125,000 ('the purchase price').

Thereafter the plaintiff entered into an asset sale agreement to sell the asset back to the first defendant at RM16,087,500 ('the sale price'), with the payment of the sale price deferred to the date stipulated in the asset sale agreement. Finally, by way of another letter of hibah the first defendant had gifted the asset back to the second defendant. The parties agreed to enter into four sets of these agreements with the intention of providing the first defendant with the liquidity to refinance its existing BBA facility ('the first BBA facility'). When the first defendant defaulted in his repayments to the plaintiff bank despite notices of demand issued to it, the plaintiff commenced an action against the defendants. This was the plaintiff's application for summary judgment to recover the outstanding sums of money, *ta'widh* or compensation and costs from the defendants. In response the defendants argued that this was not a proper case for summary judgment, namely because, the BBA facility was null and void; the amount claimed was inaccurate; the plaintiff's calculation of *ta'widh* was wrong; and the plaintiff had no claim against the second defendant.

The high court decided to allow the plaintiff's application with costs. The first defendant's argument that the transaction between the parties was not a bona fide sale under the BBA concept but rather a rescheduling of the repayments of the first BBA facility had to fail. This court found that there was nothing in the legal documentation that indicated that the present BBA facility was for rescheduling the repayment under the first BBA facility. Based on the facts and the documents, the BBA facility before this court was not for rescheduling but for refinancing the first BBA facility. The parties had agreed to be bound to give effect to the ultimate intention of refinancing the first BBA facility. In this present case, the nature of transaction embarked into by the parties was called *al-inah* or *bai-al-inah*, which the Shariah Advisory Council of Bank Negara Malaysia had officially endorsed in their legal rulings and resolutions.

As such, and in the absence of any legal factor that could vitiate a contract, this court had no reason but to uphold the transactions as contracts entered by both parties. In the present case, the relationship between the plaintiff and the first defendant was regulated by the terms and conditions they had agreed upon in their letter of offer and the assets purchase and asset sale agreements. On the plain reading of the letter of offer, the first defendant would be granted *ibra'*, or a rebate upon an early settlement of the BBA facility. Unfortunately, the defendants had made no effort to make any settlement of the sum outstanding under the BBA facility and the termination of the BBA facility before the expiry of its tenure was not considered early settlement. As such, the plaintiff was under no obligation to grant an *ibra'* to the defendants. In the circumstances of this case, it was undisputed that the plaintiff had the right to impose compensation (*ta'widh*) on overdue instalments and payments of the selling

price as agreed. In the instant case, the court was satisfied that there was no real prospect for the defendants successfully defending the claim by the plaintiff and thereby allowed the plaintiff's application.

The following case is *Bank Muamalat Malaysia Bhd v Kong Sun Enterprise Sdn Bhd & Anor* [20]. The plaintiff was a licensed finance company which was incorporated in Malaysia and the first defendant was the plaintiff's customer while the second and third defendants were directors of the first defendant company. The facts of the case was that the plaintiff had offered and the first defendant had agreed to accept the Al-Istisna facility amounting to RM22m and via a guarantee and indemnity agreement dated 3 June 2002, the second and third defendants had agreed to guarantee the first defendant's obligation on the terms and conditions stated in the agreement.

By a letter of offer dated 27 May 2005, the plaintiff offered to restructure the Al-Istisna facility to the Al-Ijarah facility for the sum of RM21,234,415.74 and the first defendant had accepted the offer by signing the letter of offer on 30 May 2005. Pursuant to the terms of the letter of offer, the plaintiff had signed the Al-Ijarah property purchase agreement where the defendant had agree to sell a piece of land to the plaintiff at the purchase price of RM21,234,415.74. The plaintiff had also signed an Al-Ijarah aset lease agreement whereby the first defendant had agreed to lease the piece if land at monthly rental for the period of 156 months. By a supplemental guarantee and indemnity signed between the plaintiff and the second and third defendants, the second and third defendants had agreed to guarantee the first defendant's obligations under the letter of offer, the purchase agreement as well as the lease agreement.

Among the conditions in the supplemental guarantee agreement was that all the terms contained in the guarantee and indemnity agreement dated 3 June 2002 were mutatis mutandis combined and would form part of the supplemental guarantee agreement. However, the first defendant had breached the lease agreement where the first defendant had failed to pay to the plaintiff the monthly rental payment amounting to RM9,440,917.78. The plaintiff subsequently terminated the lease agreement. The plaintiff con-tended that it had successfully proved its claim against the defendants. On the other hand the defendants raised five issues in defence as follows: (a) the transaction which was the basis of the claim was not possible under the law; (b) the lease was unlawful and could not be enforced; (c) the plaintiff was only entitled to claim for damages; (d) the Al-Ijarah transaction was a false transaction and therefore was not legal as it was against the public policy; and (e) the claim against the second and third defendants (the guarantors) had not been proven.

The high court decided to allow the claim with costs. In which the court stated that Islam allowed the concept of ijarah in Islamic banking. The contention by the defendant's counsel that Ijarah was unlawful, against the conventional banking, not in line with the National Land Code, was against the Contracts Act as well as a false transaction was unacceptable al-legations. The defendants in this case after having agreed to be bound by the concept of ijarah in Islamic banking, could not, after obtaining the benefits from it make superficial allegations in order to be relieved from their liability to pay to the plaintiff what they had already agreed.

The defendants had signed all the documentations including the letter of offer, the purchase of aset agreement, the aset lease agreement and the guarantee and indemnity agreement voluntarily and with full knowledge of the validity of the agreement. There was no allegation by the defendants that there were elements of duress, cheating, misrepresentation or

the like in the signing of all the documents. Therefore, the defendants were bound by the agreements.

The transaction between the parties fell under the *ijarah* to obtain cash under the concept of AITAB. As a result of the AITAB transaction, the first defendant obtained cash liquidity required of more than RM22m, the plaintiff bank would obtain its profit the rental of approximately RM16m and the parties were saved from 'riba' loan and their transaction was honest and lawful. The defendants' contention that the *ijarah* transaction was something that was false and amounted to loan was an unthoughtful and baseless accusations.

In the event of default, the asset lease agreement prescribed that the first defendant must pay the amount agreed upon under the agreement after deducting the rental paid. Therefore, the defendants' contention that the plaintiff was only entitled to claim for damages under section 75 of the Contracts Act 1950 was baseless.

Further, the plaintiff had proved its claim against the second and third defendants. The plaintiff had proven that by SP1's evidence that the second and third defendant had signed the supplemental guarantee and indemnity agreement to guarantee the payment of the first defendant. Finally, the court also decided that an advocate and solicitor did not have the qualification to testify against the Islamic law and Islamic banking system. The witness who had the qualification to give opinion and view in relation to the Islamic banking system was the member to the Shariah Advisory Council which was established under section 16B(1) of the Central Bank of Malaysia Act 1958.

Lastly is the case of *Tan Sri Abdul Khalid Bin Ibrahim v Bank Islam Malaysia Bhd* [21]. The Bank Islam Malaysia Bhd ('the bank') had granted Tan Sri Abdul Khalid bin Ibrahim ('the plaintiff') a revolving *al-Bai Bithaman Ajil* agreement ('the BBA facility'), an Islamic financing facility. In order to achieve the objective of this facility the parties had intended to bind themselves by the Shariah principles of *al-Bai Bithaman Ajil*. Pursuant to the terms of the BBA facility, the plaintiff had executed seven sets of asset purchase agreements and asset sale agreements ('the BBA facility agreements') at six monthly intervals. The plaintiff was dissatisfied with the conduct of the bank in connection with the BBA facility, which he alleged contravened the religion of Islam. The plaintiff thus commenced a suit against the bank ('the plaintiff's suit') and sought, inter alia, a declaration that the BBA agreements entered into by both parties were null and void. The bank denied the plaintiff's allegations and pleaded that under civil law and Shariah principles, parties were bound by their agreements and thus the plaintiff was bound by the clear terms of the BBA facility agreements. Subsequently, the bank commenced a debt recovery action ('the defendant's suit') against the plaintiff alleging that the plaintiff had defaulted the terms of the BBA facility. Prior to the consolidation of the two suits (the plaintiff's suit and the bank's suit), the bank applied for summary judgment in respect of its suit, which the plaintiff resisted.

The High Court allowed the summary judgment application but the plaintiff appealed to the Court of Appeal, which allowed the appeal. During case management of this consolidated action the bank filed the present application pursuant to section 56 of the Central Bank of Malaysia Act 2009 ('the Act') to refer certain questions to the Shariah Advisory Council of Bank Negara Malaysia ('SAC'). The bank submitted that the plaintiff had raised Shariah issues and that under section 56 of the Act such issues should be referred to the SAC, whose ruling would be binding on this court by virtue of section 57 of the Act. The plaintiff objected to this application, inter alia, on the grounds that there had been a prior reference to the SAC at the summary judgment stage; that section 56 and 57 of the Act did not operate

retrospectively; that section 56 and 57 of the Act contravened the Federal Constitution; and that the Shariah issues were not appropriate for reference to the SAC.

The High court decided to allow the application with costs in the cause of the court found that, based on the allegations raised by the plaintiff and the defence advanced by the bank, there were Shariah issues to be decided by this court. Based on the facts of this case it was found that there were Shariah issues for the ascertainment of the SAC, namely, whether the BBA facility agreements executed by the parties were contrary to the principles of Shariah; whether the bank was allowed to dispose of the shares pledged by the plaintiff as security under the agreements without his permission; whether the plaintiff's obligation to settle his indebtedness with the bank would be extinguished if the BBA facility agreements were found to be contrary to the principles of Shariah; whether there must be two distinct and separate contracts between the first and the second sale and if so whether there had been a violation in the present case; Whether the shares pledged with the bank which were already sold could be repurchased and resold. Both parties had also intended to bind themselves by the Shariah principles at the time the agreements were executed.

It was the plaintiff's argument that the execution of the BBA facility and the consolidation of the suits were affected before the Act came into force on 25 November 2009 and therefore section 56 and 57 of the Act could not be applied retrospectively. However, there is a presumption that amendments to purely procedural statutes should be given retrospective effect and amendments that change substantial rights be given prospective rights. In any case, there would be no adverse effect to the plaintiff's existing substantive rights by the application of a new procedure as far as Shariah issues were concerned. The only difference would be that as from 25 November 2009, the discretionary power of the court to take into consideration any written directive issued by BNM had been taken away and the ruling of the SAC was binding on the court. In any case the plaintiff's argument that he had a vested right to lead expert evidence was untenable because the SAC is a statute-appointed expert.

It is settled law that section 56 and 57 of the Act are valid federal laws enacted by Parliament and as such were not in contravention of the FC. Difference of opinion on Shariah issues relating to Islamic banking should be resolved within the SAC. It is advisable and practical that a special body like the SAC should ascertain the Islamic law most applicable to the Islamic banking industry in Malaysia.

All these cases had raised two general issues namely whether financial products offered by Islamic banking institutions are Shariah compliant and whether the terms and conditions of the contracts embodied in such products are fair to all the parties involved.

In order to obtain unbiased opinions as to the most appropriate principles of Shariah to be applied in a particular case, a new independent body had been created and it is called Shariah Advisory Council (SAC). SAC's function as an expert reference body for Shariah matters concerning Islamic banking (Section 56 of Central Bank Act 2009). Any SAC's ruling will serve as a reference for the court or arbitrator trying or arbitrating Islamic banking cases. As stated in section 57 of Central Bank Act 2009, any ruling made by the SAC *shall be binding* on the Islamic Financials and its function is to ensure that the bank's business does not involve any element which is not approved by the religion of Islam. Nonetheless, if there are conflicting views, the position of precedence in the advice/ruling given is not clear. In practice, however, the ruling of SAC on any matter referred to it is not binding on the referring forum. In the case of *Mohd Alias bin Ibrahim v RHB Bank Bhd & Anor* [22], court's

held that the ruling of Shariah Advisory Council (SAC) is not binding on it. This shows that even though SAC is an expert opinion body in respect of Islamic finance matters, it will then be up to the courts to apply the ascertained law to the facts of the case. The High Court came to the similar conclusion in *Tan Sri Abdul Khalid bin Ibrahim v Bank Islam Malaysia Bhd* [23] whereby it was held that it is upon the court to decide the matter before it and not the SAC. However, the High court acknowledge the power of SAC to resolve all issues relating to Islamic banking when involve with difference of opinion on Shariah issues.

As a result, Section 58 of Central Bank Act 2009 provides that where the ruling given by a *Shariah* body or committee constituted in Malaysia by an Islamic financial institution is different from the ruling given by the SAC, the ruling of the SAC shall prevail. The clarification of the provision indicate that the decision of the SAC will creates no opportunity for such conflicting ruling/advice to be rendered at all in the future. Consequently, this will allow any Islamic banking products to be practise according to all the parties involve (either between Muslim parties or non-Muslim parties) with the aid of SAC to achieve their demands and needs.

The diversity of the Islamic banking products that are based on the principles of Shariah has attracted interest of banking consumers, Muslims and non-Muslims alike, which resulted in increase in demand for such products. One of the attractive factors of Islamic banking products that brought about this surge in demand is that because Islamic financial products have no elements of *riba* (usury) and *gharar* (uncertainty). Further, they are also confined to lawful activities, perceived as fair and must of all it is in accordance with Islamic teachings (which is a selling factor for Muslim consumers) [24][25].

Thus, the role of SAC is very important to maintain the fair and just in our multi-ethnic society. At the higher level, there is a centralised Shariah Advisory body of the SAC which is categorised into SAC of Central Bank of Malaysia who provides decisions on Islamic banking and Takaful issues and the Securities Commission (SC) who provide rulings on Islamic capital market issues.

Plus, the appointment of the SAC members was made by the Minister on the recommendation of the Central Bank of Malaysia. According to section 53 of Central Bank Act 2009, the Ruler (King or *Yang di Pertuan Agong*) may, on advice of the Minister after consultation with the Bank, appoint from amongst persons who are qualified in the Shariah or who have knowledge or experience in the Shariah and in banking, finance, law or such other related disciplines as members of SAC. therefore, the combination of the jurisdiction of the Shariah Court, the laws and the roles of SAC is significant for achieving justice for all.

5.0 Conclusion

In summary, function of law [26] in society is mainly to ensure the existence of adequate order; it provides resolutions to conflicts; it provides a safe haven for individuals and their assets; it maintains the structured operation of the civilisation; and it protects civil liberties as set forth in each nation's constitution. Admittedly, it is a difficult task to ascertain precisely whether a particular law, in its practical application once legislated, will fulfil the requirements and the needs of the society. Nevertheless, where law is found to be unable to cope with the reality of the society, it must be amended so that it does not lose its relevancy in the society.

Law therefore must be kept current since it plays an important role in the society. The law lays down rules that govern private disputes, self-help actions or open-conflicts that may

occur in the society. Here, courts, tribunals, arbitration and other dispute resolution forums are the main secular institutions in dispensing just resolutions in a society. Also, the role of the SAC in which SAC providing any assistance necessarily relating to Islamic banking products in order to maintain fairness and justice among Malaysian society.

Religion, however, also plays an important role in ensuring justice for all walks of life by lending its principles to the day-to-day affairs of the society. In order to take advantage of what religion has to offer, Malaysia has allowed the existence of a distinct Islamic banking system based on the precepts of Shariah law. In the context of Malaysia, the move to harmonize the jurisdiction of the civil legal system with the substantive and procedural aspects of Shariah law is an effort by the relevant authorities to bring the concept of unity and integration of the conventional and Islamic legal systems into practical reality. In a nutshell, we can conclude that harmonization of the two legal systems and with the aid of SAC serves the purpose of fulfilling the demands of socio-legal reality i.e. adapting and bringing itself current with the changing surrounding.

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