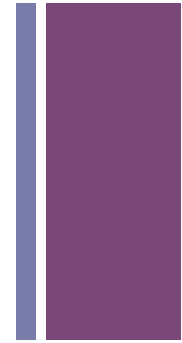


Regulation in Islamic Finance: LAB3073

Zulkifli Hasan, PhD

+ CONTENTS

- **Legal Framework of Islamic Finance**
- **Jurisdiction**
- **Guidelines on Islamic Finance**



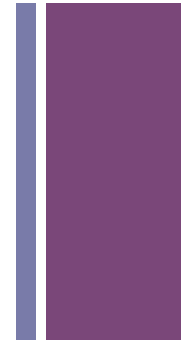
+ INTRODUCTION

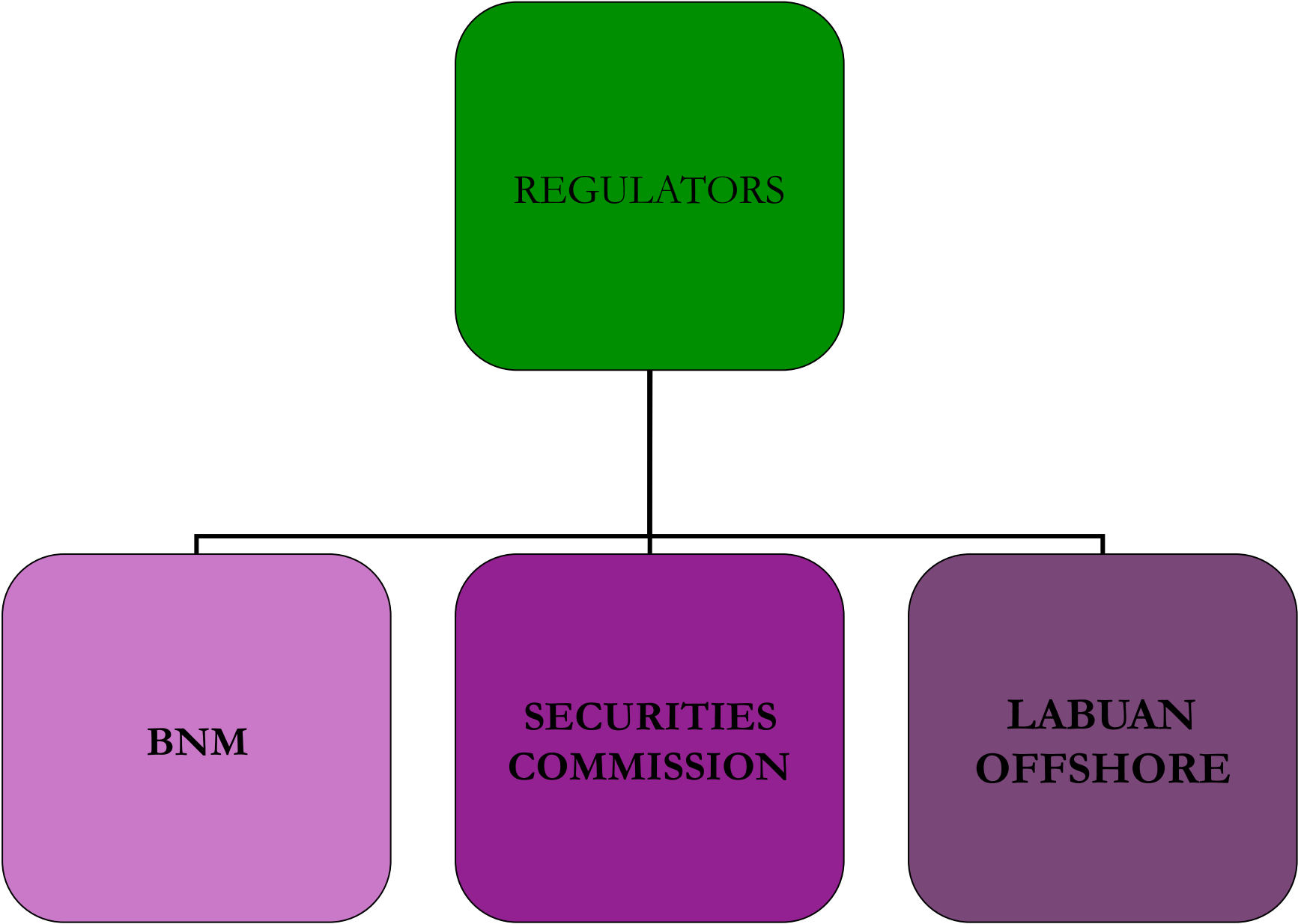
- Malaysia has a unique legislative framework consisting of mixed jurisdictions and mixed legal systems namely the common law and shariah.
- The growth and development of Islamic banking industry are supported through goods governance and its comprehensive legal frameworks. As Malaysia is one of the common law countries, it is very essential to have standard law of practice, which harmonizes both *shariah* and civil law. The integration of these two traditions is really necessary in the context of Islamic banking in Malaysia.



Legal Development

- Dual Banking system and Moderate approach
- Federal List, Fed Const
- IBA 1983 and BAFIA 1989
- GIA 1983 statutory reserves and liquidity reserve requirements, allowing them to be interest-free.
- TA 1984
- DFIA 2002
- SCA 1993, CMSA 2007
- CBA 2009
- IFSA 2013
- BNMs Guidelines





+ BNM

- 2 Objectives: 1) To promote monetary stability and a sound financial structure
- 2) To influence the credit situation to the advantage of the federation
- implementing all the regulations concerned with these matters as laid by the law, as well as issuing policies and directives to further the implementation of these regulations.
- Where and when certain of the regulations have become inadequate or new or additional regulations become necessary, it is also the Central Bank's responsibility to initiate the formulation of such changes.

+ BNM Section 5 CBA

- (a) to formulate and conduct monetary policy in Mala
- (b) to issue currency in Malaysia;
- (c) to regulate and supervise financial institutions which are subject to the laws enforced by the Bank;
- (d) to provide oversight over money and foreign exchange markets;
- (e) to exercise oversight over payment systems;

+ Cont...

- **(f) to promote a sound, progressive and inclusive financial system;**
- **(g) to hold and manage the foreign reserves of Malaysia;**
- **(h) to promote an exchange rate regime consistent with the fundamentals of the economy; and**
- **(i) to act as financial adviser, banker and financial agent of the Government.**

+ Securities Commission

- Security Commission Act 1993;
- (a) to advise the Minister on all matters relating to securities and futures industries;
- (b) to regulate all matters relating to securities and futures contracts;
- (c) to ensure that the provisions of the securities laws are complied with;
- (d) to regulate the take-overs and mergers of companies;
- (e) to regulate all matters relating to unit trust schemes;
- (f) to be responsible for supervising and monitoring the activities of any exchange holding company, exchange, clearing house and central depository;

+ Labuan FSA

- LOFSA ACT 1996
- Section 3(2) spells out the objectives of the Authority are-(a) to promote and develop Labuan as a centre for offshore financial services; (b) to develop national objectives, policies and priorities for the orderly development and administration of offshore financial services in Labuan, and to make recommendations to the Minister
- Offshore Banking Act 1990 (OBA)
- Offshore Insurance Act 1990 (OIA)
- Labuan Offshore Securities Industry Act (LOSIA)
- Labuan Offshore Financial Services Authority Act 1996
- Labuan Offshore Business Activity Tax Act 1990

Islamic Banking and Takaful

BNM

Central Bank of Malaysia Act 2009

Islamic Capital Market

SC

Securities Commission Act 1993

CBA 2009 (Section 51-58)

Part VII, Chapter 1 of the CBA 2009	Section 16B (2003)
It should be read together with the <i>Shari'ah</i> Governance Framework for IFIs 2010.	It should be read together with the (BNM/ GPS 1) 2004.
It grants authority to the BNM to establish the <i>Shari'ah</i> Advisory Council (SAC) and to specify its functions as well as the secretariat to assist the SAC in carrying out its definitive roles. This vividly clarifies the roles and responsibilities of the SAC as the highest and sole authority in Islamic financial matters	It provides the establishment of the SAC but does not clearly clarify the roles and responsibilities of the SAC. No provision mentioning the setting up of the SAC's secretariat.

Part VII, Chapter 1 of the CBA 2009

Section 16B (2003)

In parallel with the status of the SAC as the highest authority, the appointment of the SAC members shall be made by the Yang di-Pertuan Agong. The SAC's remuneration and the terms of reference shall then be determined by the BNM.

The appointment shall be made by the Minister on the recommendation of the BNM.

It sets the minimum fit and proper criteria of the SAC members. knowledgeable and qualified in *Shari'ah* or have appropriate knowledge and experience in banking, finance and law. Also allows experts in other related disciplines to be the SAC members.

It has similar provision.

Part VII, Chapter 1 of the CBA 2009

Section 16B (2003)

No similar provision with the retired section 16B (6).

No member of the SAC shall become a member of any Syariah advisory body with any IFIs.

It affirms the legal status of the *Shari'ah* pronouncement issued by the SAC to be binding upon both the court as well as arbitration.

It merely provides that *Shari'ah* rulings issued by the SAC are binding upon the arbitration.

Part VII, Chapter 1 of the CBA 2009

Section 16B (2003)

It is mandatory for the court or arbitrator to refer to the SAC for deliberation on any *Shari'ah* issue, as well as taking into account its existing *Shari'ah* rulings.

The court or arbitrator is not obligated to refer to the SAC to resolve any *Shari'ah* issue .

It clarifies the status of the *Shari'ah* rulings issued by the SAC in the event that they contradict the *Shari'ah* pronouncement of a *Shari'ah* committee at an individual IFI. The *Shari'ah* rulings of the SAC shall prevail and have binding force over the *Shari'ah* resolutions of the *Shari'ah* committees of IFIs.

It does not clearly stipulate the position of *Shari'ah* rulings in the case of conflicting with any other *Shari'ah* resolutions.

+ CMSA 2007

- The Capital Markets and Services Act 2007 is governed by the Securities Commission Malaysia.
- The practice of Capital Market and Islamic capital market in Malaysia are governed by The Capital Markets and Services Act 2007 (CMSA).
- The Act incorporates three key legislation on the capital market that are the Securities Industry Act 1983, Futures Industry Act 1993 and Part IV of the Securities Commission Act 1993. This is an Act to regulate and to provide for matters relating to the activities, markets and intermediaries in the capital markets, and for matters consequential and incidental thereto

+ Jurisdiction

- List 1 (Federal List), of the 9th Schedule of Federal Constitution includes civil, criminal procedures, contracts, *lex mercatoria* (inclusive of banking and financial laws), arbitration, the administration of justice, etc.
- Para 1 of List 11 (State List) of the 9th Schedule of the Federal Constitution. Matters under the state list, inclusive of family law, personal law, divorce, waqf, succession, and the religion of Islam, including offences against it (except what falls under the Federal Law).

+ Q: Which Court has jurisdiction to hear Islamic banking and finance cases?



**DECISION BY Y.A DATO' HJ
MOHD ZAWAWI BIN SALLEH**

IN

MOHD ALIAS IBRAHIM

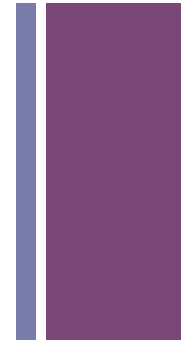
v

RHB BANK BHD & ANOR

[2011] 4 CLJ 654

[2011] 3 MLJ 26

Federal List

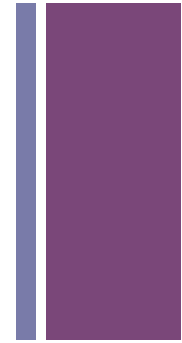


- **Islamic banking was put under Federal List since it refers to commercial dealings although it actually falls under the purview of Islamic law.**
- **Thus, it is the parliament to pass any law governing the Islamic financial institutions.**
- **The disputes will be heard in the Civil court due to Schedule Nine, List 2 of the Federal Constitution.**
- *Bank Islam Malaysia Bhd v. Adnan bin Omar.*



*Bank Kerjasama Rakyat Malaysia v
Emcee Corporation (2003) 2 MLJ 408;*

- The appellant granted the respondent a facility under the Islamic banking principle of BBA. Both parties executed two agreements on the same date. Under the first agreement, the respondent sold 22 pieces of land to the appellant for RM20Million.
- The second agreement, the appellant sold to the respondent the same properties upon deferred payment terms for 36 monthly installments. As security for the repayment of the sale price under the second agreement, the respondent charged to the appellant 15 pieces of the land under the NLC.



+ COA



- ***“The law was mentioned at the beginning of this judgment the facility is an Islamic banking facility but that does not mean that the law applicable in this application is different from the law that is applicable if the facility were given under the conventional banking” .***
- The charge was a charge under the National Land Code. The remedy available and sought was a remedy provided by the Code. The procedure was provided by the National Land Code and the Rules of the High Court 1980.

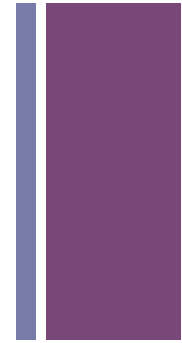
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BANK ISLAM MALAYSIA BHD V LIM KOK HOE & ANOR AND OTHER APPEALS [2009] 6 CLJ 22



“Similarly, the law applicable to BBA contracts is no different from the law applicable to loan given under the conventional banking. The law is the law of contract and the same principle should be applied in deciding these cases. Thus, if the contract is not vitiated by any vitiating factor recognised in law such as fraud, coercion, undue influence, etc. the court has a duty to defend, protect and uphold the sanctity of the contract entered into between the parties.”

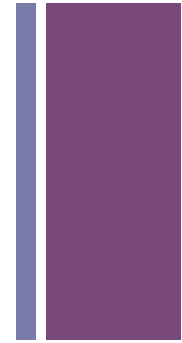
+ Co-Ordination With Judicial Body



- Lack of scholars with the right combination of knowledge of Islamic law, modern finance and technical English to serve on the *Shariah* committees of institutions based around the Gulf and beyond.
- BNM with a cooperation of judicial body has agreed to set up a special High Court in the Commercial Division known as the Muamalah bench.
- According to Practice Direction No.1/2003, paragraph 2, all cases under the code 22A filed in the High Court of Malaya will be registered and heard in the High Court Commercial Division 4 and this special high Court will only hear cases on Islamic banking.

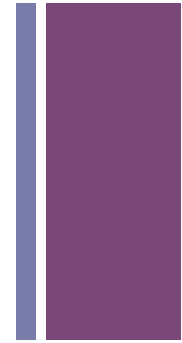
+ Shariah Guidelines

- Guidelines on the Governance of Sharī'ah Committee for the Islamic Banks, known as BNM/GPS1
- Sharī'ah Governance Framework for IFIs 2011
- the Guidelines on the Disclosure of Reports and Financial Statements of Islamic Banks known as BNM/GPS8-i
- Shariah Parameter Reference 1 - Murabahah
- Concept Paper on Shariah Parameter Reference 4: Musharakah Contract
- Concept Paper on Shariah Parameter Reference 5: Istisna' Contract



+ Guidelines

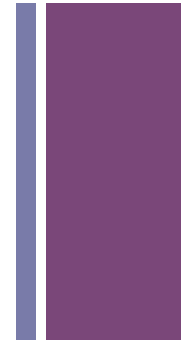
- Guidelines on International Islamic Bank
- Guidelines on Establishment of International Takaful Operator
- Guidelines on Application for Registration and Operation of Retakaful Operator.
- Guidelines on Establishment of International Currency Business Unit (Islamic, Commercial and Investment Banks)
- Guidelines on International Currency Business Unit (Takaful Operator) Guidelines on Tax Holiday for ICBUs, IIBs and ITOs
- Circular on Stamp Duty Exemption for MIFC Instruments
- Guidelines on Tax Neutrality for Islamic Banking & Takaful
- Circular on Issuance of Special Employment Pass for Islamic Finance Expatriates under the Malaysia International Islamic Financial Centre (MIFC) Initiative



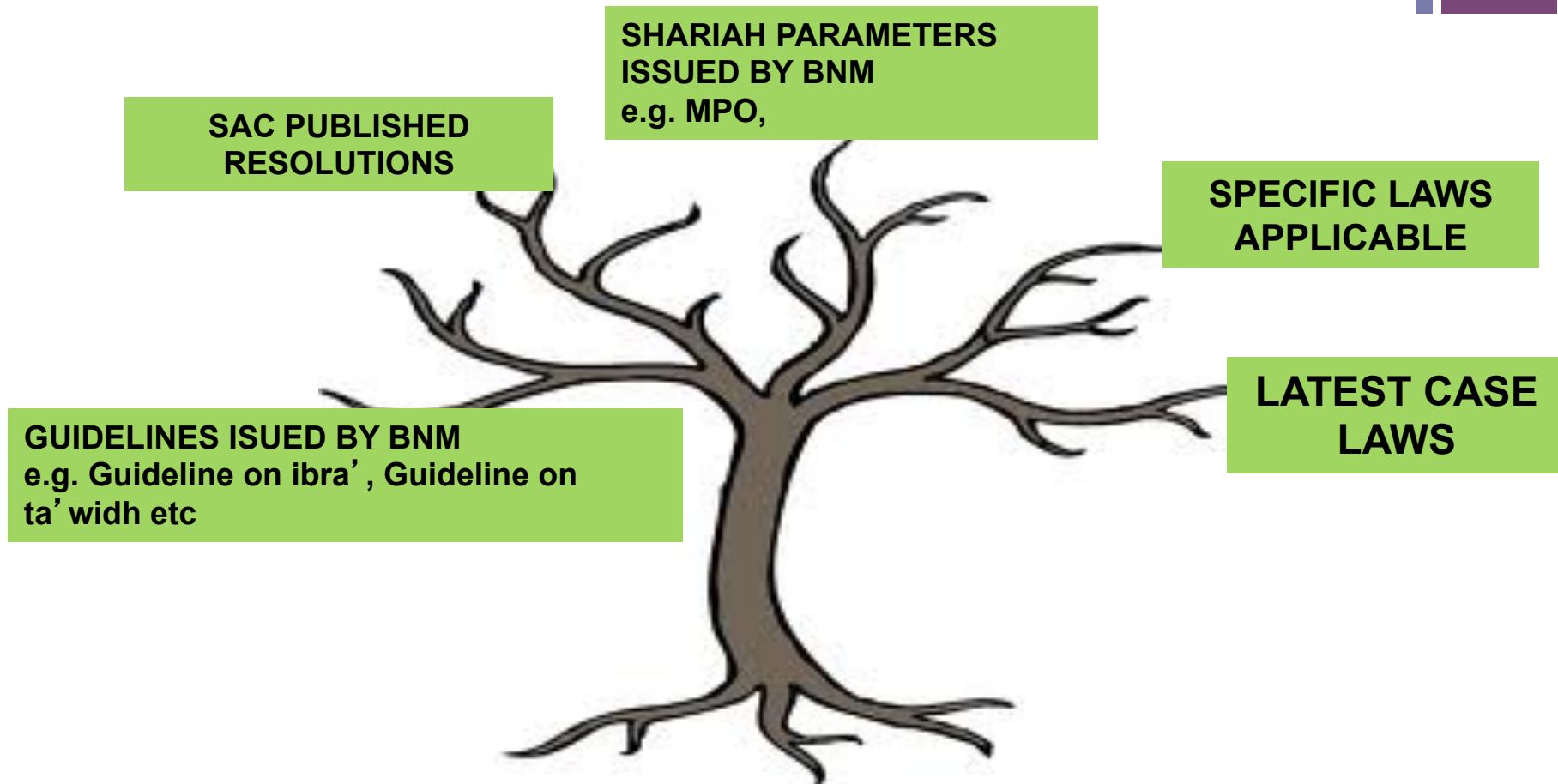
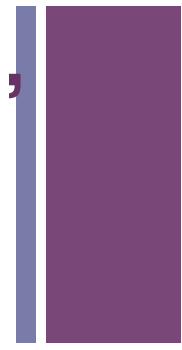


Islamic finance Litigation

- The implementation of muamalat bench shows a positive result on the increasing numbers of settled cases. From the statistic, it shows that more than 75% out of 656 cases has been settled by the court from year 2003 to 2005.
- **Cases Registered from 1.3.2003 – 1.12.2005=656**
- **Settled Cases from 1.3.2003-1.12.2005=497**
- **Balance of Cases up to 1.12.2005=388**
- **Percentage of Settled Cases from 1.3.2003 – 1.12.2005=75.7%**
- 2000 Cases 2010-2011



+ Case Law, Specific Law, Guideline, Resolution, Parameter





Sec. 56 of the CBA 2009

- **Section 56. Reference to Shariah Advisory Council for ruling from court or arbitrator.**
- (1) Where in any proceedings relating to Islamic financial business before any court or arbitrator **any question arises concerning a Shariah matter**, the court or the arbitrator, as the case may be, **shall—**
 - (a) take into consideration any **published rulings of the Shariah Advisory Council**; or
 - (b) refer such question to the **Shariah Advisory Council** for its ruling.
- (2) Any request for advice or a ruling of the Shariah Advisory Council under this Act or any other law shall be submitted to the secretariat.