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**ISSUES OF SHARIAH IN ISLAMIC LOAN IN MALAYSIA: A
REVIEW**

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Abstract

Loan is a financial method in facilitating publics in getting advance for capital. In Islam, loan has been permitted under certain rule. Among the rules are not involve with *riba* (usury), *maysir* (gambling), *gharar* (uncertainty) and *tadlis* (deception). Without those elements, the practice is compliance with the shariah regulation. To verify the procedure, there are the shariah committee of banks, which consist of intelligent in muamalat. However, in real situation, the implementation of Islamic loan in Malaysia have endured critics that the systems still commit the doubtful transaction. The shariah committee seems to be more inclined towards the profit of bank rather than the welfare of publics. For instance, publics suffer with vacant payment after the contractor default as well as they have to pay more with Islamic loan compared to conventional bank. Therefore, this study intends to investigate fiqh perspective in the loan transaction as well as the viability of Islamic banks in Malaysia. The study will be conducted in a qualitative way, by exploring on past research as well the current. The study found out that the key factor of the issues is the aim of Islamic banks in getting profit rather than to look after the welfare of the publics. They should give priority to knowledge, the welfare of publics as well as shariah objectives rather than the profit of the bank *per se*.

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Keywords: Islamic loan, shariah compliance, shariah committee, Islamic finance, Islamic banking.



1. Introduction

Islamic banking in Malaysia was started in 1983 and has been growing tremendously well hitherto, where it has attained 16 full-fledged of Islamic banking institutions now (Trakic & Tajuddin, 2016). The impressive growth portrays the magnitude of the Islamic banking market, which can safely assume to exceed USD 150 billion (Abdullah, 2017). In this study, focus is given into loan or financial aid that was practiced under the Islamic banking system. Loan is referring to a transaction whereby a property is lent or given to someone on condition of return, or where the loan is of money, a repayment. Through the scheme, the public has been facilitated under various contracts. The application of loan is vast, instead of borrowing money from a bank or single lending source, a company instead also borrows money from the public. Hence, the study will elaborate on the Islamic perspective of loan as well as the principle in facilitating public and nation.

1.1. Loan in the Islamic Perspective

The word "loan" in Islam exist in many words such as *qard* (قَرْض), '*ariya* (عَارِيَةٌ) and *taslif* (تَسْلِيف). *Qard* refers to a gratuitous contract in which a lender gives a certain homogeneous (*mithli*) property to a borrower on the condition that the latter is responsible to return a similar property to the lender immediately upon demand. '*Ariya* mean borrowing or lending, while *taslif* mean credit. '*Ariya* and *taslif* are more towards giving possession of a thing temporarily. However in term of money or cash, the principle of loan can be extracted from the word *qard al-hasan*, which mean giving loan with goodness or good debt. It is loan for welfare without usury and harm. The borrower is only required to repay the amount borrowed (Yussof, Ismail, Ahmad & Ahmad, 2017). It aims to foster love, brotherhood and unity and that's why the borrower can pay more if not specified in the contract as form of gratuitousness (Yussof et. al., 2017).

Instead terminology of loan, the approach of lending also known as debt or financing. Person who enter into loan is actually making a debt or apply for a debt. The party who provide the money is called the lender, while the party who ask for debt is known as the borrower. The act of loaning is permissible in Islamic law as a form of helping others. However, Islam have underlined several rules to be followed by Muslim in the loan activity to ensure no usury (*riba*), no oppression (*ad'afan mudha'afah*), no gambling (*maysir*), no deception (*tadlis*) as well as no uncertainty (*gharar*) in the contract (Q2:275-276; Q3:130; Q4:160-161). As a result, Islam strongly does not allow interest-based financing which involve elements of *riba*, but it allows debt financing based on equity and economic justice (Ibrahim & Kamarudin, 2014).

In general, there is no difference between loan and debt. Debt is a terminology that refer to loan with a set payment schedule over several months or years. However, there is a slightly different on the above terms, as loan applied from a bank or any other financial institution to fulfil one needs, whereas debt is a situation when an individual or a firm raises money for working capital or capital expenditures by selling bonds, bills or notes to investors. In return for lending the money, the individuals or institutions become creditors and responsible on the debt. In a meantime, an equity financing is a term that used to raise capital in the debt markets by issuing shares of stock in a public offering. Debt-based financing usually adopted by Islamic banks in the form of *murabahah*, *ijarah* and *istisna'* (Ibrahim & Kamarudin, 2014) that based on profit sharing mode. However, in Islamic home financing, the dominant products

used in sales and purchase transaction are *Bai' Bithamin Ajil* (deferred payment) and *musharakah mutanaqisah* (diminishing partnership) (Azli, Othman, Sahri, Aris, Arshad & Yaakob, 2011) that follow the interest debt-based financing (Othman, Majid & Rahman, 2015). The progress is regretted as the Islamic banks should adhere more on the safer products that agreed unanimously by Islamic jurists.

2. Problem Statement

In Malaysian, there are claims that some loaning products have involved in non-shariah activities, such as such as oppression (*ad'afan mudha'afah*), usury (*riba*), harm (*mafsadah/darar*) and uncertainty (*gharar*). These elements can be seen in the application of *bay' bithaman ajil* (BBA), *tawarruq* and *bay' inah* contracts (Azli et.al., 2011). The contract of BBA for example, has involved *gharar* where the loan does not guarantee the lender in getting a complete house (Ahmad & Rahman., 2012; Azli et al., 2011). *Gharar* also occurred in contract of *bay' al-inah* when a customer sells a house to bank under beneficial ownership in order to get money (loan), which is the ownership is not certain for the former (Asni & Sulong, 2018).

Meanwhile a *mafsadah/darar* occurred when lender has to pay for loan even though the house is incomplete. If a developer has gone bankrupt and fail to complete a house, the liabilities is incurred by the customer as lender and not by bank which only become as financier (Ahmad & Rahman., 2012; Azli et al., 2011). The longer the *mafsadah/darar* took place, will involve an implication of oppression (*ad'afan muda'afah*). The element of *mafsadah/darar* also found in BBA contract (Aris, Othman & Azli, 2013) in the event of early redemption or defiance in instalments, whereby the balance of financing is higher than conventional products. Under the concept, BBA customers need to pay four times of the original value (Aris et al., 2013). The high charge in the contracts seems against the Islamic spirit. As Islam urge to facilitate people under the concept of good debt (*qard hasan*). Ironically, customers are burdened with more liabilities compared to the conventional system (Ahmad & Rahman., 2012; Asni & Sulong, 2018).

Another issue is involving usury (*riba*) contract especially when the products of Islamic bank also linked to the concept time value of money. The concept has an element of usury under the sale and purchase contract (Khir, 2013). Time value of money is the principle adopted to rationalize the obligations of usury practices in financial activities based on the capitalist system (Asni & Sulong, 2018). In this case, the element of usury is an added value of the capital that being loaned so that the value of the payment will be equal to the current value of the capital loaned (Shahar, Jamlus & Shahar, 2014). The application was practiced through *bai' al-hilah* in order to enable an increase of payment due to inability to pay upon the term of agreement reached (Puaad, Ahmad & Yusuf, 2017). Asni & Sulong (2018) stated that an added value which exceeding the original price in sales and purchase postponement during the *aqad* is permissible, but not after the *aqad*. No additional charge should be incurred for deferment. If time value of money is acceptable in sales and purchase, then there is no difference with usury. Therefore, Shahwan, Mohammad and Rahman (2013) has likened the concept of BBA with *riba al-nasiah* where an additional charge incurred for deferment. Likewise according to Puaad et al. (2017), the application lead to the recognition of usury where the price of goods through BBA *aqad* is higher than by cash. The element of time value of money has been widely practised in the products of BBA, *bay' istisna'*, *bay' inah* and *tawarruq*. The price has been mark-up to gain profit through *murabahah* financing and this goal

is in line with the loan contract adopted by conventional banks. Ironically, the value offered by conventional banks is far more competitive rather than in the Islamic banks (Asni & Sulong, 2018).

The implication of usury also occurred in *al-tawarruq* contract. It is as claimed by Ibn Taimiyyah who quotes from Umar bin Abd al-Aziz as saying that the concept of *al-tawarruq* contract is similar to usury transaction. Likewise, it was supported by Ibn al-Qayyim and al-Syaibani (Qayyim, 2002). Based on Ahmad, Shihama, Tarmizi, Jibril, Djama and Muneza (2017) findings, a majority of middle eastern Islamic scholars reject contracts containing the element of *bai' al-'inah* because it is a trick to usury as contained in *al-tawarruq* contract. Majma' al-Fiqh al-Islami, in its 17th conference have decided that the contract of *al-tawarruq al-munazzam/al-masrafi/al-muassasi* is prohibited (Tijani, 2013). Besides that, Rahman & Manan (2014) states that most bank institutions implement *al-tawarruq* without following the terms and standards set by AAOIFI. This finding is also coincides with Kasmon and Noordin (2015) study.

3. Research Questions

Research questions is an inquiry that leads towards obtaining a solution through systematic and verifiable steps by the researcher (Schreier, 2012). The study has a few research question to be answered, as follow:

- a) What is the position of loan in Islam?
- b) What is the elements that prohibited by Islam in every transaction?
- c) What kind of loan or debt-based financing that offered by banks or institutions?
- d) What is the function of the Shariah Advisory Council towards banks activities?
- e) What is the steps to safeguard the shariah compliance products in the market?

4. Purpose of the Study

The purpose of the study is a statement of "why" the study is being conducted, or the goal of the study. The goal of a study might be to identify or describe a concept or to explain or predict a situation or solution to a situation that indicates the type of study to be conducted (Creswell, 2014). In this research, the purpose of the study is to achieve an underline goal as below:

- a) To scrutinize the position of loan in Islam
- b) To underline elements that prohibited by Islam in loaning activities
- c) To list recent contract in the market that involve Islamic loan and debt-based financing
- d) To examine function of the Shariah Advisory Council of banks and their responsibilities
- e) To suggest steps that should be followed by financial institutions to safeguard publics from encircling in the prohibited loan contract

5. Research Methods

Research method in science social studies is essential to guarantee the success, validity and reliability. The research methods in the study is using qualitative perspective.

5.1. Methods of Collecting Data

Data were collect through library research and information will be supported with expert interviews. Through library research, it has a considerable amount of literature/collections on Islam and its related disciplines are enough to provide the review that intended in the study. Pertaining to literature of Islamic law, Muslims have developed, saved, transmitted and preserved knowledge for thousands of years, even in times when it was very difficult to produce multiple volumes (Idrees, 2011). In getting the material, the information was narrowed down into four theme that is, author, title, subjects and keywords. Instead of books, the data also have been picked from scholarly journal, newspaper and magazines.

The method of interview is also essential in qualitative study, as noted by Alshenqeeti (2014), qualitative data are 'most often' collected by researchers through interviews and questionnaires. However, interviews (compared to questionnaires) are more powerful in eliciting narrative data that allows researchers to investigate people's views in greater depth (Edwards & Holland, 2013). In a similar vein, Alshenqeeti (2014) added that interviewing is a valuable method for exploring the construction and negotiation of meanings in a natural setting.

5.2.Methods of Analysing Data

Mckinney (2013) describe data analysis as the process of bringing order, structure and meaning to the mass of collected data. In short, as Ngulube (2015) so aptly points out, qualitative data analysis is a process of transformation of collected qualitative data, done by means of analytic procedures, into a clear, understandable, insightful, trustworthy and even original analysis. In the analysis tool, the analysis and interpretation of data represent the application of deductive and inductive logic to the research. Inductive approach begins with specific observations which resulted generalization in the conclusions. However the deductive approach constitutes developing of an assumption based on the existing theories (Zalaghi & Khazaie, 2016). In this study, an analysis also using a content analysis that widely used in qualitative research technique.

Content analysis is a research tool used to determine the presence of certain words or concepts within texts or sets of texts. It represents a systematic reaction to the research question through what to analyse and what to create (Elo, Kaarianinen, Kanste, Polkki, Utriainen & Kyngas, 2014). Researchers quantify and analyse the presence, meanings and relationships of such words and concepts, then make inferences about the messages within the texts, the writer(s), the audience, and even the culture and time of which these are a part. Texts can be defined broadly as books, book chapters, journals, interviews, discussions, newspapers, articles, documents, and etcetera. Content analysis have been done by scrutinizing information about loan in Islam and the practise in Malaysia nowadays. Every product have been touch the researcher before and input has been gathered into positive and negative remark to be analysed deeply.

Such analysis can be regarded as valid if it adequately represents the concepts, which captures what was intended (Schreier, 2012). Thus, in reporting cases as well as one study, results are described by selected approach either deductive or inductive. In add, inductive is moving from the specific to the general, while deductive begins with the general and ends with the specific; arguments based on experience or observation are best expressed inductively, while arguments based on laws, rules, or other widely accepted principles are best expressed deductively. Schreier (2012) say that the deductive

researcher “works from the ‘top down’, from a theory to hypotheses to data to add to or contradict the theory”. In contrast, they define the inductive researcher as someone who works from the “bottom-up, using the participants’ views to build broader themes and generate a theory interconnecting the themes”.

Based on the discussion above, the validity, reliability and trustworthy of the analysis is an ultimate goal in every study. Therefore, at the end of analysis, the researcher also compares the data with interview remark to ensure the information that was gathered is in line with the real practice outside.

6. Findings

Islam is a religion that move in parallel with the needs of human being. Muslim are urged to assist among them during living. In Muslim country, Islamic bank which has been established within the ambit of Shariah should expected to be guided by an Islamic economic objectives, in assisting people and to ensure that wealth is fairly circulated among as many hands as possible without causing any harm (Ghazali, 2014). As the Prophet have said, "The individual who fulfils the need of his Muslim brother, Allah will fulfil his need. That individual who removes a difficulty from his Muslim brother, Allah will remove his difficulty on the Day of Judgement" (Dawud, 2008). Therefore, in general, loan is an act of permissible in Islam. It was shaped to help another Muslim from difficulty, without adding further difficulty. Therefore, Islam forbid an act of usury in practicing loan.

Muslim jurist unanimously on opinion that the practice of usury is totally forbidden in Islam. There is neither flexibility nor leeway in the law. Hence, any elements of usury that are hidden under any contract, by such a delay, mark up over postponement on the time value as well as in fitting the dividend in advance, have a remark of practicing usury. The goal of prohibiting the usury is that, it bring *mafsadah* and *darar* to customer and publics. The lavish institutions will keep on oppress public through their service.

Instead juristic law in the books (*kutub fiqh*), Malaysia also promulgated a written law to facilitate the Islamic banking rule. The earliest legal foundation for the Islamic banking industry in Malaysia was Islamic Banking Act 1983 (IBA) which authorised the central bank or Bank Negara Malaysia (BNM) to supervise and regulate Islamic banks, similar to the existing licensed banks (Abdullah, 2017; Hussain, Hassan & Hasan, 2015). Six years later, Banking and Financial Institutions Act 1989 (BAFIA) was then introduced where Section 124(7) of the law allows conventional banks to open Islamic counter to offer Islamic banking products. Through the section, an establishment of the Shariah Committee was introduced in order to advise them any matter related to Islamic banking business or Islamic financial business (Abdullah, 2017; Hussain et al., 2015). In a meantime, pursuant to Section 16B of the Central Banks Act 1958 (CBA) (amendment 2003) also underlined the role of the Shariah Advisory Council of BNM in supervising the operations of every Islamic banking institution in the country. The Section 16B (1) have provided that the BNM may establish a Syariah Advisory Council, which shall be the authority for the ascertainment of Islamic law for the purposes of Islamic banking business, takaful business, Islamic financial business, Islamic development financial business, or any other business which is based on Syariah principles and is supervised and regulated by the Bank. To give a value added for the services, the Central Bank also promulgated the Islamic Financial Services Act (IFSA) 2013 in order to reinforce the Bank’s mandate to safeguard financial stability and strengthen the foundations for a regulatory and

supervisory framework that is effective, transparent and that can contribute towards an efficient and resilient financial system to face the future stresses (Abdullah, 2017; Hussain et al., 2015).

In sum, the above theoretical and statutory provisions have an ability to ensure the application of Islamic financial banking are comply with the shariah rule. It also revealed that Malaysia have sufficient regulation in guaranteeing the public's welfare from being manipulation by the said institutions or individuals.

6.1. The First Player of World-wide

Malaysia is now a leading country that offered an Islamic banking and financial facilitation. According to Bank Negara in 2016, Malaysia have 27 institutions which offering more than 100 financial products. In addition, Islamic banking assets in Malaysia now stand at more than a quarter, or 27 per cent, of the total banking system. As a result, Malaysia has ranked at the second place in global leaders of the Islamic finance industry after Saudi Arabia, out of nine Muslim majority countries according to a research conducted by Kuwait Finance House Research (Abdullah, 2017; Hussain et al., 2015).

Malaysia have specific rules and laws in ensuring a systematic structure and operation of shariah institutions in the country. The Shariah Governance Framework of 2011 for Islamic Financial Institutions (IFIs) is very important rule that practice in Malaysia. It provides a sound Shariah decision-making as well as offer an independence of the board of directors in issuing shariah resolution, in which later on will provide continuous public confidence on the industry. Furthermore, the Islamic Financial Services Act of 2013 was enacted to reinforce the BNM's mandate to safeguard financial stability as well as to statutorily monitor and enforce Shariah compliance. The more centralised of approach in shariah governance framework as implemented in Malaysia is no doubt makes the development of Islamic financial system is more systematic and transparent. However, Malaysia only applied 0.5 per cent of its Islamic banks that is based on profit and loss sharing principles (Abdullah, 2017; Yussof, 2013).

6.2. Islamic Loan or Debt-Based Financing

The first and foremost key point in Islamic loan or debt-based financing is plain from any usury, uncertainty, gambling and deception. In Malaysia, debt-based financing is widely used since 1983 by using different kinds of Islamic business contracts (Jusoh & Khalid, 2013). According to Aljifri (2013), the method of debt-based financing or Islamic loan can be seen through many contracts: (1) participatory profit loss-sharing modes like *mudarabah* and *musharakah*; (2) sales-based modes like *murabahah* (cost plus sale), *bay' bithaman 'ajil* (deferred payment sale), *bay' al-salam* (forward sale) and *bay' al-istisna'* (commission to manufacture sale); (3) lease-based modes like *ijarah*; (4) voluntary charitable contract (*tabarru'*), such as, pawning contract (*ar-rahn*) and benevolence loan (*qard al-hassan*) and (5) hybrid-modes like *musharakahmutanaqisah* (diminishing partnership), *ijarahthumma al-bay'* (hire purchase) etc.

Notwithstanding the variety of names, the Islamic bank in Malaysia has been claim of using many controversial debt-based financing. It is obvious that Malaysian banks have tendency to adopt any opinion that comfort to their business plan. Therefore, the banks seem to apply more controversial model than the safer contracts in order to gain profit. Even though such contracts claim to be as a back door to *riba* (usury). In addition, the bank prefers to choose an unfair risk avoidance strategy which pass

mafsadah/darar to customer (Asni & Sulong, 2018). For instance, the interest of home buyers is neglected in the case of contractor default and show lack of morality from the banking business. To add, some of banking institution trying to hinder upcoming risk by imposing a very high charge to overcome inherent problems of borrower (Aljifri, 2013). Even though every bank tries to evade high non-performing loan, the burden should not put on customer's shoulder alone (Shahar et. al., 2014) albeit it will increase cost for banks (Othman et al., 2015). Otherwise, it looks like the Islamic banks is always for commercial than its welfare commitments (Shahwan et al., 2013).

The Islamic banking should restrict their products to those that are all shariah compliance and released themselves from debatable contracts such as *bay al-dayn*, *bay al-innah*, *tawarruq* and *bay al-urbun*. They should go for the safe and comfortable products such as *mudaraba* and *musharaka* (equity-based products), *murabaha*, *salam* and *istisna'* (debt-based products). Unfortunately, the Feb 2014 statistic show that the *musharakah* and *mudharabah* contracts only contributed less than 6% over total aggregate financing of Islamic banking system in Malaysia (Abdullah, 2017). Therefore, the spirit of practicing Islamic loan in Malaysia need to be strengthen and added good factor. As Asni and Sulong (2018) said, the problem of Islamic world today is not about lack of fund, but lack of awareness to help Muslim as religious commitments. Several studies highlighted the issues that many Islamic banking industry today (Beck, Demirguc-Kunt & Merrouche, 2012) rely on interest rate as a benchmark in deciding the profit rate. They forgot to promote Islamic values and norms towards humanity without undermining commercial viability (Abdullah, 2017).

Islamic banking in Malaysia needs to improve more in term of equity and profit loss sharing ventures. Islamic scholars unanimously agreed that the principle can play critical role in alleviating the living standard of society (Abdullah, 2017). In this case, IFIs should play its paramount role, sustain the trust of customers as social capital and back to the objective in facilitating them (Asni & Sulong, 2018).

6.3. The Shariah Advisory Council

One of the distinctive model of Islamic banking is having the shariah advisory council or also known as Shariah board (SB) to consult on religious matter. The members are an expert of both Islamic Jurisprudence and finance (Wardhany & Arshad, 2012). Every Islamic banking/financial institutions is required to establish the board as to ensure shariah compliance instead of shariah advisory on a central level (Central Banks Act 1958, 2003). Their task is to act as an advisory at the regulator's level, centralized fatwa, issue guidelines on the governance of shariah committee for the Islamic financial institution (IFI), conduct shariah compliance review and centralized appointment of shariah committees of IFI. In sum, Islamic banking is about religious identity and duty to expose an Islamic value in the whole operation and outlook such as to social justice (Wahab, Aziz, Abuzraida, Sanousi, Hinai & Ibrahim, 2014).

Some statute has been provided to enforce the governance the SB. In 2011 BNM has introduced the guidelines for Shariah Governance Framework for Islamic Financial Institutions (IFIs), in order to develop sound as well as efficient Shariah governance. The ultimate goal of this framework is to ensure continuous public confidence on the strength and credibility of Islamic finance industry (Abdullah, 2017). Likewise, the Islamic Financial Services Act of 2013 was enacted to reinforce the BNM's mandate to

safeguard financial stability as well as to statutorily monitor and enforce Shariah compliance. Besides the local guidelines and legislations, every Islamic banking institutions in Malaysia acknowledged the Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI) standard (Abdullah, 2017). The steps is to enhance the credibility of IFIs.

However, there is a few aspects that need to be improved, such as on appointment of the shariah committee that comes from the Board of Directors with the approval of shareholders at general meeting (Wardhany & Arshad, 2012). In order to sound independent, shariah board should be appointed by shareholders during general meeting with recommendation of BODs and the shariah board is allowed to attend the BOD's meetings to discuss the religious aspects of their decision (Hussain et. al., 2015). On this practiced, the resolution of the SB will look more self-determining and impartial.

7. Conclusion

On the whole, Islamic banking and financial institutions should concerned more on achieving *maqasid shariah* in their loaning products. It is a system that aims at making a positive contribution to the fulfilment of the socio-economic objectives of Islamic society. Therefore, Islamic banks have to stay in the shariah line as underlined by Quran and hadith. The modus operandi of the Islamic banks should focus on the original goals and stand still within the ambit of Shariah. By so doing, it epitomises the objectives of Shariah in promoting economic and social justice. Hence, even though Malaysia facing a very dynamic growth in the financing facilities, the country should take into account his involvement in many debatable muamalat business contracts. It is suggested that the Islamic banks/financial institutions show focus more on profit and loss sharing based financing, such as *mudarabah* and *musyarakah*. The facilities of *qard al-hasan* (benevolence loan) should be expanded especially by IFIs as part of their contributions to the societies. The Shariah Committee Council should work independently by taking into account the welfare of both parties on equally, either bank or publics. A bank be eligible to gain profit through their service but in reasonable rate. Similarly, publics or customer of a bank should be responsible for the service given and should pay for the charge in a reasonable rate. In short, the burden of both parties is in light without *mafsadah* or excessive oppression.

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