



**ISLAMIC BANKING; THE CHALLENGES AND REALITY IN  
MALAYSIA : A CASE STUDY ON BANK ISLAM MALAYSIA  
BERHAD**

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*In the Name of Allah, Most Gracious, Most Merciful.*

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## ABSTRAK

Perkara utama yang dibincangkan di dalam projek akademik ini adalah berkenaan dengan perbankan Islam di Malaysia. Kajian ini dikhususkan kepada Bank Islam Malaysia Berhad (BIMB) sebagai bank Islam pertama di Malaysia. Kajian ini bertujuan untuk mengenal pasti cabaran-cabaran yang perlu dihadapi oleh BIMB dan realitinya di Malaysia. Method pengumpulan data telah diguna pakai bagi memperolehi data untuk kajian ini. Kaedah ini melibatkan kajian perpustakaan dan kajian dokumentasi. Hasil daripada kajian yang dijalankan, terdapat tiga cabaran yang perlu dihadapi oleh BIMB iaitu dari segi ekonomi, perundangan dan teknologi. Kajian ini juga menunjukkan bahawa perbankan Islam khususnya BIMB mampu mendominasi sistem kewangan di Malaysia.

## ABSTRACT

The main issue discussed in this academic project paper is regarding to the Islamic banking especially Bank Islam Malaysia Berhad (BIMB) which is the first Islamic banking in Malaysia. The study sought to determine the challenges faced by BIMB and its reality in Malaysia. The data gathering method has been used in order to get the data for this academic project. This method comprises of the library and documentary research. From the study, there are three possible challenges which BIMB has to face. There are from the economy, law and technology point of view. Finally, this study also shows that Islamic banking especially BIMB can dominate the financial system in Malaysia.

## ملخص البحث

هذا البحث يعتبر دراسة عن المصارف الإسلامية في ماليزيا خصصت الدراسة بأول البنوك الإسلامية في ماليزيا وهو (( البنك الإسلامي بماليزيا )) ( BIMB ). وأما الهدف الأساسي فهو معرفة حقيقة البنك الإسلامي ومستقبله وتحدياته. المنهج المتبع في هذا البحث هو جمع المعلومات من دراسة مكتبية ودراسة البيانات المطبوعة. واستنتج البحث ثلاث تحديات التي واجهها البنك. وهي التحديات في مجال الاقتصاد والقانون والتكنولوجي. ووصل البحث إلى إمكانية البنك الإسلامي في قيادة الشؤون المالية.

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## TRANSLITERATION

### 1. The Alphabet

<u>Arabic Alphabets</u>	<u>Latin Alphabets</u>	<u>Examples</u>	<u>Transliteration</u>
ء	‘	فأر	fa’r
ب	b	برد	burd
ت	t	تلّ	tall
ث	th	ثوب	thawb
ج	j	جدار	jidār
ح	ḥ	حليب	ḥalīb
خ	kh	خادم	khādim
د	d	ديك	dīk
ذ	dh	ذهب	dhahab
ر	r	رفيق	rafīq
ز	z	زميل	zamīl
س	s	سلام	salām
ش	sh	شعب	sha <sup>c</sup> b
ص	ṣ	صخر	ṣakhr
ض	ḍ	ضيق	ḍayq
ط	ṭ	طازج	ṭāzij
ظ	ẓ	ظالم	ẓālim
ع	‘	عقل	‘aql
غ	gh	غلام	ghulām
ف	f	فيل	fīl
ق	q	قلب	qalb

<u>Arabic Alphabets</u>	<u>Latin Alphabets</u>	<u>Examples</u>	<u>Transliteration</u>
ك	k	كلام	kalām
ل	l	لبّ	lubb
م	m	مال	māl
ن	n	نجم	najm
هـ	h	هول	hawl
و	w	ورق	waraq
ي	y	يم	yamm

## 2. The Short Vowel

<u>Arabic Alphabet</u>	<u>Latin Alphabet</u>	<u>Examples</u>	<u>Transliteration</u>
_____	a	كَتَبَ	kataba
_____	i	عَلِمَ	‘lima
_____	u	غُلِبَ	ghuliba

## 3. The Long Vowel

<u>Arabic Alphabets</u>	<u>Latin Alphabets</u>	<u>Examples</u>	<u>Transliteration</u>
ا ، ي	ā	عالم ، فتى	‘ālim , fatā
ي	ī	عليم ، داعي	‘alīm ., dāī
و	ū	علوم ، أدعو	‘ulūm , Ad‘ū

#### 4. Diphthong

<u>Arabic Alphabets</u>	<u>Latin Alphabets</u>	<u>Examples</u>	<u>Transliteration</u>
و	aw	نوم	nawm
ي	ay	ليل	layl
يَّ	iyy	شافعي	shafi <sup>c</sup> iyy (at last)
وَّ	uww	علوَّ	<sup>c</sup> ulluw (at last)

#### 5. Exception

5.5.1 The Arabic alphabet 'ء' (hamzah) at the beginning of a word is translated to 'a' not to ' ' .

Example: أكبر                      Transliteration: akbar (not 'akbar).

5.5.2 The Arabic alphabet 'ة' (ta' matbutah) in the word without ال (al) which is joined to another word that starts with ال (al) will transliterate to ' t ' .

Example: مكتبة الإمام                      Transliteration: maktabat al-imām

If there is (al) in the word or in the single word or in the last word, ta' marbutah will transliterate to ' h ' .

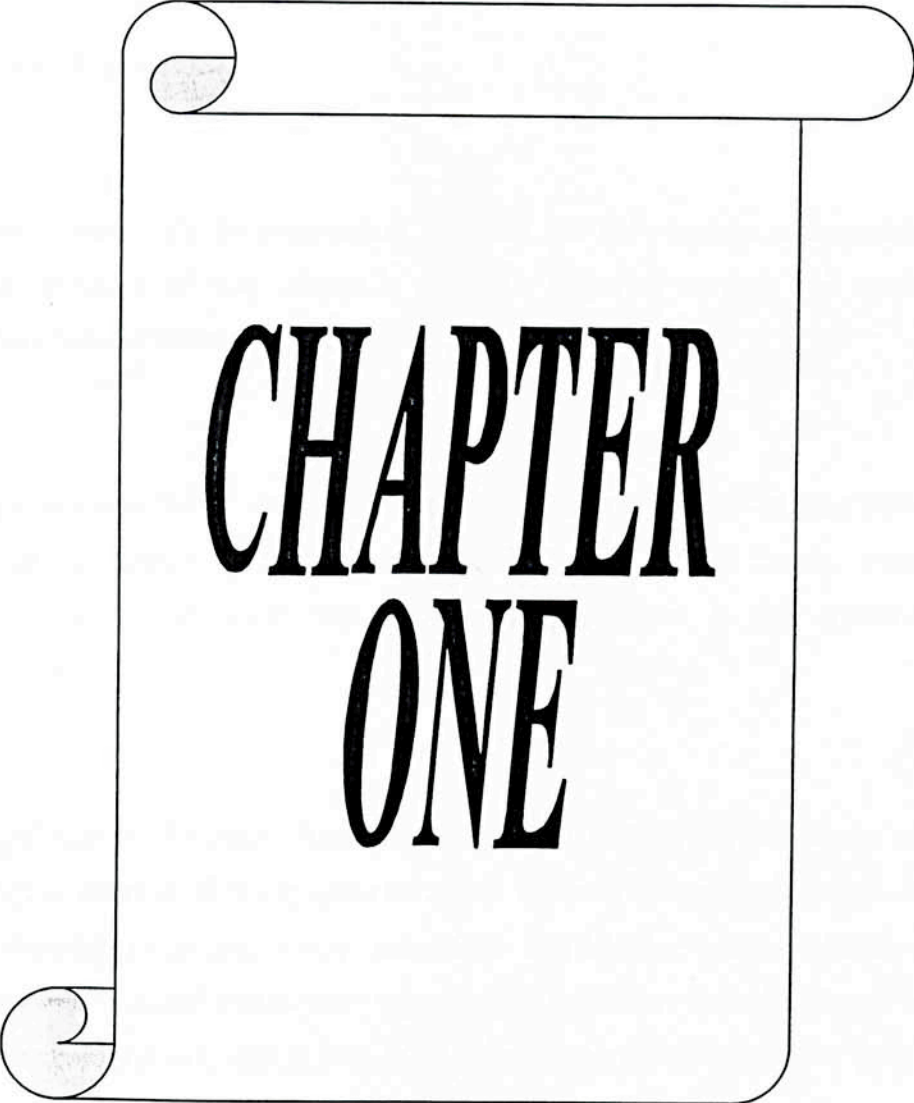
Example: المكتبة الأهلية                      Transliteration: al-maktabah al-ahliyyah

قلعة    qal<sup>c</sup>ah

دار وهبة    dār wahbah

## ABBREVIATION

ATM	Automated Teller Machine
BAFIA	Bank and Financial Institutions Act
BBA	<i>Bay' Bithaman Ajil</i>
BIMB	Bank Islam Malaysia Berhad
BNM	Bank Negara Malaysia
BSKL	Bursa Saham Kuala Lumpur
CBM	Central Bank Malaysia
Dr.	Doctor
Ed.	edition
ed.	editor
IBA	Islamic Banking Act
IBD	Islamic Banking Division
IBI	Islamic Banking Institution
IBU	Islamic Banking Unit
IFBS	Interest-Free Banking Scheme
IKIM	Institute of Islamic Understanding Malaysia
KLSE	Kuala Lumpur Stock Exchange
n.a.	no author
n.d.	no date
No.	Number
NSAC	National <i>Shari'ah</i> Advisory Council
p	page
p.b.u.h	peace be upon him
pp.	pages
s.w.t	subhānahu wa ta'ālā
SPI	Skim Perbankan Islam
SPTF	Skim Perbankan Tanpa Faedah
trans.	translated
Vol.	Volume



**CHAPTER  
ONE**

## CHAPTER ONE

### INTRODUCTION

#### 1.1 Background of research.

Nowadays, the world is progressing towards the information communication technology era. Because of that, Malaysia must be prepared to face the economy globalization based on the Islamic principles.

Malaysia has established the Islamic economic systems such as Islamic banking, insurance and capital market. However, these Islamic institutions are facing with the challenges from the conventional economics paradigm either in the national or international stages.

The significance of Islamic banking has become a progressive upward trend. Islamic banking has spurred efforts by other non-bank financial intermediaries such as the development financial institution, saving institutions and housing credit institutions to introduce Islamic schemes and instruments to meet their customers demands. In addition, the capital market has seen the rapid growth of Islamic debt securities and equity markets.

## 1.2 Aim of research.

This academic project report aims to study the challenges and realities that are faced by the Islamic banking in Malaysia especially Bank Islam Malaysia Berhad (hereinafter known as BIMB). The writer foresees three aspects of challenges in Islamic banking such as the transactional law, economic and technology. Besides that, this study also aims to show the efficiency of Islamic banking in the Malaysian financial system that contributes significantly to the effectiveness and efficiency of the Malaysian financial sector while meeting the economic needs of the nation (*ummah*).

## 1.3 Objective of research.

The objectives of undertaking this study are as follows :

- 1.3.1 To identify the challenges which are faced by Bank Islam Malaysia Berhad (BIMB) from the legal perspective, based on current economy development.
- 1.3.2 To know the *shari'ah* aspects towards the accomplishment of the finance system.
- 1.3.3 To study the efforts taken by BIMB in facing the global challenges.
- 1.3.4 To clarify that BIMB is producing the Islamic banking finance.

## 1.4 Scope of research.

The writer had selected several issues which are related to Islamic banking in Malaysia as the main study of this academic project paper. The study employs the application and the usage of this system besides conventional banking. However, the scope of the academic project paper is only based on the Bank Islam Malaysia Berhad because it is the first Islamic bank established in Malaysia.

### 1.5 Research methodology.

In employing this academic project, the writer has employed secondary data available in the library as well as from the Internet. The secondary data are taken from dictionaries, legal acts news papers, paper works, magazines, journals and reference books. This method is used to facilitate the collection of data because most of the Islamic banking studies are already facts.

Meanwhile, the library research method is a research in collecting data by using the information in the library. The writer has employed this method to gain more information about Islamic banking especially in Malaysia. Besides the Library of Islamic University College of Malaysia, the writer also did research in several other libraries like the Library of Institute of Islamic Understanding Malaysia (IKIM), Islamic Center Library, Za'aba Library of Malaya University (UM) and Tun Sri Lanang Library of National University (UKM).

### 1.6 Literature review.

Al-Harran, (1995) in his book entitled "The Islamic Stock Exchange" stated that Islam as always of life can bring an alternative and create a healthy environment to the stock exchange. The most fundamental teaching that Islam advocates in any financial transactions is "you should not do harm to others while others should not do harm to you."

The world's financial system has to look for structural changes. A possible alternative is a change towards Islamic finance based on justice and fairness. Although

this study agrees with the statement above but unlike BIMB, there are other banks which produced Islamic banking products but are not really Islamic banks.

Nor Hayati Ahmad and Sudin Haron, (1998) stated, while some independent variables such as capital ratio, liquidity, interest rate and money supply have a similar effect on Islamic banks, there are differences which could be used as evidence that Islamic banks are, in fact, distinct from conventional bank.

In this study, the writer realized that the practice of Islamic bank in providing the interest-free banking scheme encourage in the financial system are also practised by many other conventional banks. An Islamic banking system also requires a large number of dynamic and pro-active players, a wide range of products and innovative instruments, and a vibrant Islamic money market.

Wong Choo Sum, (1995) stated the performance are evaluation of BIMB from 1983-1993 in terms of growth of customers' deposit, total assets, liquidity requirements, investments and its management. He found that the progress made was encouraging and the experience was somewhat similar to those of Islamic banks. The difference is on the liquidity requirement whereby the Islamic bank observes a two-tier liquid asset ratio. The first liquid asset ratio is 10 percent of its eligible liabilities excluding investment account liabilities, and the second liquid asset ratio is set at 5 percent of its investment account liabilities.

Ismail, (2002) in his article entitled "Future Legal trend of Islamic Banking & Finance/Legal Reform" stated it is suggested that all banks, both Islamic and conventional, carrying-on Islamic banking system should jointly draw up an Islamic Banking Code that would set out the rules for the conduct of Islamic banking in this

country.

In Malaysia, Islamic banks are governed by Islamic financial transaction but it is submitted that the existing laws are not sufficient to supplement the current development. It is submitted that the current Islamic Banking Act 1983 should depart from the shadow of Bank Act (BAFIA) and capable to stand by itself.

Radiah, (1995) in her article entitled “bank Islam Malaysia : market Implications” stated it is envisaged that by the introduction of the ATMs depositors should close these accounts and bank exclusively with BIMB. The writer sees that BIMB’s peer group has started offering this service using the shared ATM networks. Besides that, BIMB is also in the internet banking so that its development is not less than the other banks.

The current academic project will explore on the possible challenges foreseen by the writer. Hence, the writer has limited its discussion to Bank Islam Malaysia Berhad only because it is the first Islamic bank established in Malaysia.



**CHAPTER  
TWO**

## CHAPTER TWO

### **THE HISTORICAL DEVELOPMENT OF ISLAMIC BANKING IN MALAYSIA**

#### **2.1 Introduction.**

The Islamic banking system in Malaysia is considered to be more progressive compared to the systems in other Muslims countries. Its history began when Bank Islam Malaysia Berhad (hereinafter known as BIMB) was established in 1983 and now this system is complemented by the Islamic financial market, Islamic window and the Islamic stock market. The Malaysian Islamic banking system served as a model for Islamic banks in Indonesia and Brunei.<sup>1</sup>

Meanwhile, BIMB is a commercial organization based on the Islamic principles for Muslims as well as non-Muslims. This is to fulfill the Muslims need as there was no Islamic bank before BIMB. Rationally, the main reason is that other commercial banks in this country used the riba' system which is clearly prohibited by Islam.<sup>2</sup>

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<sup>1</sup> Abdul Halim bin Ismail. 1999. "Modern Islamic Financial System with Particular Reference to Islamic Capital Market". *Islamic Financial : Services and Products*. Abdul Monir Yaacob & Hamiza Ibrahim (ed.). Kuala Lumpur : Institute of Islamic Understanding Malaysia (IKIM). p. 25.

<sup>2</sup> Othman Yong. 1993. *Pasaran & Institusi Kewangan di Malaysia : Teori & Amalan*. Kuala Lumpur: Dewan Bahasa & Pustaka. p. 300.

### 2.1.1 The literal meaning of Islamic banking.

According to the Oxford Advanced Learner's Dictionary, 'Islamic' comes from the word 'Islam', which means the Muslim religion, based on the belief of God and revealed through the Prophet Muhammad (p.b.u.h) while 'banking' means the business activity of banks.<sup>3</sup> The terms 'Islamic Banking' can be defined as "all business activities such as transactions, investments and other activities which are based on the Islamic principles of law".

Besides that, Timur Kuran (1992) stated that an Islamic economic system would be free on the one hand of the exploitation and severe inequalities that characteristic capitalism, and on the other of the class struggles and intolerable restrictions that are the hallmarks of socialism.<sup>4</sup> Therefore, Islamic strategy in most structured economic system is based on three factors; clearly specific objective, completed moral behavior, specific law and orders that are stated by the government.<sup>5</sup>

### 2.1.2 The definition of "Islamic Banking" from the legal perspective.

Section 2 of the Islamic Banking Act 1983 (hereinafter, known as IBA) provides, *inter alia*, the following definitions for 'Islamic Banking' :

“ 'Islamic bank' means any company which carries on Islamic banking

<sup>3</sup> Hornby, AS. 1999. *Oxford Advanced Learner's Dictionary of Current English*. 5th Ed. Great Clarendon Street : Oxford University Press. pp. 81 & 633.

<sup>4</sup> Timur Kuran. 1992. " Economic Justice in Contemporary Islamic Thought". *Islamic Economic Alternatives : Critical Perspectives & New Directions*. Jomo K.S (ed.). London : Macmillan Academic & Professional Ltd. p. 49.

<sup>5</sup> Muhammad Nejatullah Siddiqi. 1989. *Pemikiran Ekonomi Islam : Suatu Tinjauan Penulisan Semasa*. Mohd. Amin Abdullah (ed). Kuala Lumpur : Dewan Bahasa & Pustaka. p. 13.

business and holds a valid license and all the offices and branches in Malaysia of such bank shall be deemed to be one bank ; and ‘Islamic banking business’ means banking business whose aims and operations do not involve any element which is not approved by the Religion of Islam. ”<sup>6</sup>

Section 3 (1) of IBA stipulates that Islamic banking business shall not be operated except by a company which is in possession of a written license from the Minister of Finance who give the authority.

The definition of ‘Islamic banking business’ provided in IBA is wide, compared to the definition of ‘banking business’ given under section 2 (1) of the Banking and Financial Institutions Act 1989 (hereinafter, known as BAFIA) which give the following definition for ‘banking business’ :-

“Banking business’ means ;

(a) the business of :

- i. receiving deposits on current accounts, deposit, savings accounts or other similar accounts;
- ii. paying or collecting cheques drawn by or paid in by customers ; and
- iii. provision of finance ;

(b) such other business as the Bank [Bank Negara Malaysia], with the approval of the Minister, may prescribe ;<sup>7</sup>

It is appreciated that the Malaysian Parliament intentionally define the terms ‘Islamic banking business’ in general. This is because it is submitted that a very wide

<sup>6</sup> Malaysia. 1999. *Islamic Banking Act 1983* . (Act 276).

<sup>7</sup> Malaysia. 2000. *Banking and Financial Institutions Act 1989* . (Act 372), Regulations & Selected Orders.

definition would provide flexibility and scope to Islamic banks to enable them to grow, expand their operations, and to evolve into viable competitors to conventional institutions. It is submitted, although 'Islamic banking business' is a free-standing term, that is, it can be used without artless definition of so significant a term, in the long run, it will enhance the professional image or the reputation of Islamic banking particularly when compared with the comprehensive definition of 'banking business' found in the BAFIA.<sup>8</sup>

In practice, what appears to have been done to accord with this definition of Islamic banking business is to commence banking business using the modality of the conventional banking business carried on by existing banks and then Islamize its operations by stripping off its elements which are prohibited and not approved by Islam, in particular, *ribā'* (usury).<sup>9</sup>

Nevertheless it is clear that Islamic banking business does not contain the element of *ribā'* (interest). The Islamic banking business has certain underlying features :

- i. money does not earn money without a collaboration between capital and effort ;
- ii. gain is associated with risk ;
- iii. trade and partnership are the basis of Islamic banking ; and
- iv. there is no debtor-creditor relationship.<sup>10</sup>

The prohibition of *ribā'* in the *Al-Qur'ān* developed gradually. It first appeared in Verse 39 of Chapter ar-Rūm which was revealed during the Meccan period. First revelation : ar-Rūm, Verse 39 (30:39),

<sup>8</sup> Mohd Illiyas. 1995. "Islamic / Interest-Free Banking in Malaysia Some Legal Considerations". *Malay Law Journal*. Kuala Lumpur. Vol. 3. p. Cli.

<sup>9</sup> Samsar Kamar bin Hj Ab Latif (Dr.). 1997. "Legal Aspects of Interest-Free Banking in Malaysia". *Malay Law Journal*. Kuala Lumpur. Vol. 2. p. xcvi.

وَمَا آتَيْتُم مِّن رَّبٍّ لَّيْرَبُوا فِي أَمْوَالِ النَّاسِ فَلَا يَرَبُّوا عِنْدَ اللَّهِ وَمَا آتَيْتُم مِّن زَكَاةٍ

تُرِيدُونَ وَجْهَ اللَّهِ فَأُولَٰئِكَ هُمُ الْمُضْعِفُونَ ﴿٣٩﴾

Means:

“That which you put aside (your own to be spent) to grow by using the property of (other) people, (that will have no increase with Allah : but that which you give for charity, in search of Allah’s Holy Face, that will grow : these (are the people) who will get a reward many times larger .”<sup>11</sup>

The word ‘increase’ in the above verse is interchangeable with the word *ribā*’ and therefore, Muslims are strongly recommended not to deal in *ribā*’. The purpose is that any profit sought by Muslims should be through their own exertion and not through exploitation of others or at the expense of others. Muslims must also show their love for their neighbors by spending their own resources or by the utilization of their own talents and opportunities in the service of those who need them.

When this Verse was revealed, the city of Mecca was prosperous with business and trade. The Meccans were not only actively involved in import, export and facilitated the transit of goods, but participated in loan for interest, speculations and aleatory transactions. These activities were performed because of their willingness to see their

<sup>10</sup> n.a. 2002. Banking Laws in Malaysia : The Path to the Future. *Journal of Malaysian and Comparative Law*. Vol. 27. Part 1 & 2. Lembah Pantai : Faculty of Law, University of Malaya. pp. 190-191.

<sup>11</sup> All the translations are based on Syed Vickar Ahamed Homldel, (Dr.) (trans.) *Interpretation of the Meaning of The Glorious Qur’an*. 1999. Kuala Lumpur : TR Group of Companies. p. 502.

capital being unproductive while awaiting the departure or arrival of caravans.<sup>12</sup>

Second revelation: *an-Nisā'*, Verse 161 (4:161),

وَأَخَذِهِمُ الرِّبَا وَقَدْ نُهُوا عَنْهُ وَأَكْلِهِمْ أَمْوَالَ النَّاسِ بِالْبَاطِلِ وَأَعْتَدْنَا لِلْكَافِرِينَ  
مِنْهُمْ عَذَابًا أَلِيمًا ﴿١٦١﴾

Means :

“That they took interest (usury), though they were forbidden ; and that they consumed men’s belongings wrongfully ; - we have prepared for those among them who reject Faith a painful punishment.”

Third revelation: *Al-Imrān*, Verse 130 (3:130),

يَا أَيُّهَا الَّذِينَ ءَامَنُوا لَا تَأْكُلُوا الرِّبَا أَضْعَافًا مُضَاعَفَةً وَتَتَّقُوا اللَّهَ  
لَعَلَّكُمْ تُفْلِحُونَ ﴿١٣٠﴾

Means :

“O you who believe ! do not take usury , doubled and multiplied ; but fear Allah ; that you may ( really ) prosper .”

The revelations above were revealed in Medina. The second revelation created some misunderstanding among the Muslim jurists as to whether the prohibition was

<sup>12</sup> Sudin Haron & Bala Shanmugam. 2001. *Islamic Banking System; Concept & Application*. Subang Jaya : Pelanduk Publications. p. 47.

directed to Muslims or to the Jews.

While the third prohibition was revealed in the wake of the battle of *Uḥud* that took place in the Verse and the preceding one, where the polytheists had spent money on soldiers who fought in the said battle. This money was raised by practicing *riba'*. Another possibility was that the Muslims might be tempted to practice *ribā'* in order to raise money and spent it on soldiers who revenged for the polytheists.

The verse also indicated that the prohibition is for all forms and kinds of *ribā'*. The words double and multiple, however, did create anomalies among Muslim jurists and scholars. Scholars believe that the ban in this verse is no more than a partial one relative to excessive *ribā'* that keeps increasing until it becomes multiples.<sup>13</sup>

## 2.2 The history of Islamic banking in Malaysia.

The genesis of Islamic banking in Malaysia was influenced by both external and internal factors. In 1975, the establishment of the first Islamic bank was the Dubai Islamic Bank in the United Arabia Emiriah & the Islamic Development Bank in Saudi Arabia. Furthermore, between 1976 to 1985 was the period, for rapid establishments of Islamic financial institutions around the world and also the efforts by Islamic nations to convert their banking system to Islamic banking system.<sup>14</sup>

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<sup>13</sup> Sudin Haron & Bala Shanmugam. 2001. *Islamic Banking System; Concept & Application*. pp. 48-49.

<sup>14</sup> Tuan Haji Rustam bin Idris. 2002. "Development of Islamic Banking & Finance in Malaysia". (Paper work). *Seminar on Islamic Banking : Development of Islamic Banking in Malaysia*. Law Student's Society IIUM, Gombak, Selangor Darul Ehsan. 30<sup>th</sup> August. pp. 1-2 .

The internal factors were made by the Malaysian Muslims for the establishment of Islamic banks following the successful implementation of Islamic banks in the Middle East. The success of the pilgrimage Fund Board (a saving institution for intended pilgrims to perform their Haj) and the government of Malaysia's consciousness and pro-active stance help to provide an alternative banking for Muslims.

Islamic banking has been introduced in Malaysia about 20 years ago by the enforcing of the Islamic Banking Act 1983 (IBA) movement. The first formal request was made during the Bumiputera Economic Congress in 1980. This Congress passed a resolution which required the government to allow the Pilgrimage Board to establish an Islamic bank.<sup>15</sup>

On 30<sup>th</sup> July 1981, the government appointed a National Steering Committee on Islamic Banking which consisted of 14 members. The chairman was YM Raja Tan Sri Mohar bin Raja Badiozzaman who proposed to the government for the establishment of an Islamic bank.<sup>16</sup>

The recommendations made by the committee in its report was accepted by the government on July 5, 1982 :

1. The government should established an Islamic bank whose operations are in accordance to the principles of *Shari'ah*.
2. The proposed bank is to be incorporated as a company under the auspices of the Companies Act, 1965.
3. Since the Banking Act of 1973 is not applicable for the operations of an Islamic

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<sup>15</sup> Samsar Kamar bin Hj Ab Latif (Dr.). 1997. "Legal Aspects of Interest-Free Banking in Malaysia". Malay Law Journal. Kuala Lumpur. Vol. 2. p. xcii.

<sup>16</sup> Sudin Haron & Bala Shanmugam. 2001. *Islamic Banking System : Concepts & Applications*. Kuala Lumpur : Pelanduk Publication . p. 16.

bank, a new Islamic banking Act must be introduced to license and supervise the Islamic bank. The vision and administration of the proposed Act are to be the responsibility of the Central Bank of Malaysia.

4. The Islamic bank has its own *Shari'ah* Supervisory Board whose function is to ensure that the operations of Islamic bank are in accordance to the *Shari'ah*.<sup>17</sup>

The Islamic Banking Act, 1983 which was gazetted on 10th March 1983 and came into effect on 7<sup>th</sup> April 1983 paved the way for the establishment of Islamic banking in Malaysia.<sup>18</sup> This Act provides the Central Bank of Malaysia with powers to supervise and regulate Islamic banks in Malaysia. The Summary of the Act is as follows : -<sup>19</sup>

- Part I : Short title, commencement, application and interpretation.
- Part II : Licensing of Islamic bank.
- Part III : Financial requirements and duties of Islamic banks.
- Part IV : Ownership, control and management of Islamic banks.
- Part V : Restrictions on Business.
- Part VI : Powers of supervision and control over Islamic banks.
- Part VII : Others like indemnity, priority of sight and savings account liabilities and penalties on directors and managers.
- Part VIII : Consequential amendments to the others act to make sure the Islamic Bank can carry on its operation.

BIMB was established by virtue of the Act of Parliament; Islamic Banking Act (IBA) 1983 which was considered as the beginning of the effort to assimilate Islam into the Malaysian economic system. As provided in IBA 1983, BIMB carries out banking business similar to other commercial banks, but upholds the principles of *shari'ah*.

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<sup>17</sup> n.a. 1996. *Organisasi dan Operasi*. Ed. 3. Kuala Lumpur : Bank Islam Malaysia. pp. 2-3.

<sup>18</sup> Sudin Haron & Bala Shanmugam. 2001. *Islamic Banking System : Concepts & Applications*. p. 17.

<sup>19</sup> Malaysia. 1999. *Islamic Banking Act 1983 (Act 276)*.

### 2.2.1 The establishment of Bank Islam Malaysia Berhad.

The Bank Islam Malaysia Berhad was incorporated as a limited company under the Companies Act, 1965 by taking the name of Bank Islam Malaysia Berhad (BIMB) with its registered office situated in Malaysia.<sup>20</sup> BIMB is the first Islamic bank in Malaysia. It was incorporated on 1<sup>st</sup> March 1983 and commenced operations on 1st July of the same year.<sup>21</sup> It was established by virtue of Parliament ; Islamic Banking Act (IBA) 1983 which is considered as the beginning of the effort to assimilate Islam to the Malaysian economic system. It was also successfully listed on the main board of the Kuala Lumpur Stock Exchange on 17<sup>th</sup> January 1992.

The bank now has a network of more than 80 branches in Malaysia. BIMB does not only promote Islamic banking products through its own operations but actively introducing Islamic financial products and services through its own subsidiaries. At present, BIMB has subsidiaries dealing with leading business, nominee services, family and general *takaful* ( insurance ) business, trust funds and stockbroking.

### 2.2.2 The objectives of Bank Islam Malaysia Berhad.

Generally, the objective of BIMB is to encourage, and develop the using of the Islamic law and principles in the terms of transactional, business , financial and banking. It is also to encourage the investment company to uphold the Islamic principles. In its Memorandum of Association, “all business of the company will be transacted in

<sup>20</sup> Joni Tamkin bin Borhan. 1999. “Bank Islam Malaysia Berhad : Some Issues , Problems and Its Prospects in The Future”. *Shari’ah Journal*. Shah Alam : Khayrun ‘Ilmu Enterprise. Vol. 7. No. 2. July. p. 107.

<sup>21</sup> n.a. 2002. “Profail BIMB” [http://www.bankislam.com.my/kenali\\_profail.htm](http://www.bankislam.com.my/kenali_profail.htm). 19th December. p. 1.

accordance with the Islamic principles, rule and practices”.<sup>22</sup> Based on this clause, it provides a wider choice for the bankers to follow any schools of thought pertaining to Islamic transactional law.

Besides that, the corporate mission of the bank is to operate as a commercial bank functioning on the basis of Islamic principles, providing banking facilities and services to Muslims and the whole population of this country, with viability and capability to sustain itself and grow in the process.<sup>23</sup> Its corporate objectives are as follows :

- a) To provide its customers with Islamic banking facilities and services of the highest possible quality.
- b) To attain viability and sufficient level of profitability to sustain growth.
- c) To develop and foster a competent and innovative management imbued with high standard of integrity and Islamic banking professionalism.
- d) To develop a motivated work-force inculcated with the appropriate ethics, fully committed to the bank and providing efficient and courteous service to the customers.
- e) To constantly strive to protect its shareholders’ interest.
- f) To be always conscious of its responsibilities and duties as an Islamic corporate citizen.<sup>24</sup>

The overall objective is to create an efficient, progressive and comprehensive Islamic financial system that contributes significant effectiveness and efficiency to the Malaysian financial sector while meeting the economic needs of the nation. The specific

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<sup>22</sup> Joni Tamkin bin Borhan. 1999. “Bank Islam Malaysia Berhad : Some Issues , Problems and Its Prospects in The Future”. *Sharfah Journal*. Shah Alam : Khayrun ‘Ilmu Enterprise. Vol. 7. No. 2. July. p. 108.

<sup>23</sup> n.a. 2002. “Annual Report 2001”. *Bank Islam Malaysia Berhad Annual Report*. p. 3.

<sup>24</sup> Wong Choo Sum. 1995. “Bank Islam Malaysia : Performance Evaluation, 1983-1991”. *Leading Issues in Islamic Banking & Finance*. Al-Harran, Saad (Dr.) (ed.). Kelana Jaya : Pelanduk Publication. p. 8.

recommendations are formulated to complete effectively and to increase the significance of their market share in the financial system.

### 2.2.3 The Islamic principles in Bank Islam Malaysia Berhad.

BIMB offers several products based on *shari'ah* principles, such as :

- i. current deposits and savings deposits under the concept of *Al-Wāḍi'ah* (guaranteed custody) ;
- ii. investment deposits under the concept of *Al-Mudārabah* (trustee profit-sharing) ;
- iii. working capital financing under *Al-Murābahah* (cost plus) ;  
house financing under Bayc Bithaman Ājil (deferred payment sale) ;
- iii. leasing under the concept of *Al-Ijārah* ; and
- iv. project financing under the concept of *Al-Mushārahah* (joint venture profit and loss sharing).<sup>25</sup>

Currently, there are four types of product which are BIMB served on such as deposits, retail financing, corporate financing and trade financing. The products which are based on the *shari'ah* principles as presented in Table 1, 2, 3, and 4 below.

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<sup>25</sup> n.a. 2002. "BIMB Product". <http://www.bankislam.com.my/produkt.htm>. 25th December. pp. 1-2.

**Table 1 : Product at a Glance-Deposit**

Products	Features	Benefit
<b>Current Account</b>  <i>Al-Wāḍī'ah</i> (Safe Custody)	<ol style="list-style-type: none"> <li>1. Chequing facilities.</li> <li>2. Salary crediting facility.</li> <li>3. Standing instruction.</li> <li>4. Monthly account statement.</li> <li>5. RM 500 initial deposit.</li> <li>6. One introducer is needed.</li> <li>7. Type of accounts: Personal, Joint, Partnership, private Company and Company.</li> </ol>	Immediate access of funds for settlement of regular commitments.
<b>Savings Account</b>  <i>Al-Wāḍī'ah</i> (Safe Custody)	<ol style="list-style-type: none"> <li>1. Salary crediting facility.</li> <li>2. ATM Smart Card.</li> <li>3. RM 1,000 cash withdrawal, and RM 2,000 daily maximum limit.</li> <li>4. Fund transfer.</li> <li>5. Type of accounts: Personal, Entrust, and Joint.</li> <li>6. RM 10 initial deposit.</li> </ol>	Immediate access of funds through withdrawal at branches and ATM network nation-wide.
<b>Savings Account</b>  <i>Al-Muḍārabah</i> (Profit Sharing)	<ol style="list-style-type: none"> <li>1. An investment account with the flexibility of a Saving Account.</li> <li>2. Family Group <i>Takaful</i> Plan.</li> <li>3. ATM Smart Card (upon request)</li> <li>4. RM 100 initial deposit.</li> <li>5. Type of accounts: Personal, Joint, and Trust.</li> </ol>	
<b>Wadi Savings Account</b>  <i>Al-Muḍārabah</i> (Profit Sharing)	<ol style="list-style-type: none"> <li>1. A saving account designed specially for children from the age of 12 and below.</li> <li>2. RM 1 initial deposit.</li> <li>3. Family Group <i>Takaful</i> Plan.</li> <li>4. Membership to Bank Islam's "Kelab Wadi" in participating schools.</li> <li>5. 50:50 profit distribution ratio.</li> <li>6. Free promotional items(e.g.</li> </ol>	"Starting them young". The Wadi Savings Account helps educate children the importance of saving.

	<p>Wadi button badge, coin box, etc.)</p> <p>7. Type of accounts: Personal and Trust.</p>	
<p><b>Ijraa Savings Account</b></p> <p><i>Al-Muḍārabah</i> (Profit Sharing)</p>	<ol style="list-style-type: none"> <li>1. A saving account designed especially for teenagers from 13 to 18.</li> <li>2. RM 1 initial deposit.</li> <li>3. Family Group <i>Takaful</i> Plan.</li> <li>4. Membership to bank Islam's Kelab Ijraa in participating schools.</li> <li>5. 50:50 profit distribution ratio.</li> <li>6. Type of account: Personal.</li> </ol>	<p>The Ijraa Savings Account helps educate teenagers the importance of saving. It also assists them in managing their money wisely.</p>
<p><b>Pewani Savings Account</b></p> <p><i>Al-Muḍārabah</i> (Profit Sharing)</p>	<ol style="list-style-type: none"> <li>1. A saving account designed especially for women aged 18 and above.</li> <li>2. For joint accounts, a male depositor can open an account only if the account's primary holder is a female.</li> <li>3. Can be open by a male as gift for their female companion, spouse, etc.</li> <li>4. Depositors holder can only withdraw their money once a month.</li> <li>5. 60:40 profit sharing ratio if the depositor's Monthly Average Balance is RM 5,000 and above. 50:50 profit sharing ratio if the depositor's Monthly Average Daily Balance is less than RM 5,000.</li> <li>6. Depositors can also choose to have their salary credited monthly into their accounts.</li> <li>7. <i>Takaful</i> coverage of up to RM 25,000.</li> <li>8. Depositors are eligible to participate in an annual lucky</li> </ol>	<p>Pewani is a unique saving account designed to help women to save and financially planned for the future.</p>

	<p>draw. Winners will received one year subscription of a female magazine.</p> <p>9. Bank Islam also welcome any request from women's association to organize workshops or seminars on women's issues.</p> <p>10. Type of accounts: Personal, Joint and Non-resident individual.</p>	
<p><b>General Investment Account</b></p> <p><i>Al-Muḍārabah</i> (Profit Sharing)</p>	<p>1. Investment period of 1, 3, 6, 9, 12, 15, 24, 36, 48, or 60 months to choose from.</p> <p>2. For a 1 month investment period, the minimum is RM5,000. For others, the minimum is RM 500.</p> <p>3. Profit distribution is 70:30 (customer : bank).</p> <p>4. Type of accounts: Personal, Entrust, Joint, Partnership, Private Company and Company.</p>	
<p><b>Special Investment Account</b></p> <p><i>Al-Muḍārabah</i> (Profit Sharing)</p>	<p>1. Investment period of 1, 3, 6, 9, 12, 15, 24, 36, 48, or 60 months to choose from.</p> <p>2. For a 1 month investment period, the minimum is RM5,000. For others, the minimum is RM 500.</p> <p>3. Profit distribution is 70:30 (customer : bank).</p> <p>4. Type of accounts: Personal, Entrust, Joint, Partnership, Private Company and Company.</p>	
<p><b>Sakinah Investment Account</b></p>	<p>1. Investment period of 12, 15, 24, 36, 48, or 60 months to choose from.</p>	<p>“Retirement is something to look forward to. Don't let financial worries spoil</p>

<p><i>Al-Muḍārabah</i> (Profit Sharing)</p>	<ol style="list-style-type: none"> <li>2. Minimum investment is RM50,000.</li> <li>3. Profit distribution is 70:30 (customer : bank).</li> <li>4. Type of accounts: Personal, Entrust, Joint, Partnership, Private Company and Company.</li> <li>5. Benefits: <i>Takaful</i> scheme coverage, quarterly account statement &amp; investment certificate.</li> </ol>	<p>it". Sakinah is open to retirees, those about to retire, or smart individuals who plan ahead.</p> <p>With the Sakinah Investment Account, depositors can now enjoy profit being credited into their accounts monthly.</p>
<p><b>Negotiable Islamic Debt Certificate (NIDC)</b>  <i>Al-Bay<sup>c</sup></i> <i>Bithaman Ājil &amp; Bay<sup>c</sup> Ad-Dayn</i> (Deferred Payment Sale &amp; Debt Trading)</p>	<ol style="list-style-type: none"> <li>1. Minimum deposit: RM 50,000.</li> <li>2. Maximum deposit: RM 10,000,000.</li> <li>3. Minimum deposit period: 1 month.</li> <li>4. Maximum deposit period: 365 days.</li> </ol>	<p>NIDC is a short-term investment scheme which offers attractive, fixed profit rate to individual, public and corporate investors.</p>

Source : Bank Islam Malaysia Berhad 2002.

**Table 2 : Product at a Glance-Retail Financing**

Products	Features
<p><b>AL-BAY<sup>C</sup> BITHAMAN ĀJIL (BBA) CONCEPT</b></p> <p>Type of BBA Products</p> <ul style="list-style-type: none"> <li>• Bayti Home</li> <li>• Vehicle</li> <li>• Land</li> <li>• Naqad Overdraft</li> <li>• Shop &amp; Shophouse</li> <li>• <sup>c</sup><i>Umrah &amp; Ziārah</i></li> <li>• Tour Package</li> </ul>	<p>Al-Bay<sup>c</sup> Bithaman Ājil is a sales contract with a deferred payment scheme.</p> <p>Financing methods:</p> <ol style="list-style-type: none"> <li>a) Financing to customers - to acquire an asset but to defer payment for a specific period.</li> <li>b) Refinancing of assets – such as houses and vehicle. Land or other assets acceptable to the Bank for the following purpose: <ul style="list-style-type: none"> <li>- Cash</li> <li>- Working capital</li> <li>- Restructuring</li> </ul> </li> </ol>

<ul style="list-style-type: none"> <li>• Personal Computer</li> <li>• Educational Package</li> <li>• Unit Trust / ASBI</li> <li>• Golf Club</li> <li>• Consumer goods</li> </ul>	<p>c) Converting of an existing LC <i>Murābahah</i> to BBA product.</p> <p>Types of Facility:</p> <p>a) Retail Financing</p> <ul style="list-style-type: none"> <li>- Less than RM1 million.</li> <li>- Granted to individual, company or organization.</li> <li>- Retail Package financing – to an employee of a government institution, statutory bodies, established private company and an employer who has an agreement with the Bank to deduct their employee’s salary to pay the monthly installment.</li> <li>- Retail Non-Package financing – to an individual or a company as a normal financing.</li> </ul> <p>b) Corporate Financing</p> <ul style="list-style-type: none"> <li>- More than 1 million.</li> <li>- Granted to an established company or organization.</li> </ul>
<p>Bayti Home Financing</p> <p>Al-Bay<sup>c</sup> Bithaman Ājil (Deferred payment sale)</p>	<p>Financing Amount: up to 100% financing.  Eligibility: Monthly installment should not exceed 1/3 of applicant’s net monthly income.  Repayment period: Up to 30 years or upon the applicant’s reaching 65 years of age.</p>
<p>Land Financing</p> <p>Al-Bay<sup>c</sup> Bithaman Ājil (Deferred payment sale)</p>	<p>Financing Amount: Up to the collateral’s sale value or up to 100% for direct purchase from developers.  Purpose of financing: purchase of land, refinancing of land, or settlement of an existing loan.  Repayment period: Up to 15 years or upon the applicant’s reaching retirement age.</p>
<p><sup>c</sup><i>Umrah &amp; Ziārah</i> Financing</p> <p>Al-Bay<sup>c</sup> Bithaman Ājil (Deferred payment sale)</p>	<p>Financing Amount: All cost of <sup>c</sup><i>Umrah &amp; Ziārah</i> package.  Family Group <i>Takaful</i> coverage.  Financing Amount: The actual package price, up to a maximum of RM 10,000 whichever is lower.  Repayment period: Up to 3 years or upon the applicants’ reaching retirement age.  Two guarantors acceptable to the Bank.</p>
<p>Computer Financing</p> <p>Al-Bay<sup>c</sup> Bithaman Ājil</p>	<p>All types of computers for personal use, including accessories.  Financing Amount: Up to 100% of the computer price,</p>

(Deferred payment sale)	subject to an individual limit of RM 10,000 whichever is lower. Repayment period: Up to 4 years or upon the applicant's reaching retirement age.
Vehicle Financing (Al-Bay <sup>c</sup> Bithaman Ājil Deferred payment sale)	Financing Amount: Up to 75% of the purchase price, not exceeding RM 80,000. Repayment period: Up to 60 months. Security deposit of 3 months installment. One guarantor acceptable to the Bank.
Tour Package Financing Al-Bay <sup>c</sup> Bithaman Ājil (Deferred payment sale)	Financing Amount: All cost of tour package. Family Group <i>Takaful</i> coverage. Financing Amount: The actual package price, up to a maximum of RM 10,000 whichever is lower. Repayment period: Up to 3 years or upon the applicants' reaching retirement age. Two guarantors acceptable to the Bank.
Naqad Overdraft Facility Al-Bay <sup>c</sup> Bithaman Ājil (Deferred payment sale)	Applicant: Individuals and business organizations. Eligibility: Applicants must own a property acceptable to the Bank which can be offered as collateral. This includes house, land, commercial building, etc. Financing Amount: Up to the collateral's sale value. Repayment period: Up to 5 years.
Staff Financing Package Al-Bay <sup>c</sup> Bithaman Ājil (Deferred payment sale)	Staff Financing package is especially tailored to meet the needs of staff of Government agencies, statutory bodies, or reputable companies with a special financing rate. Range of financing products: house, vehicle, land, cumrah & ziārah, computer, naqad overdraft, tour package and consumer durable products
<i>Ar-Raḥnu</i> Scheme	The Ar-Raḥnu Scheme is an Islamic pawn broking scheme that provides customers with an attractive option to obtaining immediate cash. Collateral: Gold bar or gold jewelry without precious stones. Financing Amount: A maximum financing of RM 5,000 or up to 60% of the market value of the gold, whichever is lower. Financing period: Up to 6 months, and an extension of 3 months subject to approval. Eligibility: Malaysian citizens aged 18 and above, collateral is owned by applicant, their spouses, parents or children, receipt of purchase must be submitted upon

	application, present letter of authority from the owner if the collateral does not belong to the applicant.
Educational Package Financing	<p>Amount of Financing: Up to 100%, covering the package cost of tuition, registration, examination, graduation, accommodation and other related expenditures for full-time or part-time studies.</p> <p>Repayment period: Up to 15 years.</p> <p>Eligibility: Individual or joint applicant aged 18 and above, either applicant must be a confirmed employee earning a fixed/ stable income at government / private institutions.</p> <p>Others: Guarantor or collateral acceptable to the Bank. Security deposit of 3 months installment.</p>
Personal Financing	<p>Financing Amount: Up to RM 25,000 or 10 months gross salary, whichever is lower.</p> <p>Repayment period: Up to 60 months.</p> <p>Eligibility: individuals aged 18 and above, must be a confirmed employee earning a fixed/ stable income at government / private institutions, monthly income of at least RM1,500.</p> <p>Others: for financing amount of less than RM 10,000 – one guarantor acceptable to the Bank, security deposit of 3 months installment, participation in the Family Group <i>Takaful</i> Plan.</p>

Source : Bank Islam Malaysia Berhad 2002.

**Table 3 : Product at a Glance-Corporate Financing**

Products	Features
<p><b><i>Al-IJĀRAH</i> CONCEPT</b></p> <p>Type of Items for Leasing</p> <ul style="list-style-type: none"> <li>• Equipment</li> <li>• Machinery</li> <li>• Consumer goods</li> <li>• Computers</li> <li>• Motor vehicles</li> <li>• Other suitable and acceptable assets</li> </ul>	<ul style="list-style-type: none"> <li>▪ <i>Al-Ijārah</i> means lease, rent or wage. Generally, <i>Al-Ijārah</i> concepts means selling benefit or use or services of assets / equipments such as plant, motor vehicle etc for a fixed price or wage.</li> <li>▪ The usage of the assets to be leased by the customer and to be financed by the Bank must be in conformity with <i>Shari'ah</i> Principle.</li> <li>▪ The total lease rentals comprise of the amount of financing and profit. It can be derived based on the method of Sum of Digit (SOD).</li> </ul>

	<p>Types of lease financing:</p> <p>a) Financial (capital) lease</p> <ul style="list-style-type: none"> <li>- Long term agreement</li> <li>- A Lessee leases the asset for most of its economic life and returns to the Lessor the entire investment.</li> <li>- A Lessor is responsible for most of the costs normally associated with ownership</li> </ul>
<p><b><i>AL-QARDUL HASAN</i></b></p> <p>Types of facility</p> <ul style="list-style-type: none"> <li>• Al-Qarḍul Ḥasan Facility</li> <li>• Cash Note</li> <li>• Small Entrepreneur Financing Fund (SEFF)</li> <li>• <i>Ar-Rahnu</i></li> </ul>	<p><i>Al-Qarḍul Ḥasan</i> is a benevolent loan / debt financing that does not promise any excess or profit to the lender (Bank). The loan amount will be paid through deferred payment or lump sum as agreed in the <sup>c</sup>aqad.</p> <p>The financing repayment amount is equal to the loan amount without any excess but the borrower has the option to reward the lender for his benevolent deed. <i>Al-Qarḍul Ḥasan</i> may be provided for the following purposes:</p> <ul style="list-style-type: none"> <li>- Small Business</li> <li>- Benevolent Loan to Current Account Holders</li> <li>- Benevolent Loan to Low Income Individuals</li> </ul>
<p><b><i>AL-IJĀRAH THUMMA AL-BAY<sup>c</sup></i></b></p>	<p>Under the concept of <i>Al-Ijārah Thumma Al-Bay<sup>c</sup></i>, the Bank may finance its customers to use the services of given asset but subsequently to own the asset. (leasing and then purchase).</p> <p>In this concept, both parties agree that at the end of the lease period, the customer will purchase the asset concerned, at agreed price with all the lease rentals previously paid constituting part of such a price.</p>