Islamic Banking and Takaful

3rd Edition

Rusni Hassan
Ahmad Azam Othman
Safinar Salleh
Mohammad Azam Hussain

Dr Safinar Salleh
Assistant Professor
Department of Islamic Law
Ahmad Ibrahim Kulliyah of Laws
International Islamic University Malaysia
AUTHORS' PROFILE

ASSOCIATE PROFESSOR
DR RUSNI HASSAN

Associates Professor Dr Rusni Hassan is an Associate Professor and Deputy Dean at the IIUM Institute of Islamic Banking and Finance, IIUM. She graduated with LLB (Honours), LLB (Shariah) (First Class), Master of Comparative Laws (MCL) and PhD in Law. She is a member of the Shariah Advisory Council for Bank Negara Malaysia and Association of Islamic Banking Institutions Malaysia (AIBIM), Shariah Committee for HDFC and HDC Maldives. She is a registered Shariah Advisor with the Securities Commission Malaysia. She is also the Secretary for the Association of Shariah Advisors in Islamic Finance Malaysia (ASAS) and the International Council of Islamic Finance Educators (ICIFE). She has spoken extensively in seminars, workshops, conferences and trainings on various Islamic Finance issues. Her publications include books on Islamic Banking and Takaful, Islamic Banking under Malaysian Law, Corporate Governance of Islamic Financial Institutions and many articles in local and international journals. She has received awards as a Promising Researcher at IIUM in 2012. Her works and contribution to Islamic Finance has also been recognised internationally when she was listed among the Top 10 Women in Islamic Finance by CPI Financial in 2013, and has been awarded the Most Talented Women Professional in Islamic Banking, Asia Islamic Banking Excellence Awards, CMO Asia, 2014.

ASSOCIATE PROFESSOR
DR AHMAD AZAM OTHMAN

Associate Professor Dr Ahmad Azam Othman is currently an Associate Professor at the Islamic Law Department, Ahmad Ibrahim Kulliyyah of Laws (AIKOL) and International Islamic University Malaysia (IIUM). He was the Director of Harun M. Hashim Law Centre, AIKOL, IIUM and the Head of Islamic Law Department, AIKOL, IIUM. His specialised areas are Islamic Law of Property, Transactions, Personal Bankruptcy, Banking and Takaful as well as comparative laws. He has vast experience in teaching for postgraduate as well as undergraduate courses. He is also an internal examiner and supervisor to a number of PhD Theses and Master Dissertation in various areas including Islamic Banking, Islamic Microfinance, Islamic Capital Market, Takaful and Waqf. Dr Ahmad Azam Othman holds a PhD from the University of Wales, UK. In addition, he holds a Master of Comparative Laws from IIUM, where he also obtained his LLB (Bachelor of Laws) and LLB.S (Bachelor of Shariah) as his first degree.
ASSISTANT PROFESSOR  
DR SAFINAR SALLEH

Assistant Professor Dr Safinar binti Salleh obtained her Bachelor in Shari'ah (Hons) from the Al-Azhar University Cairo in 1999. She pursued her Master in Shari'ah and became a tutor at the Department of Fiqh and Usul, Academy of Islamic Studies, University of Malaya. She started developing her expertise in the area of Islamic Law of Contracts and completed a dissertation on Islamic pawn broking. Upon completion of her Master in 2005, she took up a lecturer position at Ahmad Ibrahim Kulliyyah of Laws (AlKOL), International Islamic University Malaysia (IIUM). In July 2013, she obtained her PhD from Glasgow Caledonian University and her research was on Islamic Insurance (Takaful). Presently, she is an Assistant Professor at the Department of Islamic Law, AlKOL. She is also appointed as a Shari'ah Committee member of the Bank of Tokyo-Mitsubishi UFJ (Malaysia) Berhad and Swiss Re Retakaful.

DR MOHAMMAD AZAM HUSSAIN

Dr Mohammad Azam Hussain is currently a Senior Lecturer at the School of Law at the Universiti Utara Malaysia, Kedah, Malaysia, where he has been a faculty member since 2002. He holds a Bachelor of Shariah (Honors) and Master of Shariah from the Academy of Islamic Studies, University Malaya, Kuala Lumpur. He completed his Doctor of Philosophy (PhD) in Islamic Banking & Finance at the Institute of Islamic Banking and Finance, International Islamic University Malaysia. He has approximately 15 years of teaching experience in higher learning institutions in the area of Islamic Law, Islamic Banking and Finance Law. His research interests lie in the areas of Islamic banking and finance. He has actively collaborated with other researchers in several other disciplines in the area of Islamic law. He has written and presented more than 30 articles and papers in journals and participated in conferences both locally and internationally.
CONTENTS

CHAPTER 1
Introduction to Islamic Banking 1
Modes of Financing in Islamic Banking 4
Differences between Islamic Banking and Conventional Banking 5
Salient Features of Islamic Banking 7
Conclusion 13

CHAPTER 2
Historical Development of Islamic Banking and Takaful 14
Origins of Islamic Banking and Takaful 14
Initial Development of Islamic Banking and Takaful 15
Development of Islamic Banking and Takaful in Malaysia 18
Islamic Banking and Takaful Structure in Malaysia 27
Issues and Challenges 33
Conclusion 34

CHAPTER 3
Essential Shariah and Fiqh Rulings in Commercial Contracts 35
Classification of Contracts 35
Essential Elements of a Contract 37
Mutual Consent in Islamic Contracts 44
Effects of Void and Voidable Contracts 45
Conclusion 46
CHAPTER 4
Prohibition of Riba, Gharar, Maysir and Prohibited Commodities 47
Prohibition of Riba 47
Prohibition of Gharar 54
Prohibition of Maysir 57
Prohibited Commodities 58
Conclusion 60

CHAPTER 5
Shariah Contracts in Islamic Banking 61
Sale-Based Contracts in Islamic Banking 61
Partnership-Based Contracts in Islamic Banking 91
Al-Ijarah (Lease-Based) Contracts in Islamic Banking 104
Supporting Contracts in Islamic Banking 113
Conclusion 130

CHAPTER 6
Islamic Banking Products 131
Deposit Products 131
Investment Products 140
House Financing Products 144
Vehicle Financing Products 159
Personal Financing Products 164
Trade Financing Products 171
Conclusion 187

CHAPTER 7
Takaful (Islamic Insurance) 188
Definition and Features of Takaful 188
Legality of Takaful 190
Misconceptions on Takaful 194
Differences between Takaful and Conventional Insurance 199
Underlying Contracts in Takaful
Types of Takaful Business
Takaful Operating Models
Retakaful
Conclusion

CHAPTER 8
Legal and Regulatory Framework
of Islamic Banking and Takaful in Malaysia
Law Governing Islamic Banking and Takaful in Malaysia
Other Relevant Statutes on Islamic Banking and Finance
Dispute Settlement in Islamic Banking and Takaful
Conclusion

CHAPTER 9
Shariah Advisors in Islamic Banking and Takaful
Regulatory Requirements of Shariah Advisors in Malaysia
Shariah Advisory Council (SAC)
Shariah Committees (SC)
Challenges for the Shariah Advisors
Conclusion

CHAPTER 10
Selected Cases on Islamic Banking and Takaful
List of Cases
Cases on Bai' Bithaman Ajil
Cases on Bai' Al-Inah
Cases on Murabahah/Tawarruq
Cases on Al-Ijarah
Cases on Istisna'
Insurance protection is one of the main financial necessities of life because people nowadays are more vulnerable to risk and uncertainties. Death, disability, injury, illness or destruction of property due to calamities can happen to anyone at any time. It is clear that insurance cannot prevent these events from happening; but it can provide financial assistance to reduce the burden of losses resulting from the occurrence of such contingencies. Although the basic idea of insurance embodies the elements of co-operation and mutual help which are encouraged by Shariah, its application has been a controversial and much disputed subject among Muslim scholars. They have debated about the legal status of the insurance contract in Islamic law. The majority of them perceived that it contains the elements of gharar (uncertainty), majma (gambling) and riba (usury) which are prohibited by the Shariah. Pursuant to the intense debate for and against the legality of commercial insurance, an insurance arrangement known as takaful was introduced to fulfill the needs of Muslim society for a Shariah compliant insurance scheme.

**DEFINITION AND FEATURES OF TAKAFUL**

Takaful is an infinitive noun (masdar) which is derived from the Arabic root word ‘kafala’ meaning to guarantee. Linguistically, the word takaful means joint liability or solidarity. The term takaful is based on the word ta’awun which means co-operation or mutual assistance. Technically, takaful refers to a mutual guarantee or assurance arrangement among a group of people facing the same risk or danger of incurring losses to contribute a certain sum of money which will be used to compensate any member of the group who incurs such losses. In the legal perspective, takaful is statutorily defined as

---

