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**DIMINISHING PARTNERSHIP HOME
FINANCING CONCEPT AS AN ALTERNATIVE
TO *BAI BITHAMAN AJIL* (BBA):
EMPIRICAL EVIDENCES FROM THE
PERCEPTIONS OF *SHARIAH* SCHOLARS AND
BANKERS**

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Abstract

Meera and Abdul Razak (2005) suggested that the Diminishing Partnership (DP) Home Financing concept can be a viable alternative to *Bai Bithaman Ajil* (BBA) Home Financing. They argued that DP concept can address issues faced by BBA which is still the main financing mode of Islamic financial institutions to date. The major issues that have arisen are related to the concepts used, methods of computation, pricing based on interest rate benchmark, *Shariah* compliant, justice and societal well being. On the other hand, the DP concept is claimed to be free from the above mentioned shortcomings and said to be in line with the spirit of Islam, which promotes risk sharing and its pricing based on rental is considered to be just and fair. As these issues requires in depth understanding of the *Shariah* parameter as well and banking operations, a semi-structured interviews was conducted with six *Shariah* scholars and six bankers to seek their opinions and viewpoints on the variables investigated. The *Shariah* scholars generally agreed that DP concept possess greater justice, equity and follows the true spirit of Islam. Contrary to expectation, the overall views of the bankers support the implementation of DP although there were a few reservations regarding its operations. The actual implementation of DP is a challenge for bankers which require a paradigm shift from their present role as traditional financiers.

Key words: Islamic home financing, *Bai Bithaman Ajil* (BBA), Diminishing Partnership (DP), *Shariah* scholars, Bankers and *Shariah* compliant.

1.0 Introduction

Islamic finance recorded an encouraging annual average growth in Malaysia between 18%-20% per annum (BNM, 2007). The impressive performance is mainly attributed to demand for financing products in the retail banking sector. There demand for residential property loan in commercial banks by 10% in 2008. The figure stood at RM 174 billion as at 31 December 2007 and increased to RM 192 billion as at 31 December 2008 (BNM, 2008: 40). Based on this back drop, commercial banks continue to play a major role in providing home financing products to meet the increasing demand of customers for conventional loans and Islamic financing. The motivation for this research is to examine the theoretical issues and practice of the prevailing debt financing based on *Bai Bithaman Ajil* (BBA) introduced by Bank Islam Malaysia Berhad (BIMB) in 1983 and remain as the major financing product for past 26 years.

The existing BBA operations have several contentious issues regarding the home concept used, method of computation and pricing, *Shariah* compliant, justice, societal well being and customers' satisfaction. Given these shortcoming of the BBA, there is a pressing need to look for an alternative mode of home financing. Diminishing Partnership (DP) is a model that is based on equity and focuses on joint purchase of property between customers and banks. Pricing of DP is based on rental instead of on a margin that is predetermined during the sale of the property through deferred installment sales facility. As such, DP is seen to be promoting the spirit of Islam better than BBA. The literature has so far remained silent on perceptions of *Shariah* scholars and bankers pertaining to the theoretical issues and practices that arise in the implementation of these to modes. It is the intention of this paper to explore the perception of these two prominent groups of scholars and practitioners with regard to the theoretical underpinning of the DP and acceptance of such a model by practitioners (bankers)

The remaining of the paper is organized as follows. The immediate section discusses the general concept of both models (BBA and DP) and important attributes of each model. This is followed by a study design where the details of the respondents' selection and data collection are explained. Findings of the study are synthesized in the following section before conclusions are offered.

2.0 Literature review

Islamic law (*Shariah*) of commercial transaction is fundamentally rooted on the premise of total eradication of *riba* (usury) and *gharar* (uncertainty). It balances the moral and material needs of a society to achieve socio-economic justice. The very objective of the *Shariah* is *to promote the welfare of the people, which lies in safeguarding the faith, life, intellect, posterity and property* (Al-Ghazali, 1937). The primary goal of Islamic economics is equal distribution. Islam views that inequity is created by mass exploitation of resources to obtain maximum profit. Principles of Islamic commercial transaction are nurtured to check exploitation, inequities and the creation of economic imbalances in society by means of various concepts and principles to eradicate unjust enrichment. Central to the Islamic concept is justice. All transactions whether it is judicial, political or private are subject to this concept (Quran, Al-Hijr: 85).

Islamic economic principles promote sharing of risk and rewards in wealth creation via equity rather than debt. It promotes entrepreneurship and creativity in the economic cycle. In the

Islamic economic model, each individual is involved in the economic activity. This differs from modern capitalism where profit maximization is the sole motive and the bank is broadly content with earning interest on the loan regardless of the social and financial implications of the business. In addition, the orientation of modern capitalism does not include God and society as its integral part of acquiring wealth. As such, it does not have any restriction in the way wealth is obtained. The different approaches in world view between Islam and modern capitalism is reflected in the practice of Islamic banking and finance of which the salient feature is the prohibition of *riba* (usury) and *gharar* (uncertainty)

The concept of financing in Islam differs with that of conventional financing. Loan is the main mode of financing under conventional financing using interest as a time factor for borrowed money. The Quranic injunction prohibits financial activities that has interest element and/or has no genuine connection to trading activities under the *Shariah* law. This is because money in itself has no real value and can only serve as a medium of exchange (Ayub, 2007). Hence, money cannot be traded as a commodity in Islam. This differs from conventional financing where money is treated as a commodity and loans are lent out with interest as its pricing mechanism. Trading “money with money” is tantamount to *riba* (usury), which is strictly prohibited in Islam (Rosly, 2005). *Riba* literally means an increase, addition, expansion or growth (Al Zubaydi, 1306). In *Shariah*, *riba* technically refers to the ‘premium’ that must be paid by the borrower to the lender with the principal amount as a condition for the loan or for an extension in its maturity. Ibn Manzur (1990) specifies that “*what is prohibited is the extra amount, benefit or advantage received on any loan*”.

Bai Bithaman Ajil (BBA) is among the earliest attempts in Islamic home financing products, introduced by Bank Islam Malaysia Berhad (BIMB) in 1983. It is developed as an alternative to conventional home financing and by far the most predominant and widely used concept by financial institutions in Malaysia. The attractive feature to BBA is its fixed profit and preferred by customers who do not want to be involved with fluctuating interest rate. The concept of BBA is based on deferred installment sale whereby the banks purchase the house from the customer and later sell the property back inclusive of profit margin. Bank capitalizes its profit up front in the sale of the property to the customer who in turn is required to pay a fixed monthly installment until the tenure ends. It is similar to debt financing, which results in high cost and poses a burden to one family’s budget. The critics of the product view that the existing BBA practice in Malaysia as incompatible with the *Shariah* principle as the bank does not take the risk of ownership and liability on the property (Rosly, 2005). The scholar further emphasized that the absence of risk and liability violate the legal maxim of *iwad* (equivalent counter value) which the bank has to bear to ensure that a bona fide sale has taken place. Further more, it is argued that the current practice is based on *Bai Inah* (sale and buy back) which is not acceptable to international scholars (Rosly, 2005) (Meera and Abdul Razak, 2005). Besides, the reliance on interest rate as a benchmark in determining the profit margin charged to the customer defeats the ‘interest free’ concept.

The *Musyarakah Mutanakisah* or Diminishing Partnership (DP) concept was introduced to overcome the main criticisms of BBA. The DP model is based on the highly successful Islamic Cooperative Housing Corporation (IHC) in Toronto, Canada established in 1981 out of necessity to avoid the Muslim community from engaging in *riba* (usury). It is based on an equity model different from the traditional debt-based mortgage. DP focuses on joint purchase of property between customers and banks. The product is structured using four contracts. First, the customer enters into a partnership (*musharakah*) under the concept of ‘*Shirkat-al-Milik*’ (joint ownership) agreement with the bank. (Usmani, 2007). Customer pays, for example, 10% as the initial share to co-own the house whilst the bank provides the balance of

90%. Secondly, the customer promises to purchase the banks' units of share. Thirdly, the bank leases its share (90%) in the house ownership to the customer under the concept of *ijarah* (leasing), i.e. by charging rent; and the customer agrees to pay the rental to the bank for using its share of the property. The periodic rental amounts will be jointly shared between the customer and the bank according to the percentage of share holding at the particular time. Finally, the customer redeems the financier's 90% portion through the purchase of shares until the house is fully owned by the customer. Bank takes ownership and assumes responsibility of the property until the financing amount is fully settled and customer takes possession of the property.

The DP concept is *Shariah* compliant as it promotes true spirit of Islamic banking by promoting the welfare of the people and takes care of the well being of society (Ahmad, 2000; Siddiqui, 2001; Rosly and Bakar, 2003). Since the DP rests on profit and loss sharing and not on debt financing, the concept may not cause hardship and harm to customers. Bank takes ownership and assumes responsibility of the property until the financing amount is fully settled and customer takes possession of the property. This is in line with *iwad* (equivalent counter value) of undertaking risk, liability and effort required by the legal maxim (Rosly, 2005). The DP concept also overcomes the issue of fixed interest which received criticism under BBA by replacing it with rental rates. The use of rental rate in DP reflects the actual value (usufruct) of the property compared to interest which is the price for money. Thus, using different basis for pricing would free Islamic banks from the practice of *riba* (usury) which has brought injustice to individuals and society. The profit sharing concept in DP enables the customer to purchase additional bank's share to own the house earlier thereby reducing the burden of debt inherent in conventional and BBA home financing.

3.0 Research Design

The selection of experts (comprise *Shariah* scholars and bankers) were made based on judgment sampling technique. In the case of Islamic finance, this was inevitable since the number of experts on Islamic finance is limited and due to unavailability of a sampling frame consisting of experts listing. According to Sekaran (2003), it is best to select respondents who possess the required knowledge and skills in their respective the area. Since the objective of this study is to investigate the opinions of the experts and practitioners on DP and comparing the model with BBA (and it is not intended to be generalised), it is therefore considered sufficient to select six *Shariah* scholars and six bankers. In order to ensure the validity of the respondents' opinion the selection criteria for *Shariah* scholars were based on their qualifications, area of specialization and working experience. They should have a minimum of Masters degree and specializes in teaching of fiqh (Islamic law) and/or *muamalat*. In selecting the bankers, their positions and work experiences were considered. significant. Thus, they should be directly involved with product development or supervising the Islamic Banking department/division. The respondents were identified as S1 to S6 for *Shariah* scholars and B1 to B6 for bankers to ease discussion.

3.1 Data collection and analysis

Data were collected by means of semi structured interviews. Permission was asked to tape the interview session using a media device. Semi structured interview was considered the best method as it enables the researcher to plan for the interview based on the themes of study and focus on specific questions to be discussed. Some of the questions asked were regarding their opinions on the theoretical and practical aspects of debt and equity. Their views were also

requested on its operations and issues that arise in its implementation. The interviews were conducted at the respondents' office with an average period of one hour per session.

Data collected was transcribed into field notes and analyzed using matrices (Miles and Huberman 1994, pg 240). Each matrix is built based on the answers to the research questions provided by each respondent. The process involved selecting, simplifying and coding the data collected into common themes. The process also involves identifying certain key words and phrases, direct quotes and counting their frequencies. The information gathered were placed under the respective matrices and further examined based on the research objectives and research questions as guidelines.

4.0 Findings

This section presents the results of the semi structured interviews conducted with the six *Shariah* scholars and six bankers based on the research questions. The results were analyzed based on the four themes investigated namely concept used, method of computation and pricing, *Shariah* compliant, justice and equality.

4.1 Concept of debt and equity financing

The *Shariah* allows the practice of both debt and equity concepts and this was confirmed during the interviews. Sale of asset by deferment is permissible. However, scholars and bankers have different opinions on what constitute trading in Islamic finance. Five of the six scholars agreed that the sale is permitted in Islamic finance provided that bank trade in real asset. One scholar (S5) clarified:-

“The underlying debt concept in BBA is actually based on sale. Bank can use this concept but they must follow all the rules and regulations forwarded by the scholars. This means that Islamic banks must fulfill the genuine condition of Al bay (sale) in order to make it valid from the fiqh point of view. As long as this is fulfilled there will be no problem”

Majority of the bankers (five of the six) opined that there is nothing wrong with the prevailing practice of BBA home financing as there exist buying and selling (trading) transaction between the customer and bank and is thus allowed. According to one banker (B6)

“In my view there is nothing wrong in the present practice of BBA home financing as there is a trading transaction between the customer and bank and not a loan transaction. This is because there exist buying and selling between the bank and customer (trading) which is allowed in Malaysia. Whether it acceptable or not outside Malaysia is debatable “

The bankers felt that a mere trading activity is sufficient without the real asset in existence. This view contradict majority of scholars' opinions that an asset must exist during a sale transaction. There must be real purchase of commodity and not merely trading in money as it is tantamount to giving out loans. Trading in money is not allowed in Islam as money in itself has no intrinsic value unlike an asset (Ayub, 2007). Thus, scholars argued that the existence of an asset is an essential requirement at the time of sale (Al-Zulhayli, 2003 pg 15) (Usmani, 2007 pg 97)

Meanwhile, there is no conflicting opinion between the *Shariah* scholars and bankers with regards to the concept of equity in financing. One banker (B5) remarked:

“The Diminishing Partnership concept is an alternative form of home financing by means of equity sharing instead of debt as in conventional and BBA home financing. There is ownership by both parties. Customers need to come out with their portion of money for down payment of the house. The remaining amount can be obtained from the bank as its partner”

In equity financing under the concept of Diminishing Partnership, both bank and customer are partners and jointly purchase the house. Hence, bank takes possession of the real asset property and thus does not trade in money as in debt financing. In doing so, bank and customer share the responsibility in owning the property.

4.2 Method of computation and pricing

On conventional and BBA calculations,

As both conventional home loan and BBA home financing are based on debt, there is a need to investigate whether the method of computation is the same. The analysis of the interviews indicated that majority *Shariah* scholars and bankers agreed there are similarities in the computations of BBA home financing with the conventional. One banker (B2) remarked:

“The same formula for conventional loan is also used to compute for BBA home financing i.e. by means of the Present Value of Annuity where; $PMT = PV$ (Present Value); n (tenure) and i (interest). The field for interest is substituted with profit and all other fields remain the same”.

Another banker B6 opined:

“BBA home financing cannot be transparent as it is a sale agreement which falls under the debt category. The issue on BBA is that of high selling price which remained fixed until the tenure ends. This poses a burden to customer when compared to DP home financing which is more flexible”.

One *Shariah* scholar (S6) commented:

“There is almost perfect correlation on the method of computing home financing between conventional financing and BBA because the same benchmark for interest rate is used in the process. The only difference is that we just change the word interest to profit.”

The above evidences indicated that the respondents believe that there are similarities in the method of computing profit for conventional and BBA home financing as the profit amount is computed upfront based on time value of money formula. This violated the *Shariah* as the bank is gaining profit without taking any risk, Rosly (2005). This argument is further supported by Siddiqi (2004) who opined that *time is not recognized by Shariah as a basis of claiming an excess over the principal sum.*

There are various opinions regarding the current pricing of BBA home financing which is benchmarked on interest rate. A well known scholar Usmani (2007) vehemently stated that although interest rate benchmark can be temporarily used as a benchmark, its continuous use to determine a *halal* profit is not desirable and should be removed as soon as possible because it does not advance the basic philosophy in the Islamic economy. His view is shared by all the scholars during the interview who also regard interest as an interim measurement only. Although banks are still using interest rate as a benchmark for pricing, they viewed that banks should find alternative ways to avoid the continuing use of interest rate as a benchmark in view of this exploitative element. On the other hand, a majority of the bankers felt that there is nothing wrong in using interest rate as it is only a benchmark and there is no other alternative at the moment. Nonetheless, they also agreed that it would be good for Islamic banking to have its own benchmark.

On DP calculations,

Conversely, the method of computing profit and pricing using DP home financing differ from BBA. One of the *Shariah* scholars (S6) explained:

In the case of DP home financing, the bank does not compute profit up front based on time value of money as in BBA, profit is computed based on rental rate which is then gradually shared between the customers and the bank depending on their equity balances i.e. the higher is the equity, the higher is the profit earned.

This is supported by the bankers who agreed that there is no debt element in DP home financing because the house is jointly owned between the customer and the bank. Hence, the computation differs from the conventional financing. According to one banker (B6):

The method of computing profit under DP is different than BBA which is based on debt. The customers need to come out with its initial share of capital and the remaining will be obtained from the bank. There is no element of debt in DP home financing because the property is jointly owned between the customer and the bank.

There were also various opinions on the use of rental rates as a benchmark in DP home financing.

Although banks are still currently using interest rate to benchmark for DP, majority of the *Shariah* scholars opined that it can only be used as an interim measure. They agreed that it would be more appropriate to use the actual rental price of the asset (usufruct) in the market and not interest rate. One of the scholars (S5) remarked:

“Using rental based on actual value of the property is better because it reflects the real market compared to interest rate. However, we must ensure fairness to both parties. Currently, we are still benchmarking against interest rate. We need to change our mind set”.

A majority of bankers also support the use of actual rental price as an alternative to interest rate although some voice their concern. According to banker, (B6):

“A good benchmark must be transparent and acceptable in the market. However, when we do actual value of the property, there are some factors that cannot be determined easily as

it varies from one place with another for example location, neighborhood, and economic activities. Thus, these factors need to be addressed and acceptable by both the bank and customers”

According to another banker (B1):

“In my opinion, using actual value of property as a benchmark is practicing real Islamic economics at work. It is ideal to replace interest rate in the conventional with rental as it is the actual cost of owning the asset. But is it possible to work on the actual value of the property? It may be possible for properties in Klang valley as they are homogenous but how about Kelantan and Terengganu where the houses are not homogenous?”

Hence, based on the above, the scholars and bankers seem to agree in principle on the actual rental bench mark for DP home financing. The arguments put forward by *Shariah* scholars were that it measures the real value (usufruct) or benefit of the asset and not interest rate. The reservation put forward by bankers were basically on the need to establish some kind of measurement on rental due to differences in the physical structure and location between one property with another.

4.3 Shariah compliant

There are several passages in the Quran that mentioned unjust enrichment or ‘receiving a monetary advantage without giving equivalent counter value (*iwad*) is forbidden on ethical grounds (Lewis, 2009

pg 10). In the current practice of BBA home financing, the bank is engaged in a sale and buy back transaction with the customer which absolved itself from taking risk as it does not take possession of the property before it is sold to the customer. This is similar to the contentious *Bai Inah* sale which is forbidden by all schools of thought (*mazahabs*) except for Shafie who approved it with abhorrence Mohamed (2005) one of scholar (S4) interviewed commented:

“The practice of BBA home financing in Malaysia is not globally accepted because of the ownership issue and the practice of Bai Inah. How can a customer sell his property which he didn’t even own or have possession of it yet? In the practice of Bai Inah the bank bought the house from the customer at a lower price and sells it back at a higher price. This is prohibited by all the mazhab (school of thought) except for Shafii who approved it under certain conditions. One of the conditions is that the transaction must not be prearranged with known intention between the two parties which unfortunately is being practiced here”

The bankers also share the practice of *Bai-Inah* in BBA home financing. However, only three of the six bankers (50%) seemed to be aware of the issue. One of the bankers B (4) commented:

“ I think the practice of BBA in Malaysia had undergone a lot of criticism because the way we practice the concept is based on Bai Inah as bank purchased the house directly from the customer. This is different from the practice in Middle East whereby the bank purchases the house from the developer before selling it to the customer.

According to Rosly (2001), there are three components of *iwad* namely risk (*ghorm*), liability (*daman*) and effort (*kasb*) that are essential before the bank can realize a legitimate profit Hence, there is an issue regarding the existing practice of BBA which is apparently similar to

the sale and buy transaction (*Bai Inah*) where bank does not risk and liability similar to conventional loan model

On the other hand, Scholars and bankers agreed that the DP home financing complies with the *Shariah* requirements based on the arguments put forward earlier on the existence of *iwad* (equivalent counter value). According to one scholar S (6)

“The importance of taking risk is mentioned in the hadith “Do not sell what you do not own”. Hence it is obvious that the bank is taking risk by taking ownership of the property. Thus, the bank will also be involved in maintaining it as well. There is no Bai Inah in DP home financing because the bank is not involved in buying and selling back the same property”.

This argument is supported by another banker B (6)

“As the Diminishing Musharakah concept is a joint venture between the bank and customer from the Shariah perspective, the bank has to take care of its liabilities on the property and if anything happen to it, the bank should be co-liable.”

4.4 Justice and equality

Several verses of the Quran¹ and Sunnah have both placed tremendous emphasis on justice, making it one of the central objectives of the *Shariah* (Chapra, 2000). The *Shariah* ruling on commercial transactions are fundamentally rooted on the premise of total eradication of *riba* (usury) and *gharar* (uncertainty) The analysis of interview indicated that both the *Shariah* scholars and bankers generally agreed that the debt obligation in BBA home financing is a factor that caused some form of injustice as bank's profit had been determined upfront in the sale of the property to the customer. Hence, the bank has the right to demand payment from the customer. An issue arises in financing house under construction using the sale contract whereby there is uncertainty (*gharar*) as the asset is non existence. The customers will be in a quandary if the house is not completed or abandoned by the developer as he is still required to pay the bank monthly installment because of the debt obligation in the sale contract (Rosly, 2008). This situation would pose a burden and hardship to the customers as they also have to pay rental for their family to stay in another house until it is ready for occupation. According to one scholar, S6:

“The right concept to use for house under construction is Istisna (Work in progress) and not BBA (sale). Istisna means manufacturing contract and suitable for house under construction, building a bridge or manufacturing of goods. Under the Istisna contract, the customer is only liable to commence payment when the work on project begins and subsequent payment will be proportionate to work in progress. As such, the bank cannot claim monthly installment from the customer when the house is not completed.

According to Meera and Abdul Razak (2009) due to its fixed selling price under BBA home financing, the financial structure becomes rigid and customers faced difficulties for early payments and defaults. As seen in the landmark case between Affin Bank versus Zulkifli

¹ See Qur'an : (Al-Maidah:8); (An-Nisaa:58;105;107;135); (Ad-Dukan: 38-39);(Al-Baqarah:213); (Ash-Shura:15); (Al-Sad:26); (Al-Hadid:25).

(2005) the bank did not rebate the customer the unearned profit portion in its statement of claim for the outstanding selling price on default. One of the bankers (B6) further explained this situation:

“If you take a BBA and defaulted, theoretically you are required to pay the full amount of the sales contract whether you get a rebate or not, it is subject to the bank’s discretion. So it can cause a lot of anxiety when the bank demands for the full outstanding amount because customers will expect the rebate.”

In contrast, a majority of the *Shariah* scholars and bankers viewed that there is greater flexibility in DP home financing as under equity financing as the bank does not compute its profit upfront and there is no necessity for rebate. One banker (B6) expressed this view:

“In DP home financing, the advantage is that I am able to do floating rate. Hence customers’ outstanding balance at any point in time will reflect the remaining equity that belongs to the bank. So you can find there is certainty in which customers know how much they need to pay the bank at any point in time. This is very much unlike the BBA whereby customers have to pay for the full amount and rebate be granted only at bank’s sole discretion”

One of the *Shariah* scholars (S1) further clarified:

“When we talk about Diminishing Partnership, it means that equity of the bank will be reduced from time to time until the whole share or equity is being transferred from the bank to the customer. Thus, the process is gradual and not like BBA where the ownership is at the beginning”

In addition, the bankers also felt that the flexibility in DP enables them to change the rental rates over the duration of financing. This will also facilitate them to manage their liquidity position more effectively compared to BBA home financing where the profit rate is fixed over long tenure for example 20 years.

5.0 Discussion and implication

The findings provided empirical evidences on the similarities and differences between the perceptions of *Shariah* scholars and bankers on the four themes namely concepts used, method of computation and pricing, *Shariah* compliant, justice and equality with regard BBA and DP home financing. There is a difference in the perception between bankers and *Shariah* scholars on the meaning of ‘trading’. The bankers view that the term trading in BBA simply means buying and selling between the customer and the bank without the need to have an underlying asset. However, *Shariah* scholars viewed that for a bona fide sale to take place, bank must transact in real asset as without it, both parties are exchanging in money which is similar to loans. Hence, in order to overcome this controversy, the DP concept in home financing is seen to be a more appropriate mode of home financing as both parties are involved in purchasing the physical asset and not engaged in trading of money. In doing so, banks also undertake risk and liability meeting *Shariah* requirements.

Both *Shariah* scholars and bankers agreed that the method for computing and pricing of BBA home financing is similar to conventional financing as bank computes profit upfront based on time value of money based on predetermined profit rate. *Shariah* scholars viewed

that the use on interest rate bench mark is not desirable due to its exploitative elements. However, as there is no alternative Islamic bench mark at the moment, bank's continuous use of interest rate benchmark is 'permitted' as a temporary measure Usmani (2007). However, he emphasized that steps should be taken to find the real bench mark to reflect the Islamic philosophy. The *Shariah* scholars and bankers agreed that the method and pricing for DP is not similar to debt financing. Hence, the adoption of this concept would provide greater flexibility and innovation to banks that are currently practicing BBA home financing. In addition, equity financing provides flexibility to the customers to own the house earlier by purchasing more of the bank's share hence reducing the burden of debt financing to the bank. Although the use of actual rental rates is the ideal solution to replace interest rate, the bankers expressed their reservation on its implementation due to differences in locations. Nonetheless, these factors can be looked into by developing a rental index that measures the types of house and locations. Rental rates can also be mutually agreed upon between the customer and bank for a period of time and revised at the end of duration.

The similarity of BBA home financing to *Bai Inah* is the issue in *Shariah* identified by the scholars although only three of the six (50 percent) of the bankers have some idea. This could be because the bankers are not familiar with the *fiqh* (Islamic law) aspects of the concept. Under *Bai Inah*, the bank is engaged in the sale and buys back transaction using predetermined profit rate similar to conventional loan. As the same property is being transacted, the bank does not fulfill the requirement of *iwad* (risk, liability and effort) which are equivalent counter values required by the *Shariah* before a legitimate profit can be earned (Rosly, 2005). The practice of *Bai Inah* does not bring much economic benefit as wealth is only circulated between the two parties involved in the transaction and not to the society as a whole. The issues of *Bai Inah* can be avoided by practicing the DP home financing and this was agreed by both the *Shariah* scholars and bankers. The profit and loss sharing concept also allows greater wealth distribution in the society hence promoting the true spirit of Islam (Ahmad 2000; Siddiqui, 2001; Rosly and Bakar, 2003).

The *Shariah* scholars and bankers agreed that meeting the debt obligation in conventional and BBA home financing is the main factor that caused injustice as bank's profit had been predetermined upfront regardless of the outcome of the project being financed. The customer would be obligated to pay the bank the debt incurred even though the house purchased has not been completed. This raised another issue pertaining to *gharar* (ambiguity) in debt financing whereby a sale was made for houses under construction without asset in existence (Razali, 2007). This is not allowed in Islam.

As BBA home financing is essentially a debt product, there are several drawbacks such as capitalization of profit in the principal sum and fixed selling price. As can be seen in the landmark case of Affin Bank Berhad versus Zulkifli Ahmad (2005), the bank claimed the total selling price when the customer defaulted without providing a rebate. The rigidity of the sales contract has also made it uncompetitive and poses a burden to the customers. Thus, as an alternative, *Shariah* scholars and bankers viewed that there is greater flexibility in DP home financing as the bank does not charge its profit upfront. Due to this flexibility, the customers' outstanding balance at any point in time always reflects the remaining equity that belongs to the bank. This would avoid negative equity as in debt financing where customer's balance outstanding can be higher than the value of the property as seen during the recent US sub prime 2007 financial crisis. The flexibility in owning the share also enables the customer to own the property earlier by redeeming more of the bank's share which is not available in BBA where the customer has a debt obligation at the beginning.

In summary, the analysis of the opinions of the *Shariah* scholars and bankers supported the need to implement DP home financing as an alternative to BBA home financing as its profit sharing concept is more flexible compared to debt financing. The concept further reflects the application of the principles in *Maqasid Shariah* that promotes public interest and prevents hardship to individuals and society (Al Ghazali, 1937).

6.0 Conclusion and contribution of research

This research provided empirical evidences on perceptions of *Shariah* scholars and bankers based on four themes namely concept used, method of computation and pricing, *Shariah* compliance, justice and equality, which are salient features of the BBA and DP home financing products. Theoretically, the study strengthens the knowledge, concept and assumption of debt and equity obtained from expert opinions and views of *Shariah* scholars and bankers, extending the body of knowledge.

Practically, this study serves as a useful guideline for Islamic banks to develop their products and services. It also benefits regulators and policy makers in highlighting issues in home financing and the address existing limitations of the equity framework for Islamic financial institutions. Although BBA home financing has been established for the past 26 years, findings in this research indicated that product features in DP home financing are competitive and *Shariah* - compliant which can be used to attract customers through product innovation. The departure from debt financing is timely as the local finance is becoming integrated into the international financial system. Hence, there is a need to conform to the requisite *Shariah* principles to preserve the resilience of Islamic financial transactions. This would also address the consequences of the global financial crisis by avoiding transactions that are based on *riba* (usury), *gharar* (uncertainty) and *maisir* (speculation). Nonetheless, the actual implementation of DP home financing is a challenge for bankers which require a paradigm shift from their present role as traditional financiers.

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