Sukuk Murabahah Under Malaysian Plural Legal System

Asma Hakimah Abdul Halim¹, Ruzian Markom¹

¹Faculty of Law, Universiti Kebangsaan Malaysia 43600 Bandar Baru Bangi, Selangor, Malaysia
Email: asmahakim.ah@gmail.com

Abstract. Murabahah Sukuk is one of the prevalent type of sukuk issuances in Malaysia. An IIFM 5th report shows that the issuance of murabahah sukuk as at end of June 2015 is only at 48%. Despite the huge issuance numbers of these sukuk in 2013 that reach up to 75%, the issuance based on this structure of contract has decreased. The reduction is due to several issues such as different ruling inherent from the ‘inter-madhhabic conflict’, the issue of conflict of laws and substance over the form issue. For the purpose of this paper, the issue of differences between AAOIFI ruling and Malaysian ruling inherent from inter-madhhabic conflict will be highlighted with regards to the issue of bay’ dayn. Under the Malaysian regulations, the structuring, issuance, and investment in murabahah sukuk must comply with the applicable shari’ah principles and Malaysian laws. This qualitative legal study was carried out to critically examine and analyse the legal and the shari’ah implications in the issuance, structuring, and investment of murabahah sukuk. The findings of this study are aimed at recommending methods to deal with the issues of legal pluralism in the issuance, structuring, and investment of murabahah sukuk specifically focusing on Malaysia jurisdiction. The suggested approach is the pluralist approach through codification of shari’ah law, standardisation, recognition, and validation.

Keywords: Sukuk; murabahah; legal pluralism.

1. Introduction

This paper investigates the legal and regulatory approaches in dealing with the issues in Murabahah sukuk in Malaysia. This paper highlights the various juristic opinions in determining the validity of the characteristics, as well as the elements and the conditions of the contract. Arguably, the various juristic opinions show different conditions and characteristics pertaining even to the same contract. Hence, the divergent opinions in the juristic rulings are taken into consideration in order to be addressed in current practice.

2. The Meaning of Sukuk Murabahah

This qualitative study identifies the characteristics of murabahah and sukuk based on the views of selected schools of legal thought, namely, Hanafis, Malikis, Shafi’is, Hanbalis, and sometimes, Zahiris. Murabahah derives from the word ‘ribh’, which means ‘increase’ or ‘profit’. According to Malikis, bay’ murabahah is an ‘arrangement’. Murabahah is defined as the selling of a subject matter of the sale with a mark-up price and where the exact amount of the subject matter is known by the buyer. The legality of murabahah is based on verse 2:275: ‘But Allah has permitted trade and forbidden usury …’

Literally, sukuk (plural) is derived from the Arabic word ‘sakka’, which means ‘to strike violently’. It is also known as ‘sakkun’, which refers to a contract, deed, legal instrument, document and investment certificates. It is also referred as the book containing information on business transactions between contracting parties (Mausu’ah Al-Fiqhiyyah). Based on the definition, the applicability of this instrument is wide. ‘Sakk’ is also used as the document to prove the validity in marriage, or the report that contains the confession of the guilty party in court and/or as a transaction instrument in the market. (Mausu’ah Al-Fiqhiyyah). However, the growth in the Islamic Capital Market as one of the structures in the Islamic financial system has observed the use of this term in a more specific yet diversified context. The diversity of the applicability of sukuk in modern days can be traced through the definition given.
3. Regulatory Framework of Sukuk Murabahah

It is important for the regulatory bodies to supervise the smooth running of the financial market. Generally, the governance of sukuk in Malaysia is entrusted to four main bodies namely the Securities Commission (SC), Bursa Malaysia, and the Labuan Offshore Financial Services Authority (LOFSA). There are several statutes, guidelines, and rulings that govern sukuk transactions in Malaysia. The important statute is the Capital Market Services Act 2007 (CMSA). The Guidelines on the Offering of Asset-Backed Securities 2004 (‘ABS Guidelines 2004’) provide quite substantial provisions on the characteristics of the parties, as well as the types of assets and the transactions. However, these Guidelines only provide the general requirements of characteristics of sukuk without specifically classifying them according to the types of contract. For instance, the types of asset to be transacted and the criteria of true sale in sukuk. The Guidelines were improved in 2011, 2012 and 2014 to ensure the validity of the sukuk issued.

Apart from the above, there are several international standards adopted by Malaysian regulators, such as the Accounting and Auditing of Islamic Financial Institutions (AAOIFI) Standards, the International Financial Services Board (IFSB) Guidelines, the International Organization of Securities Commission (IOSCO) Objectives and Principles, and the International Islamic Financial Market (IIFM) Standards (The World Bank). The AAOIFI Standards and pronouncements are used as a basis in issuing the Guidelines in Malaysia. In the AAOIFI Standards, the substance of sukuk is drawn in Standard 17, and several related Standards are to be observed by the regulators. The adoption of the AAOIFI Standards, however, is not mandatory.

Further analysis is carried out to the legal framework of Malaysia as it is considered as one of the successful countries in structuring, issuing, and investing in sukuk. There is an in-depth analysis of the private terms and conditions of sukuk, which have been claimed to be based on the stated contracts in order to identify the applicability of these instruments in the Malaysian legal framework. Arguably, there have been changes and modifications to suit commercial and the legal needs, which have led to the re-characterization and shari’ah risk. This is evidenced in the provision in the Guidelines of Sukuk and relevant legal documents referred.

4. The Inter-Madhabic Issues in Sukuk Murabahah

There are several issues between the Standards with the ruling by the Malaysian Shariah Advisory Council (SAC) due to the different interpretation in certain sources as stated above.

4.1. Definition of Murabahah Sukuk

Among the differences are the definition of murabahah sukuk. In details, the Guidelines on Sukuk define murabahah sukuk as ‘certificates of equal value evidencing the certificate holder’s undivided ownership of the asset, including the rights to the receivables arising from the underlying contract’ [9]. In contrast, AAOIFI defined Murabahah sukuk as murabahah certificates that refer to ‘certificates of equal value issued for the purpose of financing the purchase goods through Murabahah so that the certificate holders become the owners of Murabahah commodity’ (AAOIFI, No.17). The definition of murabahah sukuk given by the AAOIFI does not highlight the aspect of mark-up profit. However, the classical juristic definition of murabahah contract is buy and sale transaction with the disclosure of mark-up profit. Therefore, the definition of murabahah in the Guidelines 2014 and the AAOIFI Standard suggests a similarity with the definition agreed by the classical jurists. The murabahah sukuk, therefore, evidence the ownership of the parties towards the underlying asset purchased by them through the purchase of sukuk.

4.2. The Issues of Bay’ Dayn and Re-characterisation of Sukuk Murabahah

The issues in murabahah sukuk include the issues of bay’ dayn and the re-characterisation of
the contract. The conditions stated in the contract suggest that the underlying assets may comprise receivables. Therefore, it constitutes the selling of debt. *Dayn* in Arabic means ‘debt’ (Al Fared Dictionary). Technically, this transaction refers to the sale and the purchase of a debt. There are no disagreements on the permissibility of selling the debt to the debtor. (MD Bakar and Engku Rabeah, 2008). However, there are disagreements over the selling of debt to a third party, as further discussed in the following section. (Bakar & Engku Rabeah, 2008). Principally, the sale of a debt for a debt is prohibited. The prohibition is stated based on the hadiths of the Prophet on ‘bay al kali’ bil kali’. However, Al-Darir criticised the reliability of these two hadiths [10]. He claimed that the fuqaha’ has ruled that these two hadiths are essentially weak. However, Al-Darir does not comment on the hadith itself. He based his assertion on previous views stating that these two hadiths are weak. Therefore, the issue of selling a debt is still open to *ijtihad*.

In terms of the selling of debt, it is stated in the agreement that the MTNs may be offered, sold, or transferred. The selling of debt is approved by Muslim jurists if the debt is an established debt. However, the AAOIFI Standard ruled that it is not permissible to trade murabahah certificates after delivery of the murabahah commodity to the buyer (AAOIFI Shariah Standard No 17/5/2/1/5). Nevertheless, trading of murabahah certificates is permissible after purchasing the murabahah commodity and before selling it to the buyer. (AAOIFI Shariah Standard No 17/5/2/1/5).

The differences between the Malaysian laws and the AAOIFI Standard are that, under the Malaysian laws, the requirement for trading sukuk in the secondary market is not subject to the delivery taking place before the sale to the buyer. This is because Malaysia recognises the concept of a financial asset involving receivables as the underlying assets to be securitised. (SC Malaysia) while the AAOIFI Standard emphasised the existence of the real tangible assets or property as the subject matter underlying sukuk to make it permissible to be traded. These differences are due to the different interpretations in Islamic law. However, it should be understood that the ruling is according to the situation in that particular place. The ruling on permissibility of a financial asset in the Malaysian market is justified based on the need in those particular circumstances (ERE Ali, 2008). In this situation, the maslahah (benefit) is taken into account in order to facilitate the economic growth in the Malaysian market (SC, Malaysia).

The differences could lead to the issue of re-characterisation and raise the issue of the risk of non-compliance with *shari’ah* (‘*shari’ah* risk’)(IFSB) Re-characterisation is where the named contract does not represent the contract itself when examining the substance. Therefore, the judge will re-characterise the contract into another form of contract. The risk is that, in some situations, the instrument could be re-characterised to a conventional instrument. Some commentators are of the view that the assimilation with the conventional instrument could lead to *shari’ah* risk, which is one of the risks highlighted by the IFSB in the operation of Islamic financial instruments. (IFSB)

5. Adapting Legal Pluralism in Harmonization of Laws

The interaction of different rulings and later suit into the context, indicates the existence of legal pluralism and how the harmonization could be reached. Legal pluralism, as Berman asserted, is ‘… the existence of various “hybrid legal spaces”’, which include ‘more than one legal, or quasi legal, regime occupying the same social field’. Berman also noted that legal pluralism has its advantage in ‘exploring [a] myriad of ways that overlap legal systems to interact with each other and [observing] that the very existence of multiple systems can at times create openings for contestation, resistance,

---

1. باب الخلاف بين عبد الله بن عبيد الهيك/ن عن ابن عمر: أن النبي صلى الله عليه وسلم نهى عن بيع الكالئ بالكالئ، عن رافع بن خديج أنه نهى صلى الله عليه وسلم نهى عن بيع الكالئ بالكالئ. These two hadiths are considered as weak hadith by Al-Darir based on the opinion of previous fuqaha’. However, he does not specifically mention the fuqaha’ who classify these two hadith as weak hadith. Further, he advocates that the weakness of these two hadith does not make the sale of debt permissible ab initio; rather, it is debatable and requires scrutinisation according to the view of various fuqaha’ as highlighted in the discussion: Al-Darir, (n 178).
and creative adaptation. This is the creativity for the regulator or the legislator in a country to create a positive interaction between the legal systems to facilitate the transaction process. The creative adaptation stated in this opinion also has a basis in Islamic legal discourse.

In the Qur’an 5:48 Allah SWT states:

“We have sent down to you the Book with truth, confirming the Book before it, and a protector for it. So, judge between them according to what Allah has sent down, and do not follow their desire against the truth that has come to you. For each of you We have made a law and a method. Had Allah willed, He would have made a single community of people, but (He did not), so that He may test you in what He has given to you.”

Elsewhere, Allah states:

“O you who believe, obey Allah and obey the Messenger and those in authority among you. Then if you quarrel about something, revert it back to Allah and the Messenger, if you believe in Allah and the Last Day. That is good and the best at the end.”

Usmani explains this reference to the Qur’an and Sunnah as the final authority in dispute settlement [14]. Based on this, it should be noted that Shariah should be adhered to and laws that do not contradict Shariah can be applied.

During his time, The Prophet (pbuh) tried adopting other laws in order to preserve justice. As mentioned by Maulana Fazlur Rahman:

“The Holy Prophet used to administer justice according to the law to which the complainant belonged. Once a Christian of the Banu Quraiza tribe was killed by a Christian of the Banu Nazir tribe. In a complaint before the Prophet, he enforced the law according to the Torah “A life for a life.” (Karim, 2006:252)

Islam is flexible in addressing various legal and societal changes. With the aim at preserving justice, Islamic law is revealed to mankind in a very gradual and subtle manner. The higher objectives, as outlined by Imam Ghazali and later arranged by Imam Al-Shatibi, are to preserve the religion, life, mind, progeny and wealth of mankind. With the flexibility and ‘ever enduring’ nature of this religion, Ramadan is right to justify on ‘the harmonization of the law with the nature whereby he stated with quoting the relevant verse in the Qur’an explaining the same:

That is what many verses in the Qur’an recall: ‘They ask you [the Messenger] what is lawful [permitted to them (uhilla lahum) say: all things good and pure (at-tayyibat) are lawful to you. (..) This day, all things good and pure are made lawful to you.”(Al-Qur’an 5:5) The lawful naturally corresponds to what is good and nature offers itself as the essential and primary space of what is good and right, pleasant, and permitted.”

This indirectly suggests the pluralist approach as a flexible approach in dealing with these issues. In the context of Islamic law, this approach recognizes various other laws as long as they do not contradict Shariah. In contrast with Berman and Griffith, the concept of pluralism is upheld though with the recognition of the sovereignty of a particular system. Therefore, it is pertinent to highlight that other systems of law could be accepted and incorporated as long as they are not against Shariah. This is based on the maxim that ‘the origin of something is permissible unless there is evidence on its non-permissibility’(Al-Shafi’i, 1983:75). This analysis is taken based on the context of mu’amalah itself. Therefore, the ruling governing mu’amalah is established as ‘the origin of something being permissible unless there is the evidence of its prohibition’. Other ruling can be accepted as long as they do not contradict Shariah. With regards to different paradigms by Malaysian regulators, in relation to pluralist approach, Nathif J. Adams and Abdul Kader Thomas believed that the ‘transferable of paradigm’ from Malaysia could not be transferred to the Middle East due to the ‘differences in Fiqh opinion’ about trading receivables.
Therefore, effort from ‘stakeholders’ is needed to ensure that ‘standardization in Sukuk market’ could be materialized (Adams & Thomas, 2004:104). The process of harmonisation of laws is through the methodology called takhayyur (the eclectic expedient), whereby the practice is through the selection of some doctrines in the opinions of various madhhab in Islamic legal thoughts and those codified in the legislation. A general framework of harmonisation approach for solutions of several sukuk issues in this study is highlighted. It is deemed that harmonisation through a pluralist approach, such as recognition and validation, facilitates the viability of the recommended solutions. This rule could become the guidance to highlight the importance in the application of a certain ruling over another, such as the ruling that a ‘financial asset’ is to be recognised as an asset that can be traded like any other valuable asset (SAC Resolution, 2009).

Furthermore, recognition of a ruling or fatwa can be made by an authority even if that ruling or fatwa is not properly codified. Recognition of a sukuk ruling by the industrial players is vital for its successful implementation. By recognising the practice or the ruling, the contracting parties may contribute substantially towards the further development of Islamic finance. In addition, acceptability of certain practice could also be made through the rule of validation. Validation of the ruling should take place to strengthen the specified transaction according to shari‘ah. On the other hand, in English law, validity is the criteria that should be determined by the court or tribunal of competent jurisdiction. The law confers the jurisdiction upon the judge, who is appointed by the state in accordance with law (Goode, Kronke & McKendrick, 2007).

6. Conclusion

In conclusion, Malaysia has advanced significantly in the establishment of a legal infrastructure for the growth of the sukuk market. Various Guidelines and rulings have been issued and enforced through several statutes that provide the criteria for sukuk, which, in major aspects, suggest compliance with shari‘ah. Guidelines to deal with substances of sukuk contract and changes in contracts issues are progressing under the Sukuk Guidelines issued by the Securities Commission. Further, the lacuna in the Malaysian laws are also being substituted by several relevant provisions in the AAOIFI Standard, the IFSB Guiding Principles, the IOSCO Objectives and Principles, and the IIFM Standard. Evidently, it has been a pluralist approach, either explicitly or implicitly, that inform the endeavour to develop the sukuk legal framework that comply with the shari‘ah and the Malaysian laws on commercial matters. The approach has been applied effectively in dealing with issues of shari‘ah risk and sukuk re-characterisation, particularly the dispute resolution process, as witnessed in a number of cases. The approach has contributed towards a standardisation of the rulings and acceptability of certain rulings to accommodate the current needs as per the laws codified and enforced. The next level is to further refine, validate and recognise the pluralist approach for a global shari‘ah framework of standards and practices for positive growth of sukuk instruments.

7. References

[1] Baalbaki. Al-Mawrid. Dar El-‘Ilm Lil-Malayin; 1995. 698 p.
[2] Al-Zuhaily W. Financial Transactions in Islamic Jurisprudence (2nd edn, MA El Gamal tr, revised by MS Eissa, Dar Al-Fikr. 2007.
[3] Al-Quduri, A.A.; Ibn Jaafar AM. Mukhtasar Al-Quduri. Beirut: Dar al-Kutub Al-‘Ilmiyyah; 1997.
[4] Al-Khudrawi D. A Dictionary of Islamic Terms 241. (2nd ed. al-Yamamah; 2002. 241 p.
[5] R W. Overview of the Sukuk Market’ in NJ Adam and A Thomas (eds), Islamic Bonds: Your Guide to Issuing, Structuring and Investing in Sukuk. London: Euromoney Books; 2004.
[6] Black BS. The Legal and Institutional Preconditions for Strong Securities Markets’ 48. UCLA L Rev. 2001;48:781, 783.
[7] Holden K. Islamic Finance: “Legal Hypocrisy” Moot Point, Problematic Future Bigger Concern. BU Intl LJ. 2007;25:363.

[8] Ros Aniza Mohd Shariff; Abdul Rahim Abdul Rahman. An Exploratory Study of Ijarah Accounting Practices in Malaysian Financial Institutions’. Int J Islam Financ Serv. 5(3).

[9] Sukuk Guidelines. 2014.

[10] AMA Al-Darir. Al-Gharar Wa- Atharuhu Fil ‘Uqud Fi Al-Fiqh Al-Islami. Khourtum University; 1967.

[11] MM Al-Ghazali. Al-Wasit fi Al-Madhhab. Dar As-Salam; 1997.

[12] A A-R. Imam Al-Shatibi’s Theory of the Higher Objectives and Intents of Islamic Law (The International Institute of Islamic Thought 2005).

[13] Berman S. Global Legal Pluralism : Articles and Working Papers. (8). Report No.: 71.

[14] Usmani. The Meanings of the Noble Qur’an, Vol. I. 2006.

[15] T R. Radical Reform: Islamic Ethics and Liberation. UOP; 2009.

[16] AA Hassan. ‘Ijtihad dan Peranannya dalam Pengharmonian Pengamalan Undang-undang Syariah di Dunia Islam. J Syariah. 2007;15(2):1–24.