



# ISLAMIC AND NON-ISLAMIC FINANCE IN CONTEMPORARY PERSPECTIVE



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# Islamic Finance : An Overview



- In a nutshell, Islamic finance is all financial activities which are conducted according to principles which are compliant to Islam i.e. Shari'ah.
- The Islamic way of value judgment is based on the presumption of permissibility unless proven otherwise.
- Thus, Islamic tends to prescribe what is prohibited instead of what is allowed as permissible items/conducts are not exhaustive.
- To conclude, Islamic finance is prima-facie free from prohibitive list as prescribed clearly by the law of Islam.



# Salient Features Of Islamic Finance



- Interest (*riba*)-free.
- Uncertainty or lack-of-knowledge (*gharar*)-free
- Gambling (*maysir*)-free.
- Not involved in selling or leasing or partnership in something which is impure or not halal e.g. liquor, drug, non-halal food (look at DJIM's prohibitive list)
- Not in direct conflict with “established” Shari’ah principles in commerce and finance e.g. providing guarantee in Islamic equity instruments.



## Why This Prohibitive List Is So Important?



- Interest / *riba* prohibition: Because money in Islam is just a medium of exchange. It cannot earn more money by itself without putting it into real productive actions such as sale, lease, investment. Interest is based on the premise “money is a commodity”.
- Lack of knowledge / *gharar* prohibition: To avoid any dispute due to unfairness in dealing caused by the lack of knowledge. This covers fraud, misrepresentation, undue influence, duress, non-disclosure of material facts, etc.



## Why This Prohibitive List Is So Important?



- Gambling / *Maysir* prohibition: It is a zero-sum game wherein it just transfers the wealth not creating new wealth.
- Selling or leasing or investment in non-halal items: more of religious and ethical value consideration or public policy.
- Compliant to leading and established maxims and principles: To ensure every contract behaves in its proper context. This does not negate freedom of contract.



## Who Is Responsible To Ensure This Compliance?



- The management of any given financial institution, be it a bank, an insurance operator, a fund manager, a stock broker, etc.
- Normally, the management relies on the expertise of the Shari'ah Board / Advisor to advise and monitor the compliance aspect.
- Otherwise, there could be reputational risk or regulatory risk, as the case may.





# Islamic Finance: Theory And Practice



- Interest-free banking.
- Underlying assets and services in all sale and lease contracts.
- Profit and loss sharing concept in banking.
- New legal relations and legal consequences
  - (a) Stamp Duty Act.
  - (b) Real Property Gains Tax.
  - (c) Other relevant acts.
- The establishment of Shari'ah Advisory / Supervisory Board.



# Common Values To Both Islamic And Non-Islamic Finance



- Statutory Requirements.
- Prudential Standards – BASEL II and Exposure Draft(s) of Islamic Financial Services Board
  - (a) Risk Management.
  - (b) Corporate Governance.
  - (c) Capital Adequacy.
  - (d) Market Discipline and Transparency.
  - (e) Market Supervision.
- Global Legal framework.





# Unique Feature Of Islamic Finance



- The function of money in Islam
  - (a) Money lending.
  - (b) Theory of *riba* / interest / usury.
  - (c) How money could earn more money?
  - (d) Manifestations of Islamic deposit and financing.



# Unique Feature Of Islamic Finance



- Nature of valid assets and services in Islamic finance.
  - (a) Certain – saleable / leaseable.
  - (b) Pure and clean (halal).
  - (c) Exhaustive list of prohibited assets /services?



# New Development In Islamic Finance



- Derivatives instruments
  - (a) Forward FOREX
  - (b) Islamic Profit Rate Swap.
  - (c) Future Commodity Market
  
- Stock screening criteria
  - (a) KLSI
  - (b) DJIM
  - (c) FTSE



# New Development In Islamic Finance



- Islamic fixed income instruments
  - (a) *Murabahah* Commodity Fund.
  - (b) Capital Protected Fund.
  - (c) *Sukuk al-Ijarah*.
  - (d) *Sukuk al-salam*.
- Harmonisation and standardisation of Shari'ah views.



# Comparative Analysis Of Islamic And Non-Islamic Finance



- Function of money and real economic sector (wealth creation).
- Risk management.
- Taxation.
- Ethical consideration (SRI)
- Prudential standards.
- Global industry?
- Conclusion: Same Destination but Different Route of Journey



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