

Management of Community Perception Issues to Ceiling and Floating Rates on Islamic Home Financing Based on Maqasid Shariah Concept

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Abstract

The purpose of this paper is to study the method of profit-taking from the perspective of maqasid al-Shariah (objectives of Islamic law). Then, this study will analyse the practice of profit-taking in Islamic housing financing products based on bay' bithaman ajil (BBA) and tawarruq munazzam contracts in selected banks. This study is important to implement is to manage the perception of Islamic banking customers on the issue of ceiling and floating rates. The methodology of this study is qualitative, where the data is collected through library research and field study. Library research is done by examining fiqh muamalat books, related articles, and circulars. Meanwhile, the field study was conducted in an unstructured interview method with two Shariah officers from two banks offering Islamic housing financing products based on BBA and tawarruq munazzam contracts. The results show that the imposition of two rates in Islamic housing financing based on BBA and tawarruq munazzam contracts has led to confusion in the community. Indirectly, it has given rise to a negative perception of Islamic banking which imposes high and oppressive prices. Also, there are some records from the court cases as well as the weakness of the bank's SOP (standard operating procedure) in giving rebates that led to the endless public's negative perception of Islamic banking. However, Malaysian National Bank has implemented some crucial initiatives to curb confusion by requiring Islamic banks to include ibra' (rebate) clauses and complete calculations into contracts which were previously applied at the discretion of the bank. Thus, this study suggests the imposition of ceiling prices to be improved based on the amortisation formula in accordance with the concepts of maqasid al-Shariah, wasatiyyah and ihsan, so that the perception of society can be managed well. This study has a limit that only focuses on the practice of taking profit on two Islamic housing financing products and obtaining field data

from two respondents and two banks. For future study, it is suggested for researcher to focus on public's perspectives and their perceptions of profit-taking by Islamic banks.

Keywords: Community Perception, Ceiling Rate, Floating Rate, Rebate, Maqasid Al-Shariah

Introduction

In today's world, the rapid progress and development of Islamic finance and banking industry can be observed in every part of the world. Consequently, this has challenged the position of conventional banking industry, even though it has been firmly established for a long period of time. According to Abdullah (2012), the response towards the financial and Islamic banking industry does not only come from Muslims but also non-Muslims. Accordingly, the increase of reactions is clearly reflected by various factors inherent in Islamic finance and banking systems such as ethical considerations, social welfare, and real economic activities (Dakian, 2005; Hasan, 2016). Therefore, as pointed out by Aioanei (2007), it is not surprising that the bid also appears in high demand within western countries.

However, previous surveys show that the operation of Islamic institutions and banking differs from the above characteristics. This can be seen based on the court case that reported Islamic banking products as expensive and related to the element of oppression (Mohamad & Trakic, 2013). In the case of Arab-Malaysian Bank Berhad v Silver Concept Sdn. Bhd. [2008] 6 MLJ 295 and [2006] 8 CLJ 9, the judge stated that the profit rate based on the *bay' bi thaman ajil* (BBA) contract applied by the bank was burdensome (binti Kunhibava, 2017). Similarly, the decision of the High Court regarding the case of Malayan Banking Bhd v Ya'kup Oje & Anor [2007] 6 MLJ 389 stated that the amount of repayment in the BBA contract was excessive and imbalanced compared to the conventional banking (Salleh et al., 2017).

The decision of this court case has its basis when the bank sets a high ceiling price to the customer which is up to 10.6%, by referring to the product description document by Public Islamic Bank (2020). Although the rate charged during the financing period is at the current rate which is the BR rate mixed with the bank's profit rate, but the lower rate is a rebate given by the bank, where it is at the discretion of the bank to give it or not (Khir, 2016). In the name of a rebate, it has led to a lot of disputes between the bank and the customer. When a case of default is brought in court, then the bank will demand the full payment according to the ceiling price set at the beginning of the contract. According to the Research Academy for Islamic Finance, between 2003 and the end of 2009, majority of cases in court regarding Islamic banking and their clients were due to the *ibra'* issue (Dusuki et al., 2010). This can be referred to in the case of Affin Bank Bhd v. Zulkifli bin Abdullah [2006] MLJ 67.

Similarly, in the study of Mohamad and Trakic (2013), it stated the weakness of Islamic banking in applying rebates, where there is no specific rebate calculation given to customers as well as negative perceptions among judges who discuss cases of dispute between Islamic banks and customers when the Islamic banks claimed the whole amount from defaulted customers. Thus, there are several previous studies that criticise the BBA contract as in the study of Aris et al (2012) who stated that the contract as a reflection of conventional bank products. Similarly, in the study of Azli (2011), he emphasised multiplied profit as may lead to an invalid contract as a result of oppression.

Based on these cases, BNM (2013) played a role by providing a new SOP on the issuance of rebates; Islamic banks need to include *ibra'* clause and complete calculation in the financing contract. Although the new SOP is not in line with the views of the majority of Islamic scholars (Laldin et al., 2012) and IIFA (1992), this improvement is needed in order to take care of customer problems. Although the SOP on the two rate methods mentioned by

Islamic banking in taking profit has been streamlined, but the negative perception of society about Islamic banking still thickens by saying it as expensive and oppressive. This is as stated by the Malaysian Muslim Consumers Association (PPIM) through their video interview and through an article entitled "PPIM plotted bank sells the name 'Islamic Banking' for profit" which also gets support from the public (PPIM, 2020b; PPIM, 2012). This can be seen when the result of sharing the video has produced more than a thousand Facebook users who sign agree (PPIM, 2020a).

In fact, the question of price on a banking product has received significant attention among consumers. This is based on several previous studies which stated that there is a significant relationship between customer acceptance and price rates on Islamic banking products. This is as stated in the study of Amin et al., (2011), where there are three determinants that significant in influencing the intention of using Islamic personal financing, namely attitude, social influence and pricing of Islamic personal financing. Similarly, the study of Ahmed et al. (2019) shows that the price rate is a determinant of the customer's desire to subscribe to a product. Also, the empirical findings made by Rama (2020) reveal that customers experienced more price expectations in their banking decision-making process. The number and complexity of price expectations depend primarily on the customers' interest, particularly on price transparency, relative price, and price-quality ratio, and these dimensions affect the level of satisfaction and behavioural intention. Islamic banking customers in Indonesia are highly aware of price transparency, by having "relative thinking" on price differences and put price-quality ratio in their assessment. Similar findings were also obtained in the study of Wahyuni (2012); Rustam et al (2011); Thambiah et al (2011); and Amin (2008). Based on this significant connection, if there are parties who question the price of a banking product, it will get close attention from the public.

Thus, based on these problems, this study will focus on the discussion on profit-taking according to *maqasid al-Shariah*. According to Shinkafi et al (2017), the relationship between profit-taking and *maqasid Shariah* has received limited scholarly attention. Then, the researchers will analyse the profit-taking in Islamic housing financing based on BBA, *tawarruq munazzam* contract based on the concept built and suggest improvements. The *tawarruq* contract is also included as it has significant similarities with the BBA contract in terms of charging two sales price rates to the customer. The researchers will also study consumer perceptions on the price rates charged by banks in Islamic housing financing based on BBA and *tawarruq* contracts.

Literature Review

Profit-Taking from the Muamalat Perspectives

Profit means a surplus or additional gain on something (Malik, n.d.). Specifically, it is described as extra revenue which obtained by an enterprise, business, or other commercial activities from the actual capital and other related expenses (Dewan, 2010). Meanwhile, the additional increase is also explained as the return is acquired from a business. Furthermore, it should be noted that profit-income is considered as the success gained by an entrepreneur upon his endeavour in a business transaction or commercial activities. Conceptually, Islam permits profit-taking (Qur'an, 2: 16) and further urges Muslims to seek additional capital from business ventures and obtain benefit from an exchange of goods. In fact, as pointed out by Shawkani (1993), the Messenger of Allah (PBUH) encourages Muslims to work on their own hands such as collecting woods and selling them to generate income.

Regarding this matter, it should be understood that profits are the bestowal of

sustenance from Allah SWT; hence, the more the sustenance, the more benefit will be received by the people. Generally, income or profit can be used for the purpose of supporting families, purchasing goods, satisfying needs, and assisting people. In this term, sustenance and profit can be referred to the same meaning, as both are significantly described as the surplus that earned from the endeavour undertaken. Sharbini (1997) states that profit is indeed a goal of business activity, which can be obtained through the exchange of goods with cash, or goods with goods. The same view is also expressed by Khaldun (1958), by stating selling and buying activity as an endeavour to gain profit or expand a person's assets. However, it is important to emphasise that Islam prohibits its believers from making profits based on illegal transactions. According to Idris (2002), four elements that are prohibited in profit-taking are usury transactions, *ihtikar* (monopoly), *gharar* (uncertainty), and *ghabn fahisy* (fraud).

Meanwhile, Yahaya (1985) states that profit in terms of economics is defined as a balance obtained by a manufacturer once he or she has satisfied with all the costs of expenditure in the trade activity. The balance is a surplus of the actual capital possessed by an individual, thus indicating an increase in the amount of property. According to Tabari (1980), business persons would gain profit when they change their commodity with more valuable commodities. On the contrary, they will suffer losses if they change their commodity to a cheaper commodity. In other words, an increase in the returns obtained from the original price of capital is known as profit.

In general, profit-taking can occur in loans as well as buying and selling. In any case, the seller has the rights to gain profits; however, rights in Islam are bounded by certain ethics, morals, and restrictions. Specifically, an extra charge from loan activity may be regarded as profit to the lender, but it is known as usury in Islam which is prohibited by *Shariah*. On a similar note, an extra charge on goods that sold is also considered as the permissible profit according to the *Shariah*. In short, *Shariah* permits profits from purchasing activities rather than through lending that involves usury.

Regarding this matter, El-Islamy (2014) asserted that Islamic *muamalat* system does not allow the economy to be based on the principle of usury or profit-taking on lending or act as the foundation of overall economic activities. Meanwhile, it should be understood that the fundamentals of Islamic economics discourage the use of lending as a means of economic development. Hence, the function of a loan should be aimed for charity instead of commercial purposes. In fact, when the Messenger of Allah was asked "*what is the best income?*", the Prophet Muhammad (PBUH) replied that "*the income of a person from his manual labour and every authorised trade*". To be precise, this answer is in line with the word of Allah in Surah al-Baqarah, verses 275, 278, and 279, which legalise trade and prohibit usury (Qur'an, 3: 130). The principle of justice and balance in the *muamalat* and Islamic economy restricts extreme profits that are often known as tyrannical and oppressive.

Undoubtedly, Islam rejects profits that been achieved through unlawful activities such as usury or uncertainty. Likewise, being unaccountable and despotic by hoaxing the market price through price manipulation are also prohibited (Rawwas, 2002). Overall, it can be concluded that *Shariah* emphasises on fairness and accountability in *muamalat* as a form of social responsibility between a merchant and consumer (Qur'an, 4: 58).

The Rate of Profit-Taking in Islamic Perspective

Fundamentally, profit-taking in trading is a necessity that is based on the proposition of the Qur'an, hadith, and consensus of Muslim scholars. In the Qur'an, Allah SWT says: "*O you who believe! Eat not up to your property among yourselves in vanities: but let there be amongst*

you traffic and trade by mutual good-will" (Qur'an, 4: 29). Specifically, this verse suggests that it is lawful in Islam to take the property of others through profit or exchange of goods in a transaction of sale (Razi, 1420H). Shawkani (1993) further highlighted the necessity of taking profit to be mutually agreed (*ijma'*) by Islamic scholars.

Meanwhile, a hadith hint narrated that the Prophet SAW gave 'Urwah one dinar to buy a goat, but Urwah used it to buy two goats. Next, he sold one of the goats with the price of one dinar. Thus, he came back bringing one goat and one dinar with him. The Prophet -peace and prayer of Allah be upon him- then prayed for the blessing for him (Bukhari, 1422H). Accordingly, the hadith indicates that profit is among the sustenance provided by Allah, which subsequently suggests Islam as a religion that does not limit profit-taking in trading.

In terms of profitability limits under Muslim scholar consensus, Majma' Fiqh al-Islami, which published in 1988 opined that there are no certain limits set on profit-taking in business according to the principles of *Shariah*. Notwithstanding the fact, the government has the power to set certain price and profit in the event of price imbalance in the market that suppresses people with unreasonable prices as a result of monopolies, conspiracies, excessive prices, and fraud in the economic activities. In this case, the government is allowed to intervene in order to create justice and equilibrium. On another note, Islamic scholars also claimed the nature of not being excessive in making a profit because the Prophet (PBUH) encourages his people to conduct trade with good manners, as he said: "*Allah SWT blesses a generous servant in business*" (Ibn Majah, 2009). Saudi Fatwa Institute (2018) also encourages the ease of dealing with people in buying and selling, or in other words, taking a small profit and helping each other in a good course.

According to Abu Hanifah, extreme profits refer to those that surpass the market prices (Malik, n.d.). Hence, its occurrence will cause the customers to face the state of oppression, tyranny, and unfairness. Accordingly, every business transaction must be fair and equitable because the principle of *muamalat* requires the pleasure of Allah SWT. Therefore, it is important to ensure that it is parallel with the human needs while attaining the purpose of receiving the blessings of Allah SWT.

Profit According to Maqasid Shariah, Wasatiyyah, and Ihsan

Maqasid Shariah is an important concept that can be taken into account while managing the profit rate in a transaction. Generally, *maqasid shariah* is a *shariah*-defined goal that needs to be achieved for the benefits of humankind, including for the purpose of observing religious, soul, intellectual, offspring and property, as well as preventing any harm towards humans (Ghazali, 1997). Shatibi (1997) highlighted three levels of goodness (*maslahat*) that need to be protected by maintaining the followings: essential needs (*daruriyyat*), complementary needs (*hajiyyat*), and embellishment needs (*tahsiniyyat*). In particular, the requirements of *Daruriyyat* involve the preservation of five fundamental needs. Hence, the absence of those elements will cause harm and destruction towards individuals and society (Alam et al., 2015). Meanwhile, the necessity of *hajiyyat* refers to a complementary factor that facilitates life's affairs. Accordingly, life will be difficult without *hajiyyat* despite the absence of elements that can lead to destruction. Finally, *tahsiniyyat* is an embellishment requirement that is based on the tendency of manners and custom in society. However, its absence will not lead to destruction and difficulties in the life of society as it is only posited as a side requirement (Rahman et al., 2017).

Regarding this matter, the elaboration of *maqasid shariah* clearly suggests that profit-taking method should consider the position of *daruriyyat*, *hajiyyat*, or *tahsiniyyat*. However, a

profit that obtained from transactions involving the categories of *daruriyyat* is certainly different from the transactions involving the *hajiyyat* category. For example, the *maqasid* preserves the life of humans in the category of *daruriyyat*, which involves the necessities of a human being in their daily lives such as food, drinks, medicine, clothing, and residence. Therefore, this area of *maqasid syariah* should be given more attention by the government (Saleh et al., 2012). Overall, it can be concluded that every profit made in the category of transactions must provide benefits and welfare to both buyers and sellers at par among them.

Meanwhile, *wasatiyyah* in a transaction can be understood based on the term that originates from the word “*wasat*”, which specifically provides the meaning of average or middle (Ismail et al., 2017). According to Khambali@Hambali et al. (2017), *wasatiyyah* refers to every matter that is in the middle, or in other words, none should be excessive (extreme) or deficient. Likewise, Qaradawi (1997) defines *wasatiyyah* as an element that deserves a proper step and can be achieved by a middle path approach in order to avoid any extremity. Meanwhile, Razi (1420H) interpreted the word “*wasat*” as justice, by suggesting the fairness approach as deemed better if it is applied in the middle, balanced, fair, and selected. Furthermore, this concept is not in agreement with the ways of the Jews and Christians who tend to be excessive in all matters. In particular, their method often involves religious and *muamalat* issues such as usury, exaggeration of profits, and trickery which are utterly prohibited (Mazuki et al., 2013). Therefore, this clearly explains the important role of *wasatiyyah* concept in profit-taking to ensure balance and fairness.

Subsequently, *ihsan* can be described as doing things better and in an excellent manner. Meanwhile, *ihsan* in a transaction means to do good, improve affairs, and conduct diligent implementation (Madkur, n.d.). According to Dewan (2010), *ihsan* refers to goodness, virtue, good deeds, and generosity based on the understanding that was excerpted from the Qur’an and al-Hadith (Yusof et al., 2015). In the Qur’an, Allah SWT orders Muslims to do good when it comes to dealing with fellow human beings (Qur’an 4:36). as well as in managing properties (Qur’an 2:195). Moreover, Zuhaili (2011) states that the act of *ihsan* brings a tremendous impact because it creates God’s love for the servant as well as the well-being of human life. In addition, it has also been emphasised that the demand for *ihsan* is present in every matter, particularly in the act of worship, *muamalat*, and morals. Other than the Qur’an, the concept of *ihsan* has also been claimed in the hadith of the Prophet (PBUH) based on the narration that, “*If you must slaughter, slaughter in the best possible manner, sharpen your knife every time before you slaughter but not in front of the animal to be slaughtered. Do not slaughter an animal in the presence of other animals, and feed and rest the animal before slaughter*”. Therefore, it can be understood that goodness must be applied to human relationships by considering how the hadith highlights the importance of being kind to animals.

According to Yusof (2015), the approach of *ihsan* is very important in the field of the economy because Islam demands fellow human beings to help each other in fulfilling their needs. Regarding this matter, it must be noted that it is not only related to the rights of sellers and buyers, but also concerning goodness, virtue, and generosity. Moreover, the fulfilment of the rights of others in the matter of goods is an *ibadah* (worship), particularly in terms of zakat, charity, *infaq*, and *sadaqah*. The whole purpose is to reduce the burden of the public from any form of oppression, thus enabling them to satisfy their needs. According to Qaradawi (2012), the Islamic approach through *ihsan* in profit-taking seems to have a contradiction with the conventional economic system, particularly the capitalist economics. The capitalists tend to consider property as a belonging of the owner, or in other words, an absolute property of the owner. Hence, the other person does not have the right to intervene in possession of the

property. As a result, this has enabled them to have absolute freedom in determining the profit gains without any tolerance by employing any form of transactions as well as ignoring the customers' welfare. Furthermore, the presence of compassion among the capitalists often exists without any *ihسان*. Therefore, when it is more often observed, this attitude is used as a marketing strategy to enhance the image of the property owner or the dealer.

Profit-Taking in the Islamic Banking Institutions

Islamic banking institutions take profits through various financing products according to the contracts offered. In Islamic banking, every transaction made should be carried out clearly in order to avoid the issue of *gharar* (uncertainty) (Lahtasna, 2014). Thus, one of the things that need to be explained in a contract is the overall price of the financing which is fixed throughout the financing period. Therefore, Islamic banking will set a clear price and will not change from the beginning until the end of the financing period. This is because, if there is an increase in the financing period, it will bring usury implications (Ariff & Iqbal, 2011). This is in contrast to conventional banking practices where interest rates are set according to the floating rate which is not fixed and will change according to economic change factors (El-Karanshawy et al., 2015).

However, Islamic banking in Malaysia is subjected to the supervision of Malaysian National Bank (BNM), which regulates the two banking systems in Malaysia, namely Islamic and conventional banking (Asni, 2019). BNM has set the base rate (BR) that must be followed by both systems of the bank. Thus, Islamic banking needs to follow the BR rate set by BNM and the profit rate set by the bank in setting the profit rate in a financing product (BNM, 2018b). References to these rates as a method of determination in profit-taking have caused Islamic banking to be embroiled in the issue of *gharar* i.e. variable and irregular profit rates (Hasan, 2011).

To resolve the floating-rate issue, Islamic banking has offered two rates, namely the ceiling rate and the floating rate in its financing. However, the use of two rates in a financing contract is not in line with *Shariah* because *Shariah* forbids from using two types of prices in one contract. As the matter of fact, Islamic banking sets a fixed selling price according to the ceiling rate, while the floating rate is considered a rebate by the bank to the customer (BNM, 2013). Thus, the profit rate taken by the bank throughout the financing period is based on the floating rate. Although it is subjected to change, it is still below the original financing price. The rebate method used has solved many issues of *Shariah* non-compliance in Islamic banking. In addition, the compliance with BNM rate and Islamic banking competency also offers the same rate with conventional banking (Ishak, 2019a).

As an example of the calculation, by referring to the Islamic home financing based on BBA product description document by Public Islamic Bank (2020), for the financing offered for a house worth RM100,000, the profit rate set by the bank is 10.6%. Therefore, if the financing period is 30 years, then the total payment is RM331,999.20. However, the bank gives a rebate to the customer that is only charging the current EPR rate as a profit rate. Although the EPR rate is variable based on the influence of the economic situation, it is still below the profit rate set at the beginning of the contract (Public Islamic Bank, 2020).

Methodology

Research Design

This study uses a cross-sectional narrative review that using qualitative data collection methods, specifically the semi-structured interviews. Interview methods were used in this

study in order to gain a deeper understanding of the research subject matter (Robertson and Samy, 2015; Gunarathne and Senaratne, 2017).

Narrative research design is a design of inquiry from humanities in which the researcher studies the experiences of individuals and asks those individuals to provide stories about their experiences (Creswell, 2014; Riessman, 2008). According to Creswell (2014), the information is then often retold or re-storied by the researcher into a narrative chronology. In the context of the study, the data from the respondent about his/her experiences and knowledge to get a holistic view of the practice of profit-taking based on housing financing product by the bank were recorded and handwritten by the researchers.

Selecting the respondents, data management and analysis

The researchers used a purposive sampling method in conducting the interview technique by interviewing experienced and knowledgeable respondents about the problems of the study (Etikan, Musa & Alkassim 2016). In this regard, the researchers have interviewed two officers of the *Shariah* secretariat whose representing two banks. Regarding the two banks, one of which offers BBA contract-based products and the other offers *tawarruq munazzam* contract-based products. The respondents were selected because they are directly involved in the development and supply of the products studied. They are also directly involved in providing training and courses to staffs at branch banks, and this indirectly shows that they are well aware of the issues hovering in relation to the products offered. The respondents are among the individuals who know about the practice of contract holistically from the point of view of practice and the problems that arise. The interview session lasted for 50 to 60 minutes.

The interviews were conducted in order to find out the views of the respondents on the method of profit-taking by the banks studied. The unstructured interviews were used to give respondents the freedom to share their experiences on the topic of study. The interviews were recorded through audio recording and manual writing methods in notebooks as additional storage and suggestions. Therefore, if the audio recording is damaged or destroyed, the manual recording is still available for reference. The results of the interviews were then transcribed using a content analysis approach, and this is vital to obtain appropriate themes as suggested by Miles and Huberman (1994). In fact, this method provides a systematic and objective means that makes valid inferences from verbal, visual or written data to describe and quantify specific phenomena (Bengtsson, 2016). As a result, the researcher can find out in depth about the profit taking by the bank under study as well as the problems that arise.

For the profile of the respondents, the officers of the *Shariah* secretariat represent Islamic banks which are fully responsible for the development and supply of Islamic banking products. To protect the information of respondents and banks, the names of respondents and banks have been encrypted. The symbols O1 and O2 represent the officers of the *Shariah* secretariat.

Results

For the purpose of clarity, the result is summarised in the table below, then it is followed by discussion.

No.	Quotations	Themes
1	Regarding the BBA application, O1 stated, <i>“Regarding the application of BBA transaction by the bank, when the customer buys a home asset from the developer through a Sale and Purchase Agreement (S&P) by paying a 10% deposit or advance payment to the</i>	The application of BBA and <i>Tawarruq Munazzam</i> transactions.

	<p><i>developer, the buyer will benefit from ownership of the house. Then, the customer sells the asset purchased from the developer to the bank through the Property Purchase Agreement (PPA) in cash which is also the cost of the house. The bank pays the remaining 90% of the total price to the developer on behalf of the buyer, which results in the bank becoming joint owner. Then, the bank sells the asset to the customer through a Property Sale Agreement (PSA) at a deferred price which includes the cost of the asset with an additional profit margin.”</i></p> <p><i>Regarding the tawarruq application, O2 stated, “Regarding the tawarruq transaction application, it starts with the customer signing the Sale and Purchase Agreement (S&P) with the developer for the purchase of a house. Then, the customer will apply for financing from the bank as financier in the purchase of the house. Then, the bank buys the commodity from broker A, after the bank buys the commodity, then the bank sells it to the customer on debt. Then, the customer delegates the same bank to sell the commodity to broker B in cash. Then, the proceeds from the sale of the commodity are used for the settlement of the house purchased.”</i></p>	
2	<p><i>Regarding the ceiling rate, O1 said, “During the process of the Sale and Purchase Agreement (PSA), to avoid the risk of inflation fluctuations and economic uncertainty, the bank charges a very high selling price of 10.6%. For example, if the value of the house is RM300,000 and the debt period is 35 years, then the total payment to be paid by the customer to the bank is 1,141,396.20 where the total profit earned by the bank is RM841,396.20.”</i></p> <p><i>O2 said, “During the process of selling commodity goods to customers in instalments, the price is according to the ceiling rate of 10.75%. The selling price in instalments according to the high ceiling rate avoids the risk of fluctuations in the current market rate during the financing period. Therefore, if the value of financing desired by the customer is RM350,000 for 35 years, then the total payment to be paid by the customer is RM1,348,729.20 where the total profit earned by the bank is RM998,729.20.”</i></p>	High ceiling rates are charged at the beginning of the financing contract.
3	The rate used in financing is the current market rate as stated by O1,	Although the ceiling rate is charged at the beginning of the

	<p><i>“However, the bank will only charge a floating rate to the customer during the financing period; the floating rate is a rebate given by the bank to the customer. The floating rate refers to the EPR rate, the EPR rate is the result of the BR rate mixed with the bank profit rate. If the BR rate is 2.27% and the profit rate charged by the bank is 0.83%, then the effective profit rate is 3.1%. Therefore, the rebate given in the current instalment payment is 3.1%.”</i></p> <p>O2 said, <i>“However, the bank will give a rebate from the original price to the customer, which is only subject to the EPR rate. The EPR rate is the result of the BR rate mixed with the bank profit rate. If the BR rate is 2.52% and the profit rate charged by the bank is 0.73%, then the effective profit rate is 3.25%. The rebate given in the current instalment payment is 3.25%.”</i></p>	<p>financing, what is taken into account during the financing period is the EPR rate.</p>
4	<p>The reason for using two rates in financing is to avoid the risk of <i>Shariah</i> non-compliance and current market volatility. This is as stated by respondent O1, <i>“The bank needs to use two rates in financing because in Islamic muamalat, the selling price must be determined at the beginning of the financing. If the bank has determined a high price rate at the beginning of the financing, then if there is an increase in the current rate in the middle of the financing period, the bank can still increase the rate against the customer because the financing is still below the maximum ceiling price charged to the customer in early financing. This can avoid the implications of usury. As for the imposition of the rate according to the current rate that is EPR is to follow the current market price and can compete with conventional banks which is termed as rebate.”</i></p> <p>O2 said, <i>“The imposition of two rates is to avoid the risk of inflation in the future. This is because, the long financing period causes economic uncertainty in the future which fluctuates, so it makes the bank set a high ceiling rate during the beginning of financing. Also, in Islamic muamalat rules, the financing price should be determined at the beginning of the financing, if there is a change such as the current price increase during the financing period, it can lead to usury implications. Therefore, the EPR rate charged is a rebate and can</i></p>	<p>The reason for using two rates is to avoid the risk of future economic fluctuations and to avoid <i>Shariah</i> non-compliance when there is a change in the current rate.</p>

	<i>change according to the current market rate as long as it does not exceed the ceiling rate."</i>	
5	Both respondents agreed that the imposition of two rates in financing has to some extent caused confusion in the general public. This is as stated by respondent O1, <i>"The imposition of this ceiling price often leads to confusion for customers because they think that the financing price in effect is according to the ceiling price, while the actual rate charged is according to the EPR rate which is according to the floating rate and it is also used by conventional banks. However, customers are also often confused by the assumption that the rebate is only at the discretion of the bank to be given to the customer as well as assuming that the bank can increase the profit rate at any time. This is because, the customer has agreed to pay to the bank at the ceiling price at the beginning of the contract. We get a lot of information about this confusion and negative perceptions while providing training to the marketing staff at the branch banks."</i>	The imposition of two rates can lead to confusion in society.
6	Both respondents agreed that some people's perceptions of Islamic banking are negative. This is as stated by respondent O1, <i>"This confusion has led to the growing public perception that Islamic banking financing is expensive. Similarly, some say that Islamic banking is oppressive and more expensive than conventional banking. While the perception is not based on real facts."</i>	Society's perception of Islamic banking is negative with the assumption that it is expensive, oppressive, more costly than conventional banks.

Discussion

Although the BBA contract application is increasingly unpopular and the *tawarruq* contract application is the most popular in the Islamic banking industry in Malaysia, but from a practical point of view, the ceiling pricing at the beginning of the contract is the same in both contracts. Based on the findings of the study, banks A and B set a high ceiling price which is almost three times the original financing amount where the rate charged is more than 10% per annum. This is also clearly mentioned in the product document by both banks studied.

Although the ceiling rate is charged at the beginning of the financing, the selling price applied during the financing period is at the EPR or floating rate which is constantly changing according to the current market (Lahsasna, 2014). The fixed ceiling rate is determined at the beginning of the contract in order to avoid the issue of *gharar*, which is considered the principal fundamental prohibition in financial activities (Ariff and Iqbal, 2011). Similarly, if the financing price is set according to the floating rate which is fluctuating, it can also bring usury implications because the financier obtains more than the proper financing rate if the floating rate increases (Khir, 2016).

In addition to avoiding the issue of *Shariah* non-compliance, the imposition of two rates is to compete with conventional banking. This is because, if Islamic banking only charges

a ceiling rate without giving a rebate based on the floating rate, then the customer will avoid from dealing with Islamic banking due to the very high sales rate that imposed (Ishak & Asni, 2020). This is in contrast to conventional banking which sets interest rates at current market rates (BNM, 2013). Similarly, the pricing by Islamic banking at the beginning of the contract is very high because it wants to avoid the risk of economic fluctuations over a long period of time that can cause losses to the financiers (Ishak, 2019b). This is because, the home financing period is usually long up to a period of 35 years.

However, the respondents pointed out that the consequences of the imposition of two rates can cause the public to be confused by the assumption that the bank can increase the rate at any time during the financing period. This is because, the customer has agreed to the ceiling pricing during the beginning of the financing contract. Similarly, the term rebate used by the bank can be understood as discretion by the bank to be given to the customer (Khir, 2016). The term rebate is used by Islamic banking because it is included in voluntary giving (*tabarru'*) (Khir & Muhammad, 2010). The bank does not charge two prices in the contract (the ceiling price and the floating rate price) in a way to avoid the *Shariah* issue that prohibits from combining two prices in a sale and purchase transaction (Al-San'ani, 1407H). Thus, the bank decides a single price for financing which is the ceiling price rate that been determined at the beginning of the contract.

Respondents' allegations about society being confused about the price of financing are true. This can be seen from various factors, such as the scholars' disagreement over the practice of *ibra'* in Islamic banking, court cases related to the issue of *ibra'* and issues raised by NGOs such as the Malaysian Consumers Association as stated in the introduction topic. According to *ibra'* original practice, *ibra'* comes under charitable contacts in Islam, such as *hibah* (gift). Moreover, other bodies, such as the International Fiqh Academy, they have issued a similar resolution that *da' wa ta'jil* (reducing the amount for early payment), which is the underlying concept of *ibra'*, as the one that been allowed as far as it is not agreed upon in advance (IIFA, 1992). Since its original concept is based on *tabarru'* (voluntary donation), Islamic banks view granting *ibra'* as totally at their discretion (Mohammaed Fairouz, 2013). In other words, Islamic banks have full rights whether to give it or not, regardless of their customers' circumstances.

Besides, the Central Bank of Malaysia has issued a special regulation that Islamic banks must incorporate an *ibra'* clause and its calculation in their financing agreements. This clause would require Islamic banks to honour the promise to grant *ibra'* to their customers (BNM, 2013). However, this is contrary to the opinion of the majority of Islamic scholars who say that *ibra'* must be implemented unconditionally (Dusuki et al. 2010; Eldersevi & Haron, 2019). Similar to the results of a study submitted by Ishak (2019a), *Shariah* advisors in Malaysia are viewed as not in line with the practice of *ibra'*, where some state that the practice of *ibra'* in Malaysia as in its latest resolution is not in line with the original concept of *ibra'* due to the element of *tabarru'* (of it being voluntary). In its original concept, *ibra'* should be practised based on a charitable concept whereby it must not be mentioned in the contract. However, because of the order from the regulator (the Central Bank) to include an *ibra'* clause in the contract, it has affected the element of charity (Laldin et al., 2012).

In the study of Ishak (2019a) also found that, some claim that practising *ibra'* among Islamic banks nowadays is factually influenced by the interest rate. In classical practice, *ibra'* was granted by lenders to release the principal amount of debt towards their borrowers. However, in current practice, Islamic banks have already secured the principal amount, plus their profit, before granting *ibra'* to their customers for unearned profits. In other words, the

practice of *ibra'* seems to adapt Islamic financial instruments to be fixed price, or getting into something like conventional system, based on uncertainty. However, some say that modern *ibra'* is in line with the Islamic legal framework (Ishak, 2019a). Thus, differences of opinion on this matter have contributed to the confusion and various perceptions in society.

Apart from the issue of differences of opinion among Islamic scholars, court cases also contribute to this problem. According to the Research Academy for Islamic Finance, between 2003 and the end of 2009, the majority of cases in court regarding Islamic banking and their clients were due to the *ibra'* issue (Dusuki et al., 2010). This includes several court cases between Islamic banks and their customers, the weak SOP among Islamic banks in practising *ibra'* and the negative perception among judges when Islamic banks claimed the whole amount from defaulted customers (Mohamad & Trakic, 2013). In fact, before stipulating *ibra'* was required by the rules, judges tried to render this practice fairly and equitable through their judgements. For example, in the case Arab-Malaysian Merchant Bank Bhd v. Silver Concept Sdn Bhd [2005] 5 AMR 381, the judge ruled:

That right to rebate, if any, thus had dissipated not only with the precipitation of the default instalment, but also the exhaustion of time with the contractual completion time has arrived. Based on all these grounds, the issue of the defendant being deprived of the rebate, by reason of the recalling of the facilities cannot qualify as a "cause to the contrary". (A.M.R. 381)

Meanwhile, in the case of Affin Bank Bhd v. Zulkifli bin Abdullah [2006] MLJ 67, the judge also explained why *ibra'* must be granted, as unearned profit was no longer relevant:

"If the customer is required to pay the profit for the full tenure, he is entitled to have the benefit of the full tenure. It follows that it would be inconsistent with his right to the full tenure if he could be denied the tenure and yet be required to pay the bank's profit margin for the full tenure." (Affin Bank bhd vs Zulkifli Abdullah, 2006)

Based on the outcome of this dispute, it has caused BNM (2013) to issue a special rule that Islamic banks must include *ibra'* clause and its calculation in the financing agreement document. Also, the results of Ishak's (2019a) study claim that Islamic banking does not practice *ibra'* well as it does not have a specific formula for calculating *ibra'*. This in turn resulted in the Islamic bank being allowed by the court to claim the full price from the customer in case of default. This is similar when giving a rebate, when it is at the discretion of the Islamic bank to provide it with or vice versa (Fairouz, 2013). As a result, this practice has caused dissatisfaction among customers, especially when Islamic banks claim the full amount, including future profit in the case of default, which is significantly higher when compared to their conventional counterparts.

Therefore, it is not surprising when there is an effort by BNM to solve the problem of *ibra'* in Islamic banking. However, the public perceptions that claimed Islamic banking as very expensive, not fulfilling promises, more expensive than conventional banks, imitating the conventional banking system in the application of rates and others are still exists and thickens. Therefore, to eliminate the problem of negative perception in society, the study suggests the Islamic banks to be studied in order to reduce the ceiling profit margin to 1, 1.5 or twice. Alternative methods are listed as follows,

Alternative Method 1 (AM1)

The following formula can be used to determine the maximum profit rate of one-fold of financing amount as shown in the case above (Md. Ahood et al., 2016):

Total profit of PIB financing	:	Total profit of AM1 funding
RM230,068.48	:	RM226,100
4.75%	:	r_{AM1}

value r_{AM1} of the above ratio is:

$$r_{AM1} = \frac{226100}{230068.48} \times 4.75\%$$

$$= 4.67\%$$

Therefore, the rate of profit to the maximum financing amount of AM1 is at 4.67% per annum. Accordingly, the financier must pay RM1,106.81 a month for the same period of 34 years if the profit rate is substituted into Equation 1.

Alternative Method 2 (AM2)

The below formula can be used to determine the maximum profit rate of 1.5 times the amount of the financing (Md. Ahood et al., 2016):

Total profit of PIB financing	:	Total profit of AM2 financing
RM230,068.48	:	RM339,150
4.75%	:	r_{AM2}

value r_{AM2} of the above ratio is:

$$r_{AM2} = \frac{339150}{230068.48} \times 4.75\%$$

$$= 7.00\%$$

As can be observed, the rate of profit to the maximum financing amount of AM2 is at 7.00% per annum. If the profit rate is substituted into Equation 1, the financier has to pay RM1,454.46 a month for the same period of 34 years.

Alternative Method 3 (AM3)

The formula in determining the maximum profit rate of two times the amount of the financing is shown as follows (Md. Ahood, et al., 2016):

Total profit of PIB financing	:	Total profit of AM3 financing
RM230,068.48	:	RM452,200
4.75%:		r_{AM3}

value r_{AM3} of the above ratio is:

$$r_{AM3} = \frac{452200}{230068.48} \times 4.75\%$$

$$= 9.34\%$$

The above calculation shows that the rate of profit to the maximum financing amount of AM3 is at 9.34 % per annum. If the profit rate is substituted into Equation 1, the financier has to pay RM1,837.51 a month for the same period of 34 years.

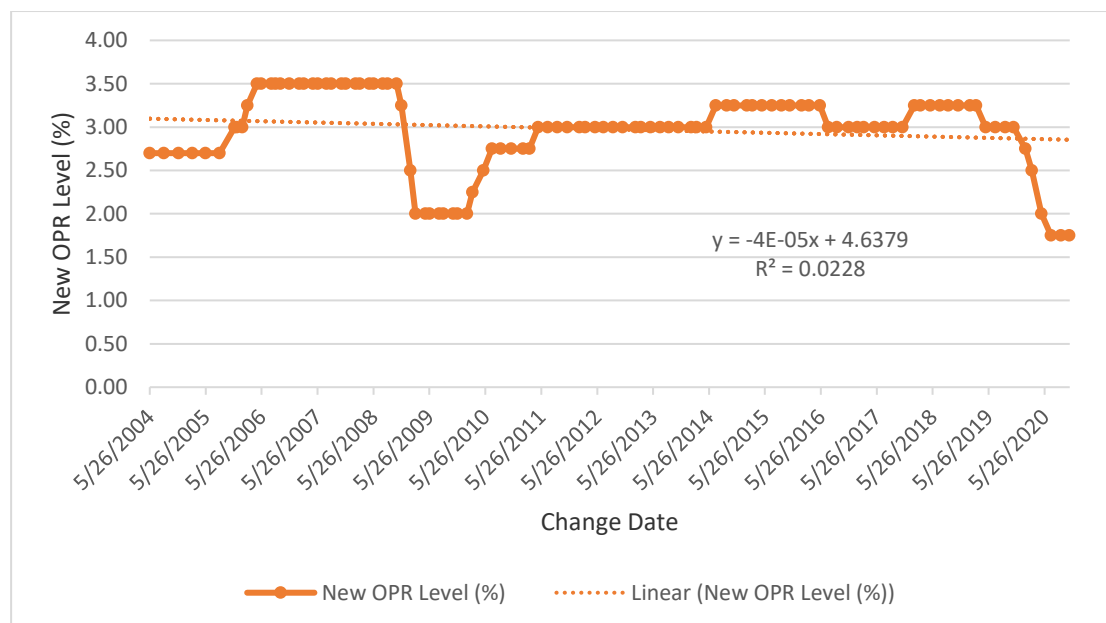
Based on the given alternative methods of above, the proposed rates are still below the ELR. Therefore, banks can still make a profit in their financing scheme without putting an excessive charge on the profit-taking rate. The situation was witnessed by the Overnight Policy Rate (OPR), where there is not much changed from the previous time, which proofing the stability of the economy. The details can be seen in the table and graph as below.

Table 1

OPR Rate

Date	Change in OPR (%)	New OPR Level (%)
7 July, 2020	-0.25	1.75
5 May, 2020	-0.50	2.00
3 March, 2020	-0.25	2.50
22 January, 2020	-0.25	2.75
7 May, 2019	-0.25	3.00
25 January, 2018	0.25	3.25
13 July, 2016	-0.25	3.00
10 July, 2014	0.25	3.25
5 May, 2011	0.25	3.00
8 July, 2010	0.25	2.75
13 May, 2010	0.25	2.50
4 March, 2010	0.25	2.25
24 February, 2009	-0.50	2.00
21 January, 2009	-0.75	2.50
24 November, 2008	-0.25	3.25
26 April, 2006	0.25	3.50
22 February, 2006	0.25	3.25
30 November, 2005	0.30	3.00
26 May, 2004	0.00	2.70

Graph 1: OPR level



Based on the OPR trend rate from the date of 26 May 2004 until 3 November 2020 (See Graph 1), there are no much changes, since the rate is almost consistent and the line projection is at linear stripe that signifies the rate as steadily posited around 2.75% up to 3.25% for the years to come (Central Bank of Malaysia, 2020). On 7 July 2020, Central Bank of Malaysia has cut its OPR level to the lowest record which is 1.75% due to Covid-19 impact and MCO enforced by the government. The current OPR level is maintained at 1.75% after the latest Monetary Policy Committee (MPC) meeting on 3 November 2020. Therefore, banking institutions are perceivable to attain a continuous earning profit when setting the value of ELR at a rate of 4.0% even without additional percentage.

Based on Graph 1, it also shows that if the ceiling price is set not more than twice the original financing price, the OPR rate will not exceed that rate over a long period of time. Thus, it is in line with the concepts of *maqasid al-Shariah*, *wasatiyyah* and *ihsan* which is to set a reasonable ceiling price for assets that are in the category of *hajiyyat* such as household needs. In addition, this modest pricing can be applied to first-time home buyers in a way to meet the demands of their *maqasid al-Shariah*.

Although the concept of *ibra'* can continue to be practised as a resolution set by BNM, society's negative perception of high ceiling rates as stated above can be eliminated or reduced as well as increase public confidence in Islamic banking. Thus, the recommendations from this study will definitely have a positive impact on Islamic banking when their image is enhanced. This proposal also does not bring any loss to Islamic banking if this formula is adopted into system.

Conclusion

It is found that although *Shariah* does not set a profit rate, there are indications from the concepts of *maqasid al-Shariah*, *wasatiyyah* and *ihsan* that help in managing the profit rate at a moderate rate, specifically when it involves necessities that are *hajiyyat* such as house or residence.

Based on the results of the study on Islamic housing financing practices based on BBA and *tawarruq munazzam* contracts from the two banks studied, these two banks set a high ceiling price which reached more than 10%. It is set in a way to avoid any *Shariah* issues and

uncertainty of the economic situation in the future. Although the high ceiling price is charged, but the bank still gives rebates to customers at the EPR rate. However, the respondents said that it brought confusion to the community about the imposition of the two rates. Furthermore, various factors contribute to the confusion, including things that based on court cases, weaknesses in SOPs from banks, and negative perspectives issued by well-known NGOs such as the Malaysian Consumers Association.

This study suggests the bank to reduce the ceiling price rate based on the amortisation formula and in line with the concepts of *maqasid al-Shariah*, *wasatiyyah* and *ihsan*. This proposal does not bring losses to the bank if being applied into system. This is because, by looking at the OPR position for several years, the position is almost even or horizontal. This study has a limit that only focuses on the practice of taking profit on two Islamic housing financing products and obtaining field data from two respondents and two banks. For future study, it is suggested for researcher to focus on public's perspectives and their perceptions of profit-taking by Islamic banks.

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