

GUARANTEE CONTRACTS IN ISLAMIC FINANCIAL TRANSACTION: ANALYSIS OF BNM RESOLUTION AND AAI OFI STANDARDS

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ABSTRACT

A guarantee (Kafalah) is considered an effective Islamic finance contract aimed at providing assurance and security by having a third party, the guarantor, commit to fulfilling the debtor's financial obligations in case of default. However, the Bank Negara Malaysia (BNM) policy document considered the guarantee as kafalah, while the Accounting and Auditing Organization for Islamic Financial Institutions (AAIOFI) considered it Damān. The term guarantee falls within the category of non-compensatory contract in classical Islamic financial contracts whereby there are no returns or compensation available for contracts like benevolence loans (Qard), gifts (Tabarru/Hibah), guarantee (Kafalah), and assignment of debt (Hawalah). In the modern financial setting, this might not fulfil one of the objectives of Islamic financial institutions, which is to offer services for profit. This study explores the application of Guarantee (Kafalah) as a non-compensatory and noncommutative contract, falling under the category of Uqud Ghair Mua'wadha in Islamic Financial Institutions. This study uses the doctrinal approach of the qualitative method in exploring juristic meaning, justification, and implications of the shariah terms. It analyses the sustainable implication of its application in contemporary Islamic finance institutions between BNM and AAIOFI. This study found that despite the classical implication of guarantee as a non-compensatory contract guarantee, contracts cannot yield a direct profit. However, they can generate income through Wakālah (agency fee), such as issuing LCs guarantees. These may be charged based on expenses incurred in amount-based (possibly slabs) but not time-based structures. The finding shows that the comparative analysis of regulatory frameworks by BNM and AAIOFI underscores the challenges of harmonizing global standards with local contexts, highlighting the necessity for ongoing dialogue and collaboration to ensure coherence and adaptability in Islamic finance regulation.

Keywords: Guarantee (Kafalah), non-compensatory, Wakalah (agency), BNM, AAIOFI

1. INTRODUCTION



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Kafālah (Guarantee) is a contractual agreement in which the guarantor conjoins with the guaranteed party to assume the latter's specified liability. Kafālah inherently aims to ensure the fulfilment of the guaranteed party's specified liability and is classically considered an act of voluntary donation from the guarantor to the guaranteed party (Bank Negara Malaysia, 2017).

The utilization of Guarantee (Kafālah) within Islamic financial transactions, specifically focusing on its role as a non-compensatory and noncommutative contract under the framework of 'Uqūd Ghair Mua'wadha (Abdulqadir Ibrahim Abikan, 2017).

Guarantee (Kafālah) as a non-compensatory contract requires further consideration in Islamic finance transactions. Kafālah, in Islamic financial contracts, plays a crucial role in providing assurance and security in financial transactions. It involves a third party, the guarantor, who commits to fulfilling the debtor's financial obligations in the event of default (Alwi et al., 2014). This arrangement helps mitigate risks and fosters a sense of trust and reliability in Islamic finance transactions. Hence, the business transaction requires the guarantor's ability to charge a fee further for providing commercial services of guarantee to a party rather than free (Hussein Kureshi & Muhsin Hayat, 2015).

The classical characteristic of Kafalah within the realm of Islamic financial contracts does not involve any returns or compensation such as contract Benevolence Loan (Qard), Gift (Tabarru/Hibah), Guarantee (Kafālah), and Assignment of Debt (Hawalah)(Muneeza & Mustapha, 2020).

The absence of returns or compensation in non-compensatory contracts aligns with the principles of Shariah, which prohibits the generation of profits from certain transactions. For example, in the case of a Benevolence Loan (Qard), the lender provides a loan without expecting any additional amount in return, emphasizing the act of charity and goodwill (Abdul Hannan, 2023 & Busari et al., 2022). Similarly, the Guarantee (Kafālah) operates on the principle of solidarity and support rather than profit-seeking. The guarantor ensures that the debtor's financial commitments are met in case of default, promoting trust and reliability in economic exchanges. This aligns with the broader ethical framework of Islamic finance, which emphasizes justice, fairness, and social responsibility (Bank Negara Malaysia, 2017).

This study shows how and why Guarantee (Kafālah) does not involve direct compensation or returns and the application of indirect compensation in service charges incurred by the guarantor in Islamic financial services, such as issuing letters of credit (LC) as a third party. Therefore, the remaining parts of this study have six main sections. The first section discusses the concept of guarantee. The second section

presents a justification for a guarantee in Islamic law. The third section highlights the pillars of the guaranteed contract in Islamic law. The fourth section explicates the concept of guarantee according to BNM and AAI OFI for Islamic financial transactions. The fifth section discusses the findings, while the final section summarises the study's conclusion.

2.0 THE CONCEPT OF GUARANTEE

Literarily, a guarantee means a commitment to something (Ibn Manzūr, 1994). Technically, a guarantee is the guarantor's obligation to someone who owes the right. It is a commitment that is permissible to act as required over any other financial right (Al-Uthaymin ala Zaad al-Mustaqniu, 2001).

The scholars of the Shafi'is and Hanbalis schools of law held that guarantees (Kafalah) are the contracts that join the guarantor's liability to the sponsored person's liability in committing to the debt; hence, their liability binds both. Therefore, the right owner can demand from whomever he wishes (Nazī Hammād, 2010). An example of an obligatory obligation: If a person buys goods from a store, and he has no money, he comes to another man and says to him: I want to buy goods from such-and-such a store, but I do not have money. Give me a security document. He gives him a security document, saying what he borrowed. This man is from this place, and his guarantee is on me. This obligation may not be due, but he has not yet fulfilled it. It is clean. The person who offers Kafālāh is a sponsor, supporter, guarantor, surety, answerable, and liable (Ali Akhbar Fayd Mishkini, 2024).

There are two main types of Kafalah: Firstly, self-guarantee: It is that he undertakes to bring someone who is owed a debt or other obligation - as retaliation - without assuming responsibility for paying the debt. Secondly, a debt guarantee Is to guarantee a debt established by a person, which the guarantor is obligated to pay if the person he owes does not pay it within its due date and it is called guarantee (Muhammad Hussain Hamd Al-Awaawadah, 2007) According to the hadith; "The leader is in debt and the debt is paid": (Abu Dāwūd, 2009, no. 3565), the debt guarantor is responsible for undertaking responsibility for liability.

The term guarantee in Islamic financial terms has been used interchangeably by different Institutions. Bank Negara Malaysia policy documents refer to guarantee as (Kafālāh) while AAI OFI refers to guarantee as (Damān). However, in conceptual usage, the two terms are considered synonyms, except that there might be technical differences in their rulings and applications. Firstly, Kafalah usually relies on a legal contract, documented by the official authorities, that provides guarantees to individuals. At the same time, Daman also depends on a valid contract and may not be documented in the court or the specialized legal department; it depends directly

on the true character of the two parties. Also, the Kafalah contract is usually attached to each party's guarantee to prove the legality of its application within the legal jurisdiction. However, the commitment in the Damān contract must be adhered to within the approved text paragraphs (Mohamed Naim et al., 2016).

3.0 JUSTIFICATION

The use of Kafālah in the Quran is derived from: "and put her under the care of Zakariya (Zachariya)" [Imran: 37]. Also, Allah says: "He who brings it shall have a camel-load of provisions; I guarantee that" [Yusuf: 72].

Hikmah (wisdom) in Kafālah stems from the need to make things easier for Muslims and achieve cooperation. A person may buy a commodity he needs but cannot find the price. The seller is not reassured, so he is not satisfied with looking at it and cannot obtain a mortgage to place it with; the seller may not be satisfied with the mortgage, so, in this case, he needs A guarantor. He may borrow the money he needs, and the lender requests a guarantor (Abdulqadir Ibrahim Abikan, 2017).

Jabir narrated: The Messenger of Allah (peace be upon him) would not perform funeral prayer over a person who died while a debt was due from him. The body of a Muslim was brought to him, and he asked: "Is there any debt due from him?" [The companions] said: "Yes, two dinars." He said: "Pray over your companion [as he has unpaid debt]." Then Abu Qatādah al-Ansari said: "I shall pay them, Messenger of Allah." The Messenger of Allah (peace be upon him) then prayed over him." (Abu Dāwūd, 2009, no. 3343)

According to Ibn Duyan Ibrahim bin Muhammad bin Salim (1982), the guarantor's consent is crucial as they are not obligated by the right unless agreed upon. If the guarantor delivers the guaranteed item to the right holder before the deadline, then the matter is absolved. However, the guarantor is not released if harm arises due to lack of proof or unjust interference. If the guarantor surrenders or the sponsored person dies, the guarantor is acquitted. The guarantor is also acquitted if they cannot bring the sponsored person while alive or if the sponsor refuses. This aligns with the hadith: "The leader (to a trust) is indebted (Abu Dāwūd, 2009, no. 3565)." Like a fine that applies to a guarantor to guarantee in an agreement.

According to Abdullahi bin Muhammad At-Tayar (2012), jurists Hanafi, Maliki, Shafi'i, and Hanbali schools view self-guarantee as permissibility. Al-Quran evident says: "So take one of us in his place. We see you as one of the doers of good" [Yusuf: 78]. The exegeses of Al-Qurtubī, (2006) explain the verse: "take one of us in his place until your friend returns to you." indicating this type of guarantee as part of self-protection.

As for the Sunnah: The statement of the Prophet- may Allah's peace and blessings be upon him; in the hadith of Abu Imamah: "The guarantor is indebted" (At-Tirmidhī, 1996, no 556/3) This includes general and self-assurance. For example: As for the sponsorship of the guarantor, the first sponsors the second, so the first is a guarantor, and the second is sponsored, so the third guarantees the first, so the third is the guarantor of the guarantor, and so on. As for the Damān (guarantee) is the same as this guarantee - an agent in the sense of an actor. Kafālah is permissible to self-guarantee for another, just as it is permissible for the Dāmin (guarantor) to guarantee another (Al-Lehyani, 2017).

4.0 THE PILLARS OF KAFALAH

Contract (Sighah): - The contract of Kafālah is the agreement of terms and conditions binding the contractual parties in the guarantee. The Malikis and Hanbalis proposition aligns with Shafi'is and Abu Yusuf opinion, which views that the form of sponsorship is based on the sponsor's offer alone and does not depend on the acceptance of the person guaranteed. This is because sponsorship is merely a commitment from the sponsor to perform the debt with no compensation; rather, it is a donation that arises from his expression alone. It is sufficient for the guarantor to offer (Muhammad Hussain Hamd Al-Awaawadah, 2007).

The Hanafi and Shafi'is schools of law opined that the form of sponsorship consists of an offer issued by the guarantor and an acceptance issued by the person being guaranteed because sponsorship is a contract through which the person guaranteed has the right to claim the guarantor or a right established in his debt that must be accepted. It follows that Sponsorship is not fulfilled by the words of the guarantor alone, whether the guarantee is in person or money, but rather the guarantor must accept it (Muhammad Hussain Hamd Al-Awaawadah, 2007).

Kafil (Guarantor): He is the guarantor who is committed to fulfilling the guaranteed right or bringing the guaranteed person, and it is a condition that he be eligible to donate and that he be sane, adult, and rational. Because sponsorship is a donation, it is required that the sponsor be qualified, so sponsorship of a minor, a fool, or an insane person is not valid (Issoufou, 2017).

Jurists stipulate that the sponsor must be qualified to donate because sponsorship is a donation, and accordingly, sponsorship from an insane person, an insane person, or a child is not valid, even if he is distinguished and authorized, or the guardian or custodian approves it (Issoufou & Abdullah, 2019).

Makful Lahu: (Guaranteed): He is the creditor. The guaranteed person must be known to the guarantor, and jurists have differed on the requirement that he be a sane adult

and on the requirement that he be satisfied with the sponsorship and accept it (Bank Negara Malaysia, 2017).

In the case of the guarantor, some jurists stipulated that the sponsored person be known to the guarantor, some of them stipulated that the sponsored person be satisfied, and some of them also stipulated that the sponsored person be able to fulfil the sponsored thing (Yahaya Adamu & Yahaya Adamu, 2018).

Makful Anhu: It is required that the sponsored person is the one claiming the right; the guarantee may be in the form of money, and many jurists call it a guarantee, or it may be in the form of the soul, and some call it: the guarantee of the body, and the guarantee of the face (Maybank Islamic, 2022).

Makfūl Bihi: It is the right for which the guarantee and guarantee of a debt or a person are signed, and it is required that the person guaranteed to be able to deliver it. So, it is not valid to guarantee the soul of an absent person whose whereabouts are unknown (Abdulqadir Ibrahim Abikan, 2017).

Related Term: *Damān* is interchangeable and refers to *Kafalah*: To guarantee linguistically: to guarantee and commit to something (Ahmad bin Muhammad Al-Fayumi, 1987).

Technically, it is permissible to transfer an obligation that is obligatory for someone else, such as a financial right (Muhammad bin Salih Al-Uthaymīn, 2002).

The Hanafis use the word “guarantee” to refer to sponsorship in both its parts, money and soul, and the Malikis call it “guarantee” and “carrier”, and this is the case among the Shafi’is who say “guarantee”, except that Imam Al-Shafi’i used the word “guarantee” in the limits of the punishments. As for the Hanbalis, they call sponsorship a “guarantee” in guaranteeing money, and they use the word “guarantee” to refer to the guarantee of the soul (Muhammad Hussain Hamd Al-Awaawadah, 2007).

5.0 KAFĀLAH AS NON-COMPENSATORY

Linking the parts of the relationship between the guarantor and the guaranteed to the offer and acceptance is legal. It is a link between the offer issued by one of the contracting parties and the acceptance of the other. Its effect is established on the contracted party, and the contract obligates each contracting party to do what he was obligated to do for the result. Giving without compensation, whether money or a benefit, immediately or in the future, for righteousness and piety. Donations are part of ownership contracts that do not receive compensation, such as gifts and endowments (Abd Rahman, 2019).

The will and purpose of these contracts is the ownership of the property without compensation and ownership contracts. In the form of donation, it is not in the form of authentication, such as the transfer of debt and the ownership of a beneficial interest. Compensation is like lending; ownership in all of the above is free (Hassan Abu Al-Hamad Ibrahim, 2022).

The permissibility of levying a fee for providing a guarantee. The Shariah Advisory Council of Bank Negara Malaysia approved using "kafalah bi al-ujr" to guarantee sukuk issuance by Danajamin, allowing Danajamin to reclaim investor payments with repayment terms based on market practices. The Council also endorsed the application of "kafalah bi al-ujr" for managing the Islamic deposit insurance fund under the Malaysia Deposit Insurance Corporation (PIDM), clarifying that premiums paid by member institutions are considered fees for PIDM's benefit. Additionally, the International Islamic Fiqh Academy determined that while administrative expenses for guaranteed issuance are permissible, charging fees for guaranteed issuance is prohibited, emphasizing the benevolent nature of guarantees in Islamic finance (Maybank Islamic, 2022).

6.0 COMPARISON OF BANK NEGARA MALAYSIA RESOLUTION AND ACCOUNTING AND AUDITING ORGANIZATION FOR ISLAMIC FINANCIAL INSTITUTIONS STANDARDS

Bank Negara Malaysia (BNM) is the central bank of Malaysia, responsible for setting monetary and financial stability policies. BNM issues resolutions and guidelines to regulate and develop the country's Islamic banking and financial sector (Bank Negara Malaysia, 2017). The BNM guidelines include Shariah requirements focusing on contract features and essential conditions and operational requirements covering governance, oversight, product structuring, risk management, financial disclosure, and market conduct (Fitria Yustiardhi et al., 2020). The Accounting and Auditing Organization for Islamic Financial Institutions (AAIOFI) is an international organization that establishes standards for accounting, auditing, and ethical practices in the global Islamic financial industry (AAIOFI, 2017). This section highlights significant dimensions in using the concept of guarantee in BNM and AAIOFI and their implications for Islamic finance transactions, products, and services. The study identifies seven main dimensions. The use of Guarantee Terminology Between BNM and AAIOFI, Rules and Juristic justifications, Legal Recourse in Default Event, Application of Guarantee in Islamic Finance, Combination of other Contracts with Guarantee, Creditors' claims from either debtor or guarantor, and Imposition of fees or charges on Guarantee Contract.

Table 1. Terminology Between BNM (2017) Kafalah Policy Document and AAIOFI (2017), Shari’ah Standards.

| Institutions | Contemporary Use | Implication |
|--------------|--|---|
| BNM | Guarantee: Kafālah i. (Meaning): “Kafālah refers to a contract where the guarantor conjoins the guaranteed party in assuming the latter’s specified liability” | According to BNM and AAIOFI, the guarantee concept involves providing security or guarantees for obligations. Kafālah focuses more on the contractual aspect between the guarantor and the guaranteed party, whereas Damān encompasses a broader range of security measures to protect against defaults and delays. |
| AAIOFI | Guarantee: Damān ii. “These standards cover securities (Guarantees) intended to secure obligations and protect debts against procrastination and default. Such securities may take the form of written documents, attestations, personal guarantees, mortgages, cheques, and promissory notes” | In summary, the distinction between Kafālah and Damān in the context of guarantees has far-reaching implications for the Islamic finance industry, shaping regulatory compliance, contractual clarity, risk management practices, product innovation, and consumer confidence. By recognizing and addressing these implications, stakeholders can foster a robust and sustainable Islamic finance ecosystem that aligns with the principles of Shariah while meeting the evolving needs of customers and markets. |

Table 2. Rules and Juristic Justifications

| Institutions | Rules | Implication |
|--------------|---|--|
| BNM | i. “S 16.1 The guarantor shall have the right of recourse against the guaranteed party even though the kafālah is given voluntarily” | It shows that both BNM and AAIOFFI concern guarantors' rights and limitations. However, while S 16.1 emphasizes the guarantor's right of recourse regardless of voluntariness, statement ii addresses the specific conditions under which a particular guarantor (IFII) can |
| AAIOFI | ii. “3/1/3 IFII is not entitled to be a non-recourse guarantor, unless authorised by its shareholders to make donations or benevolence” | act as a non-recourse guarantor, emphasizing the need for shareholder authorization. Differences in guarantors' rights and limitations have implications that underscore the importance of regulatory compliance, risk management, transaction structuring, market confidence, and innovation within the Islamic finance industry. By addressing these |

implications, financial institutions can strengthen their operations, enhance stakeholder trust, and contribute globally to the sustainable growth and development of Islamic finance.

Table 3. Legal Recourse in Default Event

| Institutions | Rules | Implication |
|--------------|--|--|
| BNM | i. "G 16.6 If the guaranteed party fails to settle the amount claimed by the guarantor within the agreed time frame pursuant to exercising the guarantor's right of recourse, the guaranteed party is subjected to the late payment charges as determined by the relevant authorities" | BNM & AAIOFFI statements in this section address consequences for the guaranteed party's failure to fulfil obligations related to guarantees or guarantors. However, while (i) focuses on late payment charges imposed on the guaranteed party for failing to settle the claimed amount, statement (ii) focuses on the creditor's entitlement to legal action if the debtor fails to provide a required guarantor as stipulated in the credit transaction contract. The implications of differences in default consequences underscore the importance of legal compliance, risk management, transaction structuring, market confidence, and legal protection within the Islamic finance industry. By addressing these implications, financial institutions can strengthen their operations, enhance stakeholder trust, and contribute globally to the sustainable growth and development of Islamic finance. |
| AAIOFI | ii. "3/3/5 If the contract of a credit transaction stipulates that the debtor shall provide a guarantor and the debtor fails to provide one, the Institution is entitled to initiate legal action to force him to provide a guarantor or to terminate the contract" | |

Table 4. Application of Guarantee in Islamic Finance

| Institutions | Rules | Implication |
|--------------|--|--|
| BNM | i. "G 14.1 The guarantor may provide kafālah without conditions (unrestricted kafālah) or with conditions (restricted kafālah). G 14.3 The guarantor may provide a restricted kafālah whereby the terms and conditions of the guarantee are specified. The specified terms and conditions may include time, | BNM (i) & AAIFFI (ii) statements address the inclusion of guarantees or security provisions in contractual agreements, but while G 14.1 and G 14.3 focus on the types of guarantees and the ability to specify terms and conditions within the guaranteed contract, Application 4 addresses the permissibility of stipulating guarantees in fiduciary contracts under certain circumstances. |

| | | |
|--------|---|--|
| AAIOFI | <p>effective date, trigger events, amount or any additional terms and conditions of the guarantee which are acceptable by Shariah”</p> <p>ii. “4. (Application): 2/2/1 It is not permissible to stipulate in trust (fiduciary) contracts, e.g. agency contracts or contracts of deposits, that a personal guarantee or mortgage of security be produced because such a stipulation is against the nature of trust (fiduciary) contracts unless such a stipulation is intended to cover cases of misconduct, negligence or breach of conditions or stipulations”</p> | <p>The implications of differences in guaranteed inclusion underscore the importance of regulatory compliance, transaction structuring, risk management, market confidence, and legal protection within the Islamic finance industry. By addressing these implications, financial institutions can strengthen their operations, enhance stakeholder trust, and contribute globally to the sustainable growth and development of Islamic finance.</p> |
|--------|---|--|

Table 5. Combination of Other Contracts with Guarantee

| Institutions | Rules | Implication |
|--------------|--|--|
| BNM | <p>i. “17. Arrangement of kafālah with other contracts or concepts G 17.1 Kafālah may be arranged with other Shariah contracts or concepts, including exchange-based contracts, agency contracts, partnership contracts, benevolent (tabarru`at) contracts, and wa`d if requirements for the arrangement of kafālah with such contracts/concepts are observed”</p> | <p>BNM (i) & AAIOFFI (ii) statements discuss the combination of contracts, particularly involving guarantees, but while G 17.1 addresses the permissibility of arranging kafālah with various Shariah contracts or concepts, statement ii prohibits the simultaneous combination of agency and personal guarantees within a single contract due to conflicts with their inherent nature.</p> |
| AAIOFI | <p>ii. “2/2/2 It is not permissible to combine agency and personal guarantees in one contract at the same time (i.e. the same party acting in the capacity of an agent on one hand and acting as a guarantor on the other hand) because such a combination conflicts with the nature of these contracts”</p> | <p>The implications of differences in contract combination underscore the importance of regulatory compliance, transaction structuring, risk management, market confidence, and legal protection within the Islamic finance industry. By addressing these implications, financial institutions can strengthen their operations, enhance stakeholder trust, and contribute globally to the sustainable growth and development of Islamic finance.</p> |

Table 6. Creditors’ claims from either debtor or guarantor

| Institutions | Rules | Implication |
|--------------|--|--|
| BNM | i. “G 14.6 The beneficiary may claim his rights from the guaranteed party or the guarantor, either for: (a) the full amount of the liability from either of them; or (b) a part of the liability from the guaranteed party and the other part from the guarantor or guarantors (based on the agreed sequence, if any)” | Both statements discuss the options available to beneficiaries or creditors regarding whom to claim their rights from, but while (i) G 14.6 focuses on the flexibility for the beneficiary to claim liabilities from either party in full or in part, statement (ii) emphasizes the rights of the creditor to claim the debt from either party and the ability of the guarantor to arrange the order of liability. |
| AAIOFI | ii. “3/3/1 The creditor is entitled to claim the amount of his debt from either the debtor or the guarantor and can claim his right from either. However, the guarantor is entitled to arrange the order of liability, for example, by stipulating (after the contract of guarantee) that the creditor shall first claim payment from the principal debtor and that the creditor is entitled to recourse to the guarantor for payment only if the principal debtor refuses to fulfil his obligation” | The implications of differences in creditor rights and beneficiary options underscore the importance of regulatory compliance, transaction structuring, risk management, market confidence, and legal protection within the Islamic finance industry. By addressing these implications, financial institutions can strengthen their operations, enhance stakeholder trust, and contribute globally to the sustainable growth and development of Islamic finance. |

Table 7: Imposition of fees or charges on Guarantee Contract

| Institutions | Rules | Analysis |
|--------------|---|---|
| BNM | i. “G 15.1 The guarantor may impose a fee for providing the kafālah service. G 15.2 Pursuant to paragraph 15.1, the fee as agreed in the kafālah contract may be (a) an agreed fixed amount or (b) a percentage of the guaranteed amount. 16. Recourse and recovery” | BNM (i) & AAIOFFI (ii) statements discuss compensation for providing guarantees, but while (i) G 15.1 and G 15.2 address the rights of the guarantor to impose a fee for providing kafālah and specify the forms of compensation allowed, statement (ii) prohibits receiving remuneration or commission for providing personal guarantees and allows only reimbursement of incurred |

AAIOFI ii. "3/1/5 It is not permissible to expenses.
take any remuneration In summary, the implications of
whatsoever for providing a differences in compensation
personal guarantee per se or to arrangements underscore the importance
pay commission for obtaining of regulatory compliance, transaction
such a guarantee. The guarantor structuring, risk management, market
is, however, entitled to claim any confidence, and legal protection within
expenses incurred during the the Islamic finance industry. By
period of a personal guarantee, addressing these implications, financial
and the Institution is not obliged institutions can strengthen their
to inquire as to how the customer operations, enhance stakeholder trust,
has obtained the guarantee and contribute globally to the sustainable
produced. [see item 7/1/1 and growth and development of Islamic
7/1/2)" finance.

7.0 DISCUSSION OF FINDINGS

The research delves into the regulatory frameworks and standards established by Bank Negara Malaysia (BNM) and the Accounting and Auditing Organization for Islamic Financial Institutions (AAIOFI) concerning guarantees in Islamic finance. BNM, serving as Malaysia's central bank, oversees monetary and financial stability policies and issues resolutions and guidelines for Islamic banking and finance. On the other hand, AAIOFI, an international organization, sets global standards for accounting, auditing, and ethical practices in Islamic finance.

One notable distinction between BNM and AAIOFI is their terminology and understanding of guarantees. While BNM emphasizes "Kafālah," focusing on the contractual aspect between the guarantor and the guaranteed party, AAIOFI stresses "Damān," which encompasses a broader range of security measures against defaults and delays. This divergence underscores differing perspectives on the nature and scope of guarantees in Islamic finance.

Regarding rules and implications, both institutions guide guarantors' rights, limitations, and legal remedies in default scenarios. BNM emphasizes the guarantor's right of recourse, even when provided voluntarily. In contrast, AAIOFI specifies conditions under which an Islamic Financial Institution (IFI) can serve as a non-recourse guarantor, necessitating shareholder authorization.

Furthermore, the research outlines the consequences for the guaranteed party's failure to meet obligations. BNM discusses late payment charges, while AAIOFI highlights the creditor's entitlement to legal action if the debtor fails to furnish a required guarantor, underscoring contractual obligations.

The guarantor can provide kafalah with or without restrictions. When it's without restrictions, it's termed unrestricted kafalah, while with conditions, it's called restricted kafalah. If it's unrestricted, the guarantor will be held accountable based on the terms and conditions of the original liability. Recourse and reimbursement: The guarantor maintains the privilege to seek reimbursement from the guaranteed party, regardless of the voluntary nature of the kafalah. However, the guarantor's right to seek reimbursement is capped at the amount paid to the beneficiary due to providing the kafalah. Notwithstanding, the guarantor may reclaim from the guaranteed party the actual costs incurred in disbursing the kafalah amount to the beneficiary (Bank Negara Malaysia, (2015).

The permissible guarantees and their applicability in various contracts are also addressed. BNM permits both unrestricted and restricted Kafālah, enabling the specification of terms and conditions within the guaranteed contract. Conversely, AAIOFI prohibits stipulating personal guarantees or mortgages in trust contracts unless for specific reasons, such as misconduct or negligence, indicating differences in contractual arrangements.

Additionally, both institutions discuss integrating guarantees with other contracts. While BNM allows combining Kafālah with various Shariah contracts or concepts, AAIOFI prohibits the simultaneous combination of agency and personal guarantees due to their conflicting nature.

Regarding creditors' rights and compensation, BNM and AAIOFI outline options for creditors and compensation for providing guarantees. BNM permits the imposition of fees for offering Kafālah, whereas AAIOFI prohibits receiving remuneration for personal guarantees but permits reimbursement of incurred expenses.

The findings underscore the nuanced disparities between BNM and AAIOFI in their approaches to regulating guarantees in Islamic finance. While both entities strive to ensure financial stability and ethical practices, differences in terminology, rules, and implications highlight the intricate challenge of reconciling global standards with local regulatory frameworks in Islamic finance.

According to Bank Negara Malaysia, (2017), *Kafalah Policy Document* a mudarib is not permitted to provide a guarantee for the performance of the mudārabah. Nevertheless, there's uncertainty regarding whether, in a mudārabah joint venture, the mudarib can guarantee the liability of a party they transact to ensure the security of the capital and/or profit. This matter led to a consultation with the SAC regarding the issue of the mudarib's guarantee on the liability of their counterparty in the mudārabah joint venture

According to AAOIFI, prohibited guarantees in financial arrangements encompass commitments such as a specific price pledge, where asset owners commit to selling at predetermined prices, investment managers' pledges to purchase assets at specific prices, often endorsed by asset owners, pledges by investment managers to buy assets from Mudarib Sukuk holders, Mudaraba participants, and parties engaged in Mushārah arrangements, and assurances made by agents, agencies, or involved parties at the contracting stage to acquire assets at predetermined prices through representation, all of which are not permitted in financial transactions(AAOIFI, 2017).

8.0 CONCLUSION

In conclusion, the comparative analysis of the regulatory frameworks set forth by Bank Negara Malaysia (BNM) and the Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI) provides valuable insights into the complexities of governing guarantees in Islamic finance. While both entities share the goal of fostering financial stability and ethical practices within the Islamic banking sector, their divergent approaches underscore the challenges of harmonizing global standards with local regulatory contexts. The nuanced distinctions in terminology, rules, and implications highlighted throughout the research emphasize the need for ongoing dialogue and collaboration among regulatory bodies, financial institutions, and Shariah scholars to ensure coherence and effectiveness in regulatory frameworks. Moreover, the findings underscore the importance of adaptability and flexibility in regulatory practices to accommodate the evolving landscape of Islamic finance and address emerging challenges effectively. Ultimately, by fostering greater alignment and coordination between regulatory bodies and stakeholders, we can enhance transparency, integrity, and confidence in Islamic financial markets, thereby advancing the broader objectives of financial inclusion, sustainable economic growth, and social development in Muslim-majority countries and beyond.

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