

CRIME PREVENTION IN ISLAMIC FINANCIAL INSTITUTIONS: PRACTICES IN BRUNEI DARUSSALAM

Noraini Mohamad

*Accounting Research Institute & Faculty of Accountancy
Universiti Teknologi MARA, Malaysia*

Mohamad Asri Abdullah

*Centre of Islamic Thoughts and Understanding
Universiti Teknologi MARA, Malaysia*

Nawal Kassim

*Accounting Research Institute & Faculty of Accountancy
Universiti Teknologi MARA, Malaysia*

Abstract

The Islamic Financial Institutions (IFIs) in Brunei Darussalam have experienced a significant growth and become new players in the banking industry. The State continues to offer new Islamic innovative banking products and services in order to gain acceptance from the public and increase market shares of the industry. Strategically, the State aims to be the global player in Islamic banking activities and this is evidenced through the mergers of their two large Islamic Financial Institutions namely, the Islamic Brunei Bank Berhad (IBB) and Islamic Development Bank Berhad (IDB) to form Bank Islam Brunei Darussalam (BIBD). Though the merger has successfully increased BIBD's total assets, branches and ATMs, BIBD in particular or the Ministry of Finance in general lacks the Islamic Financial Criminology (IFC) guidelines for Islamic Financial Crime prevention on Islamic products and services offered by IFIs in the State. Similarly, in Brunei and Malaysia the power to prevent Islamic financial criminology practices is vested within the Civil Court and not within the Syari'ah jurisdiction. Conflicts arise when the judgment of Civil Court on matters pertaining to Islamic financial criminology are based on conventional practices. Thus, this paper aims to examine the background of Islamic financial criminology crime prevention in the banking

ISSN 1675-4077

© 2010 Malaysian Accountancy Research and Education Foundation, Accounting Research Institute & Faculty of Accountancy and UPENA, Universiti Teknologi MARA, Malaysia.

system in Brunei Darussalam and suggests improvement to support the development of an Islamic financial system in the State.

Keywords: *banking, financial institutions, Islam, islamic financial criminology*

Introduction

The Islamic financial system is becoming increasingly accepted worldwide. Asma and Stella (2000) mentioned that more than 200 Islamic financial institutions are functioning in different parts of the world. Despite all the challenges, understanding of the concept and operation, availability of the trained personnel in *Syari'ah*, the non-functional of *Syari'ah* court to hear cases on the wrong doings of *mu'amalat* (business transactions) or any past cases to refer to, the progress of the Islamic banking has been remarkable.

The practices of Islamic banking are based upon the *Syari'ah* principles that are derived from the Quran and *sunnah*. Islam has provided a complete system to organise and manage all aspects of life including economy and finance. The holistic system in Islam contains *aqeedah*, *syariah*, and *aklaq* which make up of an Islamic economy that is different from the conventional economy. Consequently, the Islamic financial system must correspond to the Islamic economy. Islam promotes goodness in the world and hereafter. So, monopoly of wealth and wrong doings in business transactions are against Islamic values.

Though the development of the global Islamic financial system has received worldwide support and embraced many strategies to enhance its future growth, and credibility and competitiveness in the banking industry, there is still a vacuum that needs to be filled; Islamic financial crime prevention. There are gaps in addressing financial crimes in the conventional and Islamic financial systems. The process of prevention always ends in ambiguities because some of the Islamic financial products are built within the conventional financial framework. Thus, a guideline based on *Syari'ah* principles needs to address this problem.

Financial Criminology from the Quran and *Sunnah* Perspectives.

There are differences between the meaning of criminology or crime in Islam and conventional finance. In Islam, criminology has been described explicitly in the Quran and *Hadith*. In general, crime related to *mukallaf* deeds is towards his creator, Allah. A crime is committed when one does what has been prohibited in *Syari'ah* or is non-compliance to the *Syari'ah* principles. In Islamic finance, crime refers to transacting in prohibited Islamic financial transactions. For instance, the financial contracts of Islamic banks need to be clearly documented, be equitable and avoid the element of *Riba*, *Gharar* and *Maysir*. In *mu'amalat* (business transactions) all activities are permissible unless forbidden by revelation (Quran) or the practice of Prophet Muhammad s.a.w. Example of

prohibited business activities would include untrustworthy dealings, being involved in gambling, consuming liquor, taking interest on loans etc. In Quran *and Hadith*, there is no clear word to associate financial criminology. The common words used are: *harrama* (to forbid); *la al-nahi* (prohibit verb); *naha* (to prohibit); *la al-nafi* (denial verb); *fiil al amr* (command verb); or *bathil* (wrongful deed).

In addition, the basic of Islamic financial criminology is prescribed in the following verse:

O you who believe! Eat not up your property among yourselves in vanities: but let there be amongst you traffic and trade by mutual good-will: nor kill or destroy yourselves: for verily ALLAH hath been to you Most Merciful [4:29]

Referring to the verse, Allah forbids the Muslims from taking or consuming property in excessiveness, except in businesses or transactions that have been agreed upon. The detailed interpretation of vanity (*bathil*) is clearly prescribed in *Surah Al-Baqarah:275*, that is “Allah has permitted trade and has forbidden interest”.

The Islamic Financial Transaction

Islamic banking has the same purpose as conventional banking system except it operates in accordance with the *Syari'ah* principles, known as *Fiqh al-Muamalat* (Islamic rules on transactions). The transaction is restricted to Islamic acceptance activities which aim to engage only in ethical investing and moral purchasing. The basic principle of Islamic banking is the sharing of profit and loss and the prohibition of *riba* (usury).

The Islamic financial transactions offered by the Islamic Financial Institutions (IFIs) include *Bai'al'inah* (sale and buy-back agreement), *Bai'bithaman ajil* (deferred payment sale), *Bai'muajjal* (credit sale), *Musharakah* (joint venture), *Mudaraba* (venture capital funding), *Murabahah* (cost plus), *Musawamah* (negotiation of a selling price), *Bai Salam* (a contract of advance payment), *Hibah* (gift), *Ijarah* (leasing/rent/or wage), *Ijarah thumma al bai'* (hire purchase), *Ijarah-wal-iqtina* (real estate leasing), *Musharakah* (joint venture), *Qard Hassan/Qardul Hassan* (good loan/benevolent loan), *Sukuk* (Islamic bonds), *takaful* (Islamic insurance), *Wadiah* (safekeeping) and *Wakalah* (representative/power of attorney).

The Syari'ah Advisory Council (SAC)

As experienced in Malaysia, the National *Syari'ah* Advisory Council (NSAC) has been established as an effort to streamline and harmonise the *Syari'ah* interpretations among banks and *takaful* companies. This is the highest *Syari'ah* authority on Islamic Banking and *Takaful* in Malaysia. Its primary objectives are to act as a sole authoritative body to advise Bank Negara Malaysia (BNM) on Islamic banking and *takaful* operations; co-ordinate *Syari'ah* issues with respect to Islamic banking and finance

(including *takaful*); and analyse and evaluate *Syari'ah* aspects of new products/schemes submitted by banking institutions and *takaful* companies.

The *Syari'ah* Advisory Council (SAC) of BNM is an authority for the ascertainment of Islamic laws for the purposes of Islamic banking business, *takaful* business, Islamic financial business, Islamic development financial business or other business, which is based upon *Syari'ah* principles that are supervised and regulated by BNM. Malaysian Islamic banks are advised and provided guidelines by SAC. As a reference body and advisor to BNM on *Syari'ah* matters, the SAC is also responsible for validating all Islamic banking and *takaful* products to ensure their compatibility with the *Syari'ah* principles. In addition, it advises BNM on the *Syari'ah* aspects of the operations of these institutions as well as on their products and services. With the amendment of the Central Bank of Malaysia Act 1983 in 2003, the role and functions of the SAC are further enhanced and the SAC has been given the status of a sole authoritative body on *Syari'ah* matters pertaining to Islamic banking, *takaful* and Islamic finance. In order to preserve its independence, members of the SAC of BNM are not allowed to participate in any *Syari'ah* Committee of financial institutions.

On the other hand, the *Syari'ah* Committee for Islamic Banking Institutions in Malaysia is set up internally by the Individual Islamic banking institutions or commercial banks that offer Islamic windows. The committee plays a complementary role to the SAC of BNM. Their duties are to advise the institutions on the *Syari'ah* Compliance of banking operations; however, the SAC is the ultimate arbiter. The guidelines on the governance of the *Syari'ah* committee for the IFIs were issued by BNM in 2004 that aimed at achieving uniformity of *Syari'ah* decisions and to create and expand the pool of competent *Syari'ah* personnel in Islamic banking and *takaful*.

From the experience of Indonesia, the National *Syari'ah* Board forms the Indonesia Council of Ulemas in 1999. This council is an independent body recognised by the Bank of Indonesia and serves the same purpose as the SAC of BNM. On the other hand, regulatory authorities of some countries like Baharin, Sudan, Syria etc. have adopted the *Syari'ah* Standards issued by the Accounting and Auditing Organisation for Islamic Financial Institutions (AAOIFI), and used them as their guidelines.

Whilst in Brunei Darussalam, the banks are regulated under the Banking Act and Finance Companies Act through the Ministry of Finance in the State. There is no Central Bank, but the function of monitoring is under the jurisdiction of the Ministry of Finance through its agency Brunei Currency Board, the department of Financial Services and the Brunei Investment Agency. Although not many researches or articles referred to mentioned the availability of the *Syari'ah* Advisory Council at the Ministry of Finance or at the Brunei Currency Board or mentioned the existence of the *Syari'ah* Panel Committee at Bank Islam of Brunei Darussalam, there exists an independent body namely, the *Syari'ah* Financial Supervisory Board (SFSB) that oversees that all Islamic financial activities are in line with the *Syari'ah* principles. The roles and responsibilities of this independent body are similar to its counterparts in Malaysia, and Indonesia.

Brunei Darussalam Legal Landscape

The State legal system has the influence of the Britain's. This is evidenced when the British Residential system was introduced in the State in 1906. The 1908 Enactment was to replace the 1906 Enactment with the purpose to amend the law relating to the constitution and powers of the Civil and Criminal courts and the law and procedures to be administered by the State. Five courts were constituted in the State for the administration of Civil and Criminal justice: The Court of Resident, Courts of Magistrate of the First Class, Courts of Magistrate of the Second Class, Courts of Native Magistrates and Courts of *Kadis*. Unlike other courts, the Court of *Kadis* has the power in all matters concerning Islamic religion, marriage and divorce that may be prescribed within their power. However, matters relating to Islamic banking and financial products, services and *takaful* are not within the power of the Court of *Kadis*.

Islamic laws, namely laws relating to *mu'amalat* (commercial transactions) have been introduced into the civil legal system where parties choose Islamic banking and financial products and services, and *takaful* (Islamic insurance). This means that for those who choose the Islamic mode of transactions both the Civil and Islamic laws apply. These transactions come within the jurisdiction of the Civil law courts.

The *Syari'ah* Court, which is separate and independent, is governed by the order of the *Syari'ah* Court. Its jurisdiction extends to matters involving the Islamic faith, marriage, divorce, family, Islamic gifts, and succession to estate of deceased Muslims. Matters pertaining to Islamic financial crimes are not within the *Syari'ah* Court's jurisdiction.

The governing structure of the State rests on the country's written constitution along with the three pillars of its national philosophy, namely Malays, Islam and Monarchy. Under the constitutions, His Majesty the Sultan and Yang Di-Pertuan of Brunei Darussalam is the Head of State and is assisted by a number of advisory councils that are appointed under the constitution along with their respective functions and responsibilities, namely, the Succession and Regency Council, Privy Council, Legislative Council, Council of Cabinet Ministers and the Religious Council.

The Constitution of Brunei Darussalam was originally enacted in September 1959. This was a move towards full independence that eventually came in 1984. Since 1959, the constitution has been subjected to a number of amendments, and a newly revised Constitution has incorporated all the amendments that have been made since its inception in 1959.

Meanwhile, the source of the Islamic laws is from the Holy Quran which followed the tradition of the Prophets or *Hadith* which is the second source of the Islamic Laws. Other sources of laws in Islam include *Ijma'* (consensus of opinion), *Qiyas* (analogical deduction), *Istihsan* (equity in Islamic Law), *Maslahal Mursalah* (consideration of Public Interest), *Urf* (Custom), *Istishab* (presumption of Continuity), and *Saad al Dhara'I* (Blocking the Means). Similarly, Islamic laws in Brunei Darussalam are guided by the

principles in the Holy Quran and the Prophet's tradition or *Hadith* (*Syari'ah* principles) as well as those mentioned above.

The governance of the Islamic Law of the State is under the Religious Council and *Kadis* Court's Act, an Act which consolidates the law relating to the Religious Council and the *Kadis* Court, the constitution and organisation of religious authorities and the regulation of religious affairs. Apart from this act, there are other legislations enforced in the State to govern the conduct of Muslims in the country. Among the legislations are:

- i. The *Syari'ah* Courts' Act that specifies provisions in respect to the establishment of the *Syari'ah* Courts, appointments, power of the *Syar'ie* Judge and jurisdiction of the *Syari'ah* Courts and matters connected with the proceedings of *Syari'ah* Courts and for the determination and confirmation of the new moon. Others are the *Syari'ah* Courts' Evidence Order 2001, the Emergency (Islamic Family Law) Order 1999, the Islamic Adoption of Children Order 2001 and the *Halal* Meat Act.
- ii. Among these legislations none legislate on matters pertaining to Islamic Financial Crimes.

Development of Islamic Banking in Brunei Darussalam

Brunei Darussalam houses three financial institutions which are based on the Islamic banking system namely, the Islamic Bank of Brunei (IBB), Islamic Development Bank of Brunei (IDBB) and *Tabung Amanah* Islam Brunei (TAIB) or the Islamic Trust Fund of Brunei. In 2005, the IBB and IDBB were merged to form Bank Islam Brunei Darussalam Berhad (BIBD) and it was fully operational on 3rd July 2006. The subsidiaries under BIBD are *Takaful* BIBD Sdn Bhd that provides insurance coverage and investments and *BIBD At-Tamwill* Berhad, which offers fixed deposits, hire purchase and consumer product financing.

Before merging, IBB was to administer the financial affairs of the community in accordance to the principles of *Syari'ah* and IDBB on Islamic banking activities in 2000. The IBB and TAIB were the only banks that offered Islamic banking services before the 1990s. However, to date other financial intermediaries have provided windows for Islamic products. TAIB was established as a *Fardu Kifayah* (religious obligation) for the Muslim Community. Its initial formation was a trust fund whose prime function was to provide facilities for Muslims to make the pilgrimage to Mecca which shared similar function to that of *Lembaga Tabung Haji* Malaysia (LUTH). TAIB is owned by the government and its main function is to operate/promote Islamic financial services to raise the socio economic standards of the people. Later, TAIB operated similarly to a saving and loan institution. TAIB is to focus on the under privileged segment of the population. Meanwhile, IBB's (est. 1993) function was to provide Muslims with Islamic banking facilities mainly in trade and commercial finance.

In business, the activity of merging is common. Kusstatcher and Cooper (2005) mentioned that the reasons to merge included diversification, to achieve synergy, in response to

market conditions for business need, to increase market share, and for the sake of the shareholders. In Brunei Darussalam, IBB and IDBB were merged not only to develop Brunei as a financial center with Islamic finances but also, in an effort to further strengthen the Islamic financial institution in the country, in particular the banking sector and companies providing insurance policies to make them more competitive. The merging of both small and medium institutions is in line with the economic and banking reforms that are being implemented by regional countries and Asian regions. As a result of the mergers, BIBD became the biggest financial institution in Brunei based on the total assets (\$4.3B in 2005) and deposits compared with other seven banks in operation in the country. In addition, the merging of both banks offer better and competitive services apart from enhancing cost efficiency by avoiding duplication of services, enhancing service efficiency in new banking areas such as investment banking, fund management, corporate advisory, investment advisory and others. These measures enable the merged *takaful* companies to explore opportunities for new products in line with the activities of international insurance market. Moreover, the cost efficiency through the merger was channeled to the public through better services and at competitive rate. Furthermore, the move also had facilitated banks to further develop activities overseas and offer job opportunities for Bruneians and allowed Brunei's Islamic Financial Industry to grow at a faster rate.

Financial banking and investment activities in Brunei are supervised by the Financial Institution division of the Ministry of Finance. The Ministry of Finance is also responsible for the issuance of licenses for restricted financial activities. Banks in Brunei are regulated under the Banking Act and Finance Companies Act through the Ministry of Finance. There is no Central Bank in Brunei, but the functions of monitoring are under the jurisdiction of Ministry of Finance through the Brunei Currency Board, the department of financial services and Brunei Investment Agency. The Brunei Currency Board is in charge of controlling the money in circulation and maintaining currency interchangeability (fixed at par) with that of Singapore.

BIBD offers Islamic banking services such as personal financing, corporate and education financing. Among the new, innovative and sophisticated Islamic Banking products and services offered to the public include the introduction of the *Sukuk Al Ijarah* BLNG worth B\$100million; the launch of Electronic *Kad Inden* to replace the Government Manual *Kad Inden* that is convenient to the government offices to purchase fuel and other products available at fuel stations; administer Government *Sukuk Al Ijarah* (short term) worth B\$120 million on behalf of the Ministry of Finance; introduce BIBD *Musyarakah Musahamah* and *Al-Bai Tradable Musyarakah* Certificates as a form of investment to the general public; and introduce BBA *Baiti* Financing for the purchase of houses at affordable rates. These innovative products that receive recognition are Islamic structured products that give investors exposure to international stocks with principal protection and returns that are compliant with Islamic principles.

The merger of BIBD together with TAIB has seen an increase in market shares of up to 40% of domestic banking sector and is expected to increase up to 60% in the next three to five years (The Brunei Times, Oct. 22, 2009). As a result of the merger too, BIBD has created an Islamic banking giant with 14 branches and around 200 ATMs.

Conclusion and Recommendations

Conceptually, the process of crime prevention in Islamic banking in Brunei Darussalam is under the jurisdiction of the Civil Court. This is similar to that of Malaysia scenario. The power vested in the *Syari'ah* Court extends to matters pertaining to family law, marriage, Islamic faith, gifts, divorce but the court is not in power to deal with Islamic financial crimes of IFIs. The law relating to Islamic and financial transactions (*Mua'malat*) is embedded in the Civil law system. Consequently, this will give rise to conflicts when the judgment of Islamic banking cases is trialed within the jurisdiction of conventional banking framework that leads to injustice and non-compliance with the *Syari'ah* principles.

In the meantime, there are other independent advisory boards available, such as the *Syari'ah* Financial Supervisory Board at the Ministry of Finance and the *Syari'ah* Committee Board within the IFIs, but these lack authoritative powers to ensure the Islamic banking implementation in accordance to the *Syari'ah* principles. Similarly, in Malaysia the SAC and other advisory boards too are limited in authoritative power to ensure the Islamic banking implementation as per *Syari'ah* principles. Thus, this situation will create confusion among the public that is unable to differentiate between the practices of conventional and Islam in banking activities as the only difference to justify is in the name.

The study recommended the establishment of the Brunei National Fatwa Council to be the highest authority to determine Islamic financial cases. Other advisory bodies are to ascertain the Council's views. In theory, the *Syari'ah* court is in a better position to hear cases related to Islamic financial issues. However, due to the history of legal structure the power vested in this court has been limited to issues involving family, divorce, marriage, Islamic faith, etc.

Alternatively, there is a need to harmonise the roles and responsibilities of the Civil and *Syari'ah* courts. The *Syari'ah* Courts' roles and responsibilities are to be extended to deal with cases that are deemed fit to be trial under the Islamic law. All cases are to be recommended by the National Fatwa Council.

References

- Asma, S. and Stella, C. (2000). *Anthology of Islamic Banking*, Institute of Islamic Banking and Insurance, London.
- Allaert, A. (1995). *Negara Brunei Darussalam A Country Study on the Wealthiest State in South East Asia*, CAS Discussion Paper No.2, CIMDA.
- Al-Zuhayli, W. (2003). *Financial Transactions in Islamic Jurisprudence*, 1 and 2, Dar al Fikr, Syria.

Brunei Darussalam: The Abode of Peace. <http://www.bruneidirecthys.net/> Retrieved on August 10, 2010.

BIBD Eyes Lion Share of Brunei Banking Sector, The Brunei Times, October 22, 2009.

Ebrahim, S. M. and Tan, K. J. (2001). Islamic Banking in Brunei Darussalam, *International Journal of Science Economics*, 28, 4: 314-337.

Ezani, Y., Asmak, H., Noraini, M. (2010). Prevention of Islamic Financial Criminology: Practice in Malaysia and Iran. (unpublished).

Islamic Development Bank of Brunei. http://www.mapsofworld.com/brunei/islamic_economy, Retrieved on August 10, 2010

Kusstatcher, V. and Cooper, C. (2005). *Managing Emotions in Mergers and Acquisitions*, Edward Edgar.

Legal Systems in ASEAN. <http://www.aseanassociation.org/paper/brunei>.

Malaysia Sets Up Committee to enhance its Legal Framework as the “Law of Choice” for the Islamic financial Transaction, <http://arabnews.com/economy/islamicfinance>.

Mergers in the Pipeline. <http://www.sultanate.com/news>. Retrieved on August 10, 2010.