



**BANK NEGARA MALAYSIA**  
CENTRAL BANK OF MALAYSIA

## ***Wakalah***

Applicable to:

1. Licensed Islamic banks
2. Licensed banks and licensed investment banks carrying on Islamic banking business
3. Licensed takaful operators
4. Professional retakaful operators
5. Prescribed development financial institutions

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## PART A OVERVIEW

### 1. Introduction

- 1.1 Compliance with Shariah requirement is a prerequisite in ensuring the legitimacy and integrity of Islamic financial products and services. In meeting this expectation, it is essential for an Islamic financial institution (IFI) to establish the necessary operational framework and infrastructure to ensure that the conduct of Islamic financial transactions is consistent with Shariah.
- 1.2 The Shariah contract-based regulatory policy is intended to promote consistency of Shariah contract application in Islamic financial products and services. This policy document is envisaged to strengthen legal certainty and Shariah compliance practices by an IFI.
- 1.3 The objectives of this policy document are to –
- (a) provide reference on the applicable Shariah rulings for binding *wakalah* contract;
  - (b) set out key operational requirements for the implementation of binding *wakalah*; and
  - (c) promote end-to-end compliance with Shariah requirements which further promote sound banking practices and safeguard consumer interests.
- 1.4 This policy document sets out the following:
- (a) salient features and essential conditions of *wakalah* in Part B; and
  - (b) regulatory and supervisory expectations for the operational requirements on governance and oversight, structuring, risk management, business and market conduct as well as financial disclosure in Part C.
- 1.5 This policy document covers the application of *wakalah* contract in financial products and services offered by an IFI.

### 2. Applicability

- 2.1 This policy document is applicable to an IFI as defined in paragraph 5.2.
- 2.2 For the avoidance of doubt, where an IFI adopts *wakalah bi al-istithmar* for the purpose of investment account –
- (a) the operational requirements in Part C of this policy document are not applicable; and
  - (b) the operational requirements as provided in the policy document on *Investment Account* issued by the Bank are applicable.

### 3. Legal provision

- 3.1 The requirements in Part B of this policy document are specified pursuant to:
- (a) section 29(1) of the Islamic Financial Services Act 2013 (IFSA); and
  - (b) section 33E of the Development Financial Institutions Act 2002 (DFIA).

- 3.2 The requirements in Part C of this policy document are specified pursuant to:
- (a) sections 29(2), 57(1), 135(1) and 155 of the IFSA; and
  - (b) sections 33E(2), 41, 42C(1) and 116 of the DFIA.
- 3.3 The guidance in this policy document is issued pursuant to section 277 of the IFSA and section 126 of the DFIA.

#### **4. Effective date**

- 4.1 This policy document comes into effect on 1 July 2018, except for paragraph 28 which shall come or take effect immediately upon issuance of this policy document.

#### **5. Interpretation**

- 5.1 The terms and expressions used in this policy document shall have the same meanings as assigned under the IFSA, Financial Services Act 2013 (FSA), and DFIA, as the case may be, unless otherwise defined in this policy document.

- 5.2 For the purpose of this policy document:

**“S”** denotes a standard, an obligation, a requirement, specification, direction, condition and any interpretive, supplemental and transitional provisions that must be complied with. Non-compliance may result in enforcement action;

**“G”** denotes guidance which consist of such statements or information intended to promote common understanding and advice or recommendations that are encouraged to be adopted;

**“Islamic financial institution” or “IFI”** means:

- (a) a licensed Islamic bank;
- (b) a licensed takaful operator and professional retakaful operator;
- (c) a licensed bank or licensed investment bank approved under section 15(1)(a) FSA to carry on Islamic banking business; and
- (d) a prescribed institution under the DFIA approved under section 33B DFIA to carry on Islamic financial business.

- 5.3 A glossary of terms used in this policy document is set out in Appendix 2.

## **6. Related Shariah rulings and policy documents**

- 6.1 This policy document must be read together with other relevant legal instruments, policy documents or guidelines that have been issued by the Bank, in particular;
- (a) *Investment Account;*
  - (b) *Guidelines on Corporate Governance for Licensed Islamic Bank;*
  - (c) *Guidelines on Corporate Governance for Development Financial Institution;* and
  - (d) *Shariah Governance Framework.*

## PART B SHARIAH REQUIREMENTS AND OPTIONAL PRACTICES

### 7. Compliance with Part B

- S 7.1 An IFI which uses the *wakalah* contract for its products shall ensure that such products are in compliance with Part B of this policy document.

### 8. Definition

- S 8.1 *Wakalah* refers to a contract where a party, as principal (*muwakkil*) authorizes another party as his agent (*wakil*) to perform a particular task on matters that may be delegated, with or without imposition of a fee.

### 9. Nature

- S 9.1 The inherent nature of *wakalah* is the delegation of powers to, or authorization of, the agent by the principal which gives rise to the agent having fiduciary duties (*amanah*) towards the principal within what he has been authorized to do.
- S 9.2 A *wakalah* contract shall be binding in any of the following situations:
- (a) the *wakalah* contract involves rights of third party;
  - (b) the *wakalah* contract involves a fee (*wakalah bi al-ujrah*) to be paid to the agent;
  - (c) the agent has commenced the work that he has been authorized to do and discontinuance of the work would cause the principal or the agent to suffer damages; or
  - (d) the principal and the agent have agreed not to terminate the *wakalah* contract within a specified time.
- G 9.3 The *wakalah* contract may take the following forms:
- (a) unrestricted agency (*wakalah mutlaqah*): an agency contract in which the principal appoints someone as agent to perform a particular task without any specific restriction or condition; or
  - (b) restricted agency (*wakalah muqayyadah*): an agency contract in which the principal appoints someone as agent to perform a particular task with specific restriction or condition.
- S 9.4 The *wakalah* contract shall take effect immediately upon entering into the *wakalah* contract or, if it is a conditional *wakalah* contract, upon occurrence of the specified condition(s).
- S 9.5 Terms and conditions that have been mutually agreed upon and are consistent with Shariah principles shall be binding on the principal and the agent.

### 10. Components of *wakalah* contract

- S 10.1 A *wakalah* contract must have all of the following elements:
- (a) the principal and agent (collectively referred to as contracting parties);
  - (b) the offer (*ijab*) and acceptance (*qabul*) to enter into the *wakalah*

- contract; and  
(c) the subject matter of the *wakalah* contract.

## 11. Contracting parties

- S 11.1 The contracting parties in a *wakalah* contract shall, at minimum comprise a principal and an agent.
- S 11.2 The contracting parties shall be a natural person or legal entity that must have the legal capacity<sup>1</sup> to enter into the *wakalah* contract.
- S 11.3 A principal shall not appoint an agent to execute a particular transaction if the principal himself does not have the legal capacity to enter into such transaction.
- S 11.4 The principal must authorize the agent and notify him of his appointment under the *wakalah* contract.
- S 11.5 If a person is acting on behalf of another person without *wakalah* contract or an appointed agent act beyond the scope of his authorization under the *wakalah* contract, such person or agent is referred to as unauthorized agent (*fuduli*). The transaction entered by the unauthorized agent may be ratified, subject to conditions stipulated under paragraph 16.1.

## 12. Offer (*ijab*) and acceptance (*qabul*)

- S 12.1 The *wakalah* contract must be entered into through an offer and acceptance between the contracting parties.
- G 12.2 The offer and acceptance may be expressed orally, in writing or any other methods recognized by Shariah.

## 13. Subject matter of *wakalah*

- S 13.1 The subject matter of the *wakalah* contract must be Shariah compliant.
- S 13.2 The subject matter of the *wakalah* contract must be determined upfront by the principal, made known to and accepted by the agent.

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<sup>1</sup> From Shariah perspective, legal capacity of a natural person is defined as the capacity to assume rights and responsibilities and capacity to give legal effect to his action. Among the important conditions are that the person must possess sound mind and the capacity to distinguish between what is harmful or beneficial to one's interests. The legal capacity of a legal entity is defined as eligibility of an entity to acquire rights and assume responsibilities. In Malaysia, the legal capacity of both natural person and legal entity is governed by the Contracts Act 1950 and the Age of Majority Act 1971.

**14. Salient features of wakalah****Disclosure of the agent's authorization**

- S 14.1 Where the agent enters into a transaction with a third party and discloses that he is acting on behalf of the principal –
- (a) the rights and responsibilities arising from that transaction (*huquq al-`aqd*) must be assumed by the principal; and
  - (b) any intended effect of the transaction (*hukm al-`aqd*) entered into by the agent pursuant to the authorization shall be binding on the principal.
- S 14.2 Where the agent enters into a transaction with a third party and does not disclose that he is acting on behalf of the principal –
- (a) the rights and responsibilities arising from that transaction must be assumed by the agent; and
  - (b) any intended effect of the transaction entered into by the agent pursuant to the authorization shall be binding on the principal.

**Dual agency**

- G 14.3 Where an arrangement involves more than one principal as contracting parties (whether or not the arrangement involves one or more transactions such as seller and buyer or lessor and lessee), the agent may act for all of the principals.
- G 14.4 A person, in his capacity as agent for one principal, may enter into a subsequent transaction with himself as the other contracting party (such as the purchaser under a *tawarruq* deposit or the seller under *tawarruq* financing).
- S 14.5 In connection with paragraph 13.2, a person shall perform the role as a dual agent under paragraph 14.3 or 14.4 provided that the rights, liabilities and responsibilities of the contracting parties, including the specification of the authorized tasks of the agent is determined upfront, agreed by the principal(s), made known to and accepted by the agent.
- S 14.6 In relation to paragraph 14.5, all of the principals must agree to the appointment of the agent to act on their respective behalf.

**Appointment of second agent or sub-agent/ another agent**

- G 14.7 The principal may consent to –
- (a) the agent appointing another agent on the principal's behalf; or
  - (b) the agent appointing another agent (sub-agent) for himself (initial agent) to perform all or any part of the task.
- S 14.8 The agent shall not appoint a second agent or delegate his role to a sub-agent except with the consent of the principal.

- S 14.9 When the principal appoints more than one agent and intends for the agents to act together –
- (a) the principal must explicitly disclose the intention; and
  - (b) each of the agents must perform the task together with other agents as mandated by the principal.

### **Rights and obligations of agent**

- S 14.10 The agent must observe the general interest of the principal in *wakalah mutlaqah* where the specific condition on the subject matter has not been determined.
- S 14.11 In the event of agent's misconduct (*ta'addi*), negligence (*taqsir*), or breach of specified terms (*mukhalafah al-shurut*), the agent shall be liable and shall compensate for loss or damage including any actual cost suffered by the principal.
- S 14.12 In the event that a breach of specified terms results in gains to principal such as selling at a higher price or buying at a lower price than that the agent was authorized for, the agent shall disclose this to the principal and must not retain any portion of the gains without the consent of the principal.

## **15. Wakalah fee**

- G 15.1 A *wakalah* contract may be arranged for a fee (*wakalah bi al-ujrah*).
- S 15.2 If the *wakalah* contract is arranged with a fee, the agent is entitled to receive the *wakalah* fee for carrying out the authorized task or matters that have been delegated to him.
- S 15.3 The *wakalah* fee must be determined and agreed at the time of entering into the *wakalah* contract.
- G 15.4 The *wakalah* fee may be agreed as a fixed amount or as a percentage ratio of a certain amount or an amount linked to a benchmark.
- G 15.5 The *wakalah* fee may be paid in a manner that is mutually agreed by the contracting parties such as in one lump sum or in several payments.
- G 15.6 In addition to the *wakalah* fee, the contracting parties may agree to an additional fee, over and above the initially agreed fee (performance fee). The performance fee may be in the form of excess of a certain threshold set for the authorized task.
- G 15.7 If the *wakalah* contract involves sub-agent, the principal and the initial agent may agree on the party that should pay the *wakalah* fee for the sub-agent.

- S 15.8 Notwithstanding paragraph 15.3, in the event the parties agree that the agent shall be entitled to *wakalah* fee but the rate is not determined upfront and the task has been fully or partially performed by the agent, he is entitled to a fee based on market rate for a similar task done (*ujrah al-mithl*).
- G 15.9 The agent may waive his right to the fee.

## 16. Transaction by an unauthorized agent (*fuduli*)

- S 16.1 In relation to paragraph 11.5, a prospective principal may ratify –
- (a) a sale transaction where an unauthorized agent sells the assets of the prospective principal to a third party; or
  - (b) a purchase transaction entered into by an unauthorized agent only in the following –
    - (i) the unauthorized agent purchases an asset using prospective principal's money; or
    - (ii) the unauthorized agent purchases an asset using his own money and discloses that the purchase is made on behalf of prospective principal.
- S 16.2 In the absence of the ratification in paragraph 16.1(a), the sale contract shall be rescinded and the assets and proceeds from the sale contract shall be returned to the prospective principal and the third party respectively.
- S 16.3 In the absence of the ratification in paragraph 16.1(b) –
- (a) the purchase contract entered into by the unauthorized agent shall not be enforceable against the principal;
  - (b) any money belonging to the prospective principal shall be returned; and
  - (c) the unauthorized agent shall be accountable for such transaction.

## APPLICATION OF WAKALAH WITH OTHER CONTRACTS

### 17. Application of *wakalah* with other contracts or arrangements

- G 17.1 The *wakalah* contract may be applied with other contracts or arrangements including the following:
- (a) exchange-based contracts such as *murabahah*, *istisna`*, and *ijarah*;
  - (b) partnership contracts such as *musyarakah* and *mudarabah*;
  - (c) *murabahah* to purchase orderer;
  - (d) *ijarah muntahia bittamlik*; or
  - (e) *tawarruq*.

### 18. Arrangement of *wakalah* with *kafalah*

- G 18.1 An agent in a *wakalah* contract may enter into a separate *kafalah* contract to guarantee the performance of a third party's obligation towards the principal.
- S 18.2 Where an agent enters into a separate *kafalah* contract in accordance to paragraph 18.1, the agent shall then assume the role of a guarantor (*kafil*).

- S 18.3 If an arrangement involves *wakalah* and *kafalah* contracts is documented in one legal documentation, the following conditions must be fulfilled:
- (a) such arrangement is consistent with the inherent nature of *wakalah* and *kafalah* respectively;
  - (b) the validity of *wakalah* and *kafalah* is not made contingent to the other; and
  - (c) the agent must not guarantee his own performance under a *wakalah* contract or the investment capital or return under a *wakalah* for investment (*wakalah bi al-ishtithmar*).

## 19. Arrangement of *wakalah* with *rahn*

- G 19.1 A *wakalah* contract may be arranged with collateral (*rahn*).
- S 19.2 The collateral under a *rahn* contract shall only be liquidated in the event of misconduct, negligence or breach of specified terms by the agent under its *wakalah* contract.

## 20. Application of *wakalah bi al-istithmar*

- G 20.1 A *wakalah* contract may be entered into for the purpose of investment (*wakalah bi al-istithmar*).
- S 20.2 In accordance with paragraph 18.3(c), the agent must not guarantee the capital or return on the investment in any form.
- S 20.3 In the event of agent's misconduct, negligence, or breach of specified terms that results in a lower profit rate than the expected profit rate of such investment, the agent shall –
- (a) repay the investment capital;
  - (b) pay the actual profit up to the event of breach; and
  - (c) compensate such loss and damage which the principal is entitled to in accordance with paragraph 14.11.
- G 20.4 For the avoidance of doubt, breach of specified terms referred to in paragraph 20.3 includes, but not limited to, breach of the following terms:
- (a) the fund shall be invested in such a manner that generates a certain expected profit rate and the agent breaches that condition which results in a lower profit rate than the expected profit; or
  - (b) the fund shall be invested only in a specific instrument or portfolio and the agent breaches the condition by investing in another instrument or portfolio which results in a lower profit than the expected profit of the specified instrument or portfolio.
- S 20.5 In the event a breach of condition results in profit to be higher than the agreed expected profit, the excess profit shall be treated in accordance with the agreed terms and conditions of the performance fee. If the terms and conditions are not stipulated, the principal shall have the discretion to grant the performance fee.

- G 20.6 The principal under the *wakalah bi al-istithmar* contract may require the agent to arrange for an independent third party guarantee on the capital.
- S 20.7 For the purpose of paragraph 20.6, the following requirements must be observed:
- (a) the guarantee shall be executed as a separate contract to guarantee loss or depletion of capital; and
  - (b) where the third party guarantor is an entity, it shall not be a related party to the agent.
- G 20.8 The principal may agree to the agent retaining all or part of the excess profit as performance fee if the actual profit is higher than the agreed expected profit.
- G 20.9 In the event that the actual profit is lower than the agreed expected profit, the agent may give *hibah* to the principal to compensate for the difference.
- S 20.10 In connection with paragraph 20.9, such *hibah* must not be made obligatory on the agent.
- G 20.11 The agent may initiate the investment by advancing his own funds with the consent of the principal.
- S 20.12 In connection with paragraph 20.11, such advancement by the agent must not be made as a pre-condition for entering into the *wakalah* contract.
- S 20.13 If the agent sets aside a portion of the investment profit as reserves for the principal –
- (a) the agent must obtain the principal's prior consent; and
  - (b) all profit retained in such reserves belongs to the principal.
- S 20.14 If the capital provided under *wakalah bi al-istithmar* contract is to be invested together with other pools of funds having similar mandates, the capital must be able to be segregated from the other pools of funds.

## **DISSOLUTION (*FASAKH*) AND COMPLETION (*INTIHA'*) OF WAKALAH**

### **21. Dissolution of *wakalah***

- S 21.1 A *wakalah* contract shall dissolve under any of the following circumstances:
- (a) demise, dissolution or loss of legal capacity of the principal;
  - (b) demise, dissolution or loss of legal capacity of the agent if the *wakalah* contract stipulates that the task shall be personally performed by the agent;
  - (c) the principal loses his right to the subject matter of the *wakalah*;
  - (d) both contracting parties mutually agree to terminate the *wakalah* contract;
  - (e) the principal exercises the option to terminate the *wakalah* contract due to misconduct, negligence or breach of specified terms of the contract by the agent; or
  - (f) the agent withdraws from the *wakalah* contract due to breach of

specified terms of the contract by the principal.

- S 21.2 Upon dissolution of the *wakalah* contract, any asset or rights entrusted with the agent shall be returned to the principal, and the agent shall be entitled to a *wakalah* fee based on the market rate for a similar task, or a fair portion of the agreed fee that commensurate with the task performed, or any rate mutually agreed between the contracting parties.

## **22. Completion of *wakalah***

- S 22.1 A *wakalah* contract completes upon fulfilment of all obligations of the contracting parties under the *wakalah* contract which include settlement by the principal of the *wakalah* fee.
- G 22.2 Satisfaction of the *wakalah* fee may be made through any of the following methods:
- (a) full payment of the agreed sum by the principal;
  - (b) waiver of right to receive the outstanding *wakalah* fee by the agent;
  - (c) set-off (*muqassah*) of obligations between the contracting parties; or
  - (d) transfer of the obligation to pay the fee to a third party through transfer of debt (*hiwalah al-dayn*).
- S 22.3 Upon completion of the *wakalah* contract, the contracting parties are free from any contractual obligations under such *wakalah* contract.

## PART C OPERATIONAL REQUIREMENTS

### 23. Governance and oversight

- G 23.1 The requirements under this part complement the broad governance and oversight expectations specified under the relevant policy documents on corporate governance issued by the Bank. While broad governance and oversight principles are applicable, specific requirements are needed to manage risks and unique nature of *wakalah*.
- S 23.2 An IFI must have sufficient understanding of its risk profile and ensure the availability of personnel with the appropriate knowledge and skills to offer *wakalah*.

#### Board of directors

- S 23.3 The Board of Directors of an IFI (the Board) must establish sound governance structure to facilitate effective oversight on the management and implementation of *wakalah*. The adequacy of the governance structure must be commensurate with the nature, complexity and risk profile of *wakalah*.
- S 23.4 The Board has overall responsibility for corporate governance, Shariah governance and Shariah compliance of an IFI. As such, the Board must –
- (a) approve the business and risk strategies of the IFI with regard to the application of *wakalah*;
  - (b) approve and oversee the implementation of policies and procedures governing the application of *wakalah*, which must include the following aspects:
    - (i) purpose, roles, duties and responsibilities of the IFI;
    - (ii) applicable legal documentations<sup>2</sup>;
    - (iii) methodologies, assessment criteria and approving authorities for the appointment of agent;
    - (iv) parameter on any fees and charges;
    - (v) mechanism for monitoring and periodic reporting on the performance of the IFI in discharging its duties;
    - (vi) risk management; and
    - (vii) information disclosure;
  - (c) ensure appropriate internal controls, systems and infrastructure are in place to implement *wakalah* in accordance with Shariah requirements;
  - (d) ensure that sufficient resources are in place and that the IFI has adequate and qualified senior management with sufficient knowledge and competency on the concept, application and risks associated with the *wakalah* arrangement; and
  - (e) ensure independent reviews are conducted regularly to assess compliance with the policy documents issued by the Bank and internal policies established by the IFI.

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<sup>2</sup> Refers to contracts, agreements, master agreement or other generally acceptable documents in trade and financial transactions.

**Shariah committee**

- S 23.5 The Shariah Committee has the responsibility to advise an IFI in ensuring its business, affairs and activities comply with Shariah requirements including activities involving a *wakalah* arrangement. As such, the Shariah Committee must –
- (a) endorse the application of Shariah requirements in the relevant policies and procedures governing the *wakalah*;
  - (b) review the terms and conditions stipulated in the legal documentation and other documentation such as in the promotional material, product manual or other publications, and endorse that the terms and conditions are in compliance with Shariah;
  - (c) advise and provide clarification on relevant Shariah rulings, decisions or guidelines on Shariah matters issued by the Bank, and if relevant, any other authorities; and
  - (d) assess the work carried out by Shariah review and Shariah audit and endorse any rectification measures to ensure *wakalah* complies with Shariah requirements.

**Senior management**

- S 23.6 The senior management has the responsibility to ensure that the business and operations of an IFI complies with Shariah requirements. As such, the senior management must –
- (a) develop and implement internal control and risk management policies and procedures in line with the business strategy and risk appetite as approved by the Board;
  - (b) establish and implement policies, procedures and processes with regard to the development of product and services and where applicable, the basis for determining fees and charges, assessment of agent's or sub-agent's capabilities and competencies to effectively execute the specific tasks, proper management and execution of the *wakalah*;
  - (c) develop legal documentations with respect to *wakalah*, which clearly outlines the duties and responsibilities of the IFI as agent or principal;
  - (d) implement relevant internal systems and infrastructure and adequate mechanisms to identify, measure, control and monitor risk associated with *wakalah*;
  - (e) ensure key accountabilities has the appropriate skills to perform the roles and responsibilities under *wakalah* effectively;
  - (f) clarify the IFI's fiduciary responsibilities as agent and the manner to discharge the responsibilities effectively;
  - (g) develop and undertake regular reviews and monitoring of the IFI's performance under *wakalah* arrangement, including compliance with Shariah requirements;
  - (h) institute necessary processes and procedures to ensure the terms as specified under *wakalah* legal documentations and Shariah requirements are executed effectively; and
  - (i) ensure timely disclosure of relevant information to the Board and the Shariah Committee.

## 24. Structuring

### Purpose

- S 24.1 An IFI must clearly specify –
  - (a) the purpose of the financial product and services that apply *wakalah*; and
  - (b) the subject matter of the *wakalah*.
- S 24.2 An IFI must also ensure the overall structure and outcome of the product and services do not contravene with Shariah requirements as provided in this policy document.

### Contracting parties

- G 24.3 *Wakalah* may be applicable for the purpose of asset acquisition or executing an investment.
- S 24.4 The roles and responsibilities and the rights and obligations of contracting parties including the employment of sub-agent in *wakalah*, must be clearly described in the terms of the financial product and services.
- S 24.5 If the *wakalah* is undertaken in combination or has interlinkages with other contract, the roles and responsibilities and the rights and obligations of contracting parties in these contracts must also be clearly specified and distinguish in the terms of the financial product and services.

### Offer and acceptance

- S 24.6 In entering into a *wakalah* contract, an IFI must ensure that an offer and acceptance is clearly evidenced by appropriate documentation or record<sup>3</sup>.

### Fees and charges

- S 24.7 An IFI must clearly disclose any applicable fees and charges, requirement for delivery of asset and settlement arrangement in the terms of the *wakalah* contract, if applicable.

### IFI as agent

- S 24.8 Where an IFI undertakes the role of agent, the IFI must ensure that –
  - (a) the mandated roles and responsibilities under *wakalah* contract is in line with its business and risk appetite and do not contravene with Shariah requirements;
  - (b) the appointment of agent is executed in the manner as approved by Shariah;
  - (c) it has the necessary capacity and capability to perform the roles and responsibilities as specified by the principal and manage the risks associated with the *wakalah*;
  - (d) prior consent of principal is obtained for the appointment if sub-agent is employed to perform specific roles and responsibilities under the *wakalah*; and

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<sup>3</sup> This is to avoid legal risk as well as to safeguard the interest of the customer.

(e) proper documentations are maintained as evidence to the execution of specified duties or mandate under *wakalah*.

S 24.9 An IFI must disclose to all principals if it undertakes the role as agent for more than one principal in a financial product or services and ensure the mandated roles under each *wakalah* are executed independently.

### **IFI as principal**

S 24.10 An IFI that undertakes the role of principal must clearly specify the purpose, roles and responsibilities of agent under the *wakalah*.

G 24.11 Where an IFI acts as principal in *wakalah* for the purpose of investment, the IFI may specify –

- (a) investment portfolio or assets to be invested by the agent;
- (b) the skills or expertise required for an agent to perform specific tasks; and
- (c) compensation terms or remuneration of the agent (if any) and the expected return on investment.

S 24.12 Where an IFI acts as a principal for the purpose of asset sales and purchase transactions, the IFI must –

- (a) clearly specify the subject matter of the transaction or types of assets and roles and responsibilities of the agent;
- (b) ensure there is an established process in place for the proper appointment of the agent prior to the agent conducting specified roles and duties;
- (c) where applicable, set out the requirement on delivery, documentary evidence of asset's ownership and settlement terms; and
- (d) specify the execution process or outline any ratification process of agent's conduct, if applicable.

S 24.13 Subject to fulfilment of conditions stipulated in paragraph 16.1, an IFI can ratify and confirm that the customer has acted as the IFI's agent under the *wakalah* agreement to secure the IFI's ownership in the asset purchased.

### **Documentation**

S 24.14 An IFI must develop comprehensive and legally enforceable documentation that clearly stipulate the terms and conditions in the *wakalah* arrangement which are in compliance with Shariah and regulatory requirements.

S 24.15 In line with paragraph 24.14, legal documentation pertaining to *wakalah* arrangement must include the following terms:

- (a) description of the subject matter;
- (b) rights, duties or responsibilities of contracting parties including rights where one party elects to terminate or dissolve the *wakalah*;
- (c) where applicable, the agreed *wakalah* fee or an agreed methodology or benchmark practices to compute the fee;
- (d) circumstances which trigger the dissolution of *wakalah*;
- (e) mechanism to determine the compensation payable to contracting party that suffers losses following the event of default or breach of contractual

- terms;
- (f) treatment or specification of cost involved in performing the *wakalah* or the duration or tenure or maturity period of *wakalah*; and
- (g) in the event that there is –
  - (i) an appointment of sub-agent, record of principal's consent;
  - (ii) unauthorized agency, the ratification process of the unauthorized agent; and
  - (iii) dual agency, the contracting parties must ensure the essential criteria or specification of the authorized task must be agreed and the documentation must state clearly the roles of the contracting parties in each of the transactions.

S 24.16 An IFI shall adequately clarify or translate the use of Arabic terminology in the legal documentations to facilitate clear understanding of the contracting parties.

## 25. Risk management

S 25.1 An IFI must institute and implement sound integrated risk management system to effectively manage risks arising from its role as agent or principal in *wakalah*.

S 25.2 An IFI must establish risk management policies and procedures to identify, measure, monitor and control risks associated with *wakalah* to support the IFI in discharging its responsibilities effectively.

S 25.3 The risk management policies and procedures of an IFI must include the following:

- (a) process to ascertain that the application of *wakalah* is consistent with the business and risk strategy of the IFI and Shariah requirement;
- (b) methodologies to identify risks inherent with the IFI's roles and responsibilities under the *wakalah*;
- (c) assessment on the adequacy of the IFI's capabilities, capacities and have in place necessary system to support effective execution of its contractual obligations;
- (d) where applicable, establish the mechanism to review the suitability of the procedures for the appointment of agent or sub-agent and monitoring their performance;
- (e) establish mechanism to analyse and methodologies to measure potential financial losses arising from identified risk events associated with the IFI's roles and responsibilities under the *wakalah*;
- (f) set out risks exposure limit to mitigate potential excessive risk taking, if applicable;
- (g) where applicable, outline risks mitigation measures or instruments, such as takaful cover, acceptance of collateral, employment of guarantee or provision for exit mechanism in the *wakalah*;
- (h) establish mechanism to monitor the IFI's performance in satisfying its contractual obligations, sufficiency of the collateral value, compliance with Shariah requirements and internal policies; and
- (i) scope and frequency of risks reporting to the Board and where applicable, observation on Shariah non-compliance risks to the Shariah Committee.

**26. Financial disclosures**

- S 26.1 An IFI must maintain proper accounting and other records for the reporting of financial performance in a timely manner to ensure that financial statements are prepared in a true and fair manner.

**27. Business and market conduct**

- S 27.1 An IFI shall ensure that *wakalah* arrangement is conducted in a fair and transparent manner and give due regard to the interests of all contracting parties.

**Fair dealings**

- S 27.2 An IFI must ensure that its internal policies and procedures on business and market conduct for *wakalah* arrangements reflects transparency and fair dealing practices to all contracting parties including –
- (a) the obligation to disclose the roles and responsibilities in a timely and accurate manner and is not misleading;
  - (b) the applicable fees and charges; and
  - (c) reasonable care is taken to ensure suitability of advice and recommendations made by the IFI.
- S 27.3 Where an IFI acts as an agent, the IFI –
- (a) must inform the principal on the completion of the *wakalah* contract; and
  - (b) ensure that terms and condition of the *wakalah* contract preserves the rights and interest of the principal, including any amendments made during renegotiation or extension of contract.

**Disclosure of information**

- S 27.4 At pre-contractual stage, an IFI must provide adequate and relevant information to potential contracting parties to facilitate informed decision-making.

**PART D SUBMISSION REQUIREMENT****28. Submission requirement**

- S 28.1 An IFI that currently offers a product or service that is structured based on *wakalah* contract must assess the consistency of such product or service with this policy document and if applicable, develop necessary action plan to comply with this policy document. The action plan and the implementation plan shall be submitted to Jabatan Perbankan Islam dan Takaful (JPIT) no later than 31 October 2016.
- S 28.2 An IFI must immediately notify JPIT if the IFI identifies any cause that will affect full compliance with this policy document by 1 July 2018.

## APPENDICES

### Appendix 1 Legitimacy of *wakalah*

1. The legitimacy of the *wakalah* contract is derived from the Quran and founded on the Sunnah of Prophet Muhammad (peace be upon him) and the consensus of Muslim jurists (*ijma`*).

#### The Quran

2. The following verse of the Quran implies the general permissibility of *wakalah*:

"...فَابْعَثُوا أَحَدَكُمْ بِوَرِقِكُمْ هَذِهِ إِلَى الْمَدِينَةِ فَلْيَنْظُرْ أَيُّهَا أَزْكَى طَعَامًا فَلْيَأْتِكُمْ بِرِزْقٍ مِنْهُ..."

"...So send one of you with this silver coin of yours to the city and let him look to which is the best of food and bring you provision from it..." (Surah al-Kahf, verse 19)

#### The Sunnah of Prophet Muhammad (peace be upon him)

3. The following *hadith* implies the general permissibility of *wakalah*:

i. عن عروة أن النبي صلى الله عليه وسلم أعطاه دينارا يشتري له به شاة، فاشترى له به شاتين، فباع إحداهما بدينار، وجاءه بدينار وشاة، فدعا له بالبركة في بيعه، وكان لو اشترى التراب لربح فيه.

"Urwah reported that the Prophet (peace be upon him) gave him a dinar to buy a sheep. He bought two sheep, sold one of them for a dinar, and brought him a sheep and a dinar. So the Prophet (peace be upon him) invoked a blessing on him in his business dealing, and he was such that if he bought dust he would make a profit from it..." (Sahih Bukhari, Hadith no. 3370)."

ii. عن جابر بن عبد الله قال: أردت الخروج إلى خيبر فأتيت رسول الله صلى الله عليه وسلم فسلمت عليه وقلت له: إني أردت الخروج إلى خيبر، فقال: إذا أتيت وكيلي فخذ منه خمسة عشر وسقا، فإن ابتغى منك آية فضع يدك على ترقوته.

Jabir ibn 'Abdullah narrated, "I wanted to go out to Khaybar so I came to the Messenger of Allah (peace be upon him), greeted him and said: 'I want to go out to Khaybar.' He said: When you come to my agent, take fifteen wasq of dates from him. If he asks for proof that you are my agent, place your hand on his collarbone..." (Sunan Abi Dawud, Hadith no. 3148).

#### The consensus of Muslim jurists (*ijma`*)

4. Muslim jurists have reached *ijma`* on the permissibility of *wakalah*.

## Appendix 2 Definition and interpretation

Terms	Definition
<i>Amanah</i>	Fiduciary duties
<i>Amin</i>	Trustee
<i>Fuduli</i>	A person is acting on behalf of another person without <i>wakalah</i> appointment or an appointed agent act beyond the mandate
<i>Hibah</i>	Transfer of ownership of an asset from a donor to a recipient without any consideration and is a form of benevolent contract
<i>Hiwalah al-dayn</i>	Transfer of debt
<i>Hukm al-`aqd</i>	Effect of transaction
<i>Huquq al-`aqd</i>	Rights and responsibilities of transaction
<i>Ijab</i>	Offer
<i>Ijarah</i>	Lease or service contract
<i>Ijma`</i>	Consensus of Muslim jurists
<i>Istisna`</i>	Contract which a seller sells to a purchaser an asset which is yet to be constructed, built or manufactured according to agreed specifications and delivered on an agreed specified future date at an agreed pre-determined price
<i>Kafalah</i>	Guarantee
<i>Kafil</i>	Guarantor
<i>Mudarabah</i>	Profit-sharing contract
<i>Mukhalafah al-shurut</i>	Breach of terms and conditions
<i>Muqassah</i>	Offsetting
<i>Murabaha</i>	Sale and purchase of an asset where the acquisition cost and the mark-up are disclosed to the purchaser
<i>Musyarakah</i>	Profit-and-loss-sharing contract
<i>Muwakkil</i>	Principal
<i>Qabul</i>	Acceptance
<i>Rahn</i>	Collateral
<i>Ta`addi</i>	Misconduct
<i>Takaful</i>	Islamic insurance
<i>Taqsir</i>	Negligence
<i>Tawarruq</i>	Purchasing an asset with a deferred price, either on the basis of <i>musawamah</i> or <i>murabahah</i> , and subsequently selling it to a third party to obtain cash
<i>Ujrah</i>	Fee
<i>Ujrah al-mithl</i>	Fee based on market rate for a similar task done
<i>Wakalah</i>	Agency contract
<i>Wakalah bi al-istithmar</i>	Agency contract for investment
<i>Wakalah bi al-ujrah</i>	Fee based agency
<i>Wakalah muqayyadah</i>	Restricted agency
<i>Wakalah mutlaqah</i>	Unrestricted agency
<i>Wakil</i>	Agent