

Review

Historical development of Islamic institutions: A case of Malaysian government

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Malaysia is a modern postcolonial state with a written constitution which clearly states 'Islam as religion of the Federation'. The state gained its independence on August 31, 1957 from the British. This paper aims to discuss the establishment of significant institutions in Malaysia that became significant catalyst to develop the country within its multi-religious population. In the beginning of the 1980s, the government embarked intensively on an Islamisation programme which included an agenda to upgrade the Islamic institutions as well. In fact, much effort has been given by the government in implementing moderate Islam in Malaysia. As a direct result, many institutions were established to promote the agenda and to prove that religion is not a conundrum for progressive country. This is a secret key for the country to succeed in economics, administration, and institutions with its political stability.

Key words: Malaysia, Islamic institution, Islam in modern era, progressive.

INTRODUCTION

Since more than half a century of Malaysia's independence, Islam has become increasingly dominant in the public domain, with its multi-ethnic and multi-religious federation. Ahmad Ibrahim stated that, although, the first Malaysian Prime Minister Tunku Abdul Rahman did not claim to build Malaysia as an Islamic state and in fact said that Malaya was a secular state, yet his effort laid the foundation for the introduction of Islamic values in the government and the administration (Nair, 1997: 33, 38). It was himself and United Malay National Organization (UMNO), which insisted on the clauses in the Federal Constitution of Malaysia, article 3(1) stating that Islam is the religion of the Federation despite the opposition from

the rulers and the rejection in the draft constitution prepared by the Reid Commission. The Reid Commission consisted of five persons under the chairmanship of Lord Reid, the Scottish Judge. The other members were Sir Ivor Jennings, the Cambridge jurist; Sir William McKell, a former Judge Governor-General of Australia; Mr. Justice B. Malik, an Indian Judge; and Mr. Justice Abdul Hamid, a Pakistani Judge (Harding, 1996; Lee, 2010; Bari and Shuaib, 2004).

There was also no statement in the constitution that Malaya is a secular state (Bari, 2001). The constitution has a definition of "Malay" which emphasises that for a person to be Malay, he must be a Muslim as stated in article 160(2) of the Federal Constitution. "Malay" was made the national language of the State according to article 152. The *Yang di-Pertuan Agong* is required to include in his oath of office a statement that he will at all times protect the religion of Islam as in article 37. Special

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privileges for the Malays are included in the constitution (article 153) (Ali, 2008; Barlow and Wah, 2003) and there are provisions for the Malay reserved land. The sovereignty, prerogatives and powers of the rulers are protected. It may be remembered that Tunku Abdul Rahman was the founder and president of *Pertubuhan Kebajikan Islam Malaysia* (PERKIM) and in his later life, he served as the Secretary-General of the Islamic Secretariat in Jeddah, Saudi Arabia and later known as Organisation of Islamic Conference (OIC) (Ibrahim, 2000). According to Hussin Mutalib, under Dr. Mahathir's leadership, the Malaysian Government could be said to become more supportive of Islam (Mutalib, 1993). Shanti Nair has similar opinion by stating that the assumption of Dr. Mahathir to the office of Prime Minister in 1981 was to herald a dynamic new strategy for both domestic and foreign policy with a policy of 'Islamization' (Nair, 1997). An early signal of the Dr. Mahathir administration's interest in Islam was the official declaration by Dr. Mahathir in 1984 to 'Islamise government machinery'. In the midst of the uneasiness felt by non-Muslims, Dr. Mahathir had to clarify what he meant by such a policy:

"What we mean by Islamisation is the inculcation of Islamic values in government. Such inculcation is not the same as implementation of Islamic laws in the country. Islamic laws are for Muslims and meant for their personal laws. But laws of the nation, although not Islamic-based, can be used so long as they do not come into conflict with Islamic principles" (Mutalib, 1993).

It may be noted here that since 1983, the sphere of application of Islamic law has extended beyond family matters into economics and finance. These areas were previously the monopoly of English law, but beginning in 1983, several laws have been passed by parliament which relied on *shari'ah* principles such as the *Islamic Banking Act 1983*, *Government Investment Act 1983*, and *Takaful Act 1984*, as well as government guidelines concerning Islamic financing scheme for civil servants buying houses and motor vehicles, Islamic pawn shops and opening of Islamic banking windows in conventional banks, which evidently extend the *shari'ah* into the sphere of public life (Kamali, 2000).

Politically, in facing challenges from *PAS* who concentrates on applying Islamic policy, the federal and state governments, under the leadership of the ruling *UMNO*-led government responded by adopting policies design to out-Islamicise *PAS*, to retain Malay support and to highlight *UMNO*'s role as the champion of Malay cause. Most notably, this included a declaration in 2002 that Malaysia was already an Islamic state since it had Muslims-dominated population (Neo, 2006).

THE POLICY OF THE 'APPLICATION OF ISLAMIC VALUES IN ADMINISTRATION'

The policy of the 'application of Islamic values in

administration' introduced by Dr. Mahathir's government is in line with the status of Islam as the country's official religion. The aim is to create a society of trustworthy, efficient, effective, just and disciplined national administration and a productive nation.

A set of eleven values have been adopted for public service employees to put into practice. These values are trustworthiness, discipline, responsibility, co-operation, sincerity, morality, dedication, cleanliness, moderation, gratitude to God and diligence. These are common universal values and acceptable to all people. Mohd. Noor Deris wrote that the policy of 'application of Islamic values in administration' is a vision which is in line with Islamic teachings. It is a concrete plan relating to the steps and programmes to achieve the goal of establishing a new society which is committed in implementing Islam as their way of life (Deris, 1997).

According to Mahdi Shuid and Mohd. Fauzi Yunus, it is still too early, at this stage, to gauge the degree of success of the policy. Since the policy aims at changing and strengthening human values and way of life, it is unrealistic to expect quick results. Many factors will determine the success or failure of the policy. Among them are the allocation of funds, the political will, the machinery to carry out the policy effectively and the willingness of the target group to accept the policy (Shuid and Yunus, 2001).

Mohd. Noor Deris listed out some of the positive effects to the Muslims government officers; they are more honest in fulfilling their duties, have better relationships with public and give more cooperation to their office-mates. While some of the positive effects to non-Muslims officers are; they are more responsible in fulfilling their duties, give more respect to the superiors, have better relationships with public, give more cooperation to their office-mates and more appreciative towards the rewards and facilities that have been given to them (Deris, 1997).

Ahmad Ibrahim commented that even the Government has declared its policy of introducing Islamic values in all aspects of our life; unfortunately, this policy does not appear to have been applied in the administration of justice. The judges of the Supreme Court still pride themselves on administering a secular system of law and they have made no effort to prepare themselves nor take any positive steps to do so. Being trained in a secular system of law, they have admitted that they are not qualified to determine questions relating to the Islamic law. They have accepted that the Federal Constitution is a secular constitution and that it is their duty to apply secular law (Ibrahim, 2000).

THE ESTABLISHMENT OF ISLAMIC INSTITUTIONS

Efforts by the Malaysian government in implementing Islam in a moderate and peaceful way can also be proven by the establishment of Islamic institutions bas further discussed.

Lembaga Tabung Haji (LTH)

The first Islamic financial institution introduced to Malaysian financial system was the *Lembaga Urusan dan Tabung Haji* (LUTH), the Pilgrims Fund Board, in 1969 (Borhan, 2001). Based on the awareness of the difficulty faced by Muslims to perform the pilgrimage, Ungku Aziz after doing a research and analysis relating to the rural economy in the year 1950's, found that Muslims only save their money with the single motive of performing the pilgrimage. He then submitted the memorandum to the Government in 1959 suggesting the need for the establishment of financial body or institution to manage the funds of the future Malaysian Muslims pilgrims without being based on usury (*riba*) system but through investments which are compliance to *shari'ah* and can give benefit for them. Ungku Aziz was in the view that, if the Government agrees to establish a body to manage the saving of the future pilgrims, not only the Muslims in this country will gain benefits from it but also the fund, which are huge, can be used for the country's future development.

Based on this suggestion and with the approval of the Rector of al-Azhar University, Sheikh Mahmud al-Shaltut that the suggestions by Ungku Aziz were not contrary to Islamic teaching, *Perbadanan Wang Simpanan Bakal-bakal Haji* was established in 1962. In order to improve the administration of pilgrimage in Malaysia, in 1969, the Government combined this body, which was located in Kuala Lumpur, with *Pejabat Urusan Haji* (Office of the Pilgrimage Management) which had been established in 1951 located in Penang. The combination of both bodies has led to the establishment of the Pilgrims Management and Fund Board (*Lembaga Urusan dan Tabung Haji* - now known as *Lembaga Tabung Haji*). This body was established under the *Pilgrims Management and Fund Board Act 1969*, and *Pilgrims Management and Fund Board (Amendment) Act 1973*. The main objective of this institution is to help and improve the welfare of the Muslims while performing the pilgrimage and to unite the savings from Muslims in an effective way according to Islamic teachings (Ghani, 1999).

The administration of *Tabung Haji* also deducts and pays the *zakat* on the savings of the depositors and at one time it has been able to pay a bonus of 9.5% annually. *Tabung Haji* is now regarded as one of the strongest financial institutions in Malaysia, owned and managed by Muslims (Ibrahim, 2000).

Islamic banking

The initial demand for the establishment of Islamic banking system was stimulated by developments in Egypt where the first Islamic bank was launched in Mit Ghamr earlier in 1963 (Ariff, 1998). There was a step further in the 1973 resolution of the Islamic Conference of

Foreign Ministers and the setting up of the Islamic Development Bank in Jeddah in the following year. This was, in turn, followed by similar developments in Dubai, Sudan, Jordan and Bahrain where Islamic banking saw their early beginnings in the 1970s. In view of those developments in Muslims countries have led to the establishment of Bank Islam Malaysia Berhad (BIMB) (Ahmad and Haron, 2002) which was incorporated as a public limited company under the Malaysia *Companies Act 1965* and its activities were separately regulated under the *Islamic Banking Act 1983*. The Act amounted to making a few changes in the Banking Act 1973 by adding some additional provisions and making appropriate amendments to permit Islamic Banking operation (Ariff, 1992; Ngan and Kandiah, 2008). In launching BIMB in 1983 the fourth Prime Minister Dr. Mahathir described it as "the first step in the larger concept of an Islamic economy" and "an alternative to the western banking system" (Kamali, 2000).

In general, the provisions in the *Islamic Banking Act 1983* follow those in the *Banking Act 1973* in regard to financial requirements, maintenance of reserve funds, statutory requirements and powers of supervision and control by the Central Bank (Bank Negara) with slight modifications.

As the Islamic bank engages itself in Islamic banking business, section 30 of the *Banking Act 1973* (which forbids a bank from engaging in trade) will not apply to it and is not included in the *Islamic Banking Act 1983*. "Islamic banking business" is defined in the *Islamic Banking Act 1983* as a banking business whose aims and operations do not involve any element which is not approved by the religion of Islam. To ensure that the business of the Islamic bank does not contravene with the requirements of the Islamic religion and law, the Bank has a Syariah Advisory Body to advise it on the operations of its banking business in order to ensure that they do not involve any element which is not approved by the *shari'ah*.

It is also provided that the Islamic bank should, in addition, make provision for taxation under section 22 of the *Banking Act 1973*, and should also make provisions for the payment of *zakat*. The facilities that are provided by the Islamic Bank in general are similar to those provided by other commercial banks. Its customers can maintain current accounts and deposit accounts. However, no interest is payable. In addition, the customers can deposit their money in the investment accounts in which the profits and losses will be shared with the bank. The Islamic Bank can also provide services for the transmission and transfer of money, the purchase and sale of currency and the financing of trade documents, for all of which the Islamic Bank can charge commissions. Additionally, the Islamic banking business provides the methods of *mudarabah*, *musharakah*, *bai' bithaman ajil*, *murabahah*, *wadi'ah* and *ijarah* (Ibrahim, 2000).

The merger between Bank Bumiputra Malaysia Berhad (BBMB) and Bank of Commerce Malaysia Berhad (BOCMB) resulted in the formation of Bumiputra-Commerce Bank Berhad (BCBB – now known as CIMB) and also Bank Muamalat Malaysia Berhad (BMMB), the second bank to operate on the *shari'ah* principles. Bank Muamalat Malaysia Berhad has started its operations on October 1st, 1999 with combined assets and liabilities brought over from the Islamic banking windows of the Bank Bumiputra Malaysia Berhad, Bank of Commerce (M) Berhad and BBMB Kewangan Berhad (<http://www.muamalat.com.my>).

Islamic banking windows in conventional banks

The opening of Islamic banking windows, the so-called *Skim Perbankan Tanpa Faedah* (SPTF), which is the interest-free banking scheme in 1993 was a landmark development in the short history of Islamic banking in Malaysia (Dakian, 2005; Hasan et al., 2005). The essence of this development was to utilise the existing conventional banking system to introduce Islamic banking to the public.

In July 1993, Bank Negara Malaysia issued guidelines on the SPTF under section 126 of the *Banking and Financial Institutions Act 1989*. The conventional participating banks were then authorised to open Islamic banking counters and offer the same products and services as have been offered by Bank Islam. A pilot scheme was thus devised under the new guidelines for the first batch of conventional banking institutions that were ready to embark on the interest-free banking scheme.

It was a voluntary exercise designed to stimulate wider participation and within a short time the number of conventional banks offering Islamic banking services grew from only 3 in 1993 to 52 four years later (1997). The Islamic banks and participating banks have also developed more than 20 products since 1983 which have become widely available in the system.

More recent measures to promote Islamic banking in Malaysia include the Bank Negara decision to replace the term *Skim Perbankan Tanpa Faedah* (SPTF) with "*Perbankan Islam*" or "Islamic Banking" with effect from 1st December 1998. It was also decided that the more diversified banking products which are now available require the organisational structure of the Islamic Banking Units should be upgraded and expanded into Islamic banking divisions with wider scope and responsibility delegated to their staff (Kamali, 2000).

Islamic insurance (Takaful)

Insurance in Islam is essentially a concept of mutual help (Thanasegaren, 2008). It is generally agreed that the

system of insurance practised by the conventional insurance companies is contrary to the principles of Islam because it involves (a) *gharar* (unknown or uncertain factors in the operation of the contract) (b) *maysir* or gambling and (c) *riba* or interest. In place of that type of insurance, it has been suggested that a system of mutual insurance or *takaful* to be set up as to overcome the objections to the existing form of insurance. The difference between Takaful and conventional insurance rests in the way the risk is assessed and handled, as well as how the Takaful fund is handled (Iqbal, 2005). Shari'a scholars are generally of the opinion that to be Shari'a compliant for insurance, the premium must be paid on the basis of *tabarru'* (an Arabic word meaning donation, gift or contribution) (Jaffer, 2007).

Hence, the concept of *takaful* is based on (a) mutual liability (b) mutual co-operation and (c) mutual assistance and help. Moreover, it attempts to avoid all involvement in *riba* transactions. *Takaful* may be translated as "joint guarantee". It is a method of joint guarantee among a group of members or participants against loss or damage that may be suffered by any of them (Ibrahim, 2000).

Attempts to have a system of insurance in line with Islamic principles had been made in the Sudan, Saudi Arabia and by the *Dar al-Mal al-Islami* in Switzerland. A working committee was therefore set up in Malaysia to study the system and make recommendations for its implementation in Malaysia. The committee visited the Sudan, Saudi Arabia and Geneva to study the system and made recommendations. The report of the working committee was accepted by the government and the system of *takaful* was introduced by the *Takaful Act 1984*. This Act, drafted and recommended by the Committee, was based on the *Insurance (Amendment) Act 1983*, with such modifications and amendments as were necessary to conform to the *shari'ah* and *takaful* business practices. The main differences are related to the matters of deposits and investment, which can be, affected by the *Takaful* Company. In addition, a Syariah Supervisory Council is appointed to advise the *Takaful* Company on the operations of the *takaful* activities in order to ensure that it does not involve any element which is not approved by the *shari'ah*. Recently insurance companies run on conventional lines have also been allowed to offer *takaful* policies (Ibrahim, 2000).

In its normal operations, the Islamic bank often assumes the roles both of a trustee and entrepreneur, and it is therefore responsible to ensure the safety of capital assets and securities of its clients against loss, damage and destruction. The Islamic bank also needs to ensure the safety and security of its own assets and interests arising from the financing and credit facilities it provides to customers. *Takaful* products have thus been designed to respond to these needs.

Takaful operations in Malaysia are regulated and supervised by Bank Negara Malaysia (BNM) and the BNM Governor acts as the Director General of insurance

and *takaful* (Kamali, 2000). There are a number of *takaful* operators at present, such as Takaful Ikhlas Sendirian Berhad, BSN-Prudential Takaful, Takaful Etiqa and Takaful Malaysia.

Islamic stock index

The Islamic capital market comprises stock-broking activities in corporate securities and Islamic stock index, which are based on *shari'ah* compliant counters. They are now operating as exclusively Islamic stock-broking firm and several conventional ones that offer Islamic brokerage services. A separate stock market, based strictly on Islamic principles, is still very much at an early stage of evolution. Countries such as Malaysia are making solid progress in establishing the necessary infrastructure to facilitate stock trading in accordance with Islam (Naughton and Naughton, 2000). In April 1999, the Kuala Lumpur stock exchange (KLSE) introduced the Islamic equity benchmark index for those who wish to invest according to *shari'ah*. The KLSE Islamic index monitors *shari'ah*-compliant stocks from both the Main Board and Second Board.

Public listed, or even unlisted, companies may raise capital through the issuance of shares based on *mudarabah* and *musharakah* modes, provided they are engaged in a *shari'ah* accepted line of business. These companies are formed under the *Companies Act 1965*. Their forms, the terms of share issues and liability are similar to the *shari'ah* approved formula on limited liability company, or *inan*.

To ensure that the shares of these companies may lawfully be owned and traded by Muslims, the Syariah Advisory Council of the Securities Commission issues a list of Approved Securities, also known as the *Halal* Counters, and it is updated from time to time. The list contains names of the companies on the main and the second boards of the Kuala Lumpur Stock Exchange (KLSE) which are *shari'ah* acceptable and excludes those which are not. The list thus precludes companies whose major activities are *riba*-based or involve in gambling, alcoholic beverages and non-halal products. The BIMP stock and stocks of many other Islamic banking scheme (*Skim Perbankan Islam – SPI*) participants are listed on the Main Board and therefore full participants in the stock market activities (Naughton and Naughton, 2000).

Islamic pawn broking (*al-Rahn*)

In the place of conventional pawn broking, which also involves interest and may cause the pawner to lose his property, the system of *rahn* is being introduced in Malaysia. The introduction of the *shariah* based Islamic pawn broking system called *Ar-Rahnu* in Malaysia

provides an alternative to access an interest-free and low cost short-term cash advance (Bhatt and Sinnakkannu, 2008). The system of pawning under the *Pawnbrokers Act 1972*, with its provision for the taking of interest, is unacceptable in Islamic law. Islam in fact has an alternative system in the *rahn*. In order to ensure the repayment of a debt, the creditor may ask for a surety or sureties or for a pledge (*rahn*). In the Qur'an it is stated to the effect:

"If ye are on a journey, and cannot find a scribe, a pledge with possession (may serve the purpose) (of surety). And if one of you deposits a thing on trust with another, let the trustee (faithfully) discharge his trust, and let him fear his Lord. Conceal not evidence: for whoever conceals it - his heart is tainted with sin" (Al-Baqarah 2: 283).

Attempts have been made to introduce the Islamic system of *rahn*. The system of *rahn* was introduced in Terengganu in January 1992 and in Kelantan in March 1992. On 27th October 1993, Bank Rakyat in co-operation with the *Yayasan Pembangunan Ekonomi Islam Malaysia (YPEIM)* introduced the *Rahn* system in Kedah, Penang, Johor, Negeri Sembilan, Kuala Lumpur and Terengganu. The borrower under the system of *rahn* deposits his property and obtains the loan from the branch of bank which will charge an amount to cover the cost of deposit and insurance (if any). If the borrower is unable to repay the loan the pawnshop can sell his property to cover the cost, giving the balance back to the borrower. No interest charges are levied (Ibrahim, 2000).

Islamic higher education institution: International Islamic University Malaysia (IIUM)

The Islamic higher education institution in the country, International Islamic University Malaysia (IIUM) was established in 1983 by the Malaysian Government with support from the Organisation of Islamic Conference and a number of individual Muslim countries (Jeffreys, n.d.; Abu Bakar and al-Shboul, 2008). It aims to regain the Ummah's global leadership in the quest, acquisition and application of knowledge and skills. This duty is embodied in its vision statement:

"IIUM aims at becoming an international centre of educational excellence which seeks to restore the dynamic and progressive role of the Muslim ummah in all branches of knowledge."

IIUM is governed by a board representing eight sponsoring governments and several international organisations, including the League of Islamic Universities, the Federation of Universities in the Islamic World, the International Association of Universities and the Association of Commonwealth Universities. It is also

affiliated with a number of Malaysian-based business and professional organisations, giving IUM students in various disciplines ample opportunities to gain practical experience as temporary employees and interns (International Islamic University Malaysia, 2002).

Zakat centre (Pusat Pungutan Zakat - PPZ)

In Malaysia, there is a proposal to collect *zakat* in a more efficient and productive manner. In the Federal Territory (Kuala Lumpur, Labuan and Putrajaya), there is a *zakat* centre which has organised the collection of *zakat* on the hidden wealth including that on businesses, professions and employment, in an efficient and professional manner using trained accountants and other personnel and modern equipments including computers. The success of these centres have led the government to suggest to the state authorities that the collection of *zakat* on this hidden wealth should be done on a federal level, leaving the collection of *zakat al-fitr* and the *zakat* on unhidden wealth, including *padi* (rice) and animals to the States. In Malaysia if a person pays *zakat*, it is allowed as a rebate on his income tax, so that a total income tax payable by him is deducted by *zakat* as he has paid. This has helped to persuade the Muslims to pay the *zakat* on their inner-self (*batin*) wealth. The calculation system for *zakat* has been established by the *zakat* centre itself considering theories according to Islam (Abdul Rahman and Awang, 2003). The *Zakat* centre will pay the collections to the various states from where they are collected and the money will then be distributed to the persons entitled thereto. It is hoped that the distribution of the *zakat* will be better administered so that in time that payment is from the income of the amount invested for the various *asnaf* instead of from the total amount collected (Ibrahim, 2000).

CONCLUSION

These are some significant efforts by the Malaysian government in implementing moderate Islam by establishing institutions that are able to boost the image of the country. There are also other Islamic institutions established by the government such as Institute of Islamic Understanding Malaysia (*Institut Kefahaman Islam Malaysia* – IKIM), Islamic Centre (*Pusat Islam*), *Yayasan Pembangunan Ekonomi Islam Malaysia* (YPEIM), and others. This shows that Malaysian government is very serious in engaging with developing and managing its status within the frame of moderate Islam. The fourth Prime Minister, Dr. Mahathir had also announced that Malaysia is an Islamic state in a moderate understanding. However, there are still a lot of areas need to be improved under the leadership of the sixth Prime Minister, Najib Razak. Both the government and the opposition have their own opinions to develop the country further in

multicultural Malaysia.

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