

## Does Islamic Financial Institutions Need to Pay Zakat?

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Former Chief Justice, Tun Abdul Hamid Mohamad who is also ex-member of the Syariah Advisory Council of the Bank Negara Malaysia made a significant statement that zakat to be collected only from persons professing the religion of Islam but not for companies and this include Islamic financial institutions (IFIs). He said that the Fatwa Committees fail to make a distinction between a Muslim human being and a company when they apply the obligation to pay zakat to companies.

This statement raises an issue as to the current zakat practice by IFIs. The existing practice signifies that in some IFIs, the shareholders are paying zakat themselves and in several IFIs, the shareholders pay their own zakat and authorise IFIs to pay 2.5 or 2.577 per cent with respect to the "Retained Earnings" and "Reserves" held by IFIs. Based on the annual reports of these institutions, IFIs significantly contributed zakat to the zakat institutions. The statement by Tun Abdul Hamid hence seems to support the practice of several IFIs that do not pay zakat at all although the profit generated annually may amount to billion of ringgit.

Considering the importance of this issue, this article attempts to clarify and briefly discusses the discourse on the position of companies or corporation from Shari'ah perspective and finally to conclude whether IFIs have obligation to pay zakat or not. It is important to note that the arguments put forth in this article are not intended to refute the statement made by Tun Abdul Hamid Mohamad but rather to highlight the Islamic law position on the concept of corporation and its relation with zakat obligation. In other words, the author's concern is can zakat be imposed on companies as they are not human beings and is the concept of legal entity acceptable to Islamic law?

Generally, although the concept of partnership in the form of *musyarakah* or *mudharabah* has been well known since the early period of Islam, it is found that there is less discussion on a concept akin to 'corporation'. In fact, Professor Timur Kuran writes that 'corporations' were absent from the Middle East until the nineteenth century. The role of an unincorporated trust or *waqf*, which is able to stimulate the economy and provide additional funds to the state, leads to less demand for commercial or financial organizations in the form of corporations.

In addition, it is contended that the corporate form of business organization with a separate legal entity does not appear directly in the classical *fiqh* discussions by Muslim jurists as mentioned by Professor Schacht who argues that Islamic law does not recognize the concept of a juristic person or artificial legal entity. This is supported by a group of eminent scholars in Pakistan who argue that the concept of juristic person and limited liability are alien to *Shari'ah* and exploitative in nature. Professor Vogel and Professor Hayes also

mention that classical Islamic law only discusses a concept of partnership and not modern companies with an artificial personality.

Nevertheless, the author views that such a contention is not truly accurate as Muslim jurists have already accepted a concept of corporation known as *Shahsiyah l'tibariyah* (juristic person) based on principles of *qiyas* (analogy), *istihsan* (equity), *masalih mursalah* (public interest) and *dhimma*. In fact, the existence of public treasury (*bayt al mal*) and *waqf* implies the recognition of the concept of corporation. Even though there was no corporation during the time of the Prophet Muhammad, the notion of such concept has since existed in the form of limited partnership or *Syarikah al-Inan*, whereby the shareholders may sell their shares in the market and their liability is limited. In addition, the structure of a joint-stock company is considered as a variation on the concept of *mudharabah*, which acknowledges the notion of separation of ownership and control.

With regard to the concept of limited liability, Mufti Taqi Usmani asserts that such a concept is actually not alien or new to a *Shari'ah* point of view. While admitting that the concept of limited liability as understood in the modern practice is a new concept in traditional *fiqh* literature, various principles laid down in Islamic jurisprudence provide strong justification for its establishment, such as the concepts of *waqf* and *bait al mal*, the principle of joint stock in partnership as advocated by *fiqh* of *Shafi'i*, the principle of *khultah al syuyu* (mixture of shares) in the levy of *zakah*, the principle of inheritance under debt and an analogy of limited liability of the master of a slave. This view is also supported by many prominent Muslims scholars, such as Abdul Qadir Audah and Mustafa Zarqa. All of these principles infer and deduce the validity of the limited liability concept in Islam.

Based on the foregoing discussion, it is submitted that the concept of artificial personality or a corpus with a separate legal entity is clearly acceptable in Islam. The grounds justifying this preposition include the compatibility concept of legal entity in Islamic law and the consideration of *maslahah* (public interests). This position indicates the IFIs' obligation to pay zakat and affirms the existing practice of zakat contribution by most of IFIs all over the world.

In addition, the Islamic Fiqh Academy and the Accounting and Auditing Organizations for Islamic Financial Institutions (AAOIFI) *Shari'ah* Council affirm the acceptability and recognition of the concept of limited liability, whereby the former states "there is no objection in *Shari'ah* to setting up a company whose liability is limited to its capital" and the latter mentions in the AAOIFI *Shari'ah* Standards No. 12, which accepts its practice through incorporation by law. In the light of the above, probably, the national and state fatwa committees need to issue *Shari'ah* rulings to consider IFIs to be regarded as legal entity and hence at least to resolve this inherent issue of recognizing the company as a juristic person.

