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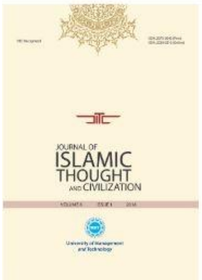

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Interest Free Banking and Finance in Brunei Darussalam: Present Realities and Future Prospects

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Abstract

Brunei is among the few countries vigorously pursuing interest-free banking. Looking at its status, there is no doubt that Islamic banking and finance remains a governmental project in Brunei. This paper examines the development and progress of this institution in Brunei highlighting the present experiences, future prospects, and imminent expectations. Islamic banking and finance has ushered in a new economic order in the country. Although the system is still in its primary stages of development, it has been successful. Indeed, it has good prospects due to political will and cooperation. Political will is fundamental to the fruitful implementation of a new economic order and efficient Islamization in Brunei has facilitated the establishment of sound socio-cultural and economic foundations vigorously promoting the essential values of Islam. Nonetheless, the 'call' for economic diversification has some implications for interest-free banking institutions in the country because diversification invariably exposes an economy to international interests and more importantly, empowers the private sector. These bring forth the likelihood of promoting interest-based banking and financial practices. We, therefore, conclude that Islamic banking has been very successful in Brunei but it still remains vulnerable to non-political future challenges subject mainly to the economic fortunes and prospects of the petro-dollar.

Keywords: Brunei, Islamic banking, *ribā*, economy, economics, petro-dollar

Introduction

Financial transactions in conventional or secular interest-based banks and economic constraints on poor people fuelled by interest have been a source of worry for

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ethically-minded scholars, both religious and secular.[1] All religious groups and societies with a considerate moral thinking, from the ancient times to Judaism and Christianity, have discouraged usury[2] or interest. For example, Christianity officially banned usury in 325 CE at the Council of Nicea, which prohibited the 'Fathers' from usury. During the reign of Prince Charles the Great, who is known in the French West as Charlemagne, both the Church and the state banned usury.[3] Interest is defined as 'any increment demanded beyond the principal of a loan.'[4] The writings of Aristotle, from *Nicomachean Ethics* to *The Politics*, produced a sequence of economic thought under the umbrella of justice.[5] In the *Nicomachean Ethics*, for example, Aristotle denounced usury[6] likewise Plato.[7]

Islamic banking has also emerged as an Islamic socio-religious reaction to the ancient economic innovation of usury or interest. It has, therefore, appeared as a new reality on the global financial scene. Its principles are, however, not new because they were detailed in the Qur'ān and the Prophetic Tradition (*SAW*). Islamic banking or financial business seems to have begun at the time of the Prophet's (*SAW*) business with Khadījah. However, conventional Islamic Banking emerged during the Islamic 'renaissance' immediately following the World War II, particularly in the 1960s, when Muslim nations bid farewell to European imperialism.[8] It was further accelerated by the petrodollar proliferation of the 1970s in the Muslim world which created the need to engender a financial system liable to Islamic values and consistent with the Islamic

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[1] R. F. Harrod, *Towards a Dynamic Economics: Some Recent Developments of Economic Theories and their Application to Theory* (London: Macmillan, 1948), 129-159; M. Lewison, "Conflicts of Interest? The Ethics of Usury," *Journal of Business Ethics,* 22 (1999): 327; T. Wilson and R. H. Tawney, *A Discourse upon Usury: by Way of Dialogue and Orations, for the better Variety and more Delight of all those that shall read this Treatise* [1572] (London: George Bell, 1925); E. L. Glaeser and J. Scheinkmann, "Neither a Borrower nor a Lender be: An Economic Analysis of Interest Restrictions an Usury Laws," *Journal of Law and Economics* 41, no. 1 (1998): 1-36; T. G. Tarpett, ed., *Trade and Usury: Selected Writings of Martin Luther (1523-1526)* (Philadelphia, PA: Fortress Press, 2007).

[2] J. Rutherford, "Usury: Necessary Evil or Evil Necessity?," in L. C. Neilson (ed.), *The Future of Marketing's Past: Proceedings of the 12th Conference on Historical Analysis and Research in Marketing, Queen Mary Long Beach* (California: 2005), 261; R. B. Ekelund, R. F. Herbert and R. D. Tollison, "An Economic Model of the Medieval Church: Usury as a Form of Rent Seeking," *Journal of Law, Economics and Organization* 5, no. 2, (1957): 307-331; D. Wood, *Medieval Economic Thought* (New York: C.U.P, 2002); Timur Kuran, *The Long Divergence: How Islamic Law Held Back the Middle East* (NY: Princeton University Press, 2011), 146.

[3] Habib A. Zuberi, "Interest free Banking and Economic Stability," *Pakistan Development Review* 31, no. 4, (1992): 1077.

[4] R. De Roover, "Scholastic Economics: Survival and lasting Influence from the Sixteenth Century to Adam Smith," *Quarterly Journal of Economics* 69, no. 2, (1955): 173.

[5] M. Wykes, "Devaluing the Scholastics: Calvin's Ethics of Usury," *Calvin Theological Journal* 38, (2003): 29.

[6] Aristotle, *The Nicomachean Ethics*, trans. F. H. Peters, 3rd ed. (London: Kegan Paul, Trench and Co, 1886).

[7] Plato, *The Republic*, trans. D. Lee, 2nd ed. (New York: Penguin Books, 1955).

[8] S. Botis, "*Shari'ah* Concepts in Islamic Banking," *Bulletin of the Transilvania University of Brasov* 6, no. 2 (2013): 143.

economic and political philosophy.[9] Therefore, the institution arose not just as the only 'body' to champion interest-free banking but, perhaps, to respond to the concerns of Muslims for a financial tradition that reflects the *Ummatic* ethical identity of Muslims. The first bank in the Muslim world named Mit Ghamar was established in Egypt on 25th July 1963[10] by the Islamic economics professor Ahmad El-Naggar. The outstanding feature of the Islamic banking system is the prohibition of interest (*ribā*).[11] Islam prohibits Muslims from taking or giving interest regardless of the purpose for which such loans are taken and regardless of the rate of interest. In the Qur'ān, Allah Almighty says, "Oh you who believe! Do not devour *ribā* (usury), doubled and multiplied; but fear Allah; that you may be successful."[12]

It goes further in 2:188 and 4:29 to enjoin Muslims to avoid the wrongful exploitation of each other's property. Ribā is thus perceived as 'a tool of oppression and a means to unjustly take [the] money of other[s] by exploiting their needs and circumstances.'[13] It is held here that no controversy currently exists about whether the

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[9]Jane Pollard and M. Samers, "Islamic Banking and Finance: Postcolonial Political Economy and the decentering of Economic Geography," *Transaction of the Institute of British Geographers* 32, no. 3 (2007): 325; Ibrahim Warde, *Islamic Finance in the Global Economy* (Edinburgh: Edinburgh University Press, 2000), 73; Philip W. Porter, David R. Faust and Richa Nagar, *A World of Difference: Encountering and Contesting Development*, 2nd ed. (New York: Guilford Press, 2009), 552.

[10]A. Chachi, "Origin and Development of Commercial and Islamic Banking Operations," *Journal of King Abdulaziz University: Islamic Economics* 18, no. 2 (2005): 16.

[11]Both the payment and receipt of it. The definition of the Arabic word *ribā* is, however, not clear. A tradition quotes, 'Umar as saying that three issues were not adequately explained by the Prophet (*SAW*), two of them involved *Mīrāth* (inheritance), while the third was about *ribā*. It is also reported in *Al-Kanz* that the early Muslims eschewed 90% of even permitted financial deals for fear of involving themselves in *ribā*; see: M. M. Iqbal, "A Broader Definition of *Riba*," *Working Paper*, Pakistan Institute of Development Economics (2006): 1; Retrieved from: http://www.pide.org.pk/pdf/psde%2018AGM/A%20Broader%20Definition%20Of%20Riba.pdf, 24/07/2015). Nonetheless, interest is understood here to mean the physical cash paid either regularly or irregularly as a legal or illegal requirement at a particular rate on a particular amount of physical money borrowed from or lent to somebody upon its repayment or before that. Muslim scholars are argued to have settled the issue of what interest (Arabic: *ribā*) means from the Islamic perspective. Abu Saud defines it as, 'the excess of money paid by the borrower to the lender over and above the principal for the use of the lender's liquid money over a certain period of time. see: M. Abu Saud, "Money, Interest and *Qirad* in Islam," in *Studies in Islamic Economics: A Selection of Papers Presented to the First International Conference on Islamic Economics, Held at Makka, Under the Auspices of King Abdul Aziz University, Jeddah, February* ed., K. Ahmad (Leicester: Islamic Foundation, 1983), 64; The Arabic word *ribā*, among other things means, "to increase," "to expand," "to inflate," to "multiply," or "to climb" (Iqbal, "A Broader Definition," 2). This sense of the word has been applied in various verses of the Qur'ān including 13:10; 22: 5; 69:11; and 23:51. In Islamic economics, there are two forms of *ribā*. These are *ribā-al-nasi'ah* and *ribā-al-faḍl*. The former is the type mentioned above, i.e., excess amount charged on borrowed money when the agreed period elapses. For detail see: A. J. Abu Bakar, *Aḥkām al-Qur'ān* (Cairo, 1935), 1; M. Umar Chapra, "The Nature and its Treatment in the Qur'ān, Hadīth and Fiqh," in *An Introduction to Islamic Finance*, edit. G. Abod, S.O.S. Agil and A. Ghazali (Kuala Lumpur: Quil Publishers, 1992), 380.

[12]Qur'ān: al-Imrān 3:130.

[13]Botis, "*Shari'ah* Concepts," 139.

Arabic word ribā used in the Qur'ān is usury or interest[14] as 'all' jurists have concurred that it is;[15] and therefore the modern-day interest-soaked banking systems are considered inconsistent with the principles of Islam.[16] Nonetheless, some Muslim scholars have distinguished between 'usury' (normally called ribā in Arabic) and 'interest' with intriguing categorizations such as "consumption loans"[17] and 'loans for investment' or productive or "commercial loans."[18] They have, therefore, questioned the popular Islamic position on interest and in some cases have even permitted it. The argument is that ribā refers to usury charged by petty money lenders and not the interest charged by modern banks which, presumably, is intentioned to 'share' in the 'profit'; assuming that all bank loans are meant for investment and therefore no ribā is explicit when interest is imposed on productive loans. Others argue that not all types of interest are exploitative enough to fulfil the description of ribā.[19] It appears the latter school holds on to the definition of ribā as "excessive interest."[20] Usury is, therefore, differentiated from bank interest.[21] These are known to belong to the "Non-Equivalence School"[22] or "the modernists" as opposed to the traditional or conservative school of thought that argues that 'usury' and 'interest' are equivalent.[23] The modernist's argument is equivalent to what Patinkin calls 'profit'[24] on capital. The above variegated opinions about ribā or interest imply that ethical business transaction in financial establishments is an important consideration in the Islamic approach to finance.

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[14]M. Umar Chapra, "The Nature of Riba in Islam," *Hamdard Islamicus: Quarterly Journal of the Hamdard National Foundation, Pakistan* 7, no. 1 (1984): 3-24; M. Ayub "Meaning of *Riba*," *Journal of Islamic Banking and Finance* 10, no. 4 (1993): 33-42; M. Ayub, "What is Riba?" *Journal of Islamic Banking and Finance* 13, no. 1 (1996): 7-24; S. Abul Ala Mawdudi, *Interest (Sood)* (Lahore: Islamic Publications, 1977).

[15]S. Al-Harran, *Islamic Finance: Partnership Finance* (Kuala Lumpur: Pelanduk Pubs, 1993), 16.

[16]Abdullah Saeed, "Islamic Banking and Finance: In Search of a Pragmatic Model," in *Islamic Perspectives on the New Millennium*, ed. V. Hooker and A. Saikal (Singapore: ISEAS, 2004), 114; Z. Zamir, "The Prohibition of Interest (*Riba*) in Islam: The Social, Moral and Economic Rationale (part I)," (2007): http://www.nzibo.com/riba/Prohibition%20of%20%20Interest%20(Riba).pdf, 24/07/2015; Imran Ahmad and Ghulam Shabbir, *Frequently asked Questions (FAQs) on Islamic Banking* (Karachi: State Bank of Pakistan, n. d.), 10-13.

[17]Kuran, *The Long Divergence*, 146.

[18]Muhammad Akram Khan, *What is Wrong with Islamic Economics? Analysing the Present State and Future Agenda* (Massachusetts: Edward Elgar, 2013), 18.

[19]For more details, see: Akram Khan, *What is Wrong*, 154ff; Miller, Judith, *God Has Ninety-Nine Names: Reporting from a Militant Middle East* (New York: Simon and Schuster, 1999), 79-80.

[20]Samah Al Agha, "Money Laundering from Islamic Perspective," *Journal of Money Laundering Control* 10, no. 4 (2007): 408.

[21]Imad-ad-Dean Ahmad, "Riba and Interest: Definitions and Implications," Paper delivered at the 22nd Conference of American Muslim Social Scientists, October 15-17, 1993, in Herndon, VA.

[22]Saima Akbar Ahmed, "Global Need for a New Economic Concept," *International Journal of Islamic Financial Services* 1, no. 4 (2000): 2.

[23]For more details, see: Abu Umar F. Ahmad and M. Kabir Hassan, "*Riba* and Islamic Banking," *Journal of Islamic Economics, Banking and Finance* 3, no. 1 (2007): 9-42.

[24]D. Patinkin, *Studies in Monetary Economics* (New York: Harper and Row, 1972), 118.

Thus, Islamic banking has been synonymous with interest-free banking.[25] For western economists, however, an economic system is inconceivable without interest. Hence, in his Wealth of Nations, Adams Smith, fittingly called 'the Father of Economics'[26] by western writers, legitimized interest.[27] On the other hand, the Turkish-American economist, Timur Kuran, argued that no interest-free economy has ever endured among Muslims on earth by saying, "As far as is known, no Muslim polity has had a genuinely interest-free economy."[28] While the latter statement is a bit general, it is understandable because the western conception of interest is not premised on the same moral or ethical framework as the Islamic system and so interest does not have such an unpopular connotation as it has in Islam. For this reason, Paul Samuelson, for example, defined it as '… the price of rental for the use of money,'[29] just as Joseph Persky defined it as '… the rental price of money.[30] Furthermore, Patinkin saw interest as a form of income from property and classified it into three types namely dividend, rent, and profit.[31] Incidentally, Islam does not proscribe dividend, rent or profit in genuine transactions provided they involve physical goods and services, but proscribes them if they are made on money itself without mediating goods and services. This is because money is not deemed in Islamic economics as a capital good on the same foundation as the other factors of production. Therefore, contrary to conventional economics, in Islam interest and all of its forms are proscribed because justice (*'adl*) and equitable distribution of wealth constitute the backbone of economic values.

As an Islamic nation with the pronounced objective to maintain ethical transactions in her financial institutions (both banking and 'non-bank financial institutions'[32]) and to gradually free the economy of ribā and all its associates in a manner that is tuned with the Islamic economic philosophy, the Bruneian state financial organizations entered into interest-free banking transactions. This was done through Sharī'ah compliant mechanisms that satisfy the moral urge of the customers in a way that gains their confidence while bearing in mind the permissible limits in the receiving and dispensing of financial resources. This paper examines the development of Islamic finance in Brunei and sheds light on the present realities as well as future prospects and imminent expectations and challenges.

[25]Zuberi, "Interest Free," 1077-87; Botis, "*Shari'ah* Concepts," 139.

[26]G. R. Crowley and R. S. Sobel, "Adam Smith: Managerial Insights from the Father of Economics," *Journal of Management History* 16, no. 4 (2010): 504, 508; A. Sen, "Adam Smith and the Contemporary World," *Erasmus Journal for Philosophy and Economics* 3, no. 1 (2010): 51; A. W. Walter, "Adam Smith and the Liberal Tradition in International Relations," in *Classical Theories of International Relations*, I. Clark and I. B. Neumann, ed. (London and New York: Macmillan and St Martin's Press, 1996), 1; A. Wyatt-Walter, "Adam Smith and the Liberal Tradition in International Relations," *Review of International Studies* 22, no. 1 (1996): 5-28.

[27]A. Smith, ed. by: Edwin Cannan, *An Inquiry into the Nature and Causes of the Wealth of Nations* (New York: Modern Library, 1776 (reprint: 1937), 339.

[28]Kuran, *The Long Divergence*, 147.

[29]P. Samuelson, *Economics*, 10th ed. (New York: McGraw Hill, 1976), 50.

[30]J. Persky, "Retrospectives from Usury to Interest," *Journal of Economic Perspectives* 21, no. 1 (2007): 227.

[31]D. Patinkin, *Studies in Monetary Economics* (New York: Harper and Row, 1972), 118.

[32]M. B. Shrestha, *Role of non-Bank Financial Intermediations: Challenges for Central Banks in SEACEN Countries* (Kuala Lumpur: SEACEN Research and Centre, 2007), iii, x, 1.

2. A Historical Overview of Islamic Banking and Finance

The origin of the Islamic financial system is not clearly known as it is difficult to determine exactly when banking operations in Muslim societies actually began. However, from its Italian origin,[33] conventional banking acquired shape going through different stages until Muslims began to promote their version of it.[34] In its pristine days, Islam gave financial transaction a maximum space when it placed trade on a similar footing with *jihād*[35] by offering the merchant 'a highly honoured place in society' and assuring him an elevated position in the hereafter if he deals honestly.[36] Financial transactions including banking regardless of the form it takes is a trap for Muslims because of the phenomenon of borrowing and lending and the accompanied temptations of *ribā*. In spite of the prohibition of *ribā*, no Muslim society has ever existed without financial transactions in one form or another because many Muslims have made a living through trade. The dominance of trade in the geographical nucleus of Islam Makkah and Madinah, and its popularity as a profession among well-known figures such as Khadījah, Abū Ṣufyān, Abū Bakr and the Prophet (*SAW*) himself implies that banking and finance, at least at the informal level, had been known to Muslims. Chachi refers to numerous 20th century scholars who mention Muslim bankers and banking facilities[37] and argues that Islamic financial services including banks existed during the Abbasid period. Thus, we could refer to the Perso-Arabic term *Jahbadh,*[38] often used for 'financial clerk,' 'expert in matters of coins,' 'government cashier,' and 'a money collector,' also used for a known 'licensed banker' at the time of the Abbasid caliphs[39] as evidence.

Nonetheless, the understanding of the word "bank" used above is unclear although expressions like 'financial clerk,' 'government cashier,' etc. which define *Jahbadh* are integral to today's banking systems. The word *jahbadh* is the Arabic form of the Persian word *gahbad*. It derives from the double-word *gah* (meaning goldsmith's vessel) and the Sanskrit *bad* (*pati*: which refers to "the master" or "the manager").[40] During the Sassanid regime, it was used for a "money-changer."[41] Institutions for interest-free financial transactions existed among Muslims in the major centres of trade which performed 'almost all the banking functions' during the Abbasid 10th century

[33]Jean-Francois Bergier, "From the Fifteenth Century in Italy to the Sixteenth Century in Germany: A New Banking Concept," in *The Dawn of Modern Banking*, ed. Centre for Medieval and Renaissance Studies (Los Angeles: University of California, 1979), 105; A. Usher, *The Early History of Deposit Banking in Mediterranean Europe* (Cambridge: Mass, 1943); R. De Roover, "New Interpretation of the History of Banking," *Journal of World History* 2, no.1 (1954): 38-76.

[34]Chachi, "Origin," 3-24.

[35]J. B. Yusuf, "Ethical Implications of Sales Promotion in Ghana: Islamic Perspective," *Journal of Islamic Marketing* 1, no. 3 (2010): 229; D. A. Mustafa, H. A. Abdulsalam, and J. B. Yusuf, "Islamic Economics and the Relevance of *al-Qawā'id al-Fiqhiyyah*," *SAGE Open 6* (2016): 1-13.

[36]Chachi, "Origin," 9.

[37]Ibid., 10.

[38]Wen-chin Ouyang, *Literary Criticism in Medieval Arabic-Islamic Culture: The Making of a Tradition* (Edinburgh: Edinburgh University Press, 1997), 95.

[39]Chachi, "Origin," 10.

[40]Ouyang, *Literary*, 95.

[41]Ibid., 95.

C.E.[42] For example, during the reign of Al-Muqtadīr (980-1032 C.E.), the *Diwān al-Jahābidhah* assumed a role similar to today's banks such as the administration of deposits, remittance of funds through the issuance of checks (*Sakk*) and bill of exchange (*Suftajah*), and the granting of loans to the caliphs, their *Wazīrs* and court officials.[43] The early Muslims contended themselves with foreign minted currencies like the Roman, Persian, and Himyarite coins. According to al-Ṭ abarī, the Umayyād caliph Abdul Mālik bin Marwan issued the first originally Arabic gold *dinārs* and silver *dirhams* in Syria in the 7th century C.E.[44] In 696 C.E., the governor of Iraq, al-Hajjāj followed his example in Kūfah.[45] Undoubtedly, these endeavours were supervised from the official outfits of financial institutions. Yet, it appears that they never caught the attention of historians.

For this reason, the sources do not provide us with vivid information about the sequence in which Islamic financial institutions sprang up in the Muslim world. Nonetheless, the first recorded Islamic bank began in Egypt in 1963, superintended by El-Naggar. In the 1970s, however, many Islamic banks were established across the Middle East. For example, the Islamic Development Bank appeared in 1974. This was followed by the Dubai Islamic Bank and in 1979 Pakistan became the first Muslim country to, as it were, attempt to fully Islamize her financial system.[46] Today, Islamic banking is a major factor for economic productivity in many Muslim countries among them are the OPEC economies of the Middle East and the Malay world, particularly, Malaysia, Indonesia, and Brunei. It continues to expand both in its infrastructure and financial assets. In the West, Britain had her first Islamic Bank in 2004.[47] Pollard and Samers list many financial institutions, both banking and non-bank, that either have '*Sharī'ah*-windows' or are rendering *Sharī'ah*-compliant services to the public.[48]

3. Islamic Banking and Finance in Brunei

Islamic banking and finance was introduced in Brunei in 1991, when the statutory body known as *Perbadanan Tabung Amanah Islam Brunei* (TAIB) was formed.[49] Since then, the industry has experienced tremendous growth. In 2010, it played a significant role in the country's banking industry with a total disposable asset of B$6.36 billion and a total deposit of B$5.167 billion. These accounted for 37% and 34.6% of the total market share, respectively.[50] Brunei has two main Islamic financial institutions; one is *Bank Islam Brunei Darussalam* (BIBD) also known in English as the Islamic Bank of

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[42] Chachi, "Origin," 10.

[43] A. Al-Qalqashandi, *Subh al-A'Asha fi-Sinaat al-Insha* (Cairo: 1913); A. Al- Jahshiyari, *Kitab al-Wuzara' wa al-Kuttāb* (Cairo: 1938); Matba'at Abd al-Hamid Ahmad Hanafi, C. Pellat and J. Schacht, *Encyclopedia of Islam* (London: L. Luzac, 1965); A. Metwally and S. Shahata, *Iqtisadiat-al-Uqud fī Itar al-Fikr al-Islāmi* (Cairo: Dar Al-Tawfiq, 1983).

[44] Al-Ṭ abarī, *Tafsīr al-Qur'ān*, vol. 2 (Bulaq, 1329), 939; P. K. Hitti, *History of the Arabs: From the Earliest Times to the Present*, 10th ed. (London: Macmillan, 1970), 217.

[45] Hitti, *History of the Arabs*, 217.

[46] Warde, *Islamic Finance*; Porter, Faust and Nagar, *A World*, 552.

[47] Pollard and Samers, "Islamic Banking," 317; Porter, Faust and Nagar, *A World*, 552.

[48] Pollard and Samers, "Islamic Banking," 317.

[49] M. J. A., Bin Abdul 'Ali, T. S. Tan, and Y. C. Lee, "Brunei: Islamic Banking and Finance," in *The Islamic Finance Handbook: A Practitioner's Guide to the Global Markets*, ed., S. Thiagaraja, A. Morgan, A. Tebbutt and G. Chan (Singapore: John Wiley and Sons, n. d.).

[50] *Autoriti Monetari Brunei Darussalam Annual Report.*

Brunei (IBB)[51] and the other is a non-bank *Perbadanan Tabung Amanah Islam Brunei* (TAIB [Brunei Islamic Trust Fund]). According to the Ministry of Finance, in 2009 these two institutions formed together 40% of the country's total banking assets.[52] The *Autoriti Monetari Brunei Darussalam* or the Monitory Authority of Brunei Darussalam (AMBD) is the outfit that more-or-less serves as the 'central bank' of Brunei Darussalam. There was also the Islamic Development Bank of Brunei (IDBB) which was established in 2000 and later merged with BIBD in 2005.[53] In connection with the former, His Majesty the Sulṭ ān of Brunei is reported to have remarked that, "It is a milestone for our country and will become much more significant in proportion to our status [as an Islamic nation]. We are confident that our way of doing business will be widely accepted by the world at large. This is not only because it brings profits but it also offers fairness and at the same time prevents exploitation."[54]

Since independence, Brunei has endorsed, supported and vigorously promoted the growth of Islamic banking and finance as an alternative to the established conventional banking system. As an Islamic nation (*Negara Dikr*), the Bruneian economic philosophy is that the banking ecosphere and for that matter all financial transactions in general fall within the full ambit of human enterprise channeled towards the establishment of socio-economic justice ('*adl'*). Thus, it operates the 'open-market economy' in which both Muslims and non-Muslims interact and are able to make financial transactions using the same operational rules which ensure that all clients are treated proportionately and justice is done without any discrimination.

4. Favorable Foundations for Interest-Free Banking in Brunei

The only Islamic institution that renders banking services in Brunei is *Bank Islam Brunei Darussalam* or the Islamic Bank of Brunei Darussalam (BIBD). This bank was inaugurated in 1993 to replace the International Bank of Brunei (IBB).[55] The financial transactions of BIBD are *Sharī'ah* compliant. This implies that the bank facilitates savings and issues loans in line with the principles of the *Sharī'ah*. The system is, therefore, free from the interest-based transactions of the conventional banks. The issue of interest-free banking advocated by the *Sharī'ah* often beats people's imaginations. This is because for the conventional economist, whose views dominate economic intellectual discourse, it is impossible to imagine an economic order without the existence of interest. The fact is that the conventional economist understands profit in its strictest or literal sense and in all its ramifications without the least consideration given to the human being who remains at the core of all economic or institutional financial transactions and interactions from an Islamic point of view. In spite of this fact, one needs to understand that Islamic interest-free banking cannot operate smoothly without the goodwill of the Muslim community and the full institutional provisions, legal support and cooperation of

[51] Angelo M. Venardos, *Islamic Banking and Finance in South-East Asia: Its Development and Future* (Singapore: World Scientific Publishing Co, 2005), 198.

[52] Venardos, *Islamic Banking*, 171.

[53] *Borneo Bulletin Yearbook* 2013, 111.

[54] Venardos, *Islamic Banking*, 198.

[55] Ibid., 199.

state actors (the government).[56] This should be born in mind in appreciating the controversial review of the bank interest case in Pakistan by the country's highest court of law, the Supreme Court (SC), in 2002, which virtually stifled the effort of interest-free banking advocates.[57] In the course of the proceedings of this case, a state council is reported to have fumed that the '*Ulamā* themselves were "the main hurdle in the Islamization process of the country."[58] Nonetheless, unlike Pakistan where certain socio-economic variables obstructed the implementation of interest-free financial transactions at the national level;[59] in Brunei the relevant state structures have gradually appeared to support the implementation of the system. The following have been the foundation for the growth of interest-free finance in Brunei.

4.1. Political Will and Determination

Political will and interest is the primary cause of success in every national or societal enterprise. For an institution to be effective in terms of its ability to engage productively with the civil society in order to accelerate and promote sustained growth and development, it is necessary that it acknowledges the diverse limiting factors of operational capacity, political will and cooperation. This is particularly important because interest-free banking as a national policy in today's mixed economy of profit-minded industrialists and business magnates, who take the control of the economy as a means for accessing and firmly controlling new business opportunities, has certain severe implications. Naturally, promoting interest-free financing in an economy demands cooperation both at the personal and institutional levels and also the devising of austerity measures to cut-down national expenditure and simultaneously control budget-deficit and the after-shocks of unemployment exacerbated by the cut in state spending.

The point is that the governments of developing countries mostly rely on foreign donors and foreign funding to finance their budgets. Since foreign financial inflow implies relying on foreign organizations like the International Monetary Fund (IMF) and

[56]Mohammad M. Khan and M. Ishaq Bhatti, "Why Interest-Free Banking and Finance Movement Failed in Pakistan," *Humanomics* 22, no. 3 (2006): 145.

[57]Ibid., 146-7. The Federal *Sharī'ah* Court of Pakistan issued a verdict in 1991 that called on the Pakistani government to prohibit interest-motivated financial transactions. This verdict was endorsed by the *Sharī'ah* Appellate Bench of the country's Supreme Court in late 1999 and earmarked for full implementation on 30th June 2002 after which the country's financial institutions, both banks and quasi-banks, would end transactions mediated by interest in all its forms. However, in a rather dramatic turn of events, the then President Pervez Musharraf, reconstituted the membership of the bench and ordered a review of the earlier verdict in an apparent attempt to possibly overturn it. See: Muhammad Qasim Zaman, *Modern Islamic Thought in a Radical Age: Religious Authority and Internal Criticism* (Cambridge: C.U.P., 2012), 127; Zulfikar K Maluka, "Reconstructing the Constitution for a COAS President: Pakistan, 1999-2002", in *Pakistan on the Brink: Politics, Economics, and Society*, ed., Craig Baxter (New York: Lexington Books, 2004), 76-7. Thus, in its new declaration in June 2002, the country's highest court of appeal on Islamic legal issues, the *Sharī'ah* Appellate Bench, dismissed the case and redirected it to the Federal *Sharī'ah* Court for fresh determination (for more details, see: Supreme Court of Pakistan, *Civil Shariat Review Petition No.1 of 2000*, 2002); see also: Baxter, *Pakistan*, 76-7.

[58]See: *Dawn*, June 19, 2002 cited by Zaman, *Modern Islamic Thought in a Radical Age*, 128.

[59]Khan and Bhatti, "Why Interest," 146.

the World Bank, where not only repellent anti-interest-free policies might apply but physical interests are also charged on loans; promoting interest-free banking, in effect, also implies withdrawing from the transactions mediated by interest in all its forms. This should be borne in mind in attempting to understand why the Pakistani President Ziaul Haq failed to eradicate interest-based transactions in his country in spite of making a pledge to do so. He, at the same time, vetoed for ten years (from 1980 to 1988) any attempt by the Federal *Sharīʻah* Court (FSC) to issue any ruling that would 'interdict' government transactions that were interest-mediated.[60] The above mentioned scenario implies that creating an Islamic economy that is free from *ribā* or interest-based transactions and financing is a governmental or 'political' responsibility that could be discharged more efficiently not necessarily through a constitutional or statutory force or order alone such as it happened, for example, in the case of Pakistan's *ribā* ruling, but also through the political will of both the government and society, lack of which is also exemplified by the same Pakistani *ribā* issue. Due to its implications on business, employment, government budgets, etc., an interest-free economy could only operate in a country where "personal and state institutions are also restructured on Islamic lines."[61]

Thus, with its will-power to establish an Islamic economy in which *ribā*-free banking and all its components could operate smoothly, the Bruneian government first attempted to formulate a thorough scheme for sequentially bringing forth the Islamic institutions that naturally created the opportunity for implementing Islamic values within the economic ring. This was, perhaps, what His Royal Majesty *Sulṭ ān Dan Yang Di-Pertuan* Hj Hassanal Bolkiah had in mind when on January 1, 1984 he pronounced that his country would, thenceforth, be *Negara Melayu Islam Beraja* (i.e., a Malay Islamic Monarchical State),[62] currently subsumed under the acronym, MIB. A part of the speech reads: "… Negara Brunei Darussalam would forever remain a Malay Islamic Monarchy state, independent, sovereign and democratic."[63] To ram home this urge to create an holistic Islamic state where the ideal Islamic institutions would be established to pave the way for the holistic Islamization of all aspects of the Bruneian life (be it social, economic, political or even cultural), His Majesty re-announced the MIB publicly for the second time in July 1990. This political move by the Sulṭ ān which apparently was made, so to speak, to legitimize his political authority within the fragile religious environment and to "promote loyalty to the new nation"[64] officially made the implementation of Islamic teachings and values in all aspects of the Bruneian life (including the economy) a national or governmental religious obligation which would facilitate the restoration of the Bruneian Islamic *Ummatic* identity that was almost lost to colonialism.

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[60]The Presidential Order, no.14, 1985; The 1991 Federal *Shari'ah* Court Judgement on *Riba*, 1991; Khan and Bhatti, "Why Interest," 147.

[61]Ibid., 147.

[62]N. S. Talib, "A Resilient Monarchy: The Sultanate of Brunei and Regime Legitimacy in an Era of Democratic Nation-State," *New Zealand Journal of Asian Studies* 4, no. 2 (2000): 142; M. Z. Serudin, *Brunei; An Islamic Nation: Islamic Background (*Brunei: Islamic Da'wah Centre, 2000), iii.

[63]Serudin, *Brunei*, iii; Z. Serudin, *The Malay Islamic Monarchy: A Closer Understanding*, trans., N. Abdul Majid (Brunei: NCMIM, 2013), 209.

[64]Talib, "A Resilient," 141.

The Islamization of the Bruneian economy and the implementation of interest-free financial transactions were aimed to achieve the following three objectives.

1. To practicalize the Islamic economic system and transact business according to the principles of the Qur'ān and the Prophetic Tradition (*SAW*). This drive brought with it the need to stand firm against interest-based transactions and the prohibition of *Maysir* (gambling and other forms of economic exploitation).[65]

2. To nurture a value-oriented economy in which financial institutions would develop and function in the natural way and in a manner whereby they would take cognizance of the interest of the poorer sections of the society in order to promote public good (*Maṣlaḥah*) and place human beings at the centre of economic transactions. This also came with the need for a drastic reduction of the cost of money through profit-and-loss-sharing and the promotion of social welfare through the projection of cash inflows (both internal and external revenue) over cash outflows (both external and internal expenditure). This would lead to favourable national and international trade (*Tijārah*) which is recommended for Muslims.[66]

3. To reduce the after-shocks of excessive productivity, liquidation and economic downturn by boosting risk-sharing through the promotion of ethical insurance (*Takāful*) and other related indemnities.

4.2. Strong Currency and Abundant Natural Resources for Investment

Interest-free banking economy should have a good opportunity of self-reliance. However, economic self-reliance also implies the availability of adequate natural resources for economic exploitation by all and sundry. Lack or inadequacy of resources that would offer the opportunity of an ethical investment could result in an unethical livelihood. It must be noted that, in every economy, the factors of production (land, labour, and capital) are integrated to bring about business and economic security. Thus, land resources, human-based resources (labour) and financial resources (capital) are interlaced and each one must be available in the right proportion to bring about the ideal economy from an Islamic perspective in which interest-based transactions are nipped in the bud.

[65] al-Maeda 5:90.

[66] Ibrahim and Joo, "Islamic Banking," 315; Yusuf, "Ethical Implications," 221.

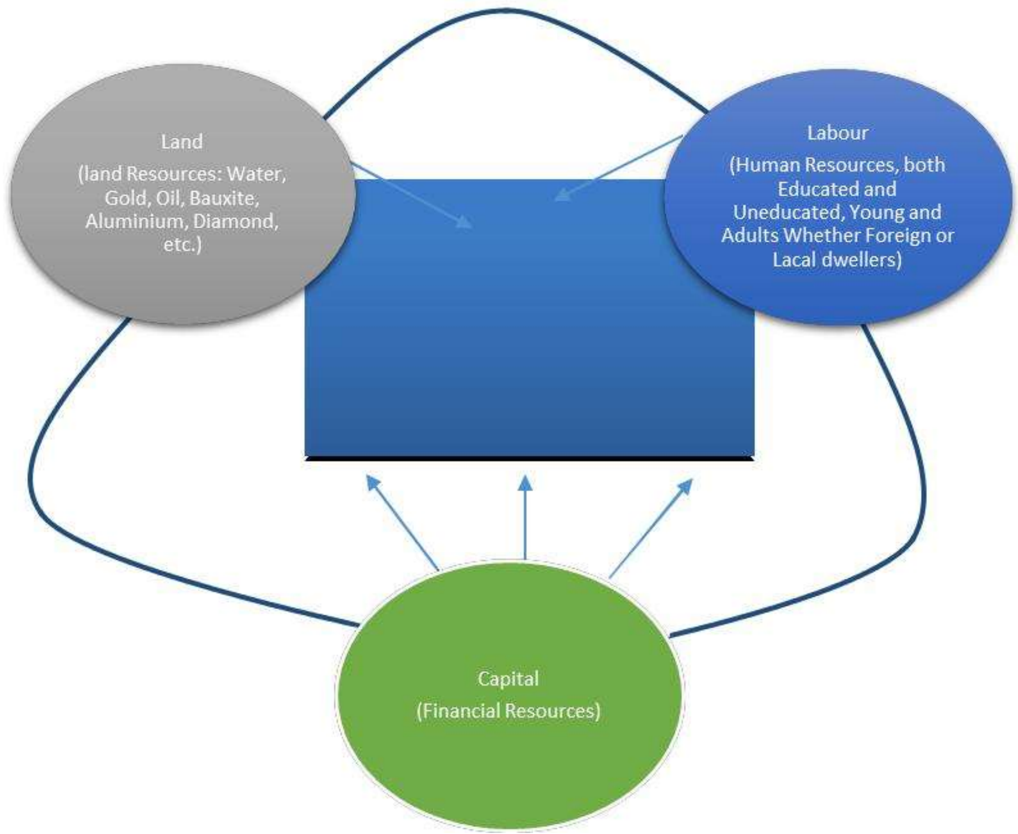

Figure 1: A Diagram illustrating the Relationship between Land, Labour, and Capital in the ideal Islamic Economy (Source: Authors' Construct)

All the above factors of production provide the wheel for driving an economy. Although a nation's economic strength often depends on the weight of her financial resources, in Brunei, natural or land resources, particularly oil, is a crucial factor for her economic growth. Oil and gas export constitute 78% of the country's revenue and formed 96.2% of her total export in 2008.[67] The 2015 figure stands at 95%. Therefore, our argument is that the disproportionate availability of any of these basic factors of production mentioned above could invariably result in an imbalanced economy. Thus, lack of natural resources (land) faced by a large number of people (labour) without having the corresponding amount of money (the capital) could lead to a trade in the latter and ultimately the promotion of interest-based transactions. Consequently, in Brunei where stringent economic management makes the above factors of production appear proportionate, interest-free banking has the opportunity for growth and expansion. Brunei has huge reserves of oil[68] and is ranked 14th in the world oil deposits and 4th in natural gas

[67] Department of Economic Planning and Development (Prime Minister's Office), *Brunei Economic Bulletin* 5 (2007), 2.

[68] Paul J. J. Welfens, Jens K. Perret, Tony Irawan, and Evgeniya Yushkova, *Towards Global Sustainability: Issues, New Indicators and Economic Policy* (New York: Springer International Publishing, 2016), 111.

deposits according to 2008 reports.[69] These huge oil reserves, judged against the country's small population, offer the citizens a lot of advantage in terms of standard of living.

Furthermore, tying her cloth to one of the 'Asian Tigers' Singapore, with which she uses equivalent currencies (Singaporean Dollar = Brunei Dollar), Brunei has a strong currency[70] to back her young Islamic economy to compete favourably with the interest-motivated conventional financial system. With this sound economic base (supported by her strong currency), the Bruneian government finances its budgets from the nation's huge oil and gas exports, 60% of which goes to Japan and her Malay sister country Indonesia.[71] Other consumers of the Bruneian oil include Thailand, Korea, the U.S. and Australia.[72] Thus, her public debt constituted only 2.6% of the country's GDP as of 2014; although these figures have observed a sluggish rise since 2006 (see figure 2 below). Yet, the current rate is far lower than even the public debt of large and established economies of USA and UK.[73]

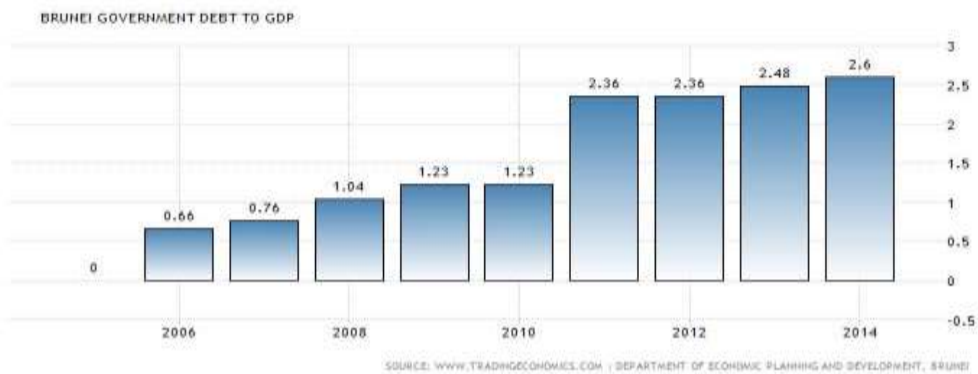

Figure 2. Brunei's Public Debt Increases (%) since 2006 (Source: Prime Minister's Office Department of Economic Planning and Development, Brunei) (Uploaded at http://www.tradingeconomics.com/brunei/government-debt-to-gdp., 21/11/2015)

The above issue of low public debt is significant because the control of interest-centered foreign-based and home-based borrowings by a government is instrumental for transforming the economy of a country and placing it on the verge of economic justice subsumed in Islam under the label of interest-free transactions. According to the Department of Economic Planning and Development, Brunei's public debt began at 0.49% of GDP in 1985, a year after her exit from the shackles of colonialism. In 2014, it

[69]Saad Al-Harran, Alfred Yong Foh Sen, *An Islamic Microfinance Enterprise: The Financial Vehicle that Will Change the Face of the Islamic World* (Xlibris Corp, 2008).

[70]Petr Polak and Rady Roswanddy Roslan, "Regional Treasury Centres in South East Asia –The Case of Brunei Darussalam," *Management* 14, no. 1 (2009): 83.

[71]Prime Minister's Office, *Brunei*, 2.

[72]Anthony Pecotich and Clifford J. Shultz, ed. *Handbook of Markets and Economies: East Asia, Southeast Asia, Australia, New Zealand* (New York: M. E. Sharpe, 2006), 57.

[73]According to the United States Bureau of Public Debt, the U.S. public debt stood at 102.98% her GDP in 2014 from 61.38% in 1940 with an all-time high of 121.70% in 1946. On the other hand, the Eurostat reports that the public debt of the United Kingdom hit 89% of its GDP in 2014 with 49.48% in 1980 and 31.3% 1991 (for details, see: www.tradingeconomics.com.

reached the relatively high level of 2.6%. In 1986, Brunei recorded 0% public debt.[74] Interestingly, to protect the over-exploitation and degradation of her natural resources, particularly, her forests, Brunei virtually imports everything she consumes with little investment in agriculture on her local lands. Nonetheless, as an oil-rich country, although her current balance of trade surplus falls below her average balance of trade at BN$ 1,115.70 million recorded in 2005, Brunei has been able to maintain a balance of trade surplus of BN$ 286.70 million as of August 2015.[75]

Figure 3. Brunei's Balance of Trade Surplus Downturn since October 2014
(Source: Department of Economic Planning and Development, Brunei)

According to Pecotich and Shultz, Brunei recorded a balance of trade surplus of BN$ 4,826 billion. Her export value was estimated at BN$ 6,734 billion and she had an import value of BN$ 1,908 billion.[76] This gives her a favourable balance of trade as she exports more than she imports. Even in 2009, a year of fallen world oil prices, Brunei's surplus was equivalent to 40% of her GDP. She has recorded fiscal surplus consistently since 2003, even during the global economic slump in 2008-09.[77] The 2015 IMF estimate in consultation with the Bruneian government, however, reports a downturn of 2% of the country's GDP with 0% inflation figure.[78] Her budget surplus formed 9.3% of her GDP in 2014 from 10.13% in 1990.[79] Consistent with the chart below, Brunei has recorded highly favourable budget surpluses and upshots.

[74]For more details, see: Department of Economic Planning and Development (Prime Minister's Office), Brunei.

[75]Department of Economic Planning and Development (Prime Minister's Office), Brunei.

[76]Pecotich and Shultz, *Handbook*, 57.

[77]Deutsche Bank, "Brunei Darussalam Frontier Country Report," Frankfurt, Germany, June 2012. This information is approved by the bank's outfits in London, Hong Kong, Korea, Singapore, Japan and Australia.

[78]International Monetary Fund (IMF), "IMF Executive Board Concludes 2015 Article IV Consultation with Brunei Darussalam," *Press Release*, no.15/259, June 4, 2015.

[79]Department of Economic Planning and Development, Brunei.

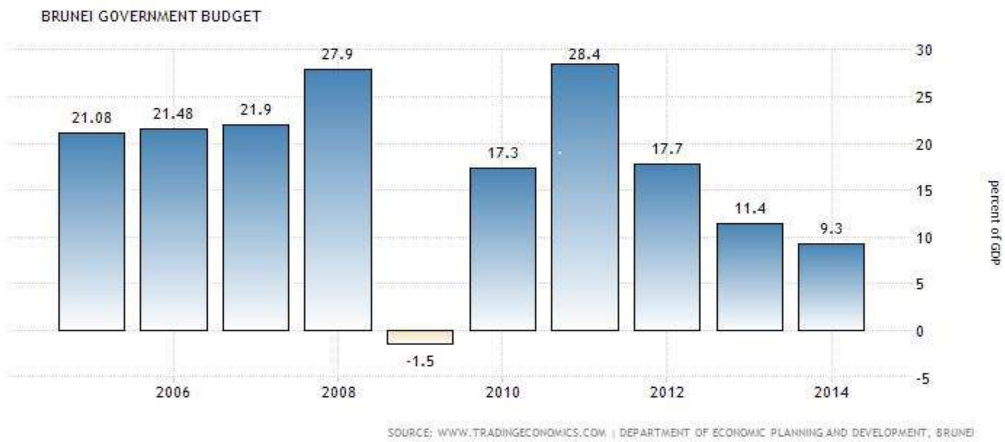

Figure 4. Brunei Government's Budget Surplus since 2006
(Source: Department of Economic Planning and Development, Brunei)

With a stable political machinery and environment, the implication of the above figures and economic indicators is that there is likely to be very little pressure on the economy and this grants it the opportunity to resist external shocks. Thus, personal income-tax which puts undue pressure on the middle class is simply non-existent in Brunei. Furthermore, balance of trade surplus reflects a favourable balance of payment and together with the tax-free income policy, it implies a high per-capita or disposable income. Brunei, therefore, has one of the highest per-capita income figures in the ASEAN community, which stood around US$ 40,000.00 according to the 2012 figures of the Deutsche Bank.[80] Thus, government's firm grip on the national economy grants it the opportunity to properly regulate the injection of the financial component of the factors of production in its right proportion so that it does not trigger unethical trade in money characterized by interest-based transactions. This calm atmosphere, therefore, accords the Islamic banking and financial system the opportunity to grow because it provides the institutional inducement and motivation to keep it running. This, however, does not mean that interest-based banking is completely obliterated from the Bruneian economy. The internationally controlled banks like the Standard Chartered Bank, Hong Kong and Shanghai Banking Corporation (HSBC) are present to not only serve the approximately 30% non-Muslim population but they even cross-over to subsume the investment of the Muslim population. Another bank was the Citibank which closed operation in March 2014 after 41 years of operation in the Sultanate.[81] Nonetheless, even at the conventional level, interest rates have remained relatively stable at 5.5% since 1999.[82] Unlike the *modus operandi* in many countries, the official financial regulator of Brunei *Autoriti Monetari Brunei Darussalam* (AMBD) does not set any benchmark for determining interest rates in the various financial institutions. For this reason, the banks usually depend on the Prime Lending Rate (PLR) as their yardstick.

[80]Deutsche Bank, "Brunei."

[81]*The Brunei Times*, 24th December 2013 Edition.

[82]Asia Pacific Economic Cooperation, *Economic Outlook*, Author, 2001, 80; World Trade Organization, *Trade Policy Review: Brunei Darussalam*, Author, 2008, 10.

4.3. Islamic Foresight, Mentality, and Patriotism Determining the Economic Course of the Nation

Bruneians, and for that matter Malays, are not only religious, ethically-minded, and dedicated to the course of Islam but are also very patriotic to their national course. Thus, although the political will and royal dedication to the course of interest-free financial business have been very instrumental, the cooperation of the Bruneian populace is also noteworthy. This is because the political instrument alone without the cooperation of the local aristocrats and business magnates would not have kept the system in a state of equilibrium. The above mentioned issue of ethical consideration is of critical importance in understanding the success of interest-free finance from the Bruneian economic perspective because as a society of classed and highly esteemed economic and socio-political nobles, interest-based lending and borrowing could have been fundamental to economic survival in their conventional sense. With a firm grip on the country's economic and natural resources, they could have sabotaged the system through a sell-out to unethical foreign investment and control that would truncate the progress of the interest-free discourse. The latter is crucial because in many Muslim countries interest-free banking exists and is indeed sanctioned by the government. Yet, the business magnates and wealthy aristocrats are still engulfed in interest-based dealings under the pretext of economic necessity (*Ḍ arūrah*). For example, in Pakistan, it appears the government has permanently stifled interest-free banking with the view that"… bank interest is not *riba* and it is utterly impossible in the present day circumstances to divorce the economy of Pakistan from the international economy by abolishing interest."[83]

Yet, the prevailing financial sector in Brunei is manned by dedicated business moguls, from the top echelons to the lower ebb, who are both committed and have the requisite knowledge that facilitates accurate personal and institutional record-keeping, openness, accountability, careful regulation and supervision. The monitoring framework also demands the formation of an ethical assessment window, known as *Sharī'ah* Supervisory Board (SSB), for providing the operational direction and guidance for Islamizing the monetary operations. These features not only confirm and deepen the Islamic economic ethic or moral belief in the system but they also enable these financial institutions to gain the trust of their customers while attracting their conventional counterparts into business. Therefore, from the Ministry of Finance, *Autoriti Monetari Brunei* to the general populace (the customers), everybody is committed to the sustenance of the system.

[83]Khan and Bhatti, "Why Interest-Free," 147.

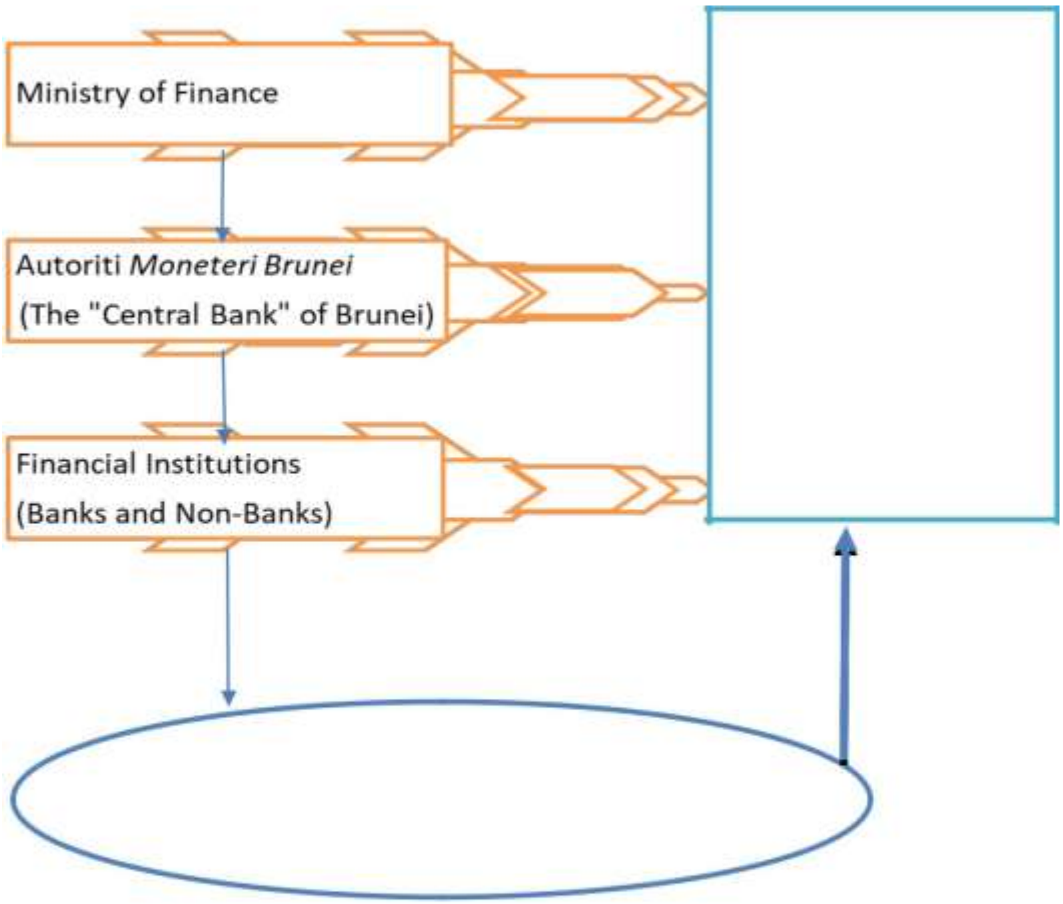

Figure 5. The Hierarchy of the Islamic Financial Authority in Brunei
(Source: Authors' Construct)

Professionalism and relevant knowledge-based business is very important in Islamic banking and finance; a lack of professional exposure has been perceived as one of the factors inhibiting Islamic finance in Pakistan.[84]

4.4. Favorable Taxation and Comprehensive Social Welfare

Taxation is one of the causes of the high cost of living fueled by perpetually high prices of goods and services known as inflation.[85] Taxes place constraints that exacerbate the cost of production which eventually reduces the margin of profit even within *ḥalāl* limits. In the end, it is the customers who suffer because the companies naturally shift their cost onto the consumers down the production cable through the wholesaler and the

[84] *CII's Consolidated Recommendations*, 24th December 1983, 109; Ministry of Finance, *The 2002 Task Force Report*, Pakistan, 2002; Khan and Bhatti, "Why Interest-Free," 149.

[85] Laurence Ball, "What causes Inflation?" *Federal Reserve Bank of Philadelphia Business Review*, March/April, (1993): 3.

retailer. This ultimately increases the per-head cost of living.[86] At the banking or institutional level, taxes not only lower cash flow for producers but they also reduce the individual's disposable income.[87] Therefore, a higher level of taxes potentially has an impact on the cost of money,[88] incentive structures of individuals and producers. When the cost of investing money in the production of physical goods and services is high, it forces the financial capital owners, and for that matter, the individuals, into the ethically challenging option of trading in physical money without the mediation of goods and services subsumed under the name 'interest-based' banking and financial transactions. Thus, in countries where the cost of doing business is exacerbated by exorbitant taxes and huge governmental levies, money owners exploit illegitimate[89] banking facilities like interest-mediated fixed deposits, treasury bills or bonds since these simply incur no production cost to justify a loss or reduction of profit. In some developing countries, like Ghana, tax officials and task forces from the metropolitan, the municipal, and the district assemblies harass the general populace, particularly petty-traders in a bid to meet their respective tax targets. Instances of these were recorded in Accra, the capital, where the actions of the officials of the Accra Metropolitan Assembly (AMA) often lead to clashes between traders and the task force. Khan and Bhatti give a similar scenario in Pakistan where taxation appears "unrealistic and oppressive after the exclusion of the social superiors from the tax bracket."[90]

The phenomenon of unfair and high tax demands provides the perfect base for keeping multiple accounts by money owners as a way to evade tax; this gradually develops into other forms of transactions that are not only inconsistent with the essential principles of Islam but could also promote interest-based banking. Workers in Brunei pay no personal income tax[91]and corporate tax has remained relatively fixed.[92] In addition, the government also gives numerous tax incentives to facilitate private sector investment. These incentives include 30% corporate tax rebate; tax exemption on the importation of plant, machinery, equipment etc. These tax incentives are further shored-up with a wide-

[86]For more details on relationship between taxes and cost of living, see: Robert Gillingham and John S. Greenlees, "The Impact of Direct Taxes on the Cost of Living," *Journal of Political Economy* 95, no. 4 (1987): 775-796; Zoe Smith, "The Petrol Tax Debate," *IFC Briefing Note*, no. 8 (2000), 5-6; Omar Aziz, Matthew Gibbons, Chris Ball, and Emma Gorman, "The Effect on Household Income of Government Taxation and Expenditure in 1988, 1998, 2007 and 2010," *Policy Quarterly* 8, no. 1 (2012): 29-38.

[87]Patrick J. Caragata, *The Economic and Compliance Consequences of Taxation: A Report on the Health of the Tax System in New Zealand* (Springer 1998), 97.

[88]Kenneth J. McKenzie and Jack M. Mintz, "Tax Effects on the Cost of Capital," in J. B. Shoven and J. Whalley, *Canada-U.S. Tax Comparisons* (Chicago: University of Chicago Press, 1992), 190.

[89]Rodney Wilson, "Regulatory Challenges posed by Islamic Capital Market Products and Services," IOSCO Task Force on Islamic Capital Market, 2003. https://zulkiflihasan.files.wordpress.com/2008/06/regulatorychanges-islamic-capital-market.pdf

[90]Khan and Bhahti, "Why Interest-Free," 156.

[91]International Business Publications, *Brunei Sultan Haji Hassanal Bolkiah Muizzaddin Waddaulah Handbook*, 4th ed. (Washington, DC: 2008), 233.

[92]Aprinto Berlianto, "Tax Competition and Harmonization in Southeast Asia," (M.A. Dissertation, Massey University, Albany New Zealand, 2009), 18.

range social welfare system that guarantees the provision of free[93] or cheap and available housing, education, and good medical care for all citizens. These facilities make Bruneians comfortable by all standards. Thus, as religious people, the unethical means of livelihood is typically out of the picture.

5. Prospects of Islamic Banking and Finance in Brunei

It is not worthy to evaluate the Islamic banking and financial experience in Brunei against that of the established conventional system. Even so, it must be said and indeed emphasized that the Islamic system has grown at a fast pace in line with the Sultanate's strategic plan to make it a hub for Islamic investment and transaction. After being attracted to the economy, international banks such as HSBC and the defunct Citibank, even if they did not grow to become totally *Sharīʻah*-compliant, did try to create windows that adjusted some of their operations to satisfy the demand for Islamic banking packages.[94] This phenomenon makes the Islamic financial transaction not only a dominant option in the country but a recognized competing partner for financial business in Brunei. According to the Oxford Business Group,[95] Brunei's two Islamic financial institutions [*Perbadanan Tabung Amanah Islam Brunei* (TAIB) and *Bank Islam Brunei Darussalam* (BIBD)] had a total asset valued at $7.9 billion, which represented 41% of the country's total banking asset in 2013. The above figure was an increase from the 2010 estimate of 37%.[96] The 2013 financial review by the business magnates also indicated that Islamic banks in Brunei had an increased non-performing loan ratio of 9.7% as compared to 4.1% ratio of interest-motivated banks.[97] Nonetheless, Islamic banks continue to gain just like their interest-based counterparts due to the former's high patronage, investments and earnings. Islamic banking proceeded on liabilities averaged 9.2% during the first nine months of 2013 as against the 10.9% of their interest-based counterparts within the same period.[98]

The socio-cultural foundation of Brunei Darussalam does not promote exploitative economic transactions in whatever form they might take. Further, through the policy of vesting almost all productive resources of the country in the hands of the central authority of the Sulṭ ān and the continuous provision of an all-inclusive social welfare pursued with all vigour, the Bruneian government has reduced control over the wealth of the country by few which is often perceived as the main obstacle to sustainable economic development in the context of social welfare.[99] In terms of foreign exchange and the frustrating challenge unleashed by the slash in 'petro-dollar' due to the fall in the worldwide prices of oil products which constitute the backbone of the economy, the

[93]Saiful Islam, "Brunei Economy and its Integration in the Regional Economic Activities," *The Hikone Ronso* 387, (2011): 82- 89.

[94]Rodney Wilson, "Development of Financial Instruments in an Islamic Framework," *Islamic Economic Studies* 2, no. 1 (1994): 103-18; M. Shahid Ebrahim and Tan Kai Joo, "Islamic Banking in Brunei Darussalam," *International Journal of Social Economics* 28, no. 4 (2001): 314; See also: *The Brunei Times*, 20th May 2007 Edition.

[95]The Oxford Business Group, *The Report: Brunei Darussalam 2014.*

[96]See also: *The Brunei Times*, 1st January 2015 Edition.

[97]Oxford Business Group, *The Report*, with IMF figures.

[98]Oxford Business Group, *The Report*; see also: *The Brunei Times*, 1st January 2015 Edition

[99]Khan and Bhatti, "Why Interest-Free," 156.

government has sharply responded with a pragmatic approach in order to counter its impact on foreign exchange, maintain balance of payment (BoP) surplus, reduce public debt to a reasonable level and to prevent its severe impact on the economy. This has been done through a provisional slash in government spending which will in turn guard against both its domestic and external borrowings, all of which have implications for interest rates in even their conventional forms. The implication is that the Bruneian Islamic economy and its interest-free banking and finance have a good opportunity for future growth and ultimately, all things being equal, interest-free banking has a good future.

6. Challenges Faced by Islamic Banking and Financial Transactions in Brunei

Despite the success chalked above, the young Bruneian 'Islamic' financial economy still faces some serious challenges.

6.1. Competition from Interest-based Counterparts

As an Islamic country with the political will to promote interest-free banking, the regulation of the domestic interest rates of conventional banks should be a priority in the economic management of the country. In the conventional system, this is achieved through the setting of a benchmark for serving as the focal point around which the interest rates of various banks revolve. This is the duty of a central bank. A central bank regulates interest rates by determining policy rates through the adjustment of the amount of business deposits.[100] It has to do with the regulation of the flow of money in-and-out of the nation's biggest financial store (the central bank). This works on the assumption that the higher the demand (for money), the higher its price (the interest rate). Thus, the central bank reduces the price of money (interest rate) through the purchase of securities such as treasury bills and by expanding its quantity of deposits. On the other hand, it increases the rate of interest through the sale of securities and a cut-down of the credit stock. In Brunei, however, there is no 'central bank' in the conventional sense. Therefore, as we indicated earlier, as an Islamic state opposed to interest-based financing, Brunei does not set any benchmark for regulating interest rates through the quasi-central monetary institution the *Autoriti Monetari Brunei*.[101] This is because it does not have it on its agenda to promote interest-based transactions by setting a benchmark. Nonetheless, it does not prohibit any bank from charging interest either. This makes interest-based banking a phenomenon of indifference (*Ibādah*) in Brunei. Citizens are given the freedom of patronizing interest or not. Thus, various banks use the prime rate as the guide to determine their interest rates. Prime rate refers to the lowest rate of interest at which a financial institution could lend money to its customers in a commercial transaction. It is the rate of interest imposed by banks on "loans to their most trustworthy corporate customers."[102] Other borrowers normally pay a rate marked above (not below) the prime rate. It is, therefore, fixed by the banks themselves. There is, therefore, a sort of

[100] Torgeir Høien, "Tell us Something New: How do Central Banks Determine Interest Rates?" SKAGEN Funds, January 3, 2011.

[101] *Borneo Bulletin Yearbook 2013* (Brunei: Brunei Press Sdn., Bhd, 2013), 111.

[102] Brian C. Gendreau, "When is the Prime Rate Second Choice?" *Federal Reserve Bank of Philadelphia Business Review*, May/June (1983), 13.

competition between the interest-free institutions and their interest-based counterparts in the country.

6.2. Uncertain Business Practices

In spite of the effort of the authorities to rid the economy of unethical characteristics through the implementation of interest-free banking, even the Islamic financial scene still seems to manifest visible features of non-*Sharīʻah*-compliant activities. The ill-perceived means of transacting business such as *gharār* (something of unknown consequence, unlikelihood, uncertainty or of speculative risk),[103] *maysir* or *qimār* (gambling)[104] are all essentially detested in Islamic banking and financial perspective because they are not based on profit and loss-sharing[105] in which all parties are entitled to a share of the outcome wherever they appear as partners.[106] Additionally, customers are expected to be paid only what they have toiled for.[107] Anything short of this is fraud (*ṭafīf* in the language of the Qur'ān.[108] Nonetheless, it is not uncommon for Islamic financial institutions in Brunei to give away expensive cars like Jaguar as rewards (*Barakah*) for lucky 'winners.' This ill-perceived means of promoting business remains a challenge not just to the interest-free bid but the entire ethical banking and finance in the country because it is inconceivable that an unethical financial transaction is suppressed while its variants are promoted at the same time.

6.3. The Continual Slash in the Petro-Dollar

Another major challenge to Islamic banking in Brunei is the petro-dollar, the backbone of the Bruneian economy. So long as the oil remains in its current abundance, Brunei has enough to shore-up the shortfalls in its infant 'Islamic' economy. However, the same 'petro-dollar' not only renders the economy more vulnerable to the unpredictable international prices of the 'precious liquid' but the liquid itself keeps plummeting in quantity. According to *The Brunei Times*,[109] Brunei's oil and gas exports will shrink by 3.5 million metric tons by 2035. The reserves of liquefied natural gas are expected to keep on decreasing because its main fields have peaked in production. The net export of oil will drop from 7.7 metric tons in 2010 to 4.5 metric tons in 2035, while the net export of liquefied natural gas will decrease from 7.6 metric tons in 2010 to 4.5 metric tons in 2035. The production of oil and gas in Brunei began to decrease from 2008.[110] The implication is that the hold of the petro-dollar on the economy is expected to weaken. Already, the country's GDP is down by 1.5% in 2015 according to ADB,[111] due perhaps to the fall in oil prices coupled with the costs of maintenance of the oil

[103] Abdulkader S. Thomas, *What is Permissible Now*? (Singapore: Muslim Converts Association, 1995); Saeed, "Islamic Banking," 114; Ebrahim and Joo, "Islamic Banking," 324; For more details, see: Ahmad Hidayat Buang, *Studies in the Islamic Law of Contracts: The Prohibition of Gharar* (Kuala Lumpur: International Law Book Services, 2000).

[104] al-Maeda 5:90.

[105] Zuberi, "Interest Free," 1077.

[106] Ebrahim and Joo, "Islamic Banking," 324; Yusuf, "Ethical Implications," 228.

[107] Yusuf, "Ethical Implications," 223-4, 228.

[108] Al-Inshiqāq 1-3.

[109] Wednesday, November 6, 2013 Edition reported from the Asian Development Bank's (ADB) Energy Outlook lease in October 2013.

[110] ADB, Asia, quoted in *The Brunei Times*, November 6, 2013 Edition.

[111] See: *The Brunei Times*, March 25, 2015 Edition.

facilities.[112] For the same reason, it has been reported that the country is expecting a budget deficit of B$2.28 billion for the 2015/2016 fiscal year.[113] This gradual development has necessitated an urgent call for the diversification of the economy.[114] Diversifying an economy has been an effective tool for increasing and sustaining long term economic growth in a country. According to Hvidt, "current development plans point unanimously to diversification as the means to secure the stability and the sustainability of income levels in the future."[115] Mature economies that can support a variety of well and firmly integrated sectors have the potential of maintaining a more sustainable growth rate. However, initiating productivity in yet-to-be-developed areas is another major hurdle that demands the collective effort of not just the government but also of the private sector and the international community which transcends the boundaries of a country's economic autonomy. Apart from the structural barriers to the diversification of the Bruneian economy, the above mentioned features of economic diversification from a global perspective also pose a predictable and indeed the main challenge to future prospects of interest-free banking. This is because it will expose the country to the exploitative and interest-oriented international community and private sector. With the entrenchment of foreign and private sector investments and domination of the economy, the Islamization policy might eventually lose its hold on the economy and thus gradually pave the way for the interest-oriented economy. The implication is that privatization or diversification brings with it the gradual shifting of the control of the country's wealth from government to the private sector because the government "gradually withdraws from parts of the economy that are best operated by the private sector."[116] After ceding its control of wealth to private sector, the government will invariably lose its exclusive power to control or direct the course of economic or financial transactions and will potentially limit its ability to fulfill its financial obligations within the current limits. This will in turn make the government more vulnerable to not only the dictates of private sector but even foreign governments and interest-based financial institutions which it might have to rely on financially to maintain the economy. All the above issues have serious implications for interest-free financing and financial transactions as the government cannot afford the risk of losing its share of foreign trade and foreign investments as well as the inflow of foreign financial resources through the frustration of still holding on to interest-free banking or financing.

7. Conclusion

From the above discussion, it is self-evident that Islamization of the Bruneian economic arena signaled the emergence of a new economic order in the country. The new eco-sphere was bound to succeed not necessarily on its own merit but also due to political will and cooperation. Political will is of utmost significance in the fruitful implementation of interest-free economy or banking and the success of its representative

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[112] *Borneo Bulletin*, June 6, 2015 Edition.

[113] *The Brunei Times*, May 13, 2015 Edition.

[114] Ibid.

[115] Martin Hvidt, "Economic Diversification in GCC Countries: Past Record and Future Trends," *Kuwait Programme on Development, Governance and Globalisation in the Gulf States, Research Paper*, no. 27 (2013): 1.

[116] Mark Crosby, *Economic Diversification* (Brunei: Centre for Strategic and Policy Studies, 2007), 4.

financial institutions.[117] Next in line is an efficient Islamization process that facilitates the establishment of socio-cultural and economic foundations that vigorously promote the essential values of Islam in their entirety. The interest-free banking advocates in Brunei Darussalam (the political leaders) never overlooked these essential prerequisites. The cooperation of the citizenry from the wealthy upper class to the indigent lower class, which in all intends and purposes interest-free banking tries to protect, afforded Brunei everything it takes to establish an Islamic order. The young 'religious' economy offers auspicious terrain for the implementation and promotion of interest-free banking and finance. The large volume of the nation's precious exports as against her imports, low public debt subsequent to low dependence on international community and private sector, and consequently a favourable balance of trade (BoT) and balance of payment (BoP) coupled with budget surpluses have facilitated the growth of interest-free banking in Brunei. The government holds the view that *ribā* and its associates are prohibited for Muslims whether it takes the form of usury or bank interest and irrespective of whether it is transacted within a banking institution or a non-bank financial institution. Nonetheless, it has been impossible, given the contemporary circumstances of mixed society and particularly the interwoven and complicated nature of modern-day trade, to divorce the economy of oil-rich Brunei from the international economy by totally abolishing interest. Thus, in the midst of these challenges, interest-free banking operates conterminously with interest-based banking in the Bruneian economy. This mixture, however, occurs at the informal level; the official national economic philosophy is channeled towards interest-free finance. Therefore, interest-free banking and finance still has the opportunity for future growth. Nonetheless, the need for the diversification of the economy is expected to have imminent implications for the application of this interest-free philosophy in the country in the course of time. This is because diversification, which does not only imply unveiling the economy internationally but more importantly suggests empowering the private sector, also brings with it the likely consequence of endorsing interest-based banking and financial practices. Thus, our main conclusion is that Islamic banking and finance has been very successful and indeed has good prospects for future in Brunei. Yet, it still remains vulnerable to non-political future challenges subject mainly to the prospects of petro-dollar. This then calls for a certain alertness so that appropriate policies could be devised to mitigate any unexpected consequences for the national Islamic economic philosophy.

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[117] Khan and Bhatti, "Why Interest-Free," 158.

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