

ZAKAH CORPORATION'S LEGAL ENTITY IN MALAYSIA

Siti Maziah Ab Rahman¹
Nurul Fatma Aziz@Awang²
Mariam Setapa³
Nur Hazelen Mat Rusok⁴
Putra Faizurrahman Zahid⁵
Shafiurrahman Hamzah⁶
Hasnun Anip Bustaman⁷

¹Faculty of Business and Management, Faculty of Business Management, Universiti Teknologi MARA, Kelantan Branch, Machang Campus, Kelantan, Malaysia (E-mail:maziah650@uitm.edu.my)

²Faculty of Accountancy, Faculty of Business Management, Universiti Teknologi MARA, Puncak Alam Branch, Malaysia (E-mail:nurulfatma@uitm.edu.my)

³Faculty of Business and Management, Faculty of Business Management, Universiti Teknologi MARA, Kelantan Branch, Machang Campus, Kelantan, Malaysia Universiti Teknologi MARA (UiTM), (E-mail:maria135@uitm.edu.my)

⁴Faculty of Business and Management, Faculty of Business Management, Universiti Teknologi MARA, Kelantan Branch, Machang Campus, Kelantan, Malaysia), (E-mail:hazelen@uitm.edu.my)

⁵Faculty of Business and Management, Faculty of Business Management, Universiti Teknologi MARA, Kelantan Branch, Machang Campus, Kelantan, Malaysia (E-mail:putraf278@uitm.edu.my)

⁶Putra Business School, Universiti Putra Malaysia (UPM), (E-mail:shafi.hamzah@gmail.com)

⁷Faculty of Business and Management, Faculty of Business Management, Universiti Teknologi MARA, Kelantan Branch, Machang Campus, Kelantan, Malaysia), (E-mail: hasnu380@uitm.edu.my)

Article history

Received date : 18-3-2023
Revised date : 19-3-2023
Accepted date : 10-5-2023
Published date : 15-5-2023

To cite this document:

Ab Rahman, S. M., Aziz, N. F., Setapa, M., Mat Rusok, N. H., Zahid, P. F., Hamzah, S., & Bustaman, H. A. (2023). Zakah Corporation's Legal Entity in Malaysia. *International Journal of Accounting, Finance and Business (IJAFB)*, 8(47), 168 - 175.

Abstract: *A corporation is a succession or collection of persons having at law an existence, rights, and duties, separate and distinct from those of the persons who are from time to time its members. Under Shariah, a company is recognized as a body corporate created by law to be an artificial person who holds few attributes inter alia the right to sue and be sued and the power to hold property under its own name. It is recommended that all Islamic commercial institutions such as zakah corporation be framed under Shariah corporate structure. Being a business entity that embraced Shariah principles, it is important for a zakah corporation to adhere to a legal framework that complies with the Shariah principles. This paper discussed the characteristics of corporations under Malaysian law and compared them to Islamic law (Shariah) principles. This paper discusses zakah corporation's legal entity in Malaysia where a business entity that has embraced Shariah principles, must adhere to a legal framework that complies with Shariah principles. The legal framework outlined above is strongly recommended for all zakah corporations. It is also proposed that the Companies Act be reviewed in order to identify provisions that do not adhere to Shariah principles.*

Keywords: *Legal entity, Shariah Principle, Zakah Corporation's*

Introduction

A corporation or company is a legal entity formed under the doctrine of corporate personality. Corporate personality is a well-established legal principle in English company law. Under this doctrine, a corporation is recognized as a legal person with distinct legal characteristics, such as a legal entity distinct from its members, perpetual succession, the right to enter into legal proceedings, deal with property in its own name, and the ability to limit the liability of its members. In other words, a company is a corporation. A corporation is a succession or collection of persons having at law an existence, rights, and duties, separate and distinct from those of the persons who are from time to time its members (Ayub, Yusoff, & Azrae, 2009). A corporation carries with it several distinguishing features, namely it is a persona at law, i.e., an artificial person; and it has perpetual succession, i.e., the company carries on and is not dissolved despite the changes in its membership since its existence is maintained by the constant succession of new persons who replace those who die or being removed. The doctrine of separate legal entity originated from the case *Salomon v. Salomon & Co. Ltd.* (1897). The facts, in this case, disclosed that a company had been incorporated by Mr. Salomon in which he and members of his family were the only shareholders. The issue arises when the company's business turns out to be a failure. The term 'body corporate' is not defined under the Companies Act 1965. However, generally, it covers both the 'companies' and 'corporations'. 'Corporation' is one of the artificial legal persons (Ariff, Nizam, Musa, Abdullah, & Bidin, 2017).

Regarding observation, it can be concluded that in Malaysia, all companies need to be registered under the Companies Act 1965 which was based on the conventional framework. And even though the application of the common-law doctrine of corporate legal personality as an artificial person could be accepted under *Shariah*, it is subject to certain modifications and therefore shall not be a direct application. Being one of the *Shariah* compliance business entities, it is important for waqf corporations to embrace the framework for *Shariah* corporations. Legal Entity of Body Corporate Under *Shariah* as mentioned earlier, under the conventional corporate structure, a company is recognized as a body corporate created by law to be an artificial person who holds few attributes inter alia right to sue and be sued and power to hold property under its own name. However, under *Shariah* law, the discussion on an artificial person is derived from the views of the *Muslim* Jurists on the entity of *shaksiyah i'tibariyah* (الاعتبارية الشخصية). Here is a character on *Zakah* Corporation in Malaysia. *Zakah* is defined as an act of worship performed to draw closer to Allah by extracting an obligation right from specific types of wealth and distributing it to specific groups at a specific time and under specific conditions. 2012 (Bouheraoua). *Zakah* on the company in Malaysia, The 31st Muzakarah (Conference) of the Fatwa Committee National Council of *Islamic* Religious Affairs Malaysia held on 9th December 1992 has discussed *zakah* on company. The Conference has decided that a business company is obliged to pay *zakah* when it fulfils these conditions:

- The company is owned by Muslims,
- The company is owned by free Muslims
- Complete ownership
- The amount of the wealth reaches the minimum zakatable [sic] limit (nisab)
- The wealth has been possessed for one lunar year (354.3 days)
- The *zakah* rate on company is 2.5%

As for the company shared by Muslims and non-Muslims, only the share owned by the Muslims is zakatable. The *zakah* is calculated based on the nett income obtained.” The establishment of companies (syarikat) is governed by the Companies Act 1965. The companies incorporated under the Act may be divided into three types:

- (a) a company limited by shares;
- (b) an unlimited company; and
- (c) a company (limited—added) by guarantee.

Scholars (*Ulamas*) had been unanimous that trading companies are obliged (wajib) to pay *zakah* when the following conditions regarding the obligation to pay trading *zakah* are met.

It can also refer to the act of paying this share. This share of wealth is known as *zakah*, according to al-Nawawi's report from al-Wahidi, because it increases the funds from which it is taken and protects them from being lost or destroyed. According to Ibn Taimiyah, the *zakah* payer's inner soul improves and his wealth is cleansed. Al-Qaradawi (Al-Qaradawi, 2000) According to Sheikh Abdul Rahman Isa and Dr. Wahbah al-Zuhaili, the imposition of *zakah* on a corporation is determined by its type of business. If it is solely for manufacturing purposes and does not engage in any business practises, it is exempt from *zakah* except for its profit, which is then combined with the shareholder's wealth and paid accordingly. If the company is of the business type, any profits are *zakahable* as a business *zakah*.

Zakah is imposed on the company's shares regardless of its status as an issuing-shares company, Sheikh Muhammad Abu Zuhrah, Abdul Wahab Khalaf, Abdul Rahman Hasan, and Dr Yusuf al-Qaradawi. The shares are classified as a *zakahable* business stock (Urudh al-Tijarah). (Al-Soifi, 2006)). As such, the researchers will look at the obligation of companies or corporations to pay *zakah* from the perspectives of Shariah and Malaysian law. This paper focuses specifically on the viability of corporations incorporated under the Companies Act 2016, which adopts common law and treats it as a fictitious legal entity to pay *zakah* as a religious obligation that is originally imposed on individual human beings under Shariah. Other issues discussed include the misunderstanding of company and partnership that influenced the current fatwas imposing *zakah* on corporations in Malaysia, as well as potential constitutional issues arising from such *fatwas*.

Legal Entity of Body Corporate Under Shariah

The *Syariah* definition of *zakah* as follows:

The technical definition of *zakah* is: an act of worship performed to draw closer to Allah by extracting an obligatory right from certain kinds of wealth and giving it to specified groups at a specified time, in accord with specific conditions. On the legal basis for *zakah*:

... *Zakah* is one of the five pillars of Islam and is obligatory upon every Muslim for whom its requisite conditions are fulfilled. ... It is mentioned along with salah in more than 80 passages of the Qur'an; for example,

“Establish prayer and pay *zakah*” (al-Qur'an, 2:43); Cf. 98:5 ...

... Among the many passages in which *zakah* is mentioned in the Qur'an are the following: “Establish prayer and pay *zakah*, and whatsoever good you send before you for your souls, you will find it with Allah”.

Also: “And they were ordered nothing else than to serve Allah, keeping religion pure for Him, to be by nature upright, and to establish prayer and to pay *zakah*. That is true religion”.

... The Sunnah has a multitude of texts confirming the Qur’an’s orders regarding the obligation to pay *zakah*; among them, the following:

... ‘Abd Allah ibn ‘Umar quoted the Prophet (r) as saying, “*Islam* is founded on five [pillars]: to bear witness that none has the right to be worshipped except *Allah* and that *Muhammad* is the Messenger of *Allah*; to establish salah, pay *zakah*, make Pilgrimage [to Makkah], and fast in Ramadan”.

According to a modern Muslim scholar, Imran Ahsan Khan Nyazee, there has been a prolonged debate among *Islamic* jurists on the existence of the concept of a fictitious person (*shakhsyah i’tibariyah*) and the majority of modern scholars insist that such a concept was known to Islamic law while some are doubtful whether Islamic law was aware of such concept (Abd Ghadas & Abd Aziz, 2017). *Shariah* does recognize the principle of an artificial person, but it does not mean that all institutions based on this concept automatically become legal. Under Shari’ah, the implementation of such a concept in different forms needs separate analysis. As an example, the existing structure of the business corporation which enables it to issue securities must be free from *riba* and it must also fulfill all the requirements for conducting business in Islam. Mustafa took the view that the theory which recognizes an entity other than a human being as a legal person can be justified through the theory of fiqh known as *al-Dhimmah* (Abd Ghadas & Abd Aziz, 2019). The term of *al-Dhimmah* has been discussed by many Muslim jurists in various opinions (Al-Zurqa, 1964). According to Madhab al-Syafie jurists, *al-Dhimmah* is an attribute of a human being with duties (*al-ilzam*) and also obligations (*al-iltizam*) (Al-Kabashi, 1989). This definition is also accepted by jurists of Madhab Maliki, Hanafi and Hanbali (Al-Buhuti, 1947). Al-Sarakhsi defined *al-Dhimmah* as a fixed attribute of a person accepting obligations and duties. This concept relates to an obligation and capacity (*al-ahliyyah*) as well. The application of this concept as discussed and applied by the jurists since the early era of the development of fiqh does not connote the same definition. The majority of the fuqaha have acknowledged the existence of other than human being which are entitled to some rights and responsibilities.

However, unlike the common law, the Islamic scholar’s discussion concerning the artificial person not only relies on the entity itself but more on whether it is subject to obligation and responsibilities as required under Islamic law. According to al Makashifi Thoha al-Kabashi, the *fiqh* of *Islam* does recognize the existence of an artificial person (*al-syakhsiyah al-I’tibariyyah*) as it is applicable to hospitals, *waqf*, and *syarikaat* and as *al-Dhimmah*, these entities have certain rights and obligations. He also claimed that this artificial person enjoys the concept of *al-ahliyyah al-kamilah* like a human being with certain rights and obligations as stated under Section 53 of the Egypt Civil Law that an artificial person enjoys full rights unless such rights are restricted only to a human being. Although there are many Muslim jurists who supported the application of the doctrine of the artificial person in *Shariah*, there are also some Muslim scholars who contested the acceptance of such principle in *Shariah*. For example, al-Bazdawi and al-Nawawi took the view that *al-Dhimmah* is a *dzat* which is real and cannot be fictitious because the *Shariah* only imposed obligations and rights on real person. Al-Tahanawi also emphasized that the term *al-Dhimmah* is synonymous to human’s attribute and not applicable to artificial entities as it has relevancy to the interpretation of liability and obligation. Al-Sarakhsi highlighted in his book that when *dhimmah* was offered to the mountains, they refused

it as they would be afraid that they cannot fulfill the required obligations, but human being accepted it.

Thus, al-Dhimmah is an attribute conferred only by Allah swt and it is a trust resulting from a covenant ('ahd). The fact that dhimmah is a covenant between Allah swt and the 'abd (servant of Allah) means that it can only be assigned to a natural person (Nyazee, 2003). As such, unlike the common law, the status of legal person in Islam cannot be conferred to entities other than human. Abdul Aziz Ahmad al-Bukhari (al-Bazdawi) took the same view as Al-Sarakhsi and emphasized that dhimmah refers to 'ahd (covenant) as Allah created a mankind with amanah, aql, dhimmah, enjoys the right of innocence ('usmah), freedom and ownership and carries the duties as Allah's rights towards him (Al-Bukhari, n.d.). Referring to the modern Muslim jurists, the theories of artificial legal person and corporate personality are generally viable, but such acceptance cannot be absolute or total adoption of the common law doctrine. A balance approach is highlighted by Nyazee, (2003b, 2003a), whereby he contended that the ruler may assign a restricted or limited *dhimmah* to a non-human on the following conditions: Firstly, no religious duties will be expected of a fictitious person.

In other words, the fictitious person will not be subject to the *khitab* of ibadat and will not be liable for any religious duty or obligation that may flow from it. Thus, it will have no liability for *zakah*, for sadaqah, or for any other religious tasks as these duties are attached to the 'ahd of human with the creator (Allah swt). Secondly, some form of 'aql must be associated with the fictitious person. This 'aql may be that of one individual or group of individuals like the board of directors. The *ahliyyat al-ada'* will always be associated with this source of 'aql, and so will the liability for such acts. Thirdly, a concept of dual title of ownership must be associated with a fictitious person. Any property held by the fictitious person in its own name must be assumed to be held on behalf of the members of this fictitious person as a result of khalt or mingling of capitals. In addition, the body corporate may have full right of disposal and transaction in the property if so, permitted by its members. Referring to the guidelines proposed by Nyazee, it is obvious that in adopting the common law doctrine of corporate personality, there should be some modifications to the obligations of the company as a legal entity and to the board of directors and members who form the "aql" of the companies.

Rather than having totally independent and separate legal entity from the directors and members, Nyazee highlighted that in *Shariah* corporations, there should be a dual ownership and liability structure. This is important because as an artificial person, the company could not in reality own and manage properties and also cannot be physically arrested and made accountable for default with the third parties. In short, although the adoption of the common law doctrine of an artificial person is possible under *Shariah*, the application of the law under *Shariah* requires certain modifications.

The debate over this issue has given rise to three approaches:

The first approach fully considers the concept of legal entity, recognises it as having full legal capacity (*ahliyyah*), and holds that the corporation is required to pay *zakah* for itself. Once the corporation's wealth reaches the nisab, no attention is paid to the nisab of the individual shareholders. The corporation pays it based on the nature of its activity (commercial or investment) and without regard for its shareholders' intentions.

The second approach acknowledges that a legal entity has *ahliyyat alwujoob* (the capacity to acquire rights) but not *ahliyyat al-adaa'* (the capacity to perform duties), and that this *ahliyyat*

alwujoob is effective to the extent that it is appropriate for it... They argued that while the shareholders have the primary obligation to pay the *zakah*, they can appoint the bank to act as their representative and pay it on their behalf. The third approach: If the state's legal system requires financial institutions to pay *zakah*, the corporation or financial institution's legal entity is taken into account.

Legal Framework for *Shariah* Corporation

In Malaysia, all *Islamic* commercial institutions were registered under the Malaysian Companies Act 1965. These institutions include Tabung Haji, *Zakah*, and *waqf* corporation. As a creature of the statute, the existence of a company is totally dependent on the provisions of the Companies Act. Thus, it is recommended that all *Islamic* commercial institutions such as *waqf* corporations be framed under *Shariah* corporate structure. *Shariah* corporate structure is not similar to the conventional structure. The legal framework for the *Shariah* corporation should fulfill all the requirements below. *Maqasid Shariah* as the Basis of the Business Framework The term *Maqasid* is derived from the verb *qasada* which means goals and purposes. *Maqasid* itself means goals or objectives and when such term is attached to the word *Shariah*, it specifically refers to the goals or objectives of *Shariah*. According to Imam al-Ghazali, the objective of the *Shariah* is to promote the well-being of all mankind, which lies in safeguarding their faith (*din*), their human self (*nafs*), their intellect (*'aql*), their lineage (*nasl*), and their wealth (*mal*) (Chapra, n.d.). The goal of sacrifice or good deeds according to *Allah* (S.W.T) is sincerity and *Taqwah* (piety). In other words, it can be said that all business activities should be carried out based on sincerity and piety. However, as is seen in the above verse, all undertakings must be done to please *Allah* (S.W.T), which is the common requirement for any good deed in Islam. Therefore, corporations and all business entities in an *Islamic* state should render their business activities only for the sake of God. The Prophet *Muhammad* (S.A.W) highlights the importance of giving rather than taking and everyone should do charity especially when one is self-sufficient.

***Shariah* Good Governance**

Corporate governance is the relationship among various participants (CEO, management, shareholders, and employee) in determining the direction and performance of corporations. It ensures that the board of directors is accountable for the pursuit of corporate objectives and that the corporation itself conforms to the law and regulations (Choudhury & Hoque, 2006). Generally, it is observed that the main objective of the corporation including the so-called 3 *Islam* does differ from normal corporate governance in the standardization of rules which must obey the *Shariah* rules stated in the holy Quran (Alnasser & Muhammed, 2012; Obaid et al., 2020). Shura Shuratic decision-making procedures provide a vehicle for ensuring that corporate activities and strategies are fully discussed and that a consensus-seeking consultative process is applied. Directors and senior managers would be expected to listen to the opinions of other executives before making a decision and shura members would include, as far as possible, representatives of shareholders, employees, suppliers, customers, and other interested parties (Amalia, 2017; Wahab et al., 2007). The institution of *hisba* offers a framework of social ethics, relevant to monitor the corporation, with the objective of encouraging the correct ethical behavior in the wider social context. It also empowers individual *Muslims* to act as "private prosecutors" in the cause of better governance by giving them a platform for social action. It provides a device to solicit juristic advice, monitor compliance with *Islamic* precepts, and collect *Zakah*. This extra layer of auditing and accountability for resource use ensures that the enterprise operates as an *Islamic* concern (Lewis & Lewis, 2005).

Conclusion

A tangle of *Shariah* and legal issues arising from fatwas requiring corporations in Malaysia to pay *zakah* necessitates that these fatwas be reviewed and revisited in order to comply with the current legal framework of corporations under the Companies Act 2016 as well as the Federal Constitution. Furthermore, it is proposed that the corporations' existing legal framework be modified in order to be consistent with *Shariah* principles, particularly in relation to *zakah* imposition. Being a business entity that embraced *Shariah* principles, it is important for a *zakah* corporation to adhere to a legal framework that complies with the *Shariah* principles. The above legal framework is highly proposed for all *zakah* corporations. It is also proposed for the Companies Act be reviewed to identify provisions that are not in compliance with *Shariah* principles.

References

- Abd Ghadas, Z. A., & Abd Aziz, H. (2017). Legal Framework Of Shari'Ah Corporations In Malaysia: Special Reference To Waqf Corporation. *Journal of Modern Accounting and Auditing*, 13(3), 121-127.
- Abd Ghadas, Z. A., & Abd Aziz, H. (2019). Analysis On The Doctrine Of Limited Liability Under Company Law And Sharī 'Ah. Al-Shajarah. *Journal of the International Institute of Islamic Thought and Civilization (ISTAC)*, 24(2), 293-310.
- Al-Buhuti. (1947). *Kashshaf al-qina* (Vol. 3). Cairo.
- Al-Bukhari, A. A. (n.d.). *Kashful Asrar an usul Fakhri al-Islam*
- Al-Kabashi, A. M. T. (1989). *Al-Zimmah wa al-Haq wa al-Iltizam wa Ta'thiruha bi al-Mawt fi al-Fiqh al-Islami*. Dirasah muqaranah. Riyadh: Maktabah al-Haramayn.
- Al-Zurqa, M. A. (1964). *Al-Madkhal ila Nazariyyat Al-Iltizam Al-Ammah Fi Al-Fiqh Al-Islami*.
- Alnasser, S. A. S., & Muhammed, J. (2012). Introduction To Corporate Governance From Islamic Perspective. *Humanomics*.
- Amalia, E. (2017). The *Shariah* Governance Framework For Strengthening Zakah Management In Indonesia: a Critical Review Of Zakah Regulations. 1st International Conference of Law and Justice-Good Governance and Human Rights in Muslim Countries: Experiences and Challenges (ICLJ 2017), 133–138.
- Ariff, Z., Nizam, M. S., Musa, M. K., Abdullah, F., & Bidin, A. (2017). Public Interest Entity. A Proposed Legal Framework For a Social Entrepreneur Entity In Malaysia. *Advanced Science Letters*, 23(9), 9305-9307.
- Ayub, Z. A., Yusoff, Z. M., & Azrae, A. N. (2009). Separate Legal Entity Under Syariah Law And Its Application On Islamic Banking In Malaysia: A Note. *International Journal of Banking and Finance*, 6(2), 139-154.
- Choudhury, M. A., & Hoque, M. Z. (2006). Corporate Governance In Islamic Perspective. *Corporate Governance*, 6(2), 116–128. <https://doi.org/10.1108/14720700610655132>
- Lewis, J. S., & Lewis, C. F. (2005). A Proposed International Legal Regime for the Era of Private Commercial Utilization of Space. *Geo. Wash. Int'l L. Rev.*, 37, 745.
- Nyazee, I. A. (2003). Islamic Law And Human Rights. *Islamabad Law Review*, 1, 1.
- Nyazee, I. A. (2003a). Islamic Law And Human Rights. *Islamabad Law Review*, 1, 1.
- Nyazee, I. A. (2003b). Islamic Law And The CRC (Convention On The Rights Of The Child). *Islamabad Law Review*, 1, 1.
- Obaid, M. M., Ibrahim, I., & Mat Udin, N. (2020). Zakah and Tax Compliance Behaviour in Yemen: A Conceptual Study. *Journal of Advanced Research in Business and Management Studies*, 19(1), 1–14. <https://doi.org/10.37934/arbms.19.1.114>
- Wahab, A. R. A., Lewis, M. K., & Hassan, M. K. (2007). Islamic Takaful: Business Models,

Shariah Concerns, And Proposed Solutions. Thunderbird International Business Review, 49(3), 371–396.