



BANK NEGARA MALAYSIA
CENTRAL BANK OF MALAYSIA

Hajah and Darurah **Exposure Draft**

Applicable to:

1. Licensed Islamic banks
2. Licensed takaful operators and professional retakaful operators
3. Licensed banks and licensed investment banks approved to carry on Islamic banking business
4. Prescribed development financial institutions approved to carry on Islamic financial business

This Exposure Draft (ED) sets out Bank Negara Malaysia's (the Bank) proposed requirements and expectations for the application of *hajah* (need) and *darurah* (dire necessity) by Islamic financial institutions (IFIs) in carrying out Islamic banking and takaful business. Specifically, this ED aims to seek feedback from IFIs on the following:

- (a) parameters of *hajah* and *darurah* and their scope of application;
- (b) requirements relating to responsibilities of the board, Shariah committee, senior management and control functions of the IFIs in ensuring a comprehensive and robust assessment as well as effective implementation of the application of *hajah* and *darurah*; and
- (c) requirements and policy guidance relating to the processes and procedures that facilitate Shariah deliberation and decision-making concerning *hajah* and *darurah* in the IFIs.

The Bank invites written feedback on the proposals in this ED, including suggestions on areas requiring further clarification, elaboration or alternative arrangement that the Bank should consider. Specifically for IFIs, the Bank requires comprehensive feedback that must–

- (a) be prepared based on inputs across key functional areas of the IFIs, including unit/section from product development, strategic management, treasury, risk management, compliance and Shariah, given the potential implications of the proposals to the IFIs' strategies, operations and product offerings;
- (b) include inputs from the Shariah committee of the IFIs; and
- (c) be supported with clear justifications, including accompanying evidence or illustrations where appropriate, to facilitate an effective consultation process.

Responses shall be submitted via email to shariahstandard@bnm.gov.my by **28 February 2023**. Submissions received may be made public unless confidentiality is specifically requested for the whole or part of the submission.

In the course of preparing your feedback, you may direct any queries to the following officers:

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PART A OVERVIEW

1 Introduction

- 1.1 The Islamic financial system in Malaysia has seen significant advancement in scale, diversity and sophistication of institutions and financial offerings in recent years, reflective of a maturing market. As the Islamic banking and takaful industry continues to develop, challenges in the business and operating environment would require attendant risks to be well-managed. This framework aims to clarify parameters on *hajah* and *darurah*¹ from contemporary finance perspectives to facilitate their application in Islamic financial business in accordance with Shariah.
- 1.2 *Hajah* and *darurah* concepts have been applied in Islamic financial business to address hardship² or difficulties in executing financial transactions or arrangements based on Shariah principles. The application of *hajah* and *darurah* arises during unfavourable circumstances or distress situations facing an Islamic financial institution (IFI) to prevent harm³ (*mafsadah*) and ultimately attain benefit (*maslahah*).
- 1.3 The Shariah Advisory Council of Bank Negara Malaysia (the SAC) has, on case-by-case basis, issued several Shariah rulings⁴ that outline broad Shariah parameters⁵ relating to the application of *hajah* and *darurah*. Taking into consideration the implementation of these rulings by IFIs, a more robust governance process and assessment approach is warranted to promote effective application of *hajah* and *darurah* by IFIs.
- 1.4 This policy document sets out the Shariah and operational requirements and expectations concerning the application of *hajah* and *darurah*, as follows:
- (a) outline *hajah* and *darurah* parameters for the application of exceptional rules;
 - (b) clarify and strengthen the accountability of individuals responsible for the assessment, deduction as well as implementation of *hajah* and *darurah*⁶; and

¹ Refer to Appendix 1 for general definition of *hajah* and *darurah* from perspectives of the classical and contemporary scholars.

² Refer to paragraph 8.1 for definition of hardship.

³ For example, in the context of Islamic finance, flexibility permitted by Shariah may be used to prevent failure of an IFI which causes systemic impact to the financial system.

⁴ Examples of the Shariah rulings, among others are as follows:

- (a) the permissibility for a licensed takaful operator to cede out its risk to a licensed insurer or a professional reinsurer in the absence of the capacity or expertise of a licensed takaful operator or a professional retakaful operator to underwrite a takaful risk;
- (b) the application of *bai' istijrar* (supply sale) for Islamic trade finance; and
- (c) the permissibility to benchmark interest rate in the pricing component of Islamic financial products.

⁵ The Shariah rulings focus on main principles without outlining the detailed processes, where some would be supported with requirements and guidance in relevant policy documents. For instance, the SAC ruling on the application of *hajah* with regard to the ceding out of takaful risk to a licensed insurer or professional reinsurer is supplemented with relevant policy expectation in the policy document on *Takaful Operational Framework*, but it does not comprehensively cover additional operational guidance as outlined in this policy document.

⁶ Refer to paragraphs 9.2, 9.4 and 9.6 for the categorisation of *hajah* and *darurah*.

- (c) outline the operational requirements and guidance in facilitating Shariah deliberation and decision-making on the application of *hajah* and *darurah*.
- 1.5 Given the specific nature of *hajah* and *darurah*, the Bank expects all governance organs in IFIs to play their role in supporting effective implementation of *hajah* and *darurah* by ensuring–
- (a) a comprehensive assessment is being carried out and supported with clear justifications and business impact analysis;
 - (b) robust deliberation and informed decision-making are performed by the Shariah committee; and
 - (c) appropriate ex-ante and ex-post assessment as well as review are performed by the control functions to serve as a check and balance to the implementation of the Shariah rulings and decisions or advice of the Shariah committee.

Overview of *hajah* and *darurah*

- 1.6 *Hajah* and *darurah* have been widely discussed by the classical and contemporary Shariah scholars. However, these discussions mostly focus on the hardships experienced by a person aiming to preserve life in mild and severe hardship situations. Both concepts have generally been divided into the following two (2) broad categories:
- (a) *usuliyyah*⁷; and
 - (b) *fiqhiyyah*⁸.
- 1.7 This policy document introduces *hajah* type 1, *hajah* type 2⁹ and *darurah* under the *fiqhiyyah* perspective in its efforts to ensure relevancy and rigour of the application of *hajah* and *darurah* by the IFIs.
- 1.8 The application of *hajah* and *darurah* under *usuliyyah* perspective is permitted¹⁰ and not subject to the requirements in this policy document. Such application is allowed permanently by Shariah to address public needs¹¹ and therefore, the permissibility does not require further deduction¹² by the Shariah committee and the SAC. For instance, the permissibility of the application of *ijarah* (lease) and *salam* (forward sale).

2 Applicability

- 2.1 This policy document is applicable to IFIs as defined in paragraph 5.2.

⁷ *Usuliyyah* means a circumstance faced by a scholar where there is an established Shariah principle on the application of *hajah* and *darurah* and it has been allowed permanently by Shariah.

⁸ *Fiqhiyyah* means a circumstance faced by a scholar where it requires a new deduction of a Shariah requirement on the application of *hajah* and *darurah*, and its permissibility of the period and quantum will be determined based on the severity of hardships faced by the people.

⁹ Refer to paragraphs 9.2 and 9.4 for the parameters of *hajah* type 1 and *hajah* type 2.

¹⁰ The permissibility has been allowed through the Bank's policy documents on relevant Shariah standards and issuance of the SAC meeting statement on Shariah rulings.

¹¹ May not only be confined to the needs related to Islamic finance sector.

¹² The Shariah evidence for *hajah usuliyyah* and *darurah usuliyyah* have been used as basis to deduce the Shariah legal judgement (*hukm shar'ie*) from *fiqhiyyah* perspective.

- 2.2 The Bank retains its discretion in assessing whether an IFI is in compliance with the policy document to the satisfaction of the Bank.

3 Legal provisions

- 3.1 The requirements in Part B of this policy document are specified pursuant to–
- (a) sections 29(1) and 155 of the Islamic Financial Services Act 2013 (IFSA); and
 - (b) sections 33E(1) and 116 of the Development Financial Institutions Act 2002 (DFIA).
- 3.2 The requirements in Part C of this policy document are specified pursuant to–
- (a) sections 29(2), 57(1) and 155 of the IFSA; and
 - (b) sections 33E(2), 41 and 116 of the DFIA.
- 3.3 The guidance in this policy document is issued pursuant to section 277 of the IFSA and section 126 of the DFIA.

4 Effective date

- 4.1 This policy document comes into effect six (6) months after its date of issuance.

Consultation 1:

- (a) Please describe any challenges in implementing the parameters and requirements of this framework within the allocated timeframe, taking into considerations views/feedback from other relevant parties beyond the Shariah department/unit; and
- (b) Please provide feedback on whether the duration provided is reasonable for IFIs to reach full compliance with the requirements of this framework.

5 Interpretation

- 5.1 The terms and expressions used in this policy document shall have the same meanings assigned to them in the Financial Services Act 2013 (FSA), IFSA and DFIA, as the case may be, unless otherwise defined in this policy document.
- 5.2 For purposes of this policy document–
- “S” denotes a standard, an obligation, a requirement, specification, direction, condition and any interpretative, supplemental and transitional provisions that shall be complied with. Non-compliance may result in enforcement action;
- “G” denotes guidance which may consist of statements or information intended to promote common understanding and advice or recommendations that are encouraged to be adopted;

“Islamic financial institutions” (IFIs) refer to—

- (a) licensed Islamic banks;
- (b) licensed takaful operators including professional retakaful operators;
- (c) licensed banks and licensed investment banks approved under section 15(1)(a) of the FSA to carry on Islamic banking business; and
- (d) prescribed development financial institutions approved under section 33B(1) of the DFIA to carry on Islamic financial business;

“hajah” refers to specific categories of *hajah* type 1 and *hajah* type 2 parameters in the context of Islamic finance application which can be referred in paragraphs 9.2 and 9.4;

“Shariah requirement” or **“Shariah principle”** refers to any existing ruling specified under the sources of Islamic laws, or any legal judgement (*hukm shar'ie*) deduced by a qualified jurist (a *mujtahid*) via the *ijtihad* process; and

“Shariah ruling” refers to any ruling made by the SAC in accordance with its functions under section 52(1)(a) of the Central Bank of Malaysia Act 2009 for the ascertainment of Islamic law for the purposes of Islamic financial business, or any published SAC resolutions.

6 Related legal instruments and policy documents

6.1 This policy document shall be read together with—

- (a) other relevant legal instruments and policy documents that have been issued by the Bank, in particular—
 - (i) *Corporate Governance* issued on 3 August 2016;
 - (ii) *Corporate Governance for Prescribed Development Financial Institutions* issued on 13 December 2019;
 - (iii) *Shariah Governance* issued on 20 September 2019;
 - (iv) *Fit and Proper Criteria* issued on 28 June 2013;
 - (v) *Fit and Proper Criteria* (for prescribed development financial institutions) issued on 14 June 2017;
 - (vi) *Recovery Planning* issued on 27 July 2021;
 - (vii) *Stress Testing* issued on 15 June 2017;
 - (viii) *Risk Governance* issued on 1 March 2013;
 - (ix) *Takaful Operational Framework* issued on 26 June 2019; and
- (b) *Manual Rujukan Institusi Kewangan Islam kepada Majlis Penasihat Shariah* issued on 15 March 2016.

PART B SHARIAH REQUIREMENTS FOR *HAJAH* AND *DARURAH* APPLICATION

7 Compliance with this part

- S** 7.1 An IFI that applies *hajah* or *darurah* shall ensure that such application is in compliance with Part B of this policy document.

8 Aspects of hardship

Definition of hardship

- G** 8.1 Hardship is a situation of unfavourable circumstances, severe adversity or intolerable levels of distress, arising from internal or external factors that require a person to pivot to a different solution(s) which may permit an exception in applying existing Shariah requirements or Shariah rulings based on the following Islamic legal maxims:
- (a) hardship begets flexibility¹³;
 - (b) harm must be removed¹⁴;
 - (c) extreme necessity lifts prohibitions¹⁵;
 - (d) the greater harm is to be removed or replaced by the lesser harm¹⁶; and
 - (e) when a matter is constricted/constrained (by the hardship), flexibility is accorded but when the hardship is addressed, the flexibility is rescinded¹⁷.

Consultation 2:

Please provide feedback on the explanation of hardship in paragraph 8.1, whether it has covered the **general** definition of hardship for the purpose of this ED.

- G** 8.2 Generally, if the hardship is not addressed, it may detrimentally affect the five (5) main objectives of Shariah (*maqasid* Shariah) which are the preservation of religion, life, intellect, lineage and wealth (property). In the context of *fiqh muamalat* or Islamic finance, the hardship experienced by a person predominantly involves Shariah rulings aiming at preserving wealth (*hifz al-mal*) (as provided in **Illustration 1**).

¹³ "المشقة تجلب التيسير" Al-Suyuti, *Al-Ashbah wa Al-Naza'ir, Dar Al-Kutub Al-'Ilmiyyah*, 1983, p. 76.

¹⁴ "الضرر يزال" Ibid, p. 83.

¹⁵ "الضرورات تبيح المحظورات" Ibnu Nujaim, *Al-Ashbah wa Al-Naza'ir, Dar Al-Kutub Al-'Ilmiyyah*, 1999, p. 73.

¹⁶ "يزال الضرر الأشد بالضرر الأخف" Muhammad Al-Zuhaili, *Al-Qawaid Al-Feqhiyyah wa Tatbiqatuha fi Al-Mazahib Al-Arba'ah, Dar Al-Fikr Dimasq*, 2006, v. 1 p. 219.

¹⁷ "إذا ضاق الأمر اتسع وإذا اتسع ضاق" Ibid, v. 1 p. 272.

Illustration 1

As part of a general takaful operator's risk management strategy, it may decide to share/cede out certain specialised risks such as aviation and oil and gas covers to another takaful or retakaful operator in managing its risk exposure. However, in cases where there is insufficient retakaful capacity and expertise to fully absorb the particular risk and/or it creates detrimental effects to the takaful funds, the takaful operator is allowed to cede out the risks to an insurer or a reinsurer on the basis of difficulty/hardship. This would ensure preservation of the takaful fund managed by the general takaful operator.

Consultation 3:

The ED views that the scope of objective of Shariah (*maqasid Shariah*) in the context of Islamic finance predominantly involves preservation of wealth.

- (a) Please provide real example(s) based on the Shariah committee's decision where preservation of wealth has been considered and applied, if any.
- (b) Please provide real example(s) based on the Shariah committee's decision where preservation of religion, life, intellect and lineage has been considered and applied, if any.

Preconditions in applying *hajah* or *darurah*

- S** 8.3 An IFI shall ensure that the following preconditions are fulfilled in evaluating the application of *hajah* or *darurah* to address hardship:
- (a) **Certainty** – There is certainty (*al-yaqin*) or high possibility (*ghalib al-zann*)¹⁸ on the materialisation or occurrence of hardship, and it is not based on mere assumption;
 - (b) **Deviation from Shariah requirement or Shariah ruling** – The elimination of hardship requires deviation from existing Shariah requirements or Shariah rulings to an exceptional rule whether temporarily or permanently;
 - (c) **Absence or impracticality of Shariah compliant alternatives** – There is an absence of a Shariah compliant alternative, or there is an available Shariah compliant alternative to address the hardship but the latter is unfeasible given the prevailing situation(s); and
 - (d) **Impact** – The application of exceptional rules does not cause greater or equal harm to stakeholders related to the hardship, and the impact shall be assessed based on the *fiqh muwazana*¹⁹.

¹⁸ Certainty (*al-yaqin*) can be achieved based on undisputable evidences and high possibility (*ghalib al-zann*) can be achieved with clear leading of signs and indicators but with insignificant dispute.

¹⁹ *Fiqh muwazana* is a structured method and processes applied by jurist in making Shariah decision through weighing up between multiple benefits (to attain), harms (to avoid), and/or to determine which between the two (2) shall prevail and be prioritised.

- S** 8.4 An IFI is prohibited from applying *hajah* or *darurah* to address hardships solely arising from commercial or business challenges²⁰.

Consultation 4:

Please provide feedback on the proposed preconditions, including suggestions to exclude any of the proposed preconditions or include additional precondition(s).

- G** 8.5 In relation to paragraph 8.3, the following method may be adopted by an IFI in applying the exceptional rule in accordance with the severity of the hardship:
- (a) **Reducing obligation** – compliance with Shariah is achieved by reducing the appropriate level of a person's capability, e.g., in ensuring the sustainability of a takaful fund particularly to prevent the situation of fund deficit which requires continuous *qard*, a licensed takaful operator may be allowed to cede out a certain percentage of its takaful risk to reinsurers instead of fully retaining the risk; or
 - (b) **Exemption/exception** – allow the utilisation or adoption of transactions that are not in compliance with Shariah in view of the absence of a Shariah compliant alternative for such transactions or widespread public needs, e.g., subscription to insurance protection in the absence of takaful protection for a particular risk or application of T+2 in the foreign currency exchange (*bai' al-sarf*) in the absence of spot exchange practices.

9 *Hajah* and *darurah* parameters

Application of exceptional rules

- G** 9.1 Exceptional rules that may be applied by an IFI can be divided into the following categories:
- (a) *hajah* type 1;
 - (b) *hajah* type 2; or
 - (c) *darurah*.

Hajah Type 1

- S** 9.2 In addition to paragraph 8.3, an IFI shall categorise any hardship under *hajah* type 1 if it meets the following parameters:
- (a) the hardship arises due to practices or situations which are difficult to avoid (*'umum balwa*) or are widely accepted as a customary commercial practice (*'urf tijari*);
 - (b) the SAC has issued a ruling on the permissibility of the application of an exceptional rule without stipulating specific conditions or limitations; and
 - (c) the Shariah ruling remains applicable until a new pronouncement is made by the SAC.

²⁰ For examples, losing profit commission from ceding out arrangement, hardship resulted from poor risk management control, business decision or negligence by the IFI or financial loss arising from the effort to rectify the Shariah non-compliance. These examples are non-exhaustive and should not be construed as the only examples available.

- G** 9.3 The examples in **Illustration 2** describe the application of *hajah* type 1.

Illustration 2

(a) Permissibility of T+2 for foreign currency exchange (bai` al-sarf)

The Shariah principle for foreign currency exchange (bai` al-sarf) transaction requires contracting parties to conclude their transaction on a spot basis (T+0). However, in the context of the current financial system, the conclusion of a contract or settlement could not be done on a spot basis due to difficulties and operational constraints. Therefore, the SAC has allowed the settlement to be done in two (2) days (T+2) after the transaction date as it has been accepted and recognised as a customary commercial practice.

(b) Use of a conventional nostro account

An Islamic window operation operates its Islamic banking business by sharing relevant services with its conventional counterpart. In the event where it needs to perform international trade or foreign exchange transactions, the Islamic window uses a conventional nostro account. This is due to the following:

- (i) lack of Shariah compliant nostro accounts available in other jurisdictions;*
- (ii) policy mandate of the group risk management; and*
- (iii) ensuring transactional efficiency.*

Typically, nostro account balances earn zero or minimal returns. Therefore, an Islamic window is allowed to use the nostro account to address frictions in its transactions with international counterparts on need basis.

Hajah Type 2

- S** 9.4 In addition to paragraph 8.3, an IFI shall categorise any hardship under *hajah* type 2 if it meets the following parameters:
- (a) the hardship does not arise from practices or situations which are widely accepted as customary commercial practice (*`urf tijari*);
 - (b) the hardship is experienced by a specific person(s) and the severity of the hardship does not reach the stage of *darurah*;
 - (c) the SAC has ruled the permissibility of the application of an exceptional rule with specific conditions or limitations; and
 - (d) the Shariah ruling needs to be applied temporarily and proportionately depending on the complexity of the hardship by considering the appropriate duration and quantum²¹.

²¹ This is based on Islamic legal maxim: "الضرورة تقدر بقدرها" (Necessity is to be assessed and treated proportionally), Ibnu Nujaim, *Al-Ashbah wa Al-Naza'ir, Dar Al-Kutub Al-Ilmiyyah*, 1999, p. 73.

- G** 9.5 The examples in **Illustration 3** describe the application of *hajah* type 2.

Illustration 3

(a) Insurance coverage for Islamic financing

In a wakalah financing deal, an IFI has appointed a client as its agent (wakeel) to source for a takaful coverage to mitigate oil and gas risk. The client has exhausted all reasonable endeavours to source for a takaful coverage, in fulfilling his duty as an agent. However, due to the huge coverage amount needed to mitigate the risk and limited accessibility due to location constraints i.e., such oil and gas businesses located outside Malaysia, the client faces difficulty in getting takaful protection for the project. Hence, the IFI as principal (muwakkil) has allowed the client to obtain insurance coverage to fulfil the project financing requirements.

(b) Liquidity risk management

A full-fledged licensed Islamic bank has been receiving huge capital support to develop its Islamic banking business, and it has translated into better capital and asset position for the Islamic banking business. However, during a financial crisis or stress event, its banking group is in needs of financial assistance. The licensed Islamic bank, as an entity within the group, can be well positioned to provide financial assistance such as transferring its funds or excess high quality liquid assets (HQLA) to the group²². The assistance provided is important to avoid the contagion risk to the licensed Islamic bank should the stress scenario become more serious and severe to the detriment of the group. This takes into account interdependencies on critical shared services, access to financial market infrastructures as well as the reputation of its conventional parent bank to obtain funding and carry out banking business.

(c) Financing Shariah non-compliant business by a prescribed institution

A prescribed institution performs its role based on mandates determined by the Government. For a full-fledged Islamic prescribed institution, the institution should not perform any Shariah non-compliant transaction or dealing such as financing non-halal food industry. However, in the event where there is no other commercial banking institution or full-fledged prescribed institution that could provide the financing and the

²² The IFI funding shall be the last resort arrangement i.e., the banking group must first exhaust the funding available at its conventional counterpart or its parent before soliciting funding from the IFI.

financing has been mandated by the Government, the full-fledged Islamic prescribed institution shall need to deliberate the issue with its Shariah committee and the SAC prior to executing the non-Shariah compliant transaction.

Darurah

- S** 9.6 In addition to paragraph 8.3, an IFI shall categorise any hardship under *darurah* if it meets the following parameters:
- (a) the hardship does not arise from practices or situations which are widely accepted as customary commercial practice (*`urf tijari*);
 - (b) the hardship experienced by a specific person(s) may or may not cause systemic impact, but trigger recovery or resolution actions²³;
 - (c) the hardship has yet to be deliberated by the SAC, or there is a need to revisit the Shariah ruling in light of the extreme stress situation; and
 - (d) the Shariah ruling needs to be applied temporarily and proportionately based on the complexity of the hardship by considering the appropriate duration and quantum²⁴.
- G** 9.7 The example in **Illustration 4** describes the application of *darurah*.

Illustration 4

An IFI has been identified to undergo a resolution phase by a resolution authority (RA). During that phase, the RA has exhausted all possible funding options in the resolution actions to avoid systemic risk to the financial industry. However, additional funding is still required, and the only possible solution to address the issue is to obtain funding from an international body – which can only be offered through a conventional loan arrangement. In this situation, the RA may execute the only possible solution due to the extreme necessity of the situation.

- G** 9.8 The hardship situations which warrant for the categories of exceptional rules in paragraph 9.1 are not fixed and they may change depending on the nature and severity of hardship as stated in the *fiqh* legal maxim “a necessity possibly falls under the category of extreme necessity whether it is in the general or specific form²⁵”. For instance, any of the Shariah rulings which are considered as *hajah* type 1 may be changed to *hajah* type 2 in the event where the hardship is no longer considered a customary commercial practice (*`urf tijari*) of the Islamic finance industry, and vice versa.

²³ Refer to policy document on *Recovery Planning*.

²⁴ This is based on Islamic legal maxim: "الضرورة تقدر بقدرها" (Necessity is to be assessed and treated proportionally), Ibnu Nujaim, *Al-Ashbah wa Al-Naza'ir, Dar Al-Kutub Al-Ilmiyyah*, 1999, p. 73.

²⁵ "الحاجة تنزل منزلة الضرورة عامة كانت أو خاصة" Muhammad Al-Zuhaili, *Al-Qawaid Al-Feqhiyyah wa Tatbiqatuha fi Al-Mazahib Al-Arba'ah, Dar Al-Fikr Dimasq*, 2006, v. 1 p. 288.

- S** 9.9 In line with paragraph 10.6 of the policy document on *Shariah Governance*, an IFI shall refer to the SAC for a ruling in the case of any hardship with no prior Shariah rulings that warrants the application of *hajah* type 2 and *darurah*.

Consultation 5:

- (a) Please provide feedback on each proposed parameter of *hajah* type 1, *hajah* type 2 and *darurah*, including suggestions on excluding any of the proposed parameters or incorporating a new additional parameter(s).
- (b) Please share some real examples or situations which may be categorised as *hajah* type 1, *hajah* type 2 or *darurah*.

PART C OPERATIONAL REQUIREMENTS

10 Compliance with this part

- S** 10.1 Part C of this policy document shall be applicable to the hardship that meets the parameters of *hajah* type 2 or *darurah* as described in paragraphs 9.4 and 9.6 respectively.

11 Governance and oversight

- G** 11.1 The requirements under Part C focus on the roles and responsibilities of key organs of the IFIs to promote effective governance arrangements and sound Shariah compliance culture within the IFIs, guided by the intended outcomes of this policy document. It complements the existing policy documents issued by the Bank which promote the long-term safety and soundness of the IFIs.
- G** 11.2 Given the specific nature of the application of *hajah* type 2 and *darurah*, the Bank expects heightened oversight and strengthened responsibilities of every key organ of the IFI to ensure rigorous assessment, deliberation, implementation and monitoring.

The board

- S** 11.3 The board, in overseeing the application of *hajah* type 2 and *darurah* within the IFI, shall have the overall responsibility to ensure establishment and operation of a clear governance structure to facilitate effective implementation of *hajah* type 2 and *darurah* that reflects the importance of strategy formulation and risk management practices and promotes end-to-end compliance with Shariah. In doing so, the board shall–
- (a) oversee the implementation of the decisions and advice of the Shariah committee and ensure that appropriate internal controls are in place;
 - (b) approve internal policies and procedures relating to the decision-making process on *hajah* type 2 and *darurah*, including policies on dissemination of decisions or advice of the Shariah committee as well as their implementation monitoring;
 - (c) provide sound and substantiated views, with due regard to the decisions or advice of the Shariah committee, on the existence of hardship and necessity of *hajah* type 2 and *darurah*; and
 - (d) constructively challenge proposal by the IFI on the application of *hajah* type 2 and *darurah*, including providing inputs on the adequacy of plausible scenarios, stress testing results, and key assumptions used in justifying the application of *hajah* type 2 and *darurah*, and give due consideration to the applicable duration and exit strategy.

Shariah committee

- S** 11.4 The Shariah committee, in providing objective and sound decision or advice to the IFI on the application of *hajah* type 2 and *darurah*, shall–
- (a) ensure that assessment on the proposed application of *hajah* type 2 and *darurah* by the IFI are in compliance with the parameters requirements as specified in paragraphs 8.3, 8.4, 9.4 and 9.6 of this policy document;
 - (b) ensure rigour in deliberating *hajah* type 2 and *darurah* cases, highlight any significant concerns and dissenting views, and provide proper justifications for any decision or advice; and
 - (c) satisfy that all possible efforts which have been demonstrated by the IFI prior to applying *hajah* type 2 and *darurah* could not address the particular hardship in line with the established internal policy on *hajah* type 2 and *darurah*.
- S** 11.5 An IFI shall ensure that deliberations relating to the application of *hajah* type 2 and *darurah* are carried out by ascertaining views and insights from all Shariah committee members, except under exceptional circumstances²⁶.
- S** 11.6 In relation to paragraph 11.5, an IFI shall ensure that views of the Shariah committee members who are not in attendance are obtained in writing.
- S** 11.7 In line with paragraph 11.8 of the policy document on *Shariah Governance*, an IFI shall, at minimum, ensure that any decision of the Shariah committee is made on the basis of simple majority.
- S** 11.8 In line with paragraph 11.14 of the policy document on *Shariah Governance* on the responsibility of the IFI to ensure clear and accurate minutes of Shariah committee meetings, the Shariah committee shall ensure that the minutes prepared relating to the proposed application of *hajah* type 2 and *darurah* are accurate, comprehensive and clear. In this regard, the Shariah committee has the responsibility to ensure the deliberations, considerations and justifications on the decision or advice, including assessment on the relevant parameters provided in this policy document for allowing the application of *hajah* type 2 and *darurah*, as well as any significant concerns and dissenting views are reflected appropriately.
- S** 11.9 Where the Shariah committee is unable to finalise its decision or has reasonable doubt on the robustness of *hajah* type 2 and *darurah* assessment performed by an IFI, as provided in paragraph 11.11 of the policy document on *Shariah Governance*, the IFI shall provide the Shariah committee with access to the advice from third party experts to enable the Shariah committee to make an informed decision.

²⁶ This would include instances due to medical reasons.

Senior management

- S** 11.10 In discharging the primary responsibility over the day-to-day management of the IFI on the application of *hajah* type 2 and *darurah*, the senior management shall–
- (a) ensure that the differences in the application of *hajah* type 2 and *darurah* (against normal operating environment) are properly understood and reflected effectively in its policies, processes and practices. This includes putting in place a robust communication plan on *hajah* type 2 and *darurah*;
 - (b) implement effective policies and procedures for the application of *hajah* type 2 and *darurah* based on the rulings of the SAC and the decision or advice of the Shariah committee;
 - (c) provide balanced assessment and opinion to the Shariah committee, supported with the relevant information during the identification and assessment stage as outlined in paragraphs 12.4 to 12.11 of this policy document; and
 - (d) ensure a robust internal control framework is in place to effectively monitor the application of *hajah* type 2 and *darurah* by the IFI.

Control functions

- S** 11.11 An IFI shall ensure the effectiveness and independence of control functions²⁷ in reviewing and monitoring the application of *hajah* type 2 and *darurah* implemented by the business organs as described in paragraph 12.19. This includes assessment on areas for improvements that can prevent an IFI from resorting to apply *hajah* type 2 and *darurah* continuously.

Consultation 6:

Please provide feedback on whether the proposed requirements on the responsibility of the key organs are appropriate, considering the specific nature of the application of *hajah* type 2 and *darurah* and the existing duties of these organs.

12 Decision-making process

- S** 12.1 An IFI shall establish a comprehensive internal policy and procedure on the application of *hajah* type 2 and *darurah*, to facilitate a more structured approach of decision-making by the Shariah committee and ensure effective implementation by the IFI.
- S** 12.2 An IFI shall ensure that the internal policy and procedure relating to the decision-making process on the application of *hajah* type 2 and *darurah* to include the following:
- (a) identification of the scope of hardship;
 - (b) assessment on the severity of the hardship and categorisation as described in paragraphs 9.4 and 9.6, as well as its impact on financial position and operations of the IFI;
 - (c) robust and objective deliberation of possible solutions by the Shariah committee and the board; and

²⁷ Roles and responsibilities of respective control functions (i.e., Shariah risk management, Shariah review and Shariah audit) as outlined in the policy document on *Shariah Governance*.

- (d) monitoring of *hajah* type 2 and *darurah* implementation by the appropriate control functions, as well as reporting to the Bank in line with paragraphs 12.13 to 12.18 of this policy document as and when *hajah* type 2 and *darurah* are being applied.

- S** 12.3 In the event where an extended period is needed for the application of *hajah* type 2 and *darurah*, an IFI is required to comply with the decision-making process requirements as described in paragraphs 12.4 to 12.18 and provide compelling justifications on the need for such extension and a feasible exit plan for deliberations by the Shariah committee and the board.

Consultation 7:

Please describe any instances or situations supported by a clear rationale where the period to apply *hajah* type 2 or *darurah* could be extended or prolonged.

Identification

- S** 12.4 In relation to paragraphs 8.1 and 8.3(a) to 8.3(c), an IFI shall prepare a comprehensive narrative of the hardship experienced by its stakeholders by gathering information on:
 - (a) the nature of the hardship; and
 - (b) the efforts performed by the IFI in complying with Shariah prior to proposing for the application of *hajah* type 2 and *darurah*, as well as the outcome of its efforts.
- G** 12.5 In relation to paragraph 12.4(a), the comprehensive narrative on the nature of the hardship may include but not limited to the following perspectives:
 - (a) institutional – issues that may affect operational resiliency of the institution;
 - (b) legal and regulatory – issues that may affect the effectiveness of regulations in achieving policy objectives;
 - (c) macroeconomic – a condition that stems from, or relates to, a large aspect of an economy;
 - (d) customer – issues that may deteriorate customers' experience or cause inability to meet customers' needs and expectations; and
 - (e) external event – incidents outside the control of the institution.

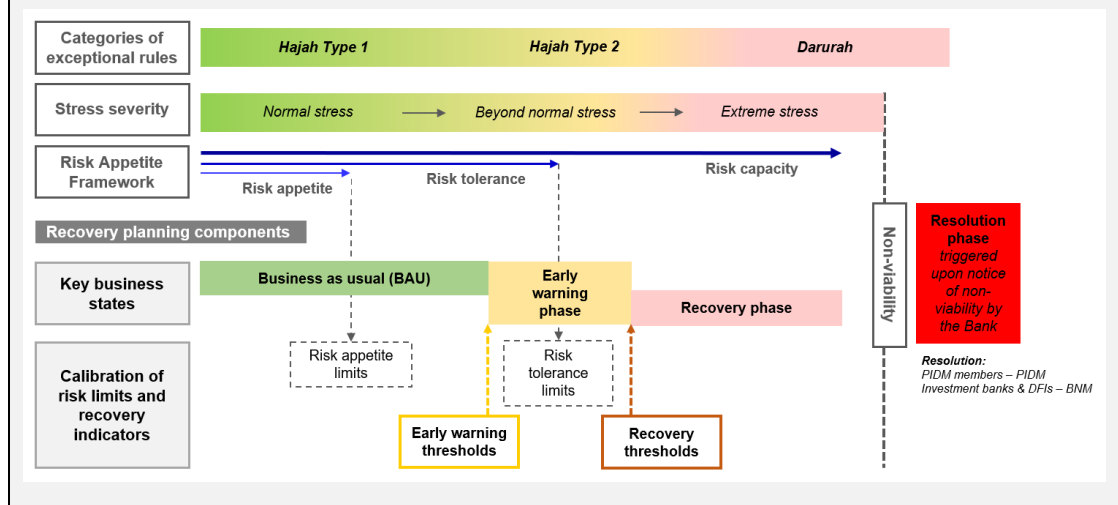
Assessment

- S** 12.6 An IFI shall demonstrate the severity of the hardship(s) based on its internal parameters taking into consideration the requirements and guidance set out by the Bank in this policy document and shall support the severity analysis by covering both qualitative and quantitative aspects.
- S** 12.7 Notwithstanding paragraph 12.6, in the case where there is difficulty in assessing the quantitative aspect of the severity, the IFI shall ensure that the absence of quantitative assessment is supported with compelling justifications.
- G** 12.8 In determining the certainty and severity of hardship in relation to paragraphs 8.3(a) to 8.3(c) as well as its categorisation in relation to paragraphs 9.2 to 9.7, an IFI may assess the certainty of the occurrence and adversity of the hardship situation based on its existing overall risk appetite framework, stress severity

analysis or recovery planning components (as described in **Illustration 5**) or any relevant data that could provide a comprehensive perspective on the accurate level of hardship experienced by the IFI. Such integration in the assessment process is essential for timely identification of stress events and the formulation of actionable and credible options to ensure the IFI is well positioned to respond to viability threats, regardless of their origins.

Illustration 5

Integration between assessment on certainty and adversity of hardship in the application of hajah type 2 and darurah level into stress severity analysis, risk appetite framework and recovery planning components of the IFI.



- G 12.9** In relation to paragraphs 8.3(d) and 12.6, a comprehensive assessment to support the severity analysis and impact on internal and external stakeholders may include the following:
- impact on customers and relevant stakeholders (e.g., counterparties related to main customers, service providers, suppliers, market utilities, public services, government) which stems from Shariah requirements, taking into account–
 - the impact and speed of disruption to financial health, customers, businesses, and short-term liquidity needs of customers and relevant stakeholders; and
 - the capacity or speed of reaction to the disruption by counterparties, customers and the public;
 - impact on other financial institutions and financial markets, taking into account the magnitude and speed at which such disruption would materially affect market participants or market functioning (e.g., liquidity, operations and structure of other financial institutions, financial markets concerned);
 - impact on economy, taking into account the lack of financial resources for an IFI to continue its operations as its customers or other stakeholders become negatively affected, both directly and indirectly e.g., defaults which may cause further financial repercussions; and

- (d) impact on environment, social and infrastructure, taking into account the non-availability of Shariah compliant options to fulfil societal and environmental needs.

- S** 12.10 An IFI shall develop proposed solutions supported with comprehensive assessment, consisting of options available in dealing with hardship circumstances, facts and rationale, Shariah justifications, impact assessment and assumption, unintended consequences, applicable duration, mitigation measures and exit strategy for each proposed solution²⁸.
- S** 12.11 In relation to paragraph 9.9, an IFI shall ensure that any reference for ruling of the SAC is supported with comprehensive assessment and proposed solutions as described in paragraphs 12.6, 12.7 and 12.10.

Deliberation

- S** 12.12 In reinforcing sound decision for the application of *hajah* type 2 and *darurah*, an IFI shall ensure completeness and robustness of the following:
 - (a) information provided in the identification and assessment steps as specified under paragraphs 8.3 and 12 of this policy document;
 - (b) deliberation of the Shariah committee and the board, particularly on the appropriateness of the proposed solutions and duration to address the risks and vulnerabilities identified in the *hajah* type 2 and *darurah* assessment as well as its exit strategy; and
 - (c) consistency in providing views on the application of the Shariah rulings.

Reporting

- S** 12.13 In the event where the Shariah committee decides that the hardship falls under the category of *hajah* type 2 and the board agrees with the proposal to pursue such application, an IFI shall notify the Bank of that fact and submit a report in line with paragraph 12.16 within 14 working days after such decision is being made.
- S** 12.14 In the event where the Shariah committee decides that the hardship falls under the category of *darurah* and the board agrees with the deliberations of the Shariah committee, an IFI shall refer to the SAC for a ruling and write to the Bank within 14 working days after such decision being made.
- G** 12.15 The SAC, with advice from the Bank or a resolution authority, will advise the IFI on the appropriate ruling and period for the application of *darurah*.
- S** 12.16 In relation to paragraphs 12.13 and 12.14, an IFI shall ensure that notification of *hajah* type 2 to the Bank to be submitted to Jabatan Penyeliaan Konglomerat Kewangan, Jabatan Penyeliaan Perbankan or Jabatan Penyeliaan Insurans dan Takaful, as the case may be, and shall submit reference for *darurah* application to the SAC²⁹ to Jabatan Sistem Kewangan Islam.

²⁸ For example, an IFI is expected to identify the profit/loss (such as profit commission on risk ceded to the reinsurers) which may arise in a situation where *hajah* is adopted and establish a proper treatment/plan to manage such profit/loss, for instance purifying the impermissible profit via charity.

²⁹ As per *Manual Rujukan Institusi Kewangan Islam kepada Majlis Penasihat Shariah*.

- S** 12.17 In relation to paragraph 12.16, an IFI shall ensure that submission to the Bank includes the following information:
- (a) detailed narrative and assessment as described in paragraphs 12.4 to 12.11;
 - (b) record of deliberations of the Shariah committee meeting(s), including resolutions, rationale and any significant concerns and dissenting views; and
 - (c) record of deliberations of the board.
- S** 12.18 An IFI shall report to the Shariah committee and the board on a timely basis the progress of the application of *hajah* type 2 and *darurah*, and its exit strategy.

Monitoring

- S** 12.19 An IFI shall perform periodic assessments on the compliance of the implementation of *hajah* type 2 and *darurah* with the rulings of the SAC and decision or advice of the Shariah committee with due regard by the board, as well as requirements set out by the Bank.

Consultation 8:

- (i) Please describe any challenges that you foresee in implementing the proposed requirements on the decision-making process.
- (ii) Given the specific nature of hardship of *hajah* type 2 and *darurah*, please provide feedback on whether the proposed reporting timeframe to the Bank is sufficient.
- (iii) Please provide any alternative proposals to ensure immediate reporting to the Bank, particularly in the case where the IFI is experiencing severe adversity.
- (iv) If the Bank wishes to impose that IFIs shall not apply the exceptional rule until the expiry of a certain period (e.g., 14 working days) from the submission of notification of *hajah* type 2 to the Bank, please provide views on the appropriate period to be imposed supported by clear rationale.

APPENDIX 1 DEFINITION OF *HAJAH* AND *DARURAH*

Definition

Classical scholars	
Hajah	<i>Hajah</i> consists of what is required by the people for the realisation of their interests and the proper execution of their affairs. The social order would not, in fact, collapse, but will not function properly, if it is ignored ³⁰ .
Darurah	A situation where one needs to consume forbidden items to prevent death or severe harm ³¹ .
Contemporary scholars	
Hajah	A situation where a need of a person or a community to be met by lifting the distress situation temporarily or permanently. If it is not addressed, it may reach the <i>darurah</i> (necessity) situation ³² .
Darurah	An extreme necessity that permits the forbidden except for what is excluded (such as murder and adultery). ³³ .

Shariah basis of *hajah* and *darurah*

The following verse of the *Quran* and the *Hadith* imply the general permissibility for application of *hajah*:

يُرِيدُ اللَّهُ بِكُمُ الْيُسْرَ وَلَا يُرِيدُ بِكُمُ الْعُسْرَ

Allah intends ease for you, not hardship.

(Surah Al-Baqarah, 2:185)

عن أنس رضي الله عنه قال: رخص رسول الله ﷺ للزبير وعبد الرحمن بن عوف رضي الله عنهما في لبس الحرير لحكة بهما. رواه البخاري ومسلم

Anas (may Allah be pleased with him) reported: The Messenger of Allah (peace and blessing of Allah be upon him) permitted Zubair and `Abdur-Rahman bin `Auf (may Allah be pleased with them) to wear silk because they were suffering from an itch.

³⁰ Al-Syatibi, *Al-Muwafaqat*, Dar Al-Kutub Al-`Ilmiyah, 2004.

أنها مفتقر إليها من حيث التوسعة ورفع الضيق المؤدي في الغالب إلى الحرج والمشقة اللاحقة لفوت المطلوب فإذا لم تراعى دخل على المكلفين - على الجملة - الحرج والمشقة ولكنه لا يبلغ مبلغ الفساد المتوقع في المصالح العامة.

³¹ Al-Suyuti, *Al-Ashbah wa Al-Nazair*, Dar Al-Kutub Al-`Ilmiyah, 1983.

فالضرورة: بلوغه حداً إن لم يتناول الممنوع هلك أو قارب، وهذا يبيح تناول الحرام

³² Ahmad Kafi, *Al-Hajah Al-Syar'iyyah Hududuha wa Qawaiduha*, Dar Al-Kutub Al-`Ilmiyah, 2004.

الحاجة هي ما يحتاجه الأفراد أو تحتاجه الأمة للتوسعة ورفع الضيق إما على جهة التأقيت أو التأييد، فإذا لم تراعى دخل على المكلفين - على الجملة - الحرج والمشقة وقد تبلغ مبلغ الفساد المتوقع في الضرورة.

³³ Abdullah bin Bayyah, *Sina`ah Al-Fatwa wa Feqh Al-Aqalliyat*, Al-Muwatta Center, 2018.

ضرورة قصوى تبيح المحرم سوى ما استثنى.

The following verse of the *Quran* and the *Hadith* imply the general permissibility for application of *darurah*:

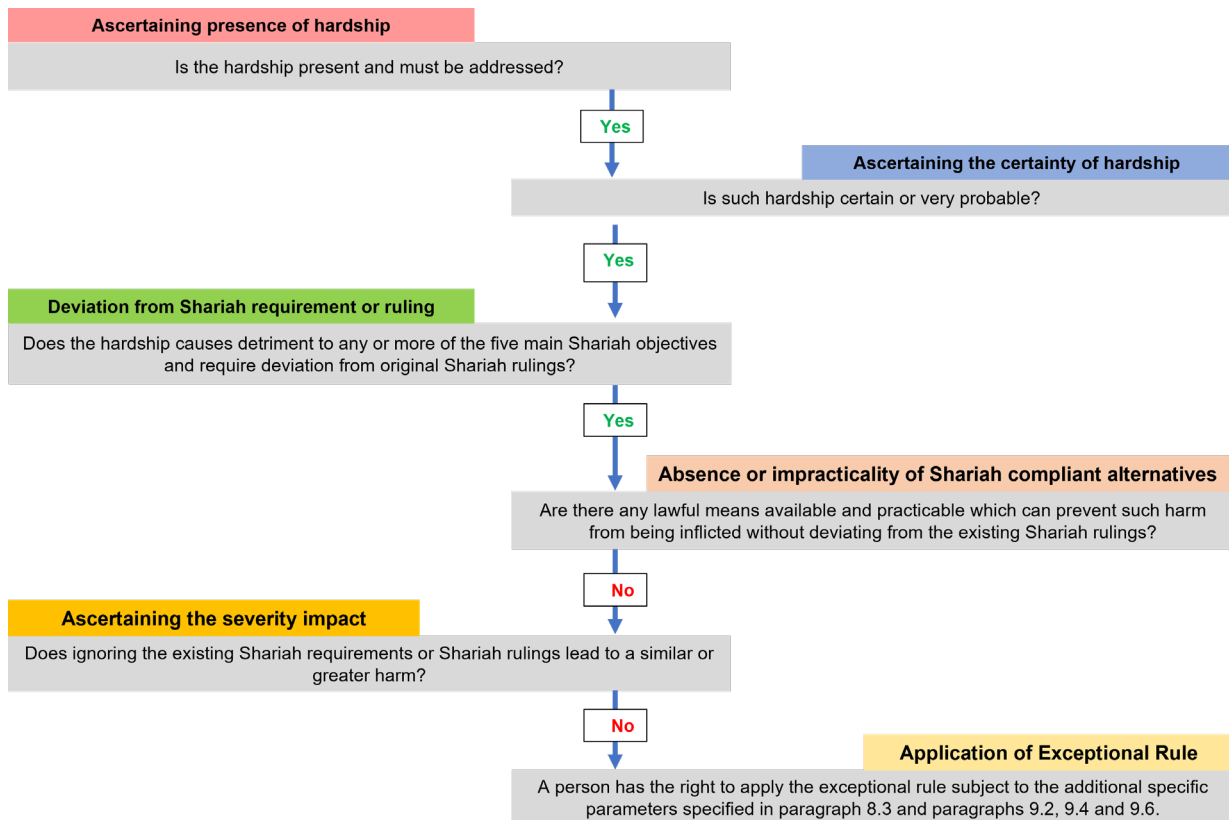
﴿فَمَنْ أَضْطَرَّ غَيْرَ بَاغٍ وَلَا عَادٍ فَلَا إِثْمَ عَلَيْهِ إِنَّ اللَّهَ غَفُورٌ رَحِيمٌ﴾ (173)

But whoever is forced [by necessity], neither desiring [it] nor transgressing [its limit], there is no sin upon him. Indeed, Allah is Forgiving and Merciful.
(Surah Al-Baqarah, 2:173)

عن أبي واقد الليثي قال: قلت: يا رسول الله، إنا بأرض تصيينا بها مخمصة، فما يحل لنا من الميتة؟ قال: (إذا لم تصطبحوها، ولم تغتبقوها، ولم تحتفتوا بقلها، فشأنكم بها) رواه أحمد وصححه الحاكم

Abu Waqid al-Laithi said, "Messenger of God, we live in a land where we are afflicted by hunger, so when may we eat animals which have died a natural death?" He replied: "As long as you do not have a morning drink or an evening drink or gather vegetables you may eat them."

APPENDIX 2 DECISION TREE IN APPLYING THE GENERAL PARAMETERS



APPENDIX 3 SUMMARY OF CRITERIA AND PARAMETERS IN DEALING WITH EXCEPTIONAL RULE

Types				
Parameters	Hajah Type 1	Hajah Type 2	Darurah	
1. Preconditions	<ul style="list-style-type: none">• Ensure certainty of the hardship• Deviation from Shariah requirements/ruling• Absence or impracticality of Shariah compliant alternatives• Does not cause greater or equal harm to stakeholders			
2. Specific parameters				
a) Nature of hardship	Difficult to avoid (<i>`umum balwa</i>) / customary commercial practice (<i>`urf tijari</i>)	Not a customary commercial practice (<i>`urf tijari</i>)		
b) Coverage of hardship	For general needs	For specific needs, but neither reach <i>hajah</i> type 1 nor <i>darurah</i>	For specific needs, may or may not cause systemic impact, but trigger recovery or resolutions actions	
c) Availability of ruling	There is Shariah ruling issued to all	There is Shariah ruling issued for specific institution application	Yet to be deliberated by the SAC or the Shariah ruling needs to be revisited in light of the extreme stress situation	
d) Time and quantum	Allowable (Until revision of rulings/policy)	Temporary and proportionately based on complexity of the issue		
Example	T+2 in currency exchange (<i>bai` al-sarf</i>), <i>nostro account</i>	Ceding out of <i>takaful</i> risk to reinsurance company	Loan from International Monetary Fund (IMF) during resolution	

APPENDIX 4 PROCESS FLOW IN APPLYING HAJAH AND DARURAH

