

ISTISNA' BASED PROTOCOL FOR SHARIAH COMPLIANCE CONTRACT FOR CONSTRUCTION WORKS

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PRODUCT
61

ABSTRACT

Construction is among the key sectors of an economy. Annually, billion ringgits worth of infrastructures were procured and completed, repaired or refurbished, and up to a million workers gained employment. Construction works are almost always performed by Contractors via complex contractual arrangements involving Employers and the other key players. In typical construction works, the two parties to a contract are the Employer and the Contractor. Their relationship is defined by the terms and conditions of the contract they signed, which is usually based on any one of the readily available standard forms of contract. Little is known whether these standard forms of contracts have, within their terms and conditions, provisions that comply with the Shariah. Under the Shariah the commonly accepted contract involving a subject matter that is yet to exist is *Istisna'*. However, *Istisna'* is widely used by Islamic Financial Institutions as a Shariah compliance financing tool instead of it being used as a primary contract between the Employer and the Contractor. In an endeavor to promote Shariah-compliant in construction contracts an intensive desk research and focus group discussions was carried out, its key objectives were to (i) identify key *Istisna'* principles related to the practice of contracting for construction works; (ii) harmonize the key *Istisna'* principles with the terms and conditions of the standard forms of contract; and (iii) based on the *Istisna'* to develop a protocol for a Shariah compliance contract for construction works. The research findings include (i) identification of the key principles of the *Istisna'* that binds a contract between the Employer and the Contractor: the nature, quality, quantity, and the description of the infrastructure to be built is known, and a time is fixed for constructing the infrastructure; (ii) in the current contract practice bills of quantities (BQs), drawings and specifications are used but their use is not always mandatory, and the start and completion dates of the works are expressly defined; (iii) it is considered apt to harmonize the identified key *Istisna'* principles with the terms and conditions of the standard forms of contract and therefore, firm contract sum and BQs, complete drawings and specifications are to be made mandatory, and time frame for the contract is fixed at the time of contracting. The harmonizing effort transformed the the current practice towards Shariah-compliant, and (iv) an *Istisna'* based protocol for Shariah compliance contract for construction works was developed. The significance of the research and its findings may be viewed as follows: (i) a pioneering effort and a paradigm shift in the practice of contracting in the construction industry i.e. a move towards Shariah-compliant; (ii) contributing to *Maqasidal al-Shariah* in the areas of *al-Din*, *nafs*, *aql*' and *mal*; and (iii) the protocol serves as guide in the application of Shariah compliance construction contract for the construction industry.

PRODUCT DESCRIPTION/ INNOVATION IN BRIEF

The product is in the form of a protocol for an *Istisna'* based Shariah compliance contract for construction works. The protocol is intended for Employers and Contractors wishing to have their contract performed in accordance with the Shariah. The protocol comprises of the following:

1. A conceptual model of an *Istisna'* based direct contract for construction works between the Employer and the Contractor. Refer to Diagram 1.
2. A set of 5 (five) documents and their pre-requisites for the purpose of forming a valid *Istisna'* based contract. Refer to Diagram 2 for the list of documents and the pre-requisites.



Diagram 1. Parties to an *Istisna'* contract for construction works

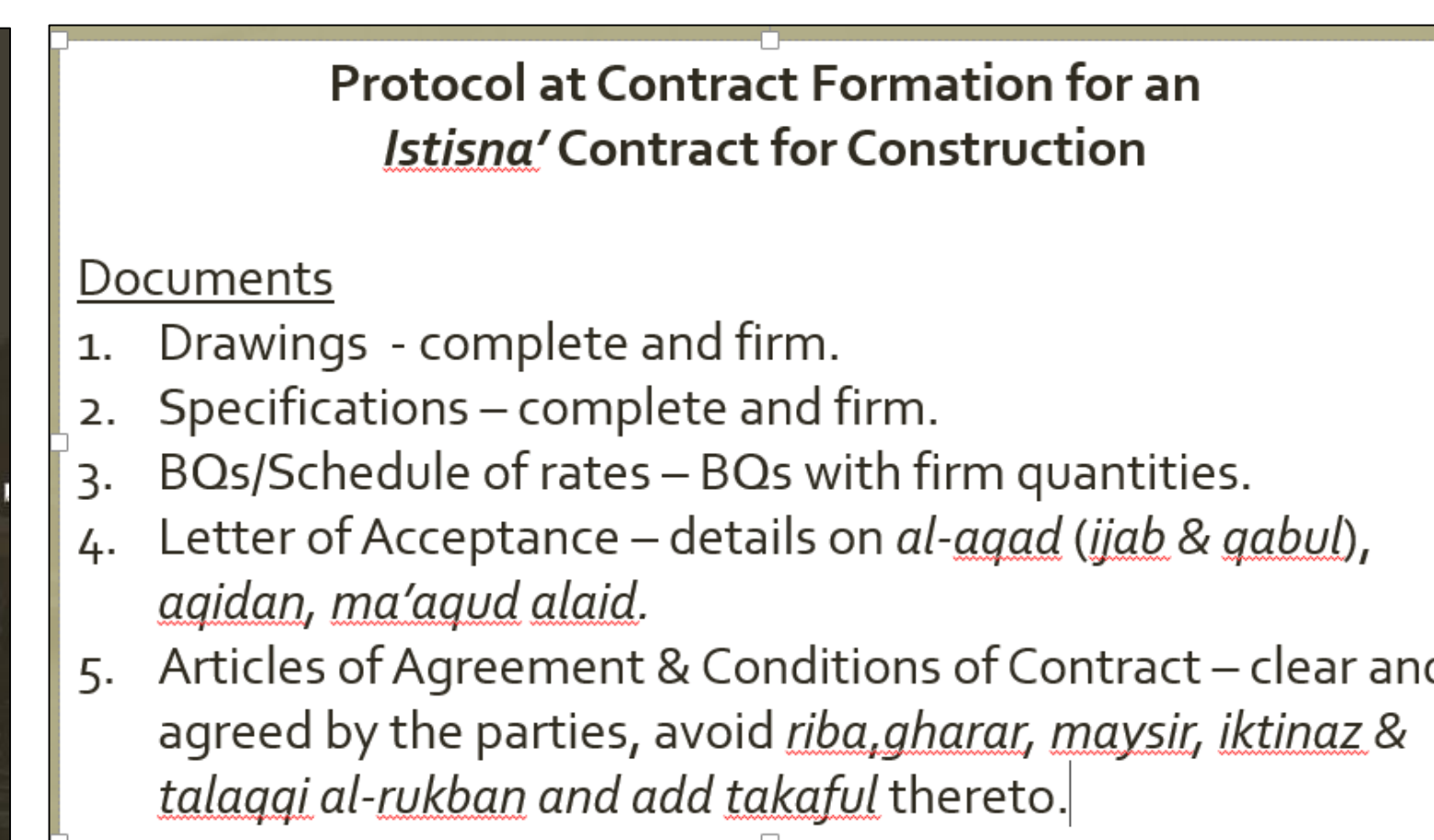


Diagram 2. Documents for a valid *Istisna'* contract

METHODOLOGY

The study was carried out through an intensive desk research and a series of 2 (two) focus group discussions (FGD). Participants to the FGDs were experts drawn from the construction industry (Employers, Contractors, Consultants), Shariah experts and related Academics. The research process is as illustrated in diagram 3 below.

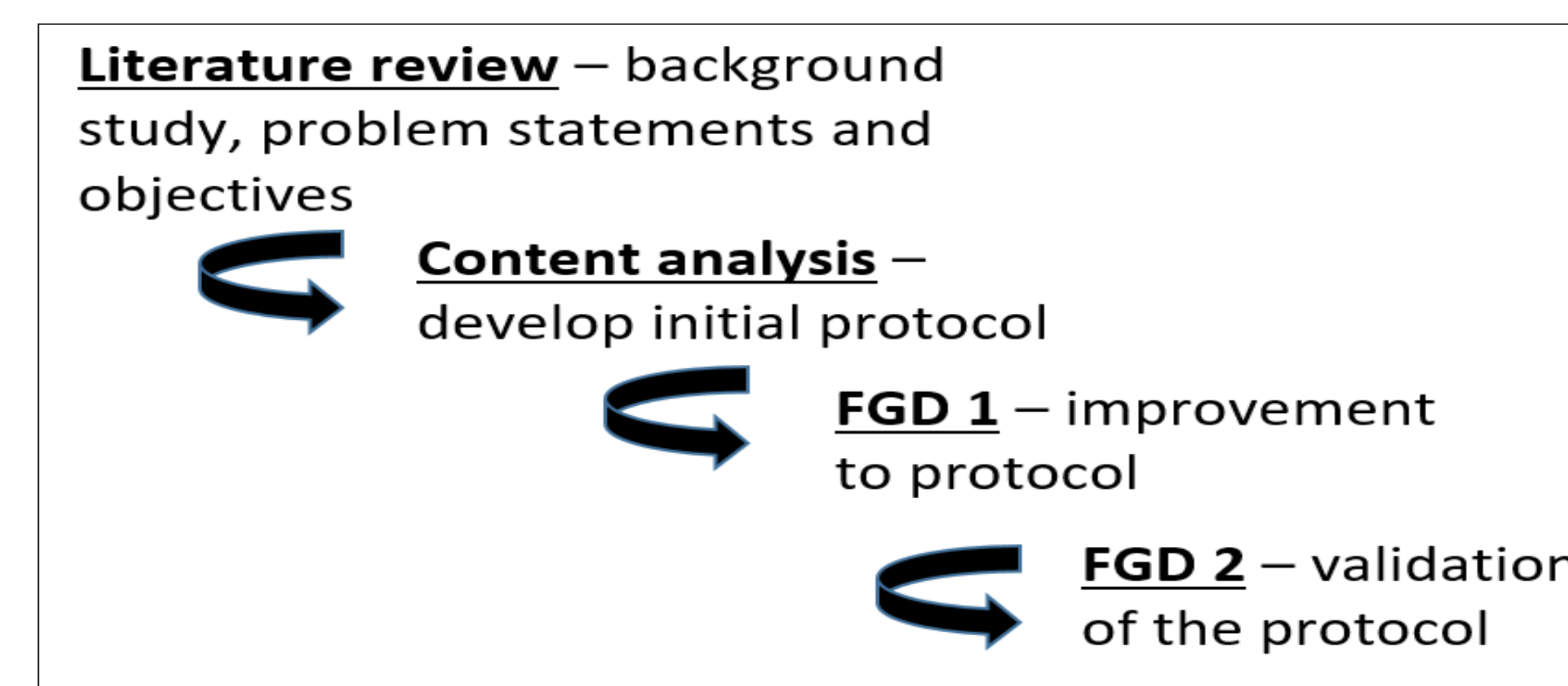


Diagram 3. The research process

SHARIAH COMPLIANCES

Istisna' based and Shariah compliance contract for construction works with key elements of the *al-aqad*, *aqidan* and *ma'aqud alaid* included therein; and elements of non-shariah in nature including *riba*, *maysir*, *iktinaz* and *talaqqi al-rukban* removed from, and *takaful* added into the conventional contract provisions (Quran including 17:34, 6:152, 4:9, 5:1, 2:282; IIFI 65/3/7, 1992; BNM, *Istisna'*, 23 Dec. 2015).

SIGNIFICANCES

1. A pioneering effort and a paradigm shift in the practice of contracting in the construction industry i.e. a move towards Shariah-compliant;
2. Complimenting and enhancing the currently well developed and well accepted Shariah compliance Islamic banking, finance, *takaful* and related business transactions;
3. The protocol serves as guide in the application of Shariah compliance contract for construction works; and
4. Contributing to *Maqasid al-Shariah* in the areas of *al-Din*, *nafs*, *aql*' and *mal*.

NOVELTY/ ORIGINALITY

A protocol for an *Istisna'* based Shariah compliance contract for construction works for the construction industry.

AWARDS :: PUBLICATION :: PATTERNS

Publications

Khairuddin Abdul Rashid (2019). Shariah-compliant contract Concepts and application for construction works. In Khairuddin, A.R, Kobayashi, K, Sharina Fariyah, H and Onishi, M. Editors (2019). Concept and application of Shariah for the construction industry: Shariah compliance in construction contracts, project finance and risk management. Singapore: World Scientific Publishing. p83-105.
 Khairuddin Abdul Rashid (2019). *Istisna'* model for construction works' contracts. In Khairuddin, A.R, Kobayashi, K, Sharina Fariyah, H and Onishi, M. Editors (2019). Concept and application of Shariah for the construction industry: Shariah compliance in construction contracts, project finance and risk management. Singapore: World Scientific Publishing. p107-120.
 Khairuddin Abdul Rashid (2019). Validity of *Istisna'* for construction works' contracts. In Khairuddin, A.R, Kobayashi, K, Sharina Fariyah, H and Onishi, M. Editors (2019). Concept and application of Shariah for the construction industry: Shariah compliance in construction contracts, project finance and risk management. Singapore: World Scientific Publishing. p121-128..