

# TAJ BANK LIMITED



## *LEASE BASED CONTRACTS*

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# RECAP/TEASERS FOR TRADE BASED CONTRACTS

## PURCHASE OF LAND THROUGH MURABAHA

### QUERY

An account holder has approached an Islamic bank seeking finance to settle the debt he has incurred as a result of purchasing a plot of land. He had entered into a purchase agreement with the owner of the property at the time of purchase and made a 20% down-payment of the purchase price whereby the balance was to be settled by upon completion of three months from the date of purchase. The unpaid amount was secured by the seller by way of a bank guarantee issued by the Islamic bank on behalf of the customer.

Due to liquidity constraints, the customer has now requested the bank to finance the payment of the purchase price in full, for a period of two years with pre-agreed payment terms. The Islamic bank is willing to accommodate the customer and has requested the Sharia board to provide a suitable structure to do so.



# RECAP/TEASERS FOR TRADE BASED CONTRACTS

## INCREASED COST OF CONSTRUCTION UNDER ISTISNAH CONTRACT

### QUERY

An Islamic bank as a buyer has signed an Istisna agreement with a customer as a seller, whereby the customer has to arrange for the construction and delivery of a building to the bank. Both parties have also signed a forward lease agreement, whereby the bank leased the described building to the customer by way of Ijara Muntahiya Bittamlik (financial lease basis). Both parties have agreed on the specifications of the building and the Istisna purchase price.

The customer, a few months after signing the Istisna agreement, pleaded that the cost of construction has substantially gone up due to strong demand for building materials, and that the bank should pay the additional amount to complete the project in accordance with the agreed specifications by way of increasing the purchase price.

Sharia guidance is sought to know if it is permissible to increase the purchase price under the Istisna agreement and at the same time to also increase the amount of the lease due to the reason mentioned above.

# OVERVIEW OF IJARAH

## IJARAH (...LEASING)

Ijarah is the lease of a specific asset or service to a client for an agreed period of time in exchange for rent which at the end of the lease period may result in transferring the subject matter's ownership to the lessee. In principle, an Ijarah contract is executed for an asset owned by the lessor or an usufruct owned by the sub-lessor.

The subject of lease must have a valuable use, so things having no usufruct at all cannot be leased.



# OVERVIEW OF IJARAH

A lease contract executed to transfer the benefits of an asset, service or usufruct in exchange for an agreed price. It does not involve the service of specific persons.

IJARAH TUL  
AAMAAL

TYPES OF  
IJARAH

IJARAH TUL  
MANAFAAY

A lease contract in which someone hire or employ a person on wages. It is a contract in which someone is hired to provide his services and skills and get paid in return for his services and expertise.



# OVERVIEW OF IJARAH

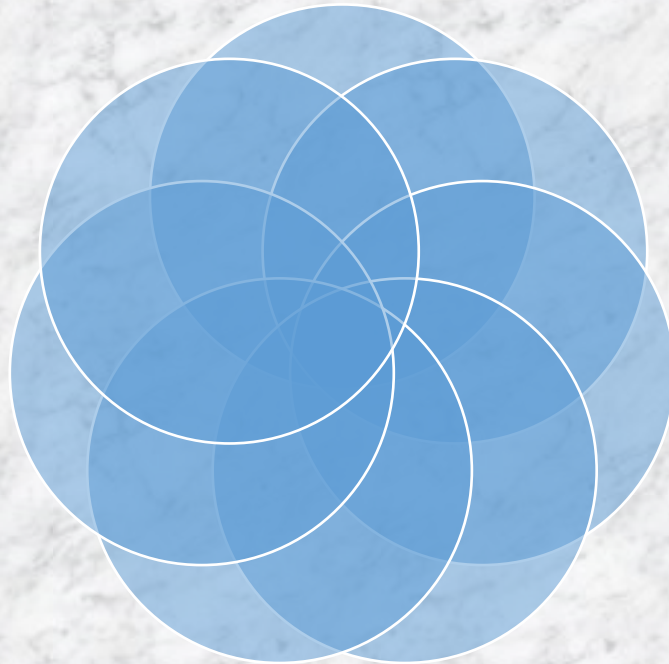
## Ijarah classification based on transfer of ownership to lessee

### Ijarah wa Iqtina

A lease contract to transfer ownership of the leased asset to the lessee gradually through the lease period.

### Ijarah Muntahiah Biitamleek

A lease contract conducted solely to transfer ownership of the leased asset to the lessee at the end of the lease period.



### Standard Ijarah

A lease contract where the lessee benefits from the asset for a specific time period but it does not result in the eventual transfer of ownership of the asset to the lessee.

# OVERVIEW OF IJARAH

The client and lessor enter into a promise to execute an Ijarah for the usufruct of a particular asset or service

The institution undertakes to provide the asset or service and the client undertakes to enter into a lease contract for it

## Pre-requisites of an Ijarah

The asset or service must be owned by the lessor and made available to the lessee before the Ijarah commences

The lease period commences once the subject matter of the lease is made available to the lessee.



# OVERVIEW OF IJARAH

## VARIOUS FORMS OF TRANSFER OF OWNERSHIP IN AN IJARAH

### IJARA MUNTAHIAH BITTAMLEEK

the lessee undertakes to purchase the Ijarah asset at the end of the Ijarah period for a mutually agreed price which may be the actual cost of the leased asset or any other nominal value. Alternatively the lessor may gift the leased asset to the lessee at the end of the Ijarah period.

### IJARA WA IQTINA

the lessee may even gradually purchase lessor's share in the asset during the lease period by making complete payment of rentals due or paying for the market value of the asset at the time. The asset is sold to the client at the end of the lease period based on a separate sale contract that represents the transfer of ownership.

# IJARAH MUNTAHIAH BITTAMLEEK

## FEATURES OF AN IJARAH MUNTAHIAH BITTAMLEEK CONTRACT

### OWNERSHIP OF ASSET

The ownership of the leased property remains in the ownership of the seller and only its usufruct is transferred to the lessee. Thus things like money, fuel, eatables which cannot be used without consuming cannot be leased out because their use is not possible unless they are consumed.

### LIABILITIES OF OWNERSHIP

As the ownership of the leased asset remains with the lessor, all the liabilities emerging from the ownership shall be borne by the lessor, but the liabilities referable to the use of the property shall be borne by the lessee

### PERIOD OF LEASE

The period of the lease must be determined in clear terms. The period of Ijarah should commence on the date of execution of the contract, unless the two parties agree on a specified future commencement date, resulting in a future Ijarah, that is, an Ijarah contract to be executed at a future date (Ijarah Mawsufah fi Zimmah)

### SUB-LEASE OF AN ASSET

A lessee of an asset may enter into a sub-lease contract with a party other than the owner unless the owner stipulates that the lessee should not assign or sublet the property to third parties, or should not do so without his approval

# IJARAH MUNTAHIAH BITTAMLEEK

## FEATURES OF AN IJARAH MUNTAHIAH BITTAMLEEK CONTRACT

### ARBOUN

It is permissible for the Institution to require the customer who has promised to lease to pay a sum of money, Arboun (Earnest money), to the Institution to ensure the customer's seriousness in accepting a lease on the asset. The lessor may retain the Arboun if the Ijarah contract is not executed for a reason attributable to the lessee.

### USE OF ARBOUN

Arboun (Earnest money) can be either held on trust in the custody of the institution, held on an investment trust basis in which case the customer permits the Institution to invest it on the basis of Mudarabah between the customer and Institution. It could also be used as advance payment of the lease rentals.

### PERMISSIBLE USE OF ASSET

The lessee cannot use the leased asset for any purpose other than that stipulated in the lease agreement. Moreover, the use of the leased asset must be permissible by Shariah.

### LIABILITIES OF LOSS OF ASSET

The lessor shall bear the risk of any harm or loss on the leased asset caused by factors beyond the control of the lessee. However, the lessee shall be liable where the harm is caused his misuse or negligence.



# IJARAH MUNTAHIAH BITTAMLEEK

## FEATURES OF AN IJARAH MUNTAHIAH BITTAMLEEK CONTRACT

### IMPAIRMENT OF ASSET

If the benefit from the leased asset is impaired wholly or partially as a result of the lessee's misconduct, while the property remains under lease, the lessee is obliged to restore or repair the usufruct, and rent for the time during which the benefit is lost is not to be waived.

### ASSETS JOINTLY OWNED

A property jointly owned by two or more persons can be leased out and the rental shall be distributed between all the joint owners according to the proportion of their respective shares in the asset. A joint owner of a property can lease his proportionate share to his co-sharer only, and not to any other person.

### LEASE RENTALS

The lease rental may be in cash or in kind (goods) or benefit (service). The rental must be specified, either as a lump sum covering the duration of the Ijarah contract, or by instalments for parts of the duration. It may also be for a fixed or variable amount, according to whatever designated method the two parties agree upon.

### DYNAMICS OF LEASE RENTAL

In case the rental is subject to changes (floating rental), it is necessary that the amount of the rental of the first period of the Ijarah contract be specified in lump sum. It is then permissible that the rentals for subsequent periods be determined according to a certain benchmark.

# IJARAH MUNTAHIAH BITTAMLEEK

## FEATURES OF AN IJARAH MUNTAHIAH BITTAMLEEK CONTRACT

### UNPAID RENTALS

No increase in the rental due may be stipulated by the lessor in case of delay in payment by the lessee. The unpaid rental becomes a debt and any penalty paid by the customer due to delay in payment of the lease rental shall be donated to charitable causes under the co-ordination of the ACE.

### TRANSFER OF THE ASSET

The method of transferring the title in the leased asset to the lessee must be evidenced in a document separate from the Ijarah contract, using any of:

a) a promise to sell for a token or other consideration, or by accelerating the payment of the remaining amount of rental, or by paying the market value of the leased property.

### TRANSFER OF THE ASSET

b) A promise to give it as a gift (for no consideration).  
c) A promise to give it as a gift, contingent upon the payment of the remaining instalments.

In all these cases, the separate document evidencing a promise of gift, promise of sale or a promise of gift contingent on a particular event, should be independent of the contract.

### TRANSFER OF THE ASSET

A promise to transfer the ownership by way of one of the methods above is a binding promise by the lessor. However, a binding promise is binding on one party only, while the other party must have the option not to proceed. This is to avoid a bilateral promise by the two parties which is Shari'ah impermissible because it resembles a concluded contract

# IJARAH MUNTAHIAH BITTAMLEEK

## FEATURES OF AN IJARAH MUNTAHIAH BITTAMLEEK CONTRACT

### TRANSFER OF ASSET

Transfer of the ownership in the leased property cannot be made by executing, along with the Ijarah, a sale contract that will become effective on a future date.

### TERMINATION OF LEASE

It is permissible to terminate the lease contract by mutual consent but it is not permissible for one party to terminate it except in case of force majeure or there is a defect in the leased asset that materially impairs its use. The lessor may also stipulate that the Ijarah contract be terminated if the lessee does not pay the rent or fails to pay it on time.

### TERMINATION OF LEASE

Ijarah contract does not terminate with the death of either party thereto. However, the heirs of the lessee may terminate the Ijarah contract if they can prove that the contract has become, as a result of the death of their legator, too onerous for their resources and in excess of their needs.

### TERMINATION OF LEASE

The Ijarah contract expires with the total destruction of the leased asset in the case of leasing a specific asset or with the inability to enjoy the usufruct owing to the loss of the benefit that the asset was intended to provide. The two parties may also terminate the Ijarah contract before it begins to run.



# IJARAH MUNTAHIAH BITTAMLEEK



Upon full settlement, the legal title of the asset is transferred to lessee either through gift, token price, equivalent price or gradual transfer.

# TEASERS FOR IJARAH MUNTAHIAH BITTAMLEEK

## PREMATURE TERMINATION OF IJARAH (LEASE) AT CUSTOMER'S REQUEST

### QUERY

An Islamic bank has approved for its customer the financing facility for a commercial property on the basis of financial lease (Ijara Muntahiya Bittamlik) for a period of seven years. Since the customer expects an increase in the property value in the near future, it has asked the bank for an option to settle the entire facility at any time during the financing period, and to acquire the title to the property free from any encumbrance if it decides to sell the property to materialize the capital gain.

How should the Islamic bank accommodate the customer's request?

# IJARAH OF SERVICES

## IJARAH OF SERVICES

Ijarah of Services is based on the contract of Ijarah i.e. the hire/acquisition of services of persons in exchange for a fee, financial or material consideration.

The bank assigns to the customer the enjoyment of the acquired service at a marked-up rate, which the customer pays up in a deferred lump sum or on agreed instalments.





# IJARAH OF SERVICES

## FEATURES OF AN IJARAH OF SERVICES CONTRACT

### PERMISIBILITY OF SERVICE

The service in an Ijarah of services contract shall be recognized by Shariah, valuable, identifiable and accessible.

The service shall be capable of being delivered by the service provider and assignable by the Bank.

### PERMISIBILITY OF SERVICE

Permissible services in this Ijarah contract will be: Intangible assets, such as trademark, patent, educational services, property rent, medical service, and other forms of services which are capable of being hired or acquired.

### AGENCY & SERVICE FEE

The Bank may appoint the customer or a third party as an agent to acquire the service.

Service fee shall be determined and agreed upon by the contracting parties at the inception of the Ijarah contract.

### SERVICE FEES

The contracting parties may mutually agree for the service fee to be paid by the customer in the form of cash or kind; in advance or in arrears; in a deferred lump sum or by instalments.

# IJARAH OF SERVICES

## FEATURES OF AN IJARAH OF SERVICES CONTRACT

### DYNAMIC OF SERVICE FEE

The contracting parties may agree for the service fee to be paid in fixed amount; to be determined via a reference to a specified benchmark or formula; or to be paid using a combination of both.

### INCREASE IN SERVICE FEE

The Bank cannot increase the service fee once it is fixed and agreed upon. No increase in the service fee due may be stipulated by the bank in case of delay in payment by the customer. The unpaid fee becomes a debt and any penalty paid by the customer due to delay in payment of the service fee shall be donated to charity.

### INITIAL SERVICE AMOUNT

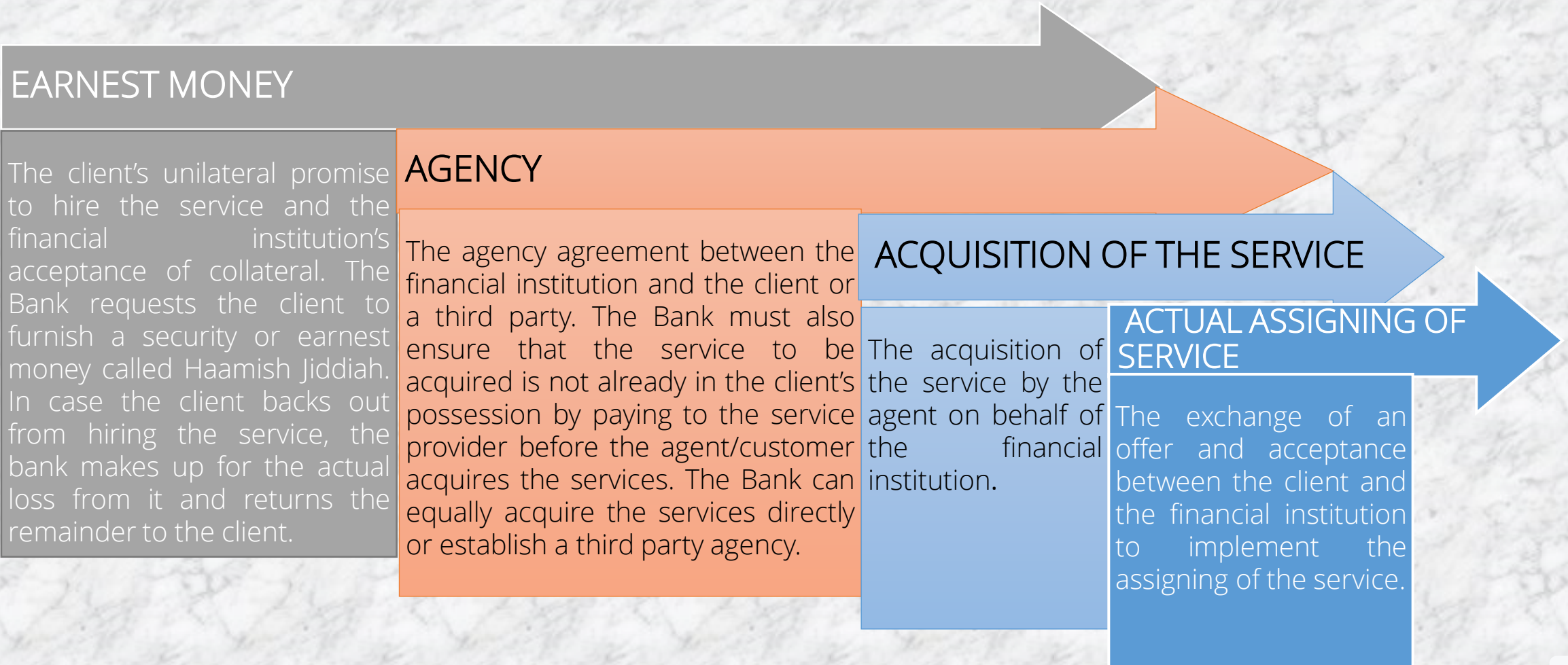
It is permissible for the Institution to require the customer to pay an initial service amount to ensure the customer's seriousness in hiring the acquired service. This amount of Customer's payment shall be adjusted against the total hire amount of the Services instalments.

### UTILIZATION OF SERVICE

The customer shall be bound to utilize the Services solely for the purpose for which it was acquired and is intended.

# IJARAH OF SERVICES

## STEPS OF IJARAH OF SERVICES CONTRACT





# IJARAH OF SERVICES

## IJARAH OF SERVICES- VARYING NATURE OF RELATIONSHIPS



# TEASERS FOR IJARAH OF SERVICES

## EDUCATION FINANCE IN ISLAMIC BANKING

### QUERY

The father of a student has approached an Islamic bank seeking finance for his son's education fees in order to complete a Master's degree in his chosen subject. The student has been selected by the university based on good grades and the fee must be paid within the deadline to secure the seat. Since the fee amount is too large a burden for the father to pay in bullet to the university, he has sought financial assistance from the bank.

Sharia guidance is sought in order to help the father meet his financial commitment to the university.



**Thank You!**