International Journal of Economics, Management and Accounting 28, no. 2 (2020): 431-456

ASSESSMENT OF *ZAKĀT*: A CASE STUDY OF SELECTED ISLAMIC BANKS IN MALAYSIA

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ABSTRACT

Zakāt is an obligatory payment imposed upon all types of business including Islamic banking institutions. This paper examines *zakāt* (alms due) assessment practices in Islamic banking institutions in Malaysia. Prior studies have mainly examined the payment trend of *zakāt* on businesses and the contributing factors of payment. This study was conducted in two *zakāt* paying Islamic banks; a local full-fledged Islamic bank and an Islamic subsidiary of a conventional bank. Primary and secondary data were collected. Interviews were conducted with relevant respondents from both banks to obtain hands-on information about *zakāt* assessment in Islamic banking institutions. The results reveal that the banks are committed to paying *zakāt*. Assessment of the *zakāt* due is jointly handled by the Finance and Shariah Departments. The whole process of *zakāt* treatment from policies, assessment, and distribution involve all levels in the bank hierarchical structure. As there is no single mandatory *zakāt* treatment regulation or standard, each bank has its own approach that led to variances in balance sheet item recognition and ultimately the amount of *zakāt* payable. While the variances are minor for one bank, they become considerably significant for the entire Islamic banking sector in Malaysia. Apart from enriching the Islamic finance literature especially in Islamic banking *zakāt* practices, this study will also provide valuable insight for practitioners and the relevant authorities.

JEL Classification: M41, G21, P43

Key words: Islamic banking institutions, Malaysia, *Zakāt* assessment, *Zakāt* on business.

1. INTRODUCTION

Business *zakāt* collection has contributed significantly to economic development and the betterment of local Muslim society. For example, in the Federal Territory in Malaysia, the total collection of *zakāt* on business from 2014 to 2018 is around RM86.2 million to 122.1 million. This contributes between 15 to 27 percent to overall distribution to *zakāt* recipients encompassing the group of *faqīr, miskīn, ʻāmil, muallaf, riqāb, ghārimīn, fī-sabīlillah* and *ibn sabīl*. The collected sum has been disbursed as various forms of assistance such as monthly allowance, housing and medical aid, scholarships, debt settlement assistance as well business grants (Federal Territory Islamic Religious Council, 2014-2018).

The same goes for *zakāt* collection in Selangor. From 2014-2018; the total collection from *zakāt* on business is between RM108 million to RM161.3 million, contributing between 17 to 26 percent of total disbursement in Selangor during that period. Selangor Zakat Authority has been providing many forms of assistance including financial allowance, food and medical aid, and scholarships to each group of *zakāt* recipients (Selangor Zakat Authority, 2014-2018).

Studies have also shown that *zakāt* contributed to poverty reduction and wealth creation (Embong, Taha and Mohd Nor, 2013). Only during the 2008 financial crisis, the data for poverty showed slightly greater poverty incidence even though more *zakāt* was collected. Even so, it can be argued that during the crisis, *zakāt* was the moderating factor limiting the impact on the poor. A more recent study in Indonesia also demonstrated that upward trajectory in *zakāt* collection occurs simultaneously with lowering level of poverty (Rini, Fatimah and Purwanti, 2020). Categorization of *zakāt* recipients in the Qur'an into eight types of recipients enable *zakāt* to be distributed to different types of people in society who need *zakāt* for various reasons. Hence, it was posited that *zakāt* contributed to improved social protection (Bilo and Machado, 2020). Because it contributes to poverty alleviation, income-gap reduction and social upliftment, with proper management and social support, *zakāt* has immense potential in national economic development (Ibrahim, 2008).

Zakāt (alms due) is an obligatory payment upon all types of businesses, including financial institutions (al-Zuhayli, 1989; Ibn

Qudamah, 1984). The obligation is based on the following commandment in the *Qurʾān*:

> Establish prayer and pay *zakāt* and whatsoever good you send before you for your souls, you will find it with Allah (*Qurʾān,* 2:110).

In Malaysia, all Muslim businesses are obliged to pay *zakāt* to the State Islamic Religious Councils (SIRCs) when certain conditions are met. More specifically, this is as mentioned in Section 86 in the Selangor Enactment (Enactment 1 Year 2003, Administration of the Religion of Islam (State of Selangor) 2003):

> Majlis is empowered to collect *zakāt* and *fitrah* due from every Muslim person in the State of Selangor in accordance with Hukum Syarak (Islamic Law) on behalf of His Royal Highness the Sultan.

The order follows the decision made by the National Fatwa Committee during its 31st Conference on 9 December 1992. The conditions include:

1. A business owned by Muslims,
2. A business owned by independent Muslims,
3. Perfect ownership,
4. *Nisāb* is reached, and
5. *Hawl* is reached (annual *qamariah*/354.3 days).

The fatwa determined that the rate of *zakāt* on the company is 2.5 percent. For a company jointly owned by Muslims and non-Muslims, payment is only mandatory for the percentage of shares owned by Muslims, which is based on net income (Zakat Collection Center-Federal Territory Islamic Religious Council, 2020).

The majority of scholars such as al-Mawdudi (1982), al-Qardawi (1994), Ibn Taimiyyah (1997), Abu ‘Ubayd (1988) are of the opinion that the previous *Qurʾānic* verse refers to the obligation of paying *zakāt* on a business as part of wealth that mankind has earned as also mentioned in a sunnah:

> “The Messenger of Allāh (peace be upon him) ordered us to issue *zakāt* from the goods that we provided for the business” (Abu Dawud, 2010).

It is clear from the word ‘ordered’ in this hadith that *zakāt* on business assets is an obligation for every Muslim (Ibn Taimiyyah, 1997; al-Qardawi, 1994; Abu ‘Ubayd, 1988; al-Mawdudi, 1982) as it is capable of fulfilling the social welfare of the poor and needy (Mikail and Ahmad, 2017; Yusoff, 2006).

Consequently, this paper investigates the concept of *zakāt* on business, with focus placed on banking institutions. Indeed, the nature of a “financial” business is slightly different from that of other business entities, and hence, entails different *zakāt* treatment. This paper also presents different implementations by various banking institutions on how they assess, and subsequently fulfil, their *zakāt* obligations. The results reveal why certain implementation policies have been adopted and practiced by the selected institutions.

2. ASSESSMENT OF *ZAKĀT* ON BUSINESSES

Many conditions determine the responsibility for z*akāt* payment on businesses. These are:

a. *Islām*
   Zakāt only applies to Muslims. For Muslim and non-Muslim business partnerships, only the equity belonging to the Muslim partner(s) is considered for *zakat*. In the case of the apostates, the Shafi’ites opine that they still have to pay for the portion of property acquired prior to apostasy. In contrast, the Hanafites argue that apostates are absolutely released from the obligation of *zakāt* (al-Qardawi, 1994).

b. Reached puberty and of sound mind
   Majority of scholars have agreed that *zakāt* is compulsory for those who have reached puberty and are of sound mind. For the children and the people not of sound mind, it is the responsibility of their caretaker to pay *zakāt* on their behalf. However, Hasan al-Basri stated that they are totally exempted from the payment ('Uqlah, 1982).

c. Full ownership of wealth
   The zakatable wealth to be taxed must be ‘perfectly owned’. Perfect ownership implies that the object possessed has been acquired lawfully. The owner must have full right to use and dispose of the said property in any way that he/she desires (al-Qardawi, 1994).

d. Assets are meant for business
Zakāt on business is subjected to assets intended for making profits. Assets not meant for trading are excluded from the calculation of *zakāt*. Additionally, fixed assets used for business (e.g., computers, chairs, machinery) are also exempted from *zakāt*, although any proceeds from these assets (e.g., rent) are subjected to *zakāt* assessment. If the fixed assets are disposed of, the proceeds gained from the process must be included in *zakāt* assessment (Department of Awqaf, Zakat and Hajj, 2010).

e. Possession of wealth for a period of one full year (*hawl*)
Wealth is only subjected to *zakāt* when held for a minimum period of one year. According to scholars, the one-year period refers to the *hijrah* year, which many other religious duties (e.g., fasting, pilgrimage) are based upon (Department of Awqaf, Zakat and Hajj, 2010).

f. Wealth reached *zakāt* minimum threshold amount (*nisāb*)
Nisāb refers to the minimum amount of assets that a Muslim must have before being obliged to pay *zakāt*. The current *nisāb* rate for *zakāt* on a business is based on the *nisāb* for gold. In this case, *zakāt* must be paid when the accumulated wealth has reached the value of 20 *mithqal* (85 grams) of gold. In January 2020, the *nisāb* value was equal to RM15,762.00 (Zakat Collection Center-Federal Territory Islamic Religious Council, 2020).

2.1 CONDITIONS FOR ASSESSING BUSINESS *ZAKĀT*

The following conditions, as stipulated by the Department of Awqaf, Zakat and Hajj (2010), are to be followed in order to assess *zakāt* payment by businesses:

a. *Halal* assets
Assets which are stated not permissible for Muslim consumption or usage (e.g., liquor, pork, gambling) and proceeds from non-*sharīʿah* compliant activities are excluded from *zakāt* calculation. If there are mixtures of *sharīʿah* compliance and non-compliance in certain assets, each portion must be determined. Only the *sharīʿah* compliant portion of assets shall be included in calculation.

b. Productive assets

A productive asset is an asset capable of generating income and profits. Productive assets include cash, *sharīʿah* compliant financial instruments classified as current assets, proceeds from fixed assets, trade net receivables, bank profits from deposit accounts and non-current assets (e.g., long-term investments), as well as purchasing investments at the end of *hawl* for cash.

c. Assets are not used for operations

Assets used for company operations (e.g., office supplies) are not subject to the assessment of *zakāt*.

According to the Department of Awqaf, Zakat and Hajj (2010), the types of items included in *zakāt* assessment are as follows:

a. Proceeds from fixed assets

Fixed assets are not subject to the assessment of *zakāt*. However, proceeds from fixed assets are subject to assessment of *zakāt* (e.g., rental revenue, proceeds from asset sales).

b. Current assets

All assets other than fixed assets and non-current assets, or non-tangible assets, are treated as current assets. This includes short-term investments. Only current assets which meet the stipulated conditions are subject to *zakāt* assessment.

c. Non-current assets

Bonds, stocks, bonuses, goodwill, patents and securities are treated as fixed assets.

d. Investments

Long-term investments that meet current asset requirements are subject to the assessment of *zakāt*.

e. Short-term liabilities/current liabilities

Short-term liabilities are the company's debt for the purchase of business goods, tax liabilities or operating liabilities. Financial liabilities (e.g., capital lease, long term loan debt due within one year, dividend liability, overdrafts) are included in *zakāt* assessment.

f. Long term liabilities

Long-term liabilities represent the liability of the company to the party who transfers debt to the company to expand its business capital (e.g., purchase of fixed assets or business operations). It is a source of capital and is subject to *zakāt* assessment.

g. Capital and shareholders' funds
This includes paid-up capital, premium accounts, revenue reserves, and accumulated gains or losses. It is considered a source of business capital and is subject to *zakāt* assessment.

2.2 METHODS OF CALCULATING *ZAKĀT* ON BUSINESSES

There are currently two methods used to calculate *zakāt* on business, as per the Department of Awqaf, Zakat and Hajj (2010):

Capital Growth Method

Current Capital	=	Owner’s Equity + Debt Financial Capital + Profit
Zakāt Payable	=	Current Capital x 2.5%

Working Capital Method

Net Current Assets	=	Current Assets - Current Operating Liability
Zakāt Payable	=	Net Current Asset x 2.5%

3. LITERATURE REVIEW OF *ZAKĀT* ON BUSINESSES

Zakāt collection from business entities in Malaysia has steadily increased nationwide over the years. However, it is likely that a bigger amount is still untapped. Razaly et al. (2013) found that only 3,983 business enterprises (4.5 percent) out of the 87,617 registered businesses in Johor paid *zakāt*. A Sabah study yielded similar results, where only 183 traders out of 629 registered Muslim Small Medium Enterprises (SMEs) paid *zakāt* (Abd Malik et al., 2015).

A significant number of banks (slightly over 50 percent) have been paying their dues. Bank Rakyat, in the Federal Territory, paid its dues on a business that amounted to RM12,586,497 from 2000 to March 2002 (Yahya, 2001). MAA Takaful, Lembaga Tabung Haji, Bank Islam Malaysia Berhad, and Bank Simpanan Nasional Berhad have also shown their commitment (Rosele, 2016; Badarulzaman, Azhar and Md Ismail, 2015). Amidst the reality, which was shown through the “less favorable” research findings, some writers are still optimistic and hope that awareness and company compliance in business *zakāt* payments will keep rising (Abdul Nasir, 2015).

Previous discussions, particularly on business *zakāt*, focused on aspects including factors influencing *zakāt* payments, assessment methods and adjustments, the rate, the legal provisions and the channel of payment such as Munandar et al. (2019), Yusuf and Derus (2013), Hasan (2018), Ahmed et al. (2016) and Mohamad Ibrahim, Ridzwan and Abdul Kadir (2016). We found a lack of discussion on actual business *zakāt* assessment practices in the Islamic banking sector. Hence this paper discusses the relevant *zakāt* discourses as highlighted in the literature in the following sub-section.

3.1 FACTORS INFLUENCING *ZAKĀT* PAYMENTS

Several factors influence companies to pay *zakāt***.** These include internal factors of the companies and efforts initiated by the government and/or *zakāt* institutions (Abdul Wahab and Borhan, 2014; Saad, Md. Idris and Bidin, 2009).

The internal factors include fulfillment of the *zakāt* duty by companies, which depends on the level of *īmān* (faith) of the owners and managers and their knowledge and awareness of the duty to pay *zakāt* (Abdul Wahab and Borhan, 2014). It is believed that more companies would pay *zakāt* if the government intensified the awareness campaign using a systematic and targeted approach. The provision and enforcement of laws, as well as the tax rebate facility, are believed to be among the needed government initiatives. As for the *zakāt* institutions, it was suggested that their management needed improvement. In this way, they could enjoy better governance, which may indirectly persuade payers to contribute more (Khamis and Che Yahya, 2015; Abdul Wahab and Borhan, 2014; Saad, Md Idris and Bidin, 2009).

Enterprises and companies that do not pay *zakāt* on business have a number of reasons for this (e.g., legal flexibility (no strict enforcement)). They also experience confusion in determining whether a company should pay *zakāt* or not (Razaly et al., 2014). Such situations stem from the widely known classical *fiqh* ruling, in that the payer must be an individual Muslim (a company is not an individual). To clarify the issue, a study has been carried out recently, which eventually concluded that a company is considered a *shakhsiyyah i'tibāriyyah* (legal entity). Hence, a company is given similar rights to that of ordinary individuals (A. Hasan, 2018; Z. Hasan, 2013; Bouheraoua, 2012; Accounting and Auditing Organization for Islamic

Financial Institutions, 2008). Consequently, *zakāt* is required for most companies as a legal entity (Hasan, 2011). It was posited that the *sharīʿah* recognizes the concept of *shakhsiyyah i'tibāriyyah*, and although imposition of *zakāt* is still largely vested on the company shareholders, the company may still pay *zakāt* at company level provided that it is authorized to do so (by way of its Articles of Association or decision made by the company's annual general meeting) or because the law dictates so (Hasan, 2018). Some companies have not paid *zakāt* because they do not know how to compute their dues and do not maintain proper financial records (Mohamad Ibrahim, Ridzwan and Abdul Kadir, 2016). In addition, there is no specific legal ruling or enactment mentioning power conferred on the enforcement body to take legal action on Islamic Banking Institutions in the case of failure to pay *zakāt* (Badarulzaman, Azhar and Md Ismail, 2016).

3.2 ASSESSMENT METHOD AND ADJUSTMENT

Two popular *zakāt* assessment methods are the capital growth method and the working capital method. These methods have been suggested by many *sharīʿah* scholars. In Malaysia, the Department of Awqaf, Zakat and Hajj (JAWHAR) has recommended the methods in its Manual of Zakat Management for Banking Institutions (2010). On 1 July 2006, the Malaysian Accounting Standard Board issued a similar statement regarding the matter. Both assessment methods are used by financial institutions in order to fit with their own business characteristics (Tajuddin, 2017).

Under the capital growth method, capital, debt capital finance and profit from capital are used as the *zakāt* base. On the other hand, the working capital method is calculated on current assets and liabilities (Department of Awqaf, Zakat and Hajj, 2010).

Some adjustments are allowed after the gross *zakāt* amount is realized. According to the JAWHAR manual, the adjustment is made by taking out the incomplete ownership items, non-permitted *sharīʿah* items and profit from operational activities. The profit is excluded as *zakāt* is based on growth or wealth creation on capital, not from the business activity itself. In order to reduce the potential of accounting manipulation, however, purchase of fixed assets and non-current assets at the end of the financial year or *hawl*, using internal operational funds is included in the *zakāt* calculation. This is based on the principle that any asset purchasing will reduce the amount of capital, which eventually lessens the *zakāt* payable amount (Department of Awqaf, Zakat and Hajj, 2010).

3.3 THE RATE

Two *zakāt* rates can be applied by banks: 2.5 percent or 2.5775 percent. It is widely agreed that the *zakāt* on business should be levied at 2.5 percent. This rate, however, must be applied when the *hawl* of one Hijri year is used. Such a *hawl* may not be as practical today, as most companies use the Gregorian calendar year as their accounting year.

The Gregorian calendar is slightly longer than the Hijri calendar, by up to 11 days. The First International Zakat Conference which was organized in Kuwait in 1980 suggested that the zakat rate for business should be revised. The recommendations were later upheld by the Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI). The AAOIFI recommended that the rate be fixed at 2.5775 percent, which is proportionate to the Gregorian calendar year (AAOIFI, 2008; 2015).

3.4 PAYMENT CHANNEL

Although state enactments in Malaysia indicated that the State Islamic Religious Councils (SIRC) are the only bodies entitled to collect zakat, some banks choose to pay *zakāt* privately, without going through the official channels (Abdul Nasir, 2015; Abd Malik et al., 2015; Razaly et al., 2013). Bank Rakyat, for example, used to distribute *zakāt* directly to selected qualified recipients (Yahya, 2001), while Bank Simpanan Nasional Berhad paid their *zakāt* to the SIRCs (Badarulzaman, Azhar and Ismail, 2015). Some financial institutions pay some *zakāt* to religious councils and distribute the balance directly to their selected recipients (Kamri, Ali and Che Seman, 2015).

The research reveals several ways banks can opt to determine their *zakāt* amount due and how they distribute the *zakāt* payment. Each bank has its own justification for choosing which method it wants to undertake, how much to pay and how to make the payment. This paper attempts to better understand these practices.

4. METHODOLOGY

Data were collected through both library and field research. Library research was used to clarify the related information about the concept of *zakāt* on business in reference to the *Qurʾān* and *Hadith*. Other documents and guidelines adopted by the Malaysian Islamic banking institutions (e.g., guidelines from JAWHAR) were also obtained as a basis for the *zakāt* assessment. Interviews were conducted to obtain information directly from stakeholders in Islamic banking institutions.

Purposive sampling has been used to identify and select research informants based on the research interest. In a purposive sampling strategy “the inquirer selects individuals and sites for study because they can purposefully inform an understanding of the research problem and central phenomenon in the study” (Creswell, 2013: p. 125). As the research focused on Malaysian Islamic banking institutions, two institutions were selected which represent different categories of banks based on their operations (i.e., full-fledged Islamic bank and Islamic bank subsidiary). Even though some banks operate as Islamic windows, they are not classified in the Islamic bank category, according to the Central Bank of Malaysia list (Central Bank of Malaysia, 2020).

Semi-structured interviews were chosen as the main source of evidence. They were triangulated by other sources (e.g., Manual of Zakat Management for Banking Institutions by JAWHAR). Silverman (2001) argued that interviews, questionnaires, observations and document analysis can be combined in qualitative research; this is because of their powerful ability in providing in-depth descriptions, understanding and knowledge of specific phenomena from the informants’ perspective (Merriam, 1998; Patton, 1990).

Interviews were conducted with a group of informants from the Shariah and Finance Departments, consisting of 2 to 4 top executives from both departments. The informants were chosen based on their authority and accessibility to each bank’s *zakāt* policy and management. Hence, practical information on the method and practice of the banks’ *zakāt* on business was obtained.

During the interview sessions, an audio recorder was used to record the data. All the recordings were transcribed verbatim. The interview transcriptions were written in the spoken language (Bahasa Melayu or Malay language) as used in the interviews. The Malay language was maintained to preserve authenticity. The interview transcripts were later returned to the respondents for verification. Afterward, each interview transcript with the respondent’s feedback was analyzed using thematic analysis. In this stage, each transcript was reviewed and verified by other members of the research team to ensure its validity.

4.1 RESEARCH SAMPLE

The Islamic financial sector has been growing rapidly in Malaysia since the early 1980s. As of January 2020, 16 banks have been granted Islamic banking licenses by Central Bank of Malaysia. They are divided into two categories: five (5) full-fledged Islamic banks and eleven (11) Islamic banking subsidiaries. Bank Islam Malaysia Berhad, Bank Muamalat Malaysia Berhad, Al Rajhi Banking & Investment Corporations (Malaysia) Berhad, Kuwait Finance House (Malaysia) Berhad and MBSB Bank Berhad are full-fledged Islamic banks. Affin Islamic Bank Berhad, Alliance Islamic Bank Berhad, AmBank Islamic Berhad, CIMB Islamic Bank Berhad, HSBC Amanah Malaysia Berhad, Hong Leong Islamic Bank Berhad, Maybank Islamic Berhad, OCBC Al-Amin Bank Berhad, Public Islamic Bank Berhad, RHB Islamic Bank Berhad and Standard Chartered Saadiq Berhad are considered Islamic bank subsidiaries.

Of the 16 banks, two were used as subjects of the study to represent the two categories. As the research deals with an extensive amount of confidential bank information, the names of the selected banks will not be revealed. They have been labeled Banks A and B.

Bank A is a full-fledged Islamic bank in Malaysia. It has played a leading role in developing the nation’s Islamic banking industry. It was established in the 1980s to fulfill the financial needs of Muslims in Malaysia. Since then, Bank A has extended its services to the wider, non-Muslim customers under its new banner, the “Banking-for-All” motto. Bank A currently offers a comprehensive range of *sharīʿah* compliant banking and financial services to its more than five million customers. It currently has 145 branches and more than 1,000 self-service terminals nationwide.

Bank B is a wholly-owned subsidiary of a full-fledged conventional commercial bank. In 2005, the Islamic Banking Division of its parent bank was incorporated as a separate entity. In April 2006, Bank B started operating as an independent Islamic bank entity with paid up capital of RM160 million. It has been continuously conducting research and development on new financial products and services to compete in the global financial arena.

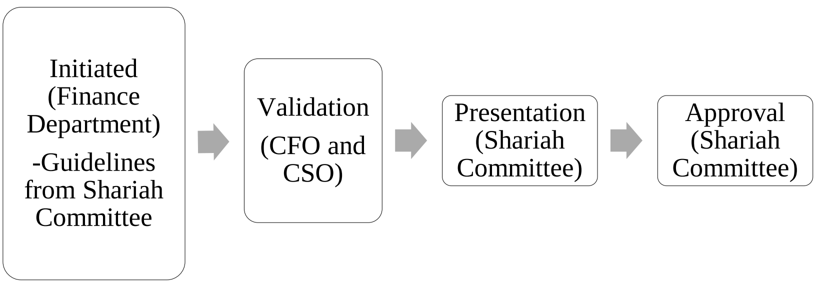
5. RESULTS AND DISCUSSION: CURRENT INDUSTRIAL REALITY

After visiting banks and conducting interviews with a number of informants from the sampled banks, several aspects pertaining to the practice of determining the total amount of *zakāt* due for payment was revealed. The findings will be presented and discussed under the following headings.

5.1 PROCESS OF ASSESSMENT OF *ZAKĀT* ON BUSINESS

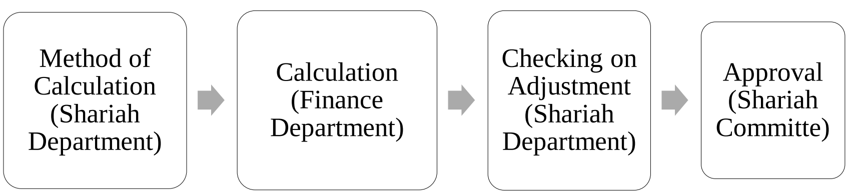
The following Figure 1 and Figure 2 illustrate how the practice of the *zakāt* assessment process differs between Banks A and B.

FIGURE 1
Process of Assessment of *Zakāt* on Business in Bank A



Note: Chief Financial Officer (CF), Chief Shariah Officer (CSO),
Source: Interview, June 5, 2017.

FIGURE 2
Process of Assessment of *Zakāt* on Business in Bank B



Source: Interview, July 4, 2017.

In both banks, the assessment is carried out by the Shariah and Finance Departments. In Bank A, the initial calculation is carried out by the Finance Department. The calculations, however, are guided by the outline prepared by the Shariah Department. After the *zakāt* amount is determined, the Chief Financial Officer (CFO) and Chief Shariah Officer (CSO) review and validate the results.

There is close communication between the Shariah and Finance Departments during the *zakāt* calculation process. In this particular case, the computation does not seem to be given solely to the finance department, as the CSO has always been actively contributing to the process. Upon completing the *zakāt* amount determination, the *zakāt* amount will subsequently be tabled in the Shariah Committee meeting which will decide whether to endorse or reject it.

Another approach depicted in the second figure refers to Bank B, which illustrates that, prior to the *zakāt* assessment process, the method of calculation is provided by the Shariah Department. Based on the guidelines, the calculation is carried out by the Finance Department. The gross amount of *zakāt* and the adjustment items will be scrutinized by the Shariah Department. Afterwards, the Shariah Department submits the reviewed amount to the Shariah Committee to be assessed and endorsed.

Figure 2 shows the clearer demarcation and division of the work between the Finance and Shariah Departments. The calculation process is solely conducted by the Finance Department, while the Shariah Department ensures that guidelines are followed correctly. It is uncertain whether close collaboration between the two occurs throughout the entire process.

During the *zakāt* assessment process, even though the assessment is conducted by the Shariah and Finance Departments for both banks, the CSO plays the most influential role. Active CSO participation contributed to and influenced the *zakāt* assessment process. The CSO was not only involved in the beginning and final stages (determination of the calculation method and endorsement of the *zakāt* amount), but the entire process. This active participation ensured elimination of blind endorsement. It also encouraged more harmonious collaboration between the two departments for better *zakāt* assessment. At the same time, issues of *zakāt* underpayment or overpayment can be resolved.

5.2 ASSESSMENT METHOD

Bank A uses the capital growth method. The *zakāt* is payable upon the shareholder funds. No depositors fund is subject to zakat, as it does not belong to the bank. Bank A uses the following formula to calculate *zakāt*:

Net Invested Fund	=	Owner Equity (+) Long Term Liabilities (–) Fixed Assets (–) Non-Current Assets (+/-) Adjustment
Zakāt Payable	=	Net invested fund after adjustment (×) % Bank Portion (×) 2.5775%

The bank's portion includes the shareholders fund, *ṣukūk* issuance and other funds (i.e., funds from the Central Bank of Malaysia).

Bank B, similar to the bank A also uses the capital growth method. The bank uses the following formula to calculate *zakāt*:

Net Assets	=	Equity (+) Long Term Liabilities (–) Fixed Assets (-) Non-Current Assets (+/) Adjustment
Zakāt Payable	=	Net assets after adjustment (×) % Bank Portion (×) 2.5775% (×) % Muslim shareholder's shares

However, a few differences in *zakāt* calculation exist between the two banks. Bank A may overpay, because it pays *zakāt* for all shareholders, regardless of their religion. Bank B only pays *zakāt* from the Muslim shareholder's funds. It should be noted that the Muslim shareholder's funds are owned by both individual and institutional shareholders. As the main shareholder is a governmental statutory body, it is classified under the Muslim shareholder category. The findings showed that both banks only follow JAWHAR's guidelines to a certain extent, as they each have their own approaches in relation to *zakāt*.

5.3 INCORPORATED ADJUSTMENTS

A number of adjustments need to be made before a bank calculates the final *zakāt* payable sum. Such adjustments are pertinent to determine the net sum subjected to *zakāt*.

Table 1 illustrates the *zakāt* adjustments for Bank A. For Bank A, some adjustments are incorporated in relation to the following items: reserves/equities, current assets, financial and fixed assets, debtor (financing), and current liabilities. Reserves/equities refers to the capital injection incurred in December. The adjustment for the current assets is calculated for current assets that are held by other parties. These assets (e.g., statutory deposits with Central Bank of Malaysia) are deducted in the *zakāt* calculation, as they are deemed to be not fulfilling the condition of full ownership (Interview, 5 June 2017). As for the financial and fixed assets, any acquisitions occurring in the month of December are added into the *zakāt* calculation. Adjustments for debtors are made if there are transactions involving short-term trade financing. Lastly, Bank A makes adjustments for the current liabilities by adding the provision for *zakāt*. These adjustments are described in Table 1.

TABLE 1
Bank A *Zakāt* Adjustments

Adjustment		Type of Adjustment's Account	
Add	Adjustments on reserves/equities Transactions in December	1.	Capital injection to subsidiaries companies
Less	Adjustments on current assets Not full ownership	1.	Other assets
		2.	Statutory deposits with Central Bank of Malaysia
		3.	Current tax assets
		4.	Deferred tax assets
Add	Adjustments on financial and fixed assets Transactions in December (purchase transactions)	1.	Financial assets available for sale
		2.	Financial assets held to maturity
		3.	Fixed assets
Add	Adjustment on debtor (financing)	1.	Trade financing
Add	Adjustment on current liabilities	1.	Provision for *zakāt*

Source: Interview, June 5, 2017.

Table 2 illustrates the *zakāt* adjustments for Bank B. Bank B's adjustments include assets, liabilities, and fixed assets. The adjustment on assets refers to the deduction of items that do not fulfil the full ownership conditions, which consists of deferred tax assets, statutory deposits with Central Bank of Malaysia, and other assets. Items categorized as liabilities, but meeting the condition of full ownership, are added. Finally, the fixed assets are deducted. The detailed adjustments are depicted in Table 2.

The findings illustrate that Banks A and B have different treatments for fixed assets. Bank A would only recognize the assets acquired prior to the month of December. Hence, all purchases of fixed assets in December are not deducted from the *zakāt* measurements. Bank A's position corresponds to the guidelines of JAWHAR. The Manual of Zakat Management for Banking Institutions (2010) states that fixed assets are exempted from *zakāt*; however, "Purchases of fixed assets and non-current assets at the end of the financial year/end of *hawl* using internal operational funds is included in *zakāt* measurement." JAWHAR, however, did not provide any explanation for the reasoning behind the recommendation.

TABLE 2
Bank B *Zakāt* Adjustments

Adjustment		Type of Adjustment's Account	
Less	Adjustments on assets *(Not full ownership)*	1.	Deferred tax assets
		2.	Statutory deposits with Central Bank of Malaysia
		3.	Other assets
Add	Adjustments on liabilities *(Full ownership)*	1.	Deposits from customers
		2.	Deposits and placements of banks and other financial institutions
		3.	Investment accounts due to designated financial institutions
		4.	Derivatives financial liabilities
		5.	Other liabilities
		6.	Amount due to holding company
Less	Adjustments on fixed assets	1.	Net fixed assets and intangibles (e.g. property, equipment and intangible assets)

Source: Interview, July 4, 2017.

In contrast, Bank B does not differentiate whether the acquisition of fixed assets is made in December or not. Bank B's position is that all fixed assets are deducted from the *zakāt* measurement, regardless of its proximity to the end of the financial year/end of *hawl*. There is no specific evidence to support either position. Nonetheless, the practice of fixed assets acquisition at the end of the financial year may indicate a plot of *zakāt* evasion. Current assets, in the form of cash and other cash equivalent assets, are subjected to *zakāt*. However, their liquidity means that they can easily be transformed into fixed assets, which are not included in the *zakāt* measurement.

Bank A prefers to practice '*ihtiyāt*' (recommended precaution) in the *zakāt* treatment. From its perspective, it is better to be more cautious regarding *zakāt* and pay more than less, as *zakāt* is a religious duty. However, it should not be assumed that Bank B's practice of disregarding the timing of a fixed asset purchase constituted malicious conduct. There are several reasons for this. First, the Manual of the Zakat Management for Banking Institutions was published as a non-binding recommendation; it has been used as guidance in the banking industry rather than a directive. Second, the practice was endorsed by the Shariah Advisory Committee of the bank, whose members are scholars in Islamic jurisprudence. Furthermore, the committee members come from different institutions and are not the bank employees, hence ensuring justice. The Shariah Committee does not make decisions without referring to strong evidence from reliable sources. Having said that, in a situation where the Shariah Committee members lack sufficient understanding of the bank operations, they are still susceptible to overlook certain unethical practices or maneuvers.

Another issue identified was Bank B's practices of adding fixed assets in the calculation of *zakāt*. The bank does not recognize fixed assets as its own assets in its balance sheet. It was explained that the practice is because Bank B operates under the same premises as its parent company, using the same personnel, assets, and facilities. Bank B does not have its own premises. Operationally, apart from having certain personnel, it only exists in the form of computer systems and networks. It is as if the bank only exists virtually. The fixed assets figure was calculated using the percentage portion of the fixed assets used.

A question arises as to whom the assets really belong. The fact that Bank B did not report the fixed assets on the balance sheet means that the assets are not its assets, and including the fixed assets in the *zakāt* calculations results in a reduction of the *zakāt* amount, which may constitute '*hilah*' (ruse in commercial transactions). Even though *zakāt* should only be calculated from assets which meet the conditions of '*al-milk al-tam*' (full ownership), Bank B can argue that the ability to utilize the assets as it pleases fulfils the condition of '*al-milk al-tam*' (full ownership). The same argument was used to determine that deposits from bank customers are considered part of full ownership. Meanwhile, one may argue that the parent bank, in actuality, is only sharing the benefit of the assets with Bank B, while maintaining full control of the assets.

5.4 *ZAKĀT* RATE

Both banks were found to use 2.5775 percent as the *zakāt* base rate. This is due to the current practice of using the Gregorian financial year, as compared to the classical annual *zakāt* rate of 2.5 percent, based on the lunar calendar. This is consistent with the *zakāt* ruling announced in the 1984 First Zakat Conference organized in Kuwait. Such a decision is not shared by all scholars (e.g., al-Qardawi) and differs from what has been suggested by JAWHAR (al-Qardawi, 1994; JAWHAR, 2010).

6. CONCLUSION

The results reveal that two banks have shown commitment to paying *zakāt*. Normally, the computation of the sum due will be jointly handled by the respective Finance and Shariah Department. Until recently, the federal and state governments have made little effort to strictly enforce *zakāt* upon business institutions, including banks. The government seems to prefer the ‘soft approach’ of persuasion and encouragement.

Our observations make it clear that, amidst the commitment shown by the two banks in performing their obligation, no single standard assessment process has been strictly followed. The guidelines prepared by JAWHAR are merely optional guidelines complementing other local and international guidelines.

Since they differ in the nature of their business and have different types of consumers, banks have many ways of computing the sum of *zakāt* payable annually. They may use different calculation methods and different adjustment items. Banks also opt for different ways to disburse their payments. Although State Religious Councils are the only bodies entitled to collect *zakāt*, banks may not submit all payments to them. Additionally, some banks prefer to surrender their *zakāt* directly to the selected recipients.

To increase the collection and improve the *zakāt* calculation and payment methods, some suggestions can be taken into consideration by banks and the related authority especially JAWHAR.

Banks need to clearly identify which assets are perfectly and non-perfectly owned by them as asset is one of the main items included in *zakāt* calculation. The study found that, banks tend to have different definition of assets; such conflicting views must be discussed and a more consistent guideline should be suggested. Such standard definitions should also cover other items related to *zakāt* such as liability and capital. In addition, the rate for *zakāt* on banking business can be fixed at 2.5775 percent as banks normally use the Gregorian year to mark their financial cycle.

JAWHAR in this context can play a significant role in initiating strong spirit of cooperation, so that a more standard practice can be proposed and accepted by all institutions in the banking and finance industry. Eventually, more comprehensive and widely accepted guidelines can be introduced.

When determining *zakāt* payable amounts, the principle of *ihtiyāt* (precaution) must always be prioritized. *Zakāt* payment is one of the social responsibilities of the banks toward the Muslim ummah, hence any excessive adjustment that may lead to under reporting payable *zakāt* amount should be avoided. Such principle should be strongly upheld by those responsible for calculating *zakāt* including bank appointed Shariah Advisors.

ACKNOWLEDGEMENT

We would like to acknowledge the financial support provided by the Ministry of Higher Education Malaysia for research grant MO004-2016.

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APPENDIX 1

Assessment of *Zakāt* on Business in Bank A and Bank B

Item	Bank A	Bank B
Assessment Method	Capital Growth-Shareholder Fund	Modified Method: 1) Capital Growth Method 2) Working Capital Method
Assessment Item	Net Invested Fund = Owner Equity (+) Long Term Liabilities (–) Fixed Assets (-) Non-Current Assets (+/-) Adjustment	1) Capital Growth Method: Net assets = Equity (+) Long Term Liabilities (–) Fixed Assets (-) Non-Current Assets (+/-) Adjustment 2) Working Capital Method: Net Asset = Current assets (-) current liabilities (+/-) Adjustment
Adjustment	1) (+) Reserves/Equities: Capital injection to subsidiaries company 2) (-) Current Assets: Other assets, Statutory deposits with BNM, Current tax assets, Deferred tax assets 3) (+) Financial and Fixed Assets: Financial assets available for sale, Financial assets held for maturity, Fixed assets 4) (+) Debtor: Trade financing 5) (+) Current liabilities: Provision for *Zakāt*	1) (-) Assets: Deferred tax assets, Statutory deposits with BNM, Other assets 2) (+) Liabilities: Deposits from customers, Deposits and placement of banks and other financial institutions, Investment accounts due to designated financial institutions, Derivatives financial liabilities, Other liabilities, Amount due to holding company 3) (-) Fixed assets: Net fixed assets and Intangible assets

APPENDIX 1 *(continued)*

Item	Bank A	Bank B
Zakāt Payable	Net assets subject to *zakāt* (×) % Bank Portion (×) 2.5775%	Net assets after adjustment (×) % Bank Portion (×) 2.5775% (×) % Muslim shareholder's shares
Rate of *Zakāt*	2.5775	2.5775

Source: Interview, June 5, 2017 and July 4, 2017