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ᶜIWAë AS A REQUIREMENT OF LAWFUL SALE: A CRITICAL ANALYSIS

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ABSTRACT

This paper will argue that replacing *ribŒ* with *al-bayᶜ* does not mean that the latter can imply any form of sale (*al-bayᶜ*) to justify Islamic legitimacy. Apart from the prohibition of uncertainties (*gharŒr*) in sale, the requirement of an equivalent countervalue (ᶜ*iwaè*) must also be met. Risk (*ghurm*) and liability (*èaman*) after sale and value-addition or effort (*ikhtiyŒr*) are the principal components of ᶜ*iwaè*. As such, any increase from sale must contain ᶜ*iwaè*, otherwise *ribŒ* is implicated. In classical Islamic commercial contracts such as *ijŒrah*, *salam* and *muèŒrabah*, ᶜ*iwaè* is evident. However, the contracts of credit of *al-murŒbaúah* or *al-bayᶜ bithaman Œjil* are widely used by Islamic banking practitioners. To prove Islamic legitimacy, this contract must show that the financiers assume the risk of ownership in making the sale. It must also show evidence that the seller is liable to the option of defect (*khiyŒr al-ᶜayb*). The same holds for *bayᶜ al-ᶜ¥nah* and *bayᶜ al-dayn* which are also widely used in Islamic money and capital markets in some Muslim countries.

JEL classification: G20, K39, Z12

Key words: Islamic banking, ᶜ*Iwaè*, *RibŒ*

1. INTRODUCTION

Differences of opinion in *fiqh* is not prohibited in Islam unless it involves the fundamentals of Islam, namely the rules (*aúkŒm*), which the *Qur'Œn* has made absolutely clear by way of its textual evidences (*na§*). For example, there can be no differences of opinion (*ikhtilŒf*) on the

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prohibition of *ribŒ* since it does not fall within the domain of *ikhtilŒf*, which can only be exercised on matters involving the branches of *fiqh* (*fur´c*). Thus, for instance, Muslim scholars can disagree on some details on the way prayers (*solŒt*) are performed, but not on whether the five daily prayers are obligatory (*wŒjib*) or not. Likewise, disagreements in Islamic banking and finance can take place involving the choice of instruments in project finance, but not on attempting to permit *ribŒ* (which is prohibited) under the disguise of *al-bayc* (which is permissible). The problem at hand involves the usage of *mucŒmalŒt* contracts such as *bayc al-c¥nah* and *bayc al-dayn* in the Malaysian Islamic financial markets, which is partly caused by a lack of theory on *ribŒ* that is both definite and decisive. This paper intends to show that if these contracts claim to command strong *Shar¥cah* legitimacy, it must conform to the requirement of *ciwaè*. That is, any profit generated from the *bayc al-c¥nah* and *bayc al-dayn* must contain an equivalent countervalue (*ciwaè*). This adds a strong theoretical base against using *ikhtilŒf* as a basis of disagreement among the ShŒfic¥, Ì anbal¥, Ì anaf¥ and MŒlik¥ schools of thought on this issue.

Awareness about Islamic banking and finance in recent years saw an overwhelming global response by both Muslim and non-Muslim practitioners. This is only logical when more than US$100 billion Islamic funds are available in the world financial market today. For that reason, an upbeat interest in Islamic finance is apparent. The New York Stock Exchange set up the Dow Jones Shariah Index, while in Malaysia, the Kuala Lumpur Shariah Index was introduced in 1998 and London too has it own. All these intend to guide investors to buy and sell stocks on the basis of *Shar¥cah* law.

Islamic funds have also found their way to the banking sector. In fact this was where it all began. In the 1960s, the Mit Ghamr Local Savings Bank in Egypt paved the way for new and innovative approaches to the banking business, which received overwhelming support from local farmers and villagers. It was a success story as the bank was able to instill a sense of belonging among its customers by way of partnership banking. Later developments included the formation of the Islamic Development Bank and the Dubai Islamic bank in 1975 and 1976, respectively. In the late 1970s, many more were set up, including the Kuwait Finance House, the Faisal Islamic Bank of Egypt,

and the Bahrain Islamic Bank. In Asia, Malaysia is well-known for her parallel banking system, where Islamic banks run their business side by side with their conventional counterparts, while banks in Pakistan, Iran and Sudan operate solely in a single Islamic banking system.

To some extent, companies engaging in the business of Islamic banking operate on the basis of profit-maximization. It is to be pursued by observing the *Shar¥ᶜah* laws, one of which is the prohibition of *ribŒ*.

Although the main thrust of Islamic banking and finance has been the prohibition of *ribŒ* or interest, which many writers have written so much about, the application of *al-bayᶜ (*trade and commerce) in financing activities has not been discussed in the same rigor. This has led many observers to think that an Islamic bank is a banking firm that operates solely on the basis of non-payment and receipt of interest. Unfortunately, this has been true. For this reason, the application of *al-murŒbaúah* credit sale as a mode of financing has been widespread.

The author shall argue that overemphasizing the prohibition of *ribŒ* as a cornerstone of Islamic banking has impacted the business in a negative way as it tends to discourage innovation and creativity in product design and development. That is, when abstention from *ribŒ* is used as the measuring rod of Islamic banking business, it opens the door for practitioners to adopt conventional products with relatively less regard for the *Qur'Œn*ic requirement of economic justice.

2. *AL-BAYᶜ* VERSUS *RIB•*

RibŒ in the *Qur'Œn* was mentioned on many occasions but it is best to understand these revelations in chronological order, so as to appreciate the Islamic approach of societal reform. There are three main stages in which *ribŒ* is discussed in the *Qur'Œn*, namely:

a. The First Stage: At this stage of Islamic history, the Prophet Muúammad (pbuh) and his followers were severely oppressed by the prominent leaders of the Quraysh tribe in Makkah. The first verse on *ribŒ* was revealed in *S´rah al-R´m* where the believers were reminded of the evil of *ribŒ* and the virtues of charity.[1] Here, the verse serves as a moral denunciation of *ribŒ* rather than a legal one since the main thrust of the Islamic movement then was *tawú¥d* and monotheism.

b. The Second Stage: After *Hijrah*, the Muslim gained military and economic power in Mad¥nah. The legal prohibition of *ribŒ* was timely here since an organized political state existed under the leadership of Prophet Muúammad (pbuh). In *S´rah •Ii ᶜImrŒn*, the categorical prohibition of *ribŒ* was announced.[2]

c. The Third Stage: In this final stage, the *Qur'Œn* provides the alternative to *ribŒ*, namely trade and commerce (*al-bayᶜ*). Since *ribŒ* is a contractual increase over a loan, a legitimate increase according to the *Qur'Œn* can only be derived through trade and commerce and not debt. Explanations were also given about the rights of creditors to the principal loans and the threats from Allah to those who disobey Him. Creditors are enjoined to practice leniency to the debtors who face difficulties in making payments. Lenders are also enjoined to give away the loans as charity when the latter failed to pay up.[3]

However, the injunction to observe *al-bayᶜ* instead of *ribŒ* in business transaction has led *Shar¥ᶜah* scholars and banking practitioners to adopt Islamic commercial contracts as a mode of financing rather than adopting them in the original way. Islamic banks are not seen able to involve themselves in real economic activities such as manufacturing, agriculture and construction. Rather, they perform the role of financiers by way of financing asset purchases but only to bypass legal acquisition involving the transfer of ownership on which they are liable for market risks. For this reason, they have been acutely selective in applying specific Islamic commercial contracts that can best suit their role as financiers. For example, *al-murŒbaúah* credit sale have been heavily employed by most Islamic banking practitioners, but it does not rank high in the order of Islamic commercial contracts. This is supported by Ibn al-ᶜArab¥, who says that *bayᶜ* is of three types; namely, (a) material substance for another material substance, i.e., an exchange of one commodity or money for another commodity or money, (b) purchase/sale by paying in advance (*salam*) in money or on the basis of manufactured goods (*istisnŒᶜ*), and (c) sale of a material substance (money) for usurfruct (*manfaᶜah*) i.e., *ijŒrah*. He continued to say that *ribŒ*, on the contrary, is an increase (*ziyŒdah*) which does not bring (in exchange) an equivalent countervalue.[4]

3. APPLYING *AL-BAYᶜ* IN THE BANKING BUSINESS

As the *Qur'Œn* has allowed trade and prohibited *ribŒ*, there is a need to understand why profit from trade is lawful while profit from loan as *ribŒ* is not. On this we refer again to Ibn al-ᶜArab¥ (d. 543/1148) according to which he says, "every increase, which is without ᶜ*iwaè* or an equal countervalue is *ribŒ*." In this sense, ᶜ*iwaè* is the basic trait or *conditio sine qua non* of a lawful sale. This is because a sale (*al-bayᶜ*) is necessarily an exchange of a value against an equivalent value.

For this reason, the *Shar¥ᶜah* law requires all legitimate exchange to contain ᶜ*iwaè*, or an equivalent countervalue. What this means is that the price that a consumer pays must be compensated with an equitable return which he enjoys from the transaction. When a trader sells at a price higher than the cost of inputs, the profit margin or an "increase over capital" must contain ᶜ*iwaè*. It follows that a theory of profit in Islam should be built on the principle of ᶜ*iwaè*.

The author shall argue that the *Qur'Œn*ic injunction of *al-bayᶜ* as the alternative to *ribŒ* intends to highlight the role of ᶜ*iwaè* which embodies both risk-taking (*ghurm*) and value-addition *(ikhtiyŒr)* in the determination of profits. When the *Qur'Œn* says, ". . . Allah hath permitted trade and forbidden usury . . ." (*al-Qur'Œn*, 2:275), the message has always been that of economic justice. The *Qur'Œn* refused to accept interest-based lending as a fair business transaction. The contract of trade (*al-bayᶜ*) instead became the alternative to the contract of debt with *ribŒ*. But trading during the Prophetic era was relatively different from what we see today. The Prophet (pbuh) acquired capital from Sayyidatin Œ Khad¥jah to purchase goods in Makkah. Through the caravan trade, these goods were sold in Iraq, Yemen and Syria at a higher price, i.e., with a profit margin. Later, after the Arab conquest, it spread to the Near-East, North Africa and Southern Europe (Udovitch, 1970, 172). This is a common trading activity where risks and danger of losing their merchandise is something that caravan merchants were accustomed with. They traveled long distances and struggled through extreme weather. Highway robberies were a common feature of desert travel while falling prey to sickness in desert terrain finds relatively no mercy (Hasan, 1997, 6-8). In fact, the *Qur'Œn* recounts the life of the Quraysh tribe as both nomadic and commercial: "For the covenants (of security and safeguard enjoyed) by the Quraysh; their covenants

(covering) journeys by winter and summer; let them adore the Lord of this House; Who provides them with food against hunger; and with security against fear (of danger)," (*al-Qur'Œn*, 106:1-4).

In view of the risks and effort involved in trading, the profit made by the Prophet (pbuh) is legitimate. Goods were sold for cash and profits were distributed on the basis of a profit-sharing ratio determined earlier. However, the present-day situation is a lot different. Banks today are financial intermediaries while the Prophet (pbuh) was not. Sayyiditin Œ Khad¥jah provided the capital, but she was not a banker. Hence, the application of trade as an alternative to *ribŒ* in the banking industry today should not be misconstrued as purely executing what the *Qur'Œn* desires man to do. The *Qur'Œn*ic ban on *ribŒ* is essentially about establishing justice (*ᶜadl*), and justice is basically an ethical precept. Taking profit from a *ribŒ* loan is unjust while making profit from trade is said to be the opposite. This is because trading, as exemplified by the Prophet (pbuh) and Khad¥jah, consists of two parts; namely, (a) the business partnership (*al-muèŒrabah*) between the Prophet Muúammad (pbuh) and Sayyidatin Œ Khad¥jah, and (b) the nature of work the Prophet (pbuh) undertook with Khad¥jah's capital, namely selling and buying (*al-bayᶜ*) of merchandise on cash basis.[5]

Trading as we observe today in the form of credit *al-murŒbaúah* has its own unique role in view of the high demand for credit, but it is not similar to the nature of business Prophet Muúammad (pbuh) ventured into. Islamic banking today has chosen the credit sale approach of '*al-bayᶜ*' about which the *Qur'Œn* is silent as it has not taken shape along the Prophetic model of *al-qirŒè*.

4. THE MEANING OF ᶜ*IWAë*

Now that *al-bayᶜ* is enjoined by the *Qur'Œn* as opposed to *ribŒ*, there is an urgent need to understand in what way profit from loans, namely *ribŒ* is different from profit from sale (*al-bayᶜ*). As mentioned by Ibn al-ᶜArab¥ earlier, "every increase, which is without ᶜ*iwaè* or an equal countervalue is *ribŒ*." This can imply that a contractual increase arising from a loan is *ribŒ* because it does not contain ᶜ*iwaè*. It follows that an increase (i.e., profit created) from a sale is not *ribŒ* because it, i.e., the profit is supposed to contain ᶜ*iwaè*.

The following illustration is useful to further explore the meaning

of ᶜiwaè and how it must exist in all legitimate sales. For example, Mr. Muúammad pays $1,000 for a Seiko watch. In other words, an exchange of goods for money has taken place. The pricing of the Seiko watch consists of cost of inputs and a profit margin in which it, i.e., the profit margin, is created from the effort (*ikhtiyŒr*) rendered and risk (*ghurm*) taken by the manufacturer. Thus, if cost of inputs is equal to $300 while the residual, i.e., $700 constitutes the profit margin, the exchange is said to contain ᶜiwaè. The surplus amounting to $700 constitutes the risk and effort elements of production while the $300 represents the cost of inputs.

Risk-taking in Islamic commercial transactions not only involves the risk incurred before sale (*ghurm*) but also risk after sale. Unlike *ghurm*, which arises from market-related risks such as price volatility or failure to dispose of goods even at cost, risk after sale is the liability that a selling party must acknowledge when the goods sold are found defective (ᶜ*ayb*). When this happens, the buyer holds the right to return the goods for money or make the seller liable for any cost incurred on repairs and other related expenses. *KhiyŒr al-ᶜayb*, or option due to defect, is a liability that the selling party must acknowledge. It is a legal right such that the buyer does not need to stipulate a reservation of option at the time of contracting in order for him to be able to resort to it later (Rayner, 1991, 327-43). The legal maxim, "the benefit of a thing is a return for loss from that thing (*al-kharŒj bi al-èaman*)," therefore, constitutes a key component of ᶜiwaè.

In other words, an equivalent countervalue or ᶜiwaè consists of three main elements; namely, (a) market risk (*ghurm*), (b) effort or value-added (*ikhtiyŒr*), and (c) liability (*èaman*). In the case of an interest-bearing loan, say $10,000 at 10 percent interest rate per annum, we are looking at an exchange of money worth $10,000 in year 1 for $11,000 in year 2. The principal component, namely $10,000, constitutes the cost of inputs while the additional $1,000 represents the profit created from the loan made to the debtor. However, this surplus or profit has not seen the involvement of risk-taking and value-added services discharged by the creditor. It does not contain ᶜiwaè and, as such, is tantamount to *ribŒ* since by definition, "every increase, which is without ᶜiwaè or an equal countervalue is *ribŒ*," (Haque, 1995, 10).

It is therefore crucial to critically highlight the *bayᶜ* requirement of ᶜiwaè, when one wishes to understand issues on Islamic banking and

finance. It would not be a good strategy to delve into *ribŒ* issues without putting *al-bay*^{c} and ^{c}*iwaè* factors in their proper places as it can cause great confusion if the one-sided approach, i.e., focusing on the *ribŒ* alone, is used to introduce the concept of Islamic banking and finance to the general public. On this point, the cause (*^{c}illah*) of *ribŒ* may not necessarily be the element of contractual increase (*faèl*) over the principal loan but also that this increase does not contain ^{c}*iwaè*. Any sale without ^{c}*iwaè* is hence invalid which means that any profit created, therefore, is illegitimate.

5. ^{C}*IWAë* IN ISLAMIC COMMERCIAL CONTRACTS

Apart from *al-bay*^{c}, it is important to identify the existence of ^{c}*iwaè* arising in *al-ijŒrah, salam, istisnŒ*^{c}, *muèŒrabah* and *musyŒrakah* transactions. These contracts, in essence, are categorized under the *bay*^{c} category when it, i.e, *al-bay*^{c}, is understood to mean trade and commercial transactions. Since generally, profit arising from trading and commercial activities is derived on the basis of risk-taking and value-addition, it is therefore not similar to the lending business since in the latter, profit is created without either one.[6] We will now look at different types of Islamic commercial contracts applied by Islamic banks today. The main objective is to identify the existence of ^{c}*iwaè* in each of them. Ability to do so will help show that profits created from these contracts are lawful and worthy in order to receive continued support in the Islamic banking business.

a. *IjŒrah*: In Islamic commercial law, the contract of *al-ijŒrah* consists of two; namely, *ijŒrah al-*^{c}*amal* and *ijŒrah al-*^{c}*ayn*. In the latter, payments are made for the services rendered by the employee. These payments, namely the price of the labor input, contain ^{c}*iwaè* since wages and salaries are paid in exchange for the skills and expertise rendered. Thus, work and effort or value-addition constitutes the ^{c}*iwaè* element in the contract of *ijŒrah al-*^{c}*amal.* Likewise, rental payments arising from *ijŒrah al-*^{c}*ayn* contains ^{c}*iwaè* since the lessee receives usurfruct arising from utilizing the rental property. On the other hand, the rental income is a legitimate one as the lessor has exerted his expertise in maintenance work and he is also exposed to losses in case the value of his property depreciates due to natural calamities or volatile market

movements. *IjŒrah wa iqtinŒᶜ* (leasing ending with ownership) and *ijŒrah thumma al-bayᶜ* (leasing ending with sale) as operational leases are expected to contain ᶜ*iwaè* since the lessee, namely the bank must hold legal ownership of the asset concerned. When this is done, the asset is rented out followed by sale of the goods at a nominal price or given away as a gift (*hibah*) at the end of rental period. However, if the bank fails to prove that it holds legal possession, and therefore assumes relatively zero market risk, ᶜ*iwaè* does not materialize and therefore the rental income cannot claim Islamic legitimacy.

b. *Salam* and *IstisnŒᶜ* (forward sale): In a *salam* and *istisnŒᶜ* sale, the price of goods or merchandise is paid on the spot while delivery is made at a specified future date. For example, the order price is $100,000, on which the buyer expects to make a 20 percent profit when sold again upon delivery. This profit is lawful since it contains ᶜ*iwaè* which is the risk taken by the buyer in case the market price falls below $100,000 when the goods are delivered. To the seller, or farmer in the case of *salam* sale, the cost of inputs may amount to $60,000. He made $40,000 in income by virtue of the effort (*ikhtiyŒr*) rendered in production, which represents the ᶜ*iwaè* component.

c. *al-MurŒbaúah* cash sale: *Bayᶜ al-murŒbaúah* is a sale in which the seller puts a mark-up onto the cost price of goods. Popularly known as the "mark-up sale", *al-murŒbaúah* can be classified into two types; namely, cash *murŒbaúah*, and deferred or credit *murŒbaúah*. The latter is also known as *bayᶜ mu'ajjal* and *bayᶜ al-bithaman Œjil*. Our concern here is in the former, namely cash *murŒbaúah*. ᶜ*Iwaè* is evident in cash *murŒbaúah* since the seller makes effort to buy the goods himself. He is also exposed to market risks because the mark-up price may fall below the cost price. He may lose his capital when nobody wants to buy his goods, say due to changes in tastes or changes in technology which can make his goods obsolete. Thus, the profit derived from *murŒbaúah* sale is a legitimate one since the element of ᶜ*iwaè* in the form of risk-taking and value-addition is readily evident.

d. *al-MurŒbaúah* deferred/credit sale: This form of *al-murŒbaúah* is used as a mode of finance in most Islamic banks today. Also known as *al-bayᶜ bithaman Œjil* (sale with deferred payment), the profit margin

or mark-up is created purely due to time.[7] This is because an Islamic bank normally purchases the goods at the market price rather than at cost or wholesale price as evident in cash *murŒbaúah*. It will then sell the goods to the customer at a selling price in which relatively no trace of risk-taking and value-addition is found. It is worthy to note that the mark-up or profit imposed on the market price in arriving at the selling price can claim legitimacy only if the element of *ᶜiwaè* exists. For example, in risk-taking, the bank must hold legal ownership before it can sell the goods to the customer.[8] With legal ownership, it bears the risk of not making a sale if the customer changes his mind, which he (the customer) has the right to do so. Without legal ownership, the bank is functioning as a financier and this is not what the *Qur'Œn* intended it to be.[9] In addition to the ownership factor, the bank is also expected to honor the option to rescind the contract by the customer under the principle of *khiyŒr al-ᶜayb*. That is, the customer holds the right to claim for damages if the goods sold are found to be defective or not delivered within the specifications required.

e. *al-MuèŒrabah*: As mentioned earlier, profit created from *al-muèŒrabah* activities contains *ᶜiwaè* since the capital provider is exposed to the risk of losing his capital. Likewise, when the agent-manager (*muèŒrib*) opts to become a partner in the *muèŒrabah* venture, he has forgone the opportunity of earning a fixed income elsewhere. This is also a risk that the *muèŒrib* must deal with in *muèŒrabah*. In addition to that, the *muèŒrib* applies his skills and expertise in managing the business. Thus, some form of risk-taking and value-addition, which make up the *ᶜiwaè* factor, is evident in the *muèŒrabah* contract.

f. *al-MusyŒrakah*: The term *musyŒrakah* is popularly used in Islamic banking to imply the application of *al-shar¥kah al-amwŒl* as a mode of finance. This contract can either take the form of *shar¥kah al-ᶜinŒn* (unequal-share partnership) or *shar¥kah al-mufŒwaèah* (equal-share partnership). In both ways, the element of *ᶜiwaè* is evident since the essence of any partnership venture involves risk-taking and value-added activities. The partnership neither gives guarantee on the safety of the invested capital nor promised a fixed return. Capital can appreciate and depreciate on the basis of performance, which aptly requires the

business to assume market risks and to ensure that the provision of skills and expertise is executed in the most efficient way.

g. *Bayᶜ al-dayn*: *Dayn* or debt is the right to future cash payments arising from a loan (*qarè*). *Bayᶜ al-dayn* is the sale of such right. Generally, the selling of *dayn* at *par* value is allowed as this comes under the contract of *úiwŒlah* (transfer of debt). However, when exchanges of debt take place at above or below the debt's *par* value, the payment and receipt of interest as *ribŒ* is implicated. One main argument against *bayᶜ al-dayn* is the fact that *dayn* is not property (*mŒl mutaqawwim*). That is, *dayn* is money and not property. In a contract of sale, the subject matter or object of sale (*maúŒl al-ᶜaqd*) must qualify as *mŒl mutaqawwim*, that is, it must generate usurfruct (*manfaᶜah*) to the buyer. For example, people buy food for consumption or buy houses to protect them from the heat and cold. For this reason, the contract of *bayᶜ al-dayn* is void (*bŒ‹il*) as the subject matter, namely *dayn*, is not an acceptable form of asset or property. Hence, any profit created from the sale of debt is unlawful.[10] In addition to this, *bayᶜ al-dayn* at a discount or premium as a sale of debt is similar to the unequal exchange of money for money, i.e., exchange of money for money without an equal countervalue (*ᶜiwaè*). In the case of Islamic bonds as practiced in Malaysia, a bond that matures at *par* value can be sold at a discount before maturity. As this involves an unequal exchange of money for more money, *ribŒ al-faèl* may be implicated here. The excesses (*faèl*) arising from the exchange contain no *ᶜiwaè*, thus making it an unlawful gain.[11]

h. *Bayᶜ al-ᶜ¥nah*: Quite a number of interest-free products today, especially in Malaysia, have applied the contract of *bayᶜ al-ᶜ¥nah*.[12] These include personal financing, short-term deposits, Islamic bonds and money market instruments. It is worth noticing that the contract of *bayᶜ bithaman Œjil* or *al-murŒbaúah* is instrumental in making the *bayᶜ al-ᶜ¥nah* transaction possible. It is important to note that in this contract two separate contracts are applied in sequence; namely, (i) *al-bayᶜ al-mu‹laq* (cash sale), and (ii) *al-bayᶜ bithaman Œjil* (deferred sale), both of which are executed after one another. Sometimes the deferred sale is preceded by a spot sale and vice versa, but in both ways each party gets what it intended to achieve.

For example, when sale by deferred payment is preceded by a spot sale, it is a case where the bank sells an asset to the customer with payments made on equal installment, say for $24,000 payable in ten months. The installment sale saw the customer executing his right to sell back the asset to the bank on cash basis, say at $20,000. The installment price has to be higher than the cash price if the bank desires to profit from the sale. In essence, the bank and customer have both achieved what both wanted. The customer gets the $20,000 cash he wanted and the bank makes the $4,000 profit from the $20,000 invested. The object of sale comes into play by virtue of a trick to get away with interest payments and receipts.

However, the existence of *ᶜiwaè* is unlikely in the creation of profits arising from *al-bayᶜ al-ᶜ¥nah*. The sale and resale contracts initiated by either the bank or the customer saw no event by which either party has assumed risk-taking and value-addition in rationalizing the profit taken. In both transactions, each party has made a prior guarantee that in every sale there will exist an automatic resale. As such, neither are exposed to market risks and liability arising from say, defective goods sold, if any. In other words, the principle of *al-ghurm bi al-ghurm* and *al-kharŒj bi al-èaman* is nowhere applied in this sale.

6. CONCLUSION

When the *Qur'Œn* legally prohibited the payment and receipt of *ribŒ* and replaces it with *al-bayᶜ*, it was observed that many writers on Islamic banking have put relatively less rigor into fully articulating the meaning of *al-bayᶜ* or how the *Qur'Œn* sees it as superior to *ribŒ*. Instead, *al-bayᶜ* is now promoted as a mode of finance rather than a real economic transaction involving the exchange of goods with equal countervalue (*ᶜiwaè*). As the *Qur'Œn* has allowed *al-bayᶜ* and Muslim jurists have, in general, agreed that all legitimate sale (*al-bayᶜ*) must contain *ᶜiwaè*, it follows that any gain created from a sale (*al-bayᶜ*) without associating *ᶜiwaè* is equivalent to *ribŒ*. It is therefore crucial to ensure that contemporary Islamic modes of finance must not discount the *ᶜiwaè* factor. Failure to do so will discount the principle of economic justice which Islamic banking and finance it supposedly able to promote. It is thus critical to see that the elements of risk (*ghurm*), value-added (*ikhtiyŒr*), and liability (*èaman*) as an embodiment of *ᶜiwaè* are fully

imputed into Islamic modes of finance. In the contract of *al-bayᶜ mu'ajjal* (credit *murŒbaúah*), the bank as a purchaser must hold the risk of ownership in executing the sale and purchase transaction. Inability to do so will lead more banking practitioners to continually promote the application of legal devices (*úiyal*) such as *bayᶜ al-ᶜ¥nah* and *bayᶜ al-dayn* in Islamic finance. Both contracts run against the cardinal principles of justice expounded in the maxims of *fiqh* (*qawŒᶜid fiqhiyyah*) that, "liability is an obligation accompanying gain." That is, a person who enjoys the benefits of a thing must submit to the disadvantage attaching thereto," (Mahmassani, 1961,15-6). Even if some argue that these contracts are valid, Muslims who apply them will not be able to take the lesson that in pursuing Allah's bounties they must be willing to take risks.

ENDNOTES

1. "That which ye lay out for increase through the property of (other) people, will have no increase with Allah; but that which ye lay out for charity, seeking the Countenance of Allah (will increase): it is these who will get the recompense multiplied," (*al-Qur'Œn*, 30:39).

2. "O ye who believe! Devour not usury, doubled and multiplied, but fear Allah, that ye may (really) prosper," (*al-Qur'Œn*, 3:130).

3. ". . . But Allah hath permitted trade and forbidden usury . . . Oh ye who believe! Fear Allah, and give up what remains of your demand for usury, if ye are indeed believers. If ye do it not, take notice of war from Allah and His Messenger, but if ye turn back, ye shall have your capital sums; deal not unjustly, and ye shall not be dealt with unjustly. If the debtor is in a difficulty, grant him time till it is easy for him to repay. But if you remit it by way of charity, that is best for you if ye only knew," (*al-Qur'Œn*, 2:275-280).

4. Haque (1995, 11-2). The author quoted the original source of reference, namely, Ibn al-ᶜArab¥ (1376/1957, 242).

5. Cash sales can include *bayᶜ musŒwamah* (bargain sale) *bayᶜ waè¥ᶜah* (discount sale) and also *bayᶜ al-murŒbaúah* (spot sale with a mark-up). It should be pointed out that present-day *al-murŒbaúah* sale is not a sale with cash payments but a sale with deferred payments. However, credit *murŒbaúah*

was observed in Prophetic tradition. In a *úad¼th* narrated by Anas, the Prophet (pbuh) bought some foodstuff on credit for a limited period and mortgaged his armor for it (*êaú¥ú BukhŒr¥*, Vol. 3, Book 45, No. 685). This tradition is related to a sale of commodities from a genuine seller who must have acquired the goods by way of production or trading.

6. It is worthy to note that prudent banking requires all loans to be supported by collaterals or guarantors as this removes the risk of default. To protect lenders from inflation risk, an inflation premium is added to the real rate of interest. Literally speaking, loans will not be approved until they are 100 percent safe or default-free with the borrower capable of paying the contractual rate of return.

7. When the profit rate on deferred *murŒbaúah* sale is relatively equal to the market loan rate, which turns out to be true in most cases in modern Islamic banks today, it is rather difficult to discount the fact that the imputation of risks due to time was introduced to the *murŒbaúah* credit sale. These risks include risks from inflationary pressures as well as default. The compensation due to abstinence, namely the real interest rate plus inflation and default risk plus operational cost make up the nominal interest rate. The issue now is to understand what constitutes the profit margin, namely the mark-up made from *bay*^{c} *mu'ajjal* (deferred *murŒbaúah*). Certainly, it will not include a contractual compensation due to abstinence or a fixed payment to protect the bank from losses due to default.

8. The ownership issue can be resolved by looking at the legal documentation of deferred *murŒbaúah*. The sale-purchase agreement must be able to show that the bank is the legal owner of the goods on sale. For example, in motor financing, the name of the bank must be evident in the grant document, otherwise the bank is merely acting as a financier.

9. For a discussion on the impact of *al-murŒbaúah* financing on bank performance, see Rosly (1999).

10. *Bay*^{c} *al-dayn* at a discount or premium as a sale of debt is similar to the exchange of money for money but at different amounts. In the case of Islamic bonds as practiced in Malaysia, a bond which matures at *par* value can be sold at a discount before maturity. As this involves the exchange of money for more money, *ribŒ al-faèl* is implicated here. The excesses (*faèl*) arising from the exchange contain no ^{c}*iwaè*, thus representing an unlawful gain.

11. For example, a *MurŒbaúah* note issuance facility (MuNif) holds a *par* value at $1000 per unit. MuNif is a debt certificate, i.e., a *dayn*, meaning that the holder has a legal claim on future cash payment or redemption worth $1000. However, this *dayn* can be exchanged for cash before it matures, normally at a discount price, say $900 in the secondary market. Here, an unequal exchange of money for money has taken place by virtue of a time element, which is as good as *ribŒ*. However, according to the jurists at Malaysia's Security Commission, this transaction is legal since the bond is asset-backed, which means it qualifies as *mŒl mutaqawwim*, and therefore can be traded at any price.

12. For a more detailed discussion on *al-bayᶜ al-ᶜ¥nah*, see Rosly and Sanusi (1998).

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