

SALE OF GOODS AND SALE OF DEBTS: A COMPARATIVE ANALYSIS

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Abstract

Islam clearly identifies not only lawful (halal) activities, but also unlawful (haram) activities as well. Differences of opinion may arise in these two areas too. In order to achieve the ultimate in Islam, we should exercise caution when practicing Islamic finance. In Islamic banking and finance, most of the contracts deal with exchange contracts (al-muawadat) that are essentially trading-based activities. Whereas, conventional banking and finance mainly deals with only one contract involving lending and borrowing activities. Settlement of price consideration can be made on the spot (cash) and on a deferred payment basis (credit sale). However, the credit sale has resulted in a lack of consensus (ijma) amongst jurists regarding the validity of selling a debt to a third party. Injustices (zulm), uncertainty (gharar) and usury (riba) are typically the reasons cited by the jurists in order to support their opinions. This paper will look into the validity of the sale of goods and debt, as well as, the problems associated with these two kinds of sale.

Keywords: *Muamalat*, contract, sale, goods, debt.

Introduction

What are the makes differences between Islamic and conventional banking and finance? In Islamic banking and finance, most of the contracts deal with exchange contracts (*al-muawadat*) that are essentially trading-based activities. Whereas, conventional banking and finance mainly deal with lending-based activities.

Most contemporary Islamic finance transactions are done based on the concept of *murabaha*, *ijara*, *mudharabah*, *musharakah*, *sukuk*, *istisna*, *ujr*, Islamic Bills of Exchange, *kafalah*, *hawalah*, Islamic Banker’s Acceptance, Islamic Promissory Notes and Islamic Debt Notes. Some of these are purely sales transactions, while others are in the form of sale of debt (*dayn*). Sale of debt (*dayn*) had contributed considerably to the exponential growth of the Islamic finance market. However, Islamic jurists have differing opinions on the validity of the sale of debt products developed by Islamic Bank that had been practiced worldwide.

The following table summarized Islamic banking and financing products based on concepts and contracts¹:

In order to practice Islam according to true *shari’ah* principles, it is crucial to understand the difference between sale of goods and sale of debt. This paper will analyze the different opinions of jurists relating to sale of goods and sale of debt on selective products. However, this paper does not intend to individually address all the sales mentioned above.

Table 1: Islamic banking and financing products based on concepts and contracts

Deposits	
<i>Wadiah</i>	Current Account <i>Wadiah</i> Savings Account
<i>Mudarabah</i>	<i>Ijraa</i> Savings Account <i>Wadi</i> Savings Account <i>Mudarabah</i> Savings Account Pewani Savings Account General Investment Account

¹ Summary of Middle East and Malaysian Islamic banking practices.

	Special Investment Account <i>Sakinah</i> Investment Account
<i>Bai Dayn</i>	Negotiable Islamic Debt Certificate
Retail Financing	
<i>Bai Bithaman Ajil</i>	Baiti House Financing Land Financing Shop & Shophouse Financing Umrah & Ziarah Financing Tour Package Financing Naqad Overdraft Facility Vehicle Financing Golf Financing Education Financing Negotiable debt certificate-i
<i>Bai Istisna'a</i>	Baiti Home Financing Shop & Shophouse Financing Machinery/Equipment Financing Scheme
<i>Ijarah</i>	Shop & Shophouse Financing Personal Computer Financing Machinery/Equipment Financing Scheme
<i>Bai Inah</i>	Personal Financing Consumer Goods Financing Sell and buy back agreements (Repo-i) Credit card-i
<i>Rahnu</i>	<i>Al-Rahnu</i> Scheme
Trade Financing	
<i>Bai Murabahah</i>	Letter of Credit <i>Murabahah</i> Working Capital Financing
<i>Kafalah</i>	Letter of Guarantee Shipping guarantee-i
<i>Bai Dayn</i>	Islamic Accepted Bill - Import Islamic Accepted Bill - Export

	Islamic Export Credit Refinancing Scheme
Other Services	
<i>Hiwalah</i>	Remittances
<i>Bai Naqdi</i>	Sale/Purchase of Foreign Currency Sale/Purchase of Travelers' Cheque
<i>Ujr</i>	Debit card-I Telebanking ATM service Standing instruction Demand draft Cashiers' order TT/funds transfer

To facilitate the discussion and understanding of the sale of debt issues, this paper will begin with the explanation on the concept of *muamalat* in Islam. Thereafter, the discussion will continue with the general *Shari'ah* principles within the law of transactions (*fiqh muamalat*). These general *Shari'ah* principles are the basis of all contracts in *muamalat*. Subsequently, this paper will focus on the contract of sale. Definition and conditions of sale pertaining to the object or subject matter of sale will be discussed in detail. Finally, this paper will attempt to elaborate the *Shari'ah* compliance issue on the sale of debt with comparison to the sale of goods, such that the contemporary application of sale of debt will also be discussed.

1.1 Objectives of Research

- To define Contract of Sale from an Islamic perspective.
- To explain sale of goods.
- To explain sale of debt (*dayn*).
- To compare sale of goods and sale of debt (*dayn*).
- To analyze the contemporary issues relating to sale of debt (*dayn*).

1.2 *Muamalat*

Islam is not only a “*din*” (religion), it is also a way of life which comprises a set of *Shari’ah* rules relating to *ibadat* (devotional acts), *muamalat* (transactions), *munakahat* (marriage) and *jinayat* (criminal). All activities of a Muslim are guided and governed by these *Shari’ah* principles in order to achieve the five objectives of *Shari’ah* known as *maqasid al-Shari’ah*. The *maqasid al-Shari’ah* are:

- i. Protection of *din* (religion)
- ii. Protection of *nafs* (life)
- iii. Protection of *nasl* (progeny)
- iv. Protection of *aql* (intellect)
- v. Protection of *mal* (property)

For the objective of this paper our focus shall be on matters that fall under the ambit of *muamalat* only. *Muamalat* is an Arabic term that refers to financial or economic transaction. *Muamalat* are matters pertaining to individuals interacting amongst themselves. Various interactions are neither foreseeable nor capable of being complied with a regime of fixed rules. They are also changeable in different eras of time within various geographical entities. In view of this, the *shari’ah* has laid down rules in connection with *muamalat* in general terms so that different people at different places and at different times may seek guidance² from it. Observation and compliance of these rules are crucial in achieving the *maqasid al-Shari’ah*.

2. Contract of Sale

The contract of sale is one of the most crucial contracts for the exchange of goods. Sale in Arabic term is known as *bay* and it refers both to the activities of buying and selling³. It is defined as “an exchange of a useful and desirable thing for similar thing by mutual consent in a specific manner”⁴.

² M. Tahir Mansuri, *Islamic Law of Contracts and Business Transaction*, (2006).

³ Wahbah Al Zuhayli, *Financial Transactions in Islamic Jurisprudence*, Vol 1., (2003)

⁴ Mansuri, op.cit.,187.

Sale is one of the most important financial transactions in Islamic *muamalat*. The evidences on permissibility of it comes from the *Qur'an*, *sunnah* and *ijma'*⁵.

In the *Qur'an*, it states:

“But Allah has permitted trade” [2:275], “But take witnesses whenever you make a commercial contract” [2:282], “But let there be among you traffic and trade by mutual goodwill” [4:29], and “It is no crime to seek the bounty of your lord” [2:198]

In a hadith, it is narrated,

“The Prophet s.a.w. was asked: Which are the best forms of income generation?”. He replied: “A man’s labour and every legitimate sale”⁶, i.e. devoid of cheating or treason. Another saying of Prophet s.a.w. is: “A sale must be by mutual consent”⁷.

Ijma':

Muslims have no doubt that sales are permissible, and it only stand to good sense since it allows each individual to meet his needs in cooperation with others trying to meet their own. Therefore, the general rule in sales (*al-buyu*) is permissible.

2.1 Essentials of Sale

In this section, we shall elaborate briefly on essentials of a sale. More will be discussed in the following sections. The essentials of a sale are as follows⁸:

⁵ Al Zuhayli, op.cit.

⁶ Al-Suyuti, *Al-Jami' Al-Saghir*, cited by El-Gamal, Mahmoud A., “A Basic Guide to Contemporary Islamic Banking and Finance”, (June, 2000), 10, accessed on 15 Oct. 2015, <http://www.nubank.com/islamic/primer.pdf>

⁷ Ibn Majah, *Sunan*, cited by El-Gamal, op. cit., 9

⁸ Liaquat A. K. Niazi, *Islamic Law of Contract*, (Lahore: Dyal Sing, 1991), 176-179.

Table 2: The essentials of a sale

The essentials of a sale	
What constitutes a sale	Offer and acceptance constitute a complete sale.
Who is competent to sell	The parties to all contracts including sale, must have a sense of the obligation of the contract into which they enter.
Minor	A minor cannot contract unless with the consent of his guardian.
Unsoundness of mind	Nor can an unsound person unless during lucid intervals.
Disease	Nor can a person contract to sell who is affected with moral disease.
Four types of sale	Exchange of goods for goods; money for money; goods for money; and money for goods;
When is equality in quantity is must	Where the goods to be exchanged are similar in their nature, such as money for money: equality in quantity is an important condition.
Four denominations of sale	<p>Either absolute or conditional, or imperfect, or void.</p> <p>Absolute sale – that which takes effect immediately: there are no legal impediment.</p> <p>Conditional sale – which is suspended on the consent of the proprietor or on the consent of his guardian, in which there is no legal impediment and no condition requisite to its completion, by such consent.</p> <p>An imperfect sale – which takes effect on <i>seisin</i>, the legal defect being cured by such <i>seisin</i>.</p> <p>A void sale – which can never take effect, in which the goods are opposed to each other or one of them does not possess any legal value; hence the contract is nude.</p>

May be expressed or implied	A sale may be expressed, for example, by the agreement of parties, or implied, as in the case of reciprocal delivery.
Certainty of subject matter	It is important that subject matter of the sale, and the consideration should be so certain and determinate as to admit of no future contention as to the meaning of contracting of parties.
Boundaries	The non-specification of the boundaries of an estate can not invalidate its sale. And it is must that the subject matter of contract should either be in actual existence of the moment of sale, or capable enough to be delivered in a definite time in the future.
Of the consideration	The consideration may include whatever goods, possessing a legal value, the seller and buyer may agree upon, and the <i>mal</i> may be sold for the initial cost or for more or for less than the initial cost.
Of the parties	It is essential that there should be two contracting parties in every sale, except where the seller and buyer employ the same agent or where a father or a guardian makes a sale on behalf of a minor person.
Delay of delivery	In an exchange of goods for goods or of money for money, it is invalid to stipulate a future time of delivery. However, in an exchange of money for goods, of goods for money, such stipulation is valid.
Subject-matter should be in existence	The subject-matter of the contract should be in actual existence at the time of making the contract, and it must be susceptible to delivery, either in an immediate manner or at some definite future period.

Unlawful conditions	It is illegal to stipulate for any extraneous conditions involving a favour to either party, or any uncertainty which might lead to future litigation; however, if the extraneous conditions be actually performed or the uncertainty removed, the contract will hold good.
Delay of payment	When payment is delayed to a future time, it must be determinate, and cannot be suspended on an event, an uncertain time of occurrence, though inevitable. For example, it would be illegal to delay payment the next occurrence of precipitation.
Warranty implied	A warranty as to freedom from defect and blemish is implied in every contract of sale.
When the buyer may breach	Where the property sold differs in quantity or quality from the description given by the tender, the buyer may breach the contract.

According to the majority of jurists, there are four cornerstones (*rukun*) for the contract of sales: seller, buyer, language of contract, and its subject matter (*mal*)⁹. The subject matter will be discussed in detail here.

As a general rule, the subject matter in a contract of exchange should be property (*mal*) that is valuable (*mutaqawwam*) and capable of ownership (*milkiyyah*). Thus, analysis of the concept of subject matter is crucial.

2.2 Definition of Subject Matter (*Mahal al-Aqd*)

According to Hanafi jurists, subject matter involves things that are desired by people and stored for use at the time of need. It does not include benefits and incorporeal rights. The Shafi'i jurists, however, include the benefits and incorporeal rights as subject matter; hence both ownership can be transferred. The Maliki, just as the Hanafi jurists, do not regard benefits and incorporeal rights as subject matter

⁹ Al Zuhayli, op.cit.

and consequently do not allow their sale¹⁰. Zarqa had defined subject matter as everything that has legal and material value amongst people¹¹. The property in this sense refers to any tangible and intangible thing that gives determinate capacity to a person to use to the exclusion of the whole world¹².

2.3 Classification of Subject Matter

Subject matter includes a number of things such as commodity, performance, consideration and object of the contract. In a contract of sale, the commodity is the consideration for the buyer and the price is the consideration for the seller, and the subject matter may be classified into five categories as follows:

2.3.1 Tangible Asset (*Mithliyy* and *Qimiyy*)

Mithliyy relates to asset that have similarities whether physically or according to value and can be easily replaced. It is also known as fungible assets. *Qimiyy* relates to a unique asset that is difficult to be replaced such as antiques. It is also referred to as non-fungible asset.

2.3.2 Usufruct of Asset

Usufruct is the legal right to use and derive profit or benefit from property that belongs to another person, as long as the property is not damaged. According to the Hanafi school of thought, usufruct is not an asset except under three conditions:

- a. Assets that are normally employed for productive purposes such as renting a car and renting air time for broadcasting.
- b. Usufruct from a *waqf* property that was used to generate income for the benefit of society.

¹⁰ M. Tahir, Mansuri, *Islamic Law of Contracts and Business Transactions*, (New Delhi: Adam Publications), 187-188.

¹¹ Al-Zarqa, Mustapha, *Al-fiqh Al-Islami fi Thawhihi Al-Jadid. Al-Madkhal Al-Fiqhi Al-Am*, (Damascus, Dir Al-Fikr, 1967), 1, 260, cited by Mahdi Zahraa and Shafaai M. Mahmor, "Definition and Scope of the Islamic Concept of Sale of Goods", *Arab Law Quarterly*, Vol. 16, No. 3 (2001), 218

¹² Mansuri, op. cit.

- c. Usufruct from an orphanage property that was utilized for the benefit of the orphan themselves.

2.3.3 Work/Labor of Individual

Work or labor of an individual includes the hiring of labor and any contract of work for anyone against a return (wage) like the work of an engineer, doctor, tailor, carpenter, etc¹³. The contract of hiring labor or work is known as *ijarah*. Its permissibility comes from the *Qur'an* [65:6]: “And if they suckle your offspring, give them their due payment”, and Rasulullah (s.a.w) said, “Pay the hired worker his wages before his sweat dries”¹⁴.

2.3.4 Debt or Receivables (*Dayn*)

Dayn is defined¹⁵ as the thing due, such as an amount of money owed by a debtor. It represents the liability of a debtor/buyer/consumer to the creditor/seller/provider. Liabilities may include¹⁶ the price of a purchased object, the compensation for a loan, *mahr* before or after the completion of a marriage, wages compensating for a benefit, indemnity (*arsh*), fines for destruction of property, financial compensation for divorce in favor of the wife, and the object of a deferred sale. Any prospective debt or “unconfirmed” debt cannot be considered as subject matter.

2.3.5 Rights and Privileges

Rights are entitlements or permissions, usually of a legal or moral nature and privileges are a special entitlement or immunity granted by a government or an other authority to a restricted group, either by birth or on a conditional basis. Such that a person has no right to drive without a license, but driving is a privilege given to a driving license holder.

Not all rights are tradable. A right concerning *hadhanah* (guardianship) is not tradable, since it is personal to the holder only.

¹³ Mansuri, op.cit.

¹⁴ Ibn Majah, *Sunan*.

¹⁵ *Majallah al-Ahkam al-Adliyah*

¹⁶ Al Zuhayli, op.cit.

On the other hand, examples of tradable rights might include strata title, water passage, air time, and intellectual Property.

2.4 Conditions of Sale of Subject Matter

There are four specific conditions of sale on subject matter that has been governed by the *shari'ah*. The conditions are as follows:

2.4.1 The Subject Matter must be duly Specified /Known

The subject matter of sale and the price are known beyond dispute and that both contracting parties must be able to identify the subject matter exactly in terms of *al-naw'* (species), *al-jins* (genus), *al-sifah* (attributes) and quantity. It can also be realized by the examination of the subject matter if it is present in the session of contract or by a precise description if it is not available at the time of contract. The descriptions should be detailed enough to avoid all vagueness and uncertainty¹⁷. However Shafi'i jurists do not allow sale by description and stipulate actual examination at the time of the contract as a necessary condition.

2.4.2 The Subject Matter must be Deliverable

All jurists agree that deliverability of subject matter is a must in a contract of sale. Ability to deliver proved that the subject matter, either movable or immovable, is the property and in the actual possession of the seller. Therefore, a sale contract for an animal at large, which the seller cannot pass to the buyer, is invalid¹⁸. Moreover, it is not legal to conclude a contract for performing a job, which is not possible to be accomplished. The reason for this ruling is to escape from any element of risk and uncertainty that can lead to dispute between the contracting parties.

¹⁷ Mansuri, op.cit.

¹⁸ Ibid., 188

2.4.3 The Subject Matter must exist at time of Contract

The Prophet (s.a.w) prohibited the selling of goods, which do not exist. The Prophet (s.a.w) said: “do not sell what you do not have”¹⁹. Example of prohibition is selling of an animal embryo and selling of grains or fruit before they mature. It is not valid to sell the offspring of an animal, what a tree or animal carries, perfume in its container, onions or turnips before extracting them, a folded cloth, or a cloth the weaving of which has not been completed²⁰.

However this rule is not applicable for the *salam* and *istisna* contract because the subject matter does not exist at the time of the contract. *Shari'ah* allows it with strict conditions (by descriptions) such as genus, type, and amount of goods sold, date of delivery, etc. have been determined at the time of contract²¹.

2.4.4 The Subject Matter must be Permissible, *Halal*, Valuable

In Islam, clearly the subject matter of contract must be permissible (*halal*) in accordance with the *shari'ah*. This means it should be pure substance and ritually clean. Therefore, any substance, which is religiously and legally unclean and upon whose disposal there are restrictions, cannot serve as an object of sale, such as wine, pig, intoxicants, blood, and the carcasses of an animal²². Dealing with individuals whose assets are essentially of *haram* origin is not permissible and the sale of an object that is likely to be used for illegal purposes is forbidden by the *shari'ah*.

2.5 Conditions of Sale

According to Wahbah Zuhayli (2001), a sale contract must satisfy four sets of conditions as follows:

¹⁹ Abu Dawud, *Sunan*.

²⁰ Al Zuhayli, op.cit. Condition of Sale for the Hanbalis.

²¹ INCEIF, *Introduction to Applied Shari'ah in Financial Transactions*, (2006).

²² Mansuri, op.cit.

Table 3: Four conditions of sale

Conditions of conclusion	If the conditions of conclusion are not satisfied, then the contract is null.
Conditions of validity	If the conditions of validity are not satisfied, then the contract is invalid.
Conditions of execution	If the conditions of executability are not satisfied, then the contract is suspended and ownership is transferred only if the appropriate permission is given.
Bindingness conditions	If the bindingness of conditions are not satisfied, then the parties to the contract have the option to conclude or nullify it.

The justification behind all those conditions is the avoidance of disagreement and protection of the rights of parties to the contract. Those conditions also eliminate all uncertainty that can lead to excessive risk.

2.5.1 Conditions of Conclusion

The Hanafi jurists have imposed four sets of conditions for the conclusion of a contract²³. The sets of conditions are based on the following:

1. The Contracting Parties

The contractors must satisfy the following two conditions:

- 1) The contractors must be sane and able to run their own affairs, so no contract may be concluded by an insane person or a child who cannot run his affairs²⁴.
- 2) The multiplicity of contractors: A sale may not be concluded by one legal proxy for both parties; except for a father, a legal guardian, a judge or a messenger from both parties. A sale contract induces opposing rights, as related to the delivery and

²³ Al Zuhayli, opt. cit.

²⁴ Ibid.

receipt of goods, the request to deliver the goods and receive the price, the act of returning the goods in case of discovery of defect or the request to exercise a valid option²⁵.

2. The Contract

The only condition in the contract itself is that the offer and acceptance correspond to one another²⁶.

3. The Place of the Contract

There is only one condition here as well, which is that the offer and acceptance are both made during the same session²⁷.

4. The Object of the Contract

The object of the contract must satisfy four conditions as:

- 1) The object of the sale must exist. Therefore, it is not permitted to sell a non-existent object or an object that may cease to exist such as selling the fruits of a tree before they appear, sale of an unborn *animal* in its mother's womb or sale of the milk in a cow's udder, since both of those may cease to exist. The proof of all those conditions is that the Prophet (s.a.w) did not allow the sale of fruit before it was known to be of acceptable quality²⁸.
- 2) The object of sale must be a currently owned and temporarily non-perishable good that may be saved for future use. Therefore, no contract may be concluded for the sale of what may not be owned such as a free man or forbidden foods such as wine, pork and blood²⁹.
- 3) The object must be privately owned by and in the possession of the seller. This excludes the sale of non-owned entities such as grazing grass (even in owned land), uncontained waters,

²⁵ Ibid.

²⁶ Ibid.

²⁷ Ibid.

²⁸ Ibid.

²⁹ Ibid.

wildlife, the sands of the desert and its minerals, sun light, and air.

- 4) The object of the sale must be deliverable at the conclusion of the sale. Therefore, a sale may not be concluded if the object is impossible to deliver, even if owned by the seller such as escaped animals, birds, or fish after having been in the possession of the seller.

3. Sale of Debt

Islam encourages transaction of exchange of goods (subject matter) to be satisfied by cash (spot) sale and/or credit (deferred payment). Cash payment has always been encouraged by *shari'ah*. However, not all contracts can be concluded by cash. Many reasons and purposes had been cited for the delay in making the full payment and it is known best to the contracting parties. *Shari'ah* issues arise when the creditor or seller wish to liquidate the asset (debt receivables) by transferring or selling the debt to the debtor himself or to a third party. All jurists have no objection to selling debt to the debtor himself. However, they have different opinions on selling of debt to a third party. We shall look into the differences and justifications.

“*Dayn*” means “debt” and “*bay*” means sale. “*Bay’-al-dayn*”, therefore, connotes the sale of debt. According to *Majallah*³⁰; *dayn* is defined as the thing due, such as an amount of money owed by a certain debtor. *Al-Dayn* can be either monetary or a commodity. *Bay’ al-dayn* or debt trading or sale of debt can be defined as the sale of payable right or receivable debt either to the debtor himself or to any third party. This type of sale is usually for immediate payment or for deferred payment. After going through the general and specific *Shari'ah* principles on contract of sale, we shall look into the sale of debt and its *Shari'ah* compliant issues.

The *shari'ah* allows the selling of debt by its equivalent in quantity and time of maturity by way of *hawalah*. This form of debt trading is accepted by all schools of Islamic law provided it is paid in full and thus gives no benefit to the purchaser. The reason for this ruling is that financial transactions involving debt should never allow

³⁰ *Majallah*, opt. cit., no.158

deferred payment, as this would be regarded as *riba* or *Bay' al-kali bi al-Kali* which is prohibited by the Prophet (s.a.w)³¹.

According to most Hanafi, Hanbali and Shafi'i jurists, one is not allowed to sell *Al-dayn* to a non-debtor or a third party at all. On the other hand, some Maliki, Hanafi and Shafi'i jurists allow selling of debt to a third party with condition:³²

- 1) The ability of the seller to deliver the debts;
- 2) The debt should be *mustaqir* or confirmed and the contract must be executed on the spot;
- 3) The debt cannot be created from the sale of currency (gold and silver) to be delivered in the future and the payment is not of the same type as debt, and if it is so, the rate should be the same to avoid *riba*.
- 4) The debt should be goods that are marketable, even before they are received. This is to make sure that the debt is not of the food type which cannot be traded to the debtor.

3.1 Sale of Debt to Debtor

3.1.1 First Opinion - Permissible

The majority of jurists from the four schools have ruled as valid the sale of debt to a debtor or forgiving it as gift³³. The creditor has the full right to sell his debt to the debtor at any price he likes as far as the debt is raised from the cost of damage, *qard*, price of commodity, cost of services or dowry of a woman. It is the rights of the creditor to decide on the price as it is he that sells the subject matter in the first instance. This opinion was based on a *hadith* narrated by Ibn Umar:

³¹ Saiful A. Rosly and Mahmood M. Sanusi, "The Application of Bai-al-Inah and Bai-al-Dayn in Malaysian Islamic Bonds: An Islamic Analysis" *International Journal of Islamic Financial Services*, Vol. 1 No.2, (1999)

³² Zaharuddin Hj Abd Rahman, "Rulings On Debt Trading In Shari'ah", *New Straits Business Times*, (21 June 2006), accessed on 16 Oct. 2015, www.kantakji.com/media/8237/169.txt

³³ Al Zuhayli, op.cit.

“One day he came to see the Prophet (s.a.w) and told him: I sell camels in Baqi in *dinars* (debt) and accept *dirhams* (payment), and I sell in *dirhams* (debt) and accept *dinars* (payment). The Prophet (s.a.w) said: There is no harm in it, but you should try to accept it at the current price for each before you conclude your contract.”³⁴

Based on this *hadith* sale of debt to debtor is allowed if it fulfills all conditions of sale.

3.1.2 Second Opinion - Not Permissible

The Zahari jurists ruled that it is not valid to sell a debt to the debtor due to the possibility of *gharar*³⁵. By nature, sale of debt is equal to a sale of uncertainty, hence it is not permissible.

3.1.3 Third Opinion - Depends on Status of Debt

Based on Hanbali jurists, legality of sale for debt to the debtor depends on the confirmation status of the debt. The sale of a confirmed debt to the debtor is allowed based on the same logic given by the majority of jurists. An unconfirmed debt such as the cost of labor or services before completion, dowry of a woman before marital consummation and the capital of *salam* are not allowed because the creditor does not bear the non-confirmed debt³⁶.

3.2 Sale of Debt to a Third Party

3.2.1 First Opinion - Permissible

According to Shafi'i jurists, it is valid to sell a confirmed debt at maturity (*al-dayn al-mustaqirr*) to the debtor or third party before receipt. Their arguments were based on the following³⁷:

- 1) There is no authentic source that forbids such types of selling or giving. Thus it should be allowed and permitted.

³⁴ Abu Dawud

³⁵Hanudin Amin, “An Analysis of the Classical and Contemporary Juristic Opinions on Bay Al-Dayn”, *Labuan e-Journal of Muamalat and Society*, (2007), accessed on 16 Oct. 2015, www.kal.ums.edu.my/ljms/vol1_2007/hanudin_article4.pdf

³⁶ Ibid

³⁷ Ibid.

- 2) A creditor has full rights on possession of debt and full right to sell it to a third party;
- 3) According to a legal maxim, it is permissible, that all transactions are permissible until they are proven non-permissible by an authentic source. So, since there is no authentic source forbidding the transaction, then, it should be permissible.

Examples of such confirmed and matured debts are compensation for destroyed property and monies in the possession of the debtor³⁸. However, the Shafi'i jurists' permissibility is subject to some conditions. If the liability is not confirmed or not currently due (*ghayr mustaqirr*), then,

- 1) If it is of a forward sale (*Salam*), then it is invalid to resell it prior to receipt. This follows from the general forbiddance of selling what one has not received, since the subject-matter of a deferred sale is not certain to be delivered.
- 2) If the liability is a price in a sale contract, then it may be resold prior to receipt. This is based on the narration of Ibn Umar that the Prophet (s.a.w) said: "There is no harm as long as you did not depart with the unfinished business between you".

On the other hand, there is a consensus that the sale of debt in exchange for a deferred debt is not valid in monies, foods and other properties that can result in *riba*.

3.2.2 Second Opinion - Not Permissible

The majority of jurists (Hanbali, Hanafi, some Shafi'i & Zahari jurists) did not allow the sale of debt to a third party regardless of whether the debt is confirmed or non-confirmed. Their opinion is based on a *hadith* of the Prophet (s.a.w), who said, "Do not sell what you do not possess"³⁹.

³⁸ Al Zuhayli, op.cit.

³⁹ Tirmidhi, an-Nasa'i, Abu Dawud

The Hanbali jurists ruled that it is not valid to sell a debt to any party other than the debtor. Moreover, it is not valid to give it as a gift to any party other than the debtor, since a gift necessitates the existence of an identified object (the gift), which is not available in this case. Examples are selling rental of a property prior to the time the rent is due, the dowry of a woman prior to consummation of the marriage or the object of a forward sale prior to receipt.

In fact, the forbidden in the sale of debt is a logical consequence of the forbidden in *riba*. A “debt” receivable in monetary terms corresponds to money, and every transaction where money is exchanged from the same denomination of money, the price must be at par value. Any increase or decrease from one side is tantamount to *riba* and has no room in *shari’ah*⁴⁰.

3.2.3 Third Opinion – Permissible with Strict Conditions

The Maliki jurists allow the sale of debt to a third party subject to eight conditions as follows⁴¹:

The sale must not violate a legal prohibition such as *riba*, *gharar*, etc. Thus

1. The debt must be an item that may be resold prior to receipt (e.g. in the case of loans) and the object of debt must not be food;
2. The price of the sale must be paid immediately when selling a debt for another debt;
3. The price must be of a different genus than the debt or – if it is the same genus – equal to it to avoid *riba*;
4. The price must not be gold if the debt is silver to avoid selling money for deferred money (*riba*).
5. The repayment of the debt must be most likely, e.g., the debtor should be present where the contract is concluded so that his financial condition will be known.

⁴⁰ Abd Rahman, op.cit.

⁴¹ Al Zuhayli, op.cit.

6. The debtor must acknowledge the debt so that he may not deny it later. Thus it is not valid to sell a right under disagreement.
7. The debtor must be eligible to take responsibility for the debt (e.g. he may be underaged or under legal supervision), thus the debt may be deliverable.
8. There should be no enmity between the debtor and the purchaser of the debt so that the purchaser would not be exposed to an additional risk and so that the debtor will not be subjugated to an adversary.

3.3 Resolutions by the Islamic *Fiqh* Academy of Jeddah

The Islamic Fiqh Academy of Jeddah, which is the largest representative body of the *Shari'ah* scholars and is represented by all the Muslim countries, in its 16th convention at Makkah on 5-10 January 2002, discussed the sale of debt and stated that it is prohibited as per the following:

- a. Sale of debts to debtors with a deferred payment plan exceeding the debt amount as this can be considered as *riba al-fadl* and *riba an-nasiah* (*Jadwalah ad-Dayn*).
- b. Sale of debts to a third party with a deferred payment plan whether the debt is paid with the same type of kind or not since this can be considered as a sale of debt with debt (*bai' al-kali bi al-kali* which is clearly prohibited by Prophet Muhammad (s.a.w).

According to the academy, commercial papers such as cheques, promissory notes and bill of exchange are not allowed to be sold at a discount due to the element of *riba*. It is not permissible to deal, issue, distribute or trade with *riba* based bonds because the element of *riba* is present. It is also not permissible to deal with debt notes in the secondary market as it involves discounts and sale of debts to third parties, which contain *riba* elements. The Islamic *Fiqh* Academy proposed a *shari'ah* approved alternative that for the discounted papers and sale and purchase of bonds is sale in the form of goods with the condition that the seller delivers the good during

the *aqad* (contract), with this it is permissible even though the price of the good is less than the value of the commercial paper.

Meanwhile, it is important to recognize and respect the differences in opinion even though the opposite view seems tenuous⁴², especially that involving scholars who are qualified with evidences and interpretations, which are presented in accordance with the correct guidelines associated with *ijtihad* (intellectual effort). Indeed, there is capacity for *ijtihad*, particularly with regard to *fiqh muamalat* issues, as with other aspects of *shari'ah* “matters are determined according to intention”⁴³ and “contract emphasis given to intention and meaning and not to words and phrases”⁴⁴. Nonetheless, as long as there is no *ijma'* (consensus of jurist) that forbids *bay' ad-dayn*, the Prophet (s.a.w) did remark that, “My community will never agree on an error”⁴⁵. Hence, in order to avoid the possibility of an error, given the prevailing differences of opinion, it would be better to avoid *bay' ad-dayn* by, at the very least, exercising caution (*wara'*).

3.4 Summary of Opinion on Sale of Debt

As can be seen in the last section, most jurists agree the sale of debt to debtor. This is because the creditor has every right to release the debtor from the liability to repay debt to him. It is the prerogative of the creditor either to give discount or cancel the debt. There is no room uncertainty (*gharar*).

However, jurists have different views on the sale of debt to a third party (other than the debtor). The differences are due to the issue of risk that might be faced by the purchaser of debt, which opens room for the element of *gharar*, issues concerning ownership (*qabadh*) and *riba*. In view of this, the majority of jurists (Hanafis, Hanbalis, Zaharis and some Shafi'is) do not allow the sale of debt to a third party. Even though some other jurists allow it, some strict conditions had to be applied (eight conditions by Malikis). The conditions imposed by Malikis were meant to distance the sale from

⁴² Abd Rahman, op. cit.

⁴³ *Majallah*, no.2

⁴⁴ *Majallah*, no.3

⁴⁵ Tirmidhi, Ibn Majah, Abu Dawud

gharar, *riba* and prohibited sales such as selling food prior to its receipt.

3.5 Case of Derivatives

Derivatives involve excessive uncertainty. They facilitate to manage certain market risks such as that related to prices, rates of exchange, and so on. Chance remains the basic element in the situation, however, expectations are based on pure speculation. Furthermore, derivatives are also a zero-sum game, unlike the win-win situations in trade involving risk-sharing. The claim that derivatives actually increase liquidity and improve operational market efficiency in financial markets remains unsubstantiated. What can be empirically established is that, whatever the initial benefits for a certain class of investors, availability of derivatives invites speculative activities.

Dusuki⁴⁶ argued that derivative instruments are permissible for hedging purposes only. They are not permissible to use as speculation tools. Moreover, if the current Islamic banking activities follow the conventional activities (where the implied leverage far outweighs bank equity or indeed real output⁴⁷), such that, sooner or later, the Islamic finance industry will also face a financial crisis in the same manner as their conventional counterparts. This paper therefore seeks to analyze derivative instruments, such as futures, as example.

3.5.1 Case of Futures

Futures trading may be said to proceed over deferred and unpaid debts. A debt is normally created by a trader who enters the market either as buyer or seller without any physical exchange of values. The

⁴⁶ Asyraf W. Dusuki, "Shariah Parameters on Islamic Foreign Exchange Swap as Hedging Mechanism in Islamic Finance", University of Leicester, (2-3 July, 2009), accessed on 15 Oct 2015, www.kantakji.com/media/8431/n398.pdf

⁴⁷ Adam Abdullah and Mohd J. Abu Bakar, "The gold Market and the Value of the U.S. Dollar", *International Business Research*, Vol.8, No.3, (2015), 193-194. Abdullah established that J. P. Morgan's implied leverage, in terms of its total notional value of derivatives to equity, was 447:1 in 2010, being 5.33 times the total output of the United States.

debt so originated may subsequently become the subject of an offset or a reverse transaction and a chain of sales and purchases may follow that amount essentially of the sale of debts. The offsetting transaction in futures also consist of sales involving a debt that one party owes to another and settles it through the modality of sale and purchase. Many types of sales have been included under *bay al duyuun* (sale of debts, also known as *bay al kali bi al kali*), and it has been disputed as to whether some of them do in fact qualify as “sale of debts”.

Sale of debt basically envisaged sale over an unpaid debt involving either two, or in some cases, three parties. The basic logic of the prohibition of sale of debt was over uncertainty in its repayment. Furthermore, unfavorable price changes also contribute to uncertainty. The situation is very different in the futures market where technically all transactions are concluded involving guaranteed debts.

Conclusion

Islam encourages transaction of exchange of goods (subject matter) to be satisfied by cash (spot) sale and/or credit (deferred payment). Cash payment has always been encouraged by the *shari'ah*. However, *Shari'ah* issues arise when the creditor or seller wish to liquidate the asset (debt receivables) by transferring or selling the debt to the debtor himself or to a third party. All jurists have no objection to selling debt to the debtor himself. However, they have different opinions on the selling of debt to a third party.