

## The Issues in Islamic Financial Products: Based on the Scientific *Maqasid al-Shari'ah* *Perspective*

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### Abstract

In fact, Islamic financial industry constitutes one important area of Islamic financial transactions (*fiqh al-mu'amalat*). Since its formation in early 1970s, Islamic financial practice has been demonstrating its tremendous progress in offering *Shari'ah* compliant products which eventually becomes a new banking alternative in Malaysian financial system. Even though the Islamic financial practice is compliant with Islamic law (*Shari'ah*), but it is not immune from any controversies and issues. One of these was the divergence of Islamic legal opinion (*ijtihad*) and interpretations of *Shari'ah* among Muslim jurists in assessing *Shari'ah* compliant products. Hence, Islamic financial industry needs to find the ways in which explore the objectives of *Shari'ah* (*maqasid al-Shari'ah*) through the theory of *Maqasid-cum-Masalih* (the objectives of *Shari'ah* for the public interests), towards strengthening the *Shari'ah* compliant products in order to bring the social welfare and justice, among others. *Maqasid* are the key to better understand the *Shari'ah* in its true perspective. Significantly, *maqasid al-Shari'ah* can be seen as the main proxy to cater main proxy to unify the divergence of legal opinion (*ijtihad*) among the Muslim juristconsults (*Usuliyun*) of different schools of law. Therefore, this study discusses issues related to Islamic financial products via the scientific of *Maqasid al-Shari'ah* Perspective, which could be used by the *Shari'ah* scholars as guidelines and source of reference in the assessment with proper solutions to the financial products from *maqasid al-Shari'ah* perspective.

**Keywords:** Maqasid al-Shari'ah, legal opinion (*ijtihad*), Muslim juristconsults (*Usuliyun*), maqasid-cum masalih, Islamic financial transactions (*fiqh al-mu'amalat*), Maqasid al-Shari'ah Framework (MSF)

## 1. Introduction

The theory and application the objectives of the *Shari'ah* or *maqasid al-Shari'ah* started to develop after the era of Prophet's Companions.<sup>1</sup> Significantly, during the first three centuries, the idea of *maqasid* have been discussed and developed by the four Muslim jurists, Hanafi (d. 150 AH/ 767 CE), Maliki (d. 179 AH/ 795 CE), Shafi'i (d. 204 AH/ 819 CE) and Hanbali (d. 241 AH/ 855 CE), in their legal judgments and writings by using different modes of reasoning (*ra'y-ijtihad*), such as analogical reasoning (*qiyas*), juristic preference (*istihsan*), presumption of continuity (*istishab*), public interest (*masalih al-mursalah*), blocking the means (*Sadd al-Dhara'i*), companion's opinion (*Qawl al-sahabi*), earlier scriptures (*Shar' man Qablana*) and custom (*'urf*). In fact, the *maqasid al-Shari'ah* has portrayed several objectives and purposes to be pursued by Muslims in their daily activities which cover many areas of Islamic financial transactions (*fiqh al-mu'amalat*). It have become increasingly significance especially for the purpose of transforming human activities into positive and normative dimensions in this worldly life and the life in the hereafter.

Islamic financial industry constitutes one important area of Islamic financial transactions (*fiqh al-mu'amalat*). Since its formation in early 1970s, Islamic financial practice has been demonstrating its tremendous progress in offering *Shari'ah* compliant products which eventually becomes a new banking alternative in Malaysian financial system. Its philosophy and principles are however, not new, having been outlined in the Holy Qur'an and the Sunnah of Prophet Muhammad (saw) more than 1,400 years ago.<sup>2</sup> Today, Islamic financial has spread to all corners of the globe and received wide acceptance by all everybody concern of Muslims and non-Muslims. Even though the Islamic financial practice is compliant with Islamic law (*Shari'ah*), but it is not immune from any controversies and issues. One of these was the divergence of Islamic Islamic legal opinion (*ijtihad*) and interpretations of *Shari'ah* among Muslim jurists in assessing *Shari'ah* compliant products.<sup>3</sup> For example, the practice of *bay' al-'Inah*<sup>4</sup> contract has gained overwhelming popularity in the South-East Asian region based on Shafi'i's School of law, but not for Hanafis, Malikis and Hanbalis Schools. The question may be raised here with respect to the Muslim jurists' justification in validating certain Islamic financial products.

Due to different interpretations and incoherent Islamic legal methodology on a products development issues among *Shari'ah* advisors, may create confusion among the general public as well as *Shari'ah* regulators, *Shari'ah* scholars and practitioners of Islamic financial industry.<sup>5</sup> As a resulted, it leads another hindrance to the development of the Islamic financial system.<sup>6</sup> Hence, Islamic financial industry needs to find the ways in which explore the objectives of

<sup>1</sup> Raysuni, A. (2009), *Muhadharat fi Maqasid al-Shariah*, Dar al-Salam, p. 46

<sup>2</sup> Government of Malaysia (2011). *Malaysia Banking and Financial Market Handbook: Strategic Information & Regulations*. USA: International Business Publications. Vol. 1. pp. 52

<sup>3</sup> Dusuki, A. W. et al. (2011). *Islamic Financial System: Principles & Operations*. Kuala Lumpur: International Shari'ah Research Academy for Islamic Finance (ISRA). pp. 837

<sup>4</sup> *Bay' al-'Inah* can be defined as a contract which involves sale with immediate repurchase transactions of an asset by the seller. In this transaction, the seller sells the asset to the buyer at a deferred price and subsequently buys back the asset on cash basis at a lower price. It may also be conducted where the seller sells an asset to the buyer on cash basis and then buys back the asset at a deferred price which is higher than the cash sale price. For example, in the standard BBA facilities offered in Malaysia, the client sells the asset to the bank through Property Purchase Agreement (PPA) on cash basis of \$100,000.00 and then the client buys back the asset immediately through Property Sale Agreement (PSA) from the bank at deferred price of \$200,000.00.

<sup>5</sup> Shahaaruddin, A. (2010). *Maslahah-Mafsadah Approach in Assessing the Shari'ah Compliance of Islamic Banking Products*. International Journal of Business and Social Science. Vol. 1 No. 1.

<sup>6</sup> Dusuki, A. W. et al. (2011). *Islamic Financial System: Principles & Operations*. Kuala Lumpur: International Shari'ah Research Academy for Islamic Finance (ISRA). pp. 843

*Shari'ah (maqasid al-Shari'ah)*, towards strengthening the *Shari'ah* compliant products in order to bring the social welfare and justice, among others.<sup>7</sup>

Therefore, there are a number of issues which have been debating among *fiqh* scholars with respect to certain finance products from the perspectives of the objectives of *Shari'ah (maqasid al-Shari'ah)*, especially in debt-based financing contract, such as *Bai' Bithaman Ajil* (BBA) and *Bay' al-Tawarruq*.

## 2. *Bai' Bithaman Ajil* (BBA) Contract

Regarding the debt or asset-based financing, there are issues in relation to *al-Bai' Bithaman Ajil* (BBA). BBA is a sale contract of commodity immediately on deferred price payment basis and payable at a certain particular time in the future.<sup>8</sup> It is also known as *Bay' al-Mua'jal* or *Bay' al-Taqsit*.<sup>9</sup> The Shafi'is, Hanafis, Malikis, Hanbalis, Zayd Ibn 'Ali, al-Mu'ayyad Billah and the majority of Muslim jurists have unanimously ruled it valid to sell an object immediately, with deferred price.<sup>10</sup> This sale is valid as long as the contract is clearly specified and contains no element of ignorance (*jahalah*), such as the subject matter (*mahal al-'Aqd*) must be existing or precisely determined and clearly known when the contract is concluded. The *maqasid* behind this ruling is to avoid any injustice, dispute and harm to the contracting parties. On the legality of BBA, it is reported in one *hadith* that the Prophet (saw) purchased a quantity of grain from a Jew on the basis of deferred payment and he pledged his armour by way of security.<sup>11</sup> This *hadith* shows that the Prophet (saw) did not prohibit the transaction of deferred payment contract, even though the deferred price greater than cash price.

Some of the Muslim jurists consults (*usuliyyun*) have not recognised the BBA as a valid contract, among them are Zainul Abidin Ali Ibn Hussain, al-Nasir, al-Mansur Billah, Hadawiyyah and Imam Yahya.<sup>12</sup> They argue that the BBA contract is a form of mechanism to open the back door to interest based (*riba*) transaction as a legal device (*hilah*), in order to achieve the purposes of illegal or non-*Shari'ah* compliant. This argument based on *hadith* that narrated by Abu Daud from Abu Hurairah said, the Prophet (saw) prohibited two sales in one, which is a sale contract with two different prices that is one price in spot payment with less or same with actual price (*al-aukas*) and the other deferred payment with higher price from the actual price (*riba*).<sup>13</sup> Hence, the BBA contract is a resembles of an interest-based sale (*bay' ribawi*) which is a form of deferment usury<sup>14</sup> (*riba al-nasa'i*).<sup>15</sup>

Those who allow the practice of BBA, they argue this *hadith* is considering the case where the seller makes the single offer: "I sold you for 1,000 cash, or 1,300 in installment" and the buyer says: "I accept", without specifying which of two contracts he wants. In this case, the contract is invalid according to the majority of Muslim Jurists due to ignorance (*jahalah*).<sup>16</sup> Apart from that, a sale with deferred price, which paid in installments are different from *riba*. The

<sup>7</sup> Ibid

<sup>8</sup> Ibid

<sup>9</sup> Ibid

<sup>10</sup> Ibid

<sup>11</sup> Zuhaili, W. (2007). *Al-Muamalat al-Maliyyah al-Muasarah*. 4<sup>th</sup> ed. Damsyik: Dar al-Fikr. pp. 318

<sup>12</sup> Nil Authar, Vol 5, pp. 152; *Subulu al-Salam*, Vol 3, pp. 16

<sup>13</sup> Nil Authar, Vol 5, pp. 152

<sup>14</sup> Meaning: The increase on immediately price ( وهو علي الثمن الحال الزيادة )

<sup>15</sup> Zuhaili, W. (2007). *Al-Muamalat al-Maliyyah al-Muasarah*. Beirut: Dar al-Fikr.

<sup>16</sup> Al-Zuhayli, W. (1997). *al-Fiqh al-Islami wa Adillatuhu*, 4<sup>th</sup> ed, (Vol. 5), p. 3461; Al-Zuhayli, W. (2007). *Financial Transactions in Islamic Jurisprudence*, ed. Al-Gamal, M. & Eissa, M. 2<sup>nd</sup> ed., Dar al-Fikri, Dimashq, Syria, p. 120

different is that Allah has permitted sales and has prohibited *riba*.<sup>17</sup> In another word, the increment of price is allowed in case of deferment of price in a sale contract. The increase of price is permissible because it is against the commodity and not against money. The BBA contract is only considered to be amounting to *riba* where the subject matter is money on both sides. Hence, this contract is not *riba*, but it is tolerance (*al-tasamuh*) and ease (*al-taisir*)<sup>18</sup> in sales, since the buyer receives the merchandise, and not money. Therefore, BBA is a valid contract because of necessity (*darurah*) for the society which provides *maslahah* to them in dealing with Islamic Financial transactions (*Fiqh al-Mu'amalat*).

BBA is the second most popular mode of Islamic financing practiced by financial institutions in Malaysia, especially in housing financing. According to the Bank Negara Malaysia (BNM) report in December 2016,<sup>19</sup> total financing given by Islamic banking institutions based on the BBA (deferred payment sale) contract around RM Million 69,408.9, constituting 16% of total financing. In Malaysian practices, BBA has been referred to as the sale and purchase transaction for the financing of an asset on a deferred and installment basis with a pre-agreed payment period. BBA financing facility is applied over property under construction as well as completed property. As for the completed property there are no problem arises due to the fact that existing property can be sold by any form of permissible contract. As for the property under construction, there is an issue which coursed the divergence opinions of *fiqh* scholars whether the BBA contract is valid or vice-versa. Partly, in BBA financing for house under construction, the property as a subject matter of the contract is non-existence. If the opinion of the majority of Muslim jurists is to be applied, the BBA facility on property under construction is not allowed and also contrary to the actual definition of BBA. This was based on the *hadith* of the Prophet (saw) which prohibited a sale of an unborn baby camel and a sale of a non-existing object, due to the uncertainty (*gharar*) of delivery.<sup>20</sup> The element of uncertainty is forbidden, where the Prophet s.a.w. was forbade the sale of uncertainty (*gharar*).<sup>21</sup> For example, abandoned housing projects under BBA contract will lead to occurrence of exorbitant uncertainty (*gharar al-fahish*) elements. This element typically causes enmity, dispute, hardship, injustice, which is contradicted to the public interest (*maslahah*) as well as the objectives of *Shari'ah* (*maqasid al-Shari'ah*).

However, Ibn Qayyim and his teacher Ibn Taimiyyah from Hanbalis School allowed the selling of non-existent subject base on the certainty (*muhaqqiq*) of subject matter in the future delivery.<sup>22</sup> They base their opinion on the lack of any prohibition of the sale of that which is not mentioned in the Qur'an or the Sunnah. What was narrated in the Sunnah is the prohibition of sales with excessive risk and uncertainty (*gharar*), where the object may be undeliverable. Therefore, if the objects can be assured of their future existence with certainty through specific laws or legal provisions that guaranteed the removal of the element of uncertainty, then the contract is permissible. If some quarters argue that the current practice of BBA in Malaysia is for the public interest (*maslahah*) and necessity (*darurah*), the question may be raised as to whether this arguments are in conformity with the objectives of *Shari'ah*

<sup>17</sup> Al-Baqarah, 2: 275

<sup>18</sup> Al-Quran, 2: 185 (يريد الله بكم اليسر ولا يريد بكم العسر) = "God wills that you should have ease, and does not will you to suffer hardship".

<sup>19</sup> Sources: Statistics of Bank Negara Malaysia

<sup>20</sup> Al-Zuhayli, W. (1997). *al-Fiqh al-Islami wa Adillatuhu*, 4<sup>th</sup> ed, (Vol. 5), p. 3398

<sup>21</sup> Al-Nawawi. (1392). *Al-Manhaj Sharah Muslim bin al-Hajjaj*. Beirut: Dar Ihya' al-Turath al-'Arabi. Vol. 10. pp. 156.

<sup>22</sup> Al-Zuhayli, W. (1997). *al-Fiqh al-Islami wa Adillatuhu*, 4<sup>th</sup> ed, (Vol. 5), p. 3398; Al-Zuhayli, W. (2007). *Financial Transactions in Islamic Jurisprudence*, ed. Al-Gamal, M. & Eissa, M. 2<sup>nd</sup> ed., Dar al-Fikri, Dimashq, Syria, p. 76

(*maqasid al-Shari'ah*) or vice versa. Regarding the delay in delivery that has caused a lot trouble to the house buyers, consequently would give harm of well-being, rights and cannot ensure satisfactory outcomes, justice, and fairness in their contractual dealings.

### 3. *Bay' al-Tawarruq Contract*

Another issue is regarding the permissibility of the *bay' al-tawarruq* among the Muslim jurists. *bay' al-tawarruq* is the transaction where a person buys a commodity with a deferred payment, then sells it to a third party (other than the original seller) for an immediate cash price.<sup>23</sup> It is also known as the *tawarruq* on an individual basis (*al-tawarruq al-fardi*) and the classical *tawarruq*. This transaction is called *tawarruq* because when the purchaser bought the commodity with deferred payment, he has no intention of using or getting benefit from it, but merely to facilitate him to obtain cash. In the current practices of Islamic financial institutions (IFIs), *bay' al-tawarruq* is also termed as the banking *tawarruq* (*Al-tawarruq al-masrafi*) or the organised *tawarruq* (*Al-tawarruq al-munazzam*). It is a process where the IFIs formally organises the sale of commodity (other than gold or silver) between an (international commodity market or others market) and the client (*al-mutawarriq*). For example the client buys a commodity on deferred payment from the IFI. The IFI will represent the *mutawarriq* in selling it to another buyer (International commodity market or others market) for cash, whereupon the bank will deliver its payment to the *mutawarriq*.<sup>24</sup>

Generally, the majority of Muslim jurists of the Hanafis, the Shafi'is, the Malikis and the Hanbalis consider *bay' al-tawarruq* as a valid and acceptable contract of Financial transactions in Islamic jurisprudence. Their argument is based on a Qura'nic verse in which "*Allah has permitted sale and forbidden usury (riba)*".<sup>25</sup> Hence, in their views, *tawarruq* is a form of a valid 'sale contract' which fulfill all necessary requirements of a sale contract and there was no specific evidence to prove otherwise. In the form of reasoning method, the permissibility is required to fulfill the needs of people (*hajiyyat*) and provide sufficient liquidity (cash money) through lawful means as approved by the *Shari'ah*, and it is extremely effective in realising the objectives of *Shari'ah* (*maqasid al-Shari'ah*).

However, the Ibn Qayyim and his teacher Ibn Taimiyyah of the Hanbalis School have prohibited the *bay' al-tawarruq* because it is a means which lead to usury (*riba*) transaction and evil act (*mafsadah*). In a *tawarruq* contract, in their view, the transaction involves the exchange of immediate cash (less amount) for deferred payment (larger amount) of money.

The issue becomes more complicated when the Islamic bank applied banking *tawarruq* (*Al-tawarruq al-masrafi*) which also known as organised *Tawarruq* (*Al-Tawarruq al-Munazzam*). The practice of this product has been declared invalid and unacceptable by a recent declaration of the Organisation of Islamic Conference (OIC) *Fiqh* Academy, in April 2009.<sup>26</sup> In the real practise of Islamic financial institution, the financier arranges the sale agreement either himself or through his agent. Simultaneously, the *mutawarriq* and the financier

<sup>23</sup> Ibid, p. 117

<sup>24</sup> Dusuki, A. W. & et al. (2011). *Islamic Financial System: Principles & Operations*. Malaysia: International *Shari'ah* Research Academy for Islamic Finance (ISRA). pp. 227

<sup>25</sup> The Quran, 2: 275

<sup>26</sup> The International Council of Fiqh Academy, which is an initiative of the Organization of Islamic Conferences (OIC), in its 19th session which was held in Sharjah, United Arab Emirates, from 1 - 5 of Jamadil awwal 1430 AH, corresponding to 26 – 30 April 2009. [The resolution in English translation](#) is available at [www.isra.my](http://www.isra.my).

execute the transactions, usually at a lower spot price. In this case, the (*mutawarriq*) is the financial institution, and it acts as a client. Hence, according to the resolution 179 (19/5) by the *Fiqh* Academy, it is not permissible because simultaneous transactions occur between the financier and the *mutawarriq*, whether it is done explicitly or implicitly or based on common practice, in exchange for a financial obligation. This is considered a deception, i.e. in order to get the additional quick cash from the contract. As indicated earlier, this transaction is a quick similar to *bay' al-'inah* and containing *riba*, whereas the majority of Hanafis and Malikis scholars have prohibited *bay' al-'inah*.

Based on the above resolution, the Islamic financial institutions are required to avoid all dubious and prohibited financial techniques, in order to conform to *Shari'ah* rules so that the techniques are in conformity with the objectives of the *Shari'ah* (*maqasid al-Shari'ah*). In analyzing the used of the objectives of *Shari'ah* (*maqasid al-Shari'ah*) on *bay' al-tawarruq* contract in Islamic banking, Siddiqi applied the approach of *maslahah-mafsadah* calculus.<sup>27</sup> In his analysis, he discovered that the harmful consequences of *bay' al-tawarruq* are much greater than the benefits.<sup>28</sup>

However, the proponents of *bay' al-tawarruq* argue that the contract of *bay' al-tawarruq* is important modes of transaction in resolving their basic needs (i.e. to purchase houses, vehicles and other needs). They claimed that the *bay' al-tawarruq* contract could be applied as an alternative sale needed contracts (*al-hajiyah*) without resorting to *riba*-based transaction. The acceptable of *bay' al-tawarruq* contract is also seen as the act of choosing between the lesser of two evils: between *riba* which is explicitly prohibited and *bay' al-tawarruq* which is disputed. The decision to take a lesser harm action is supported by a *fiqh* maxims (*qawa'id al-fiqhiyyah*) which states "a greater harm is eliminated by means of a lesser harm" (*yuzal al-darar al-ashaddu bid-darar al-akhaf*). Therefore, this argument is rationally acceptable and in conformity with the objectives of *Shari'ah* (*maqasid al-Shari'ah*).

#### 4. Conclusion

Based on the above discussion, the ultimate purpose of the objectives of *Shari'ah* (*maqasid al-Shari'ah*) is nothing but for the seeking of benefit and repelling of harm (*jalb al-manfa'ah wa daf' al-madarrah*) in order to bring the social welfare and justice of human-beings. However, there are a number of issues regarding few of Islamic financial products, which created confusion among members of the general public as well as *Shari'ah* regulators, *Shari'ah* scholars and practitioners as to whether those issues are in conformity with the objectives of *Shari'ah* (*maqasid al-Shari'ah*) or vice versa. Since each school of law has its own modes of legal reasoning (*ijtihad*) in resolving certain issues related to Islamic Financial transactions (*Fiqh al-Mu'amalat*), the contemporary Muslim jurists of the four major schools of law are not unanimous in their deduction of *fiqh* rulings (*ahkam al-fiqhiyyah*) and occasionally reached different perspectives on Islamic financial products.

<sup>27</sup> Siddiqi, M. N. (2007). *Economics of Tawarruq, how its mafasid overwhelm the masalih*. Paper presented in Workshop on *Tawarruq* and its methodological issues, London: London School of Economics.

<sup>28</sup> Ibid. This is based on the fact that *Bay'al-Tawarruq* is manipulated by Islamic banks to create debt instruments. Siddiqi opposes the excessive of debt creation instruments in governing Muslim financial affairs. He warns the creation of debt market instruments under the banner of Islam. This is because the market of debt instruments created through the application of *Bay'al-Tawarruq* will inherit similar problems of the capitalist economic system (i.e. speculation activity, inefficient allocation of funds and inequitable wealth distribution). He contends that the application of *Bay'al-Tawarruq* will broaden the dichotomy between the theory and practice of Islamic economic, therefore should not be pursued.

It is because in the development of the Islamic financial system, so far there was no specific analysis and discussion on a well-defined *maqasid-cum-masalih* theory of previous writings of the Muslim jurists and the Muslim scholars. Therefore, it is a necessity to study and analyse a views and legal opinions on the theory of *maqasid-cum-masalih* (the objectives of *Shari'ah* for the public interests) in order to become more easier as its dynamic *ijtihadi* model and could be used by the *Shari'ah* scholars as guidelines and source of reference in the assessment with proper solutions to the financial products from *maqasid al-Shari'ah* perspective.

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