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Murabaha, Sales of Trust, and the Money-value of Time

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ABSTRACT

It is estimated that *murabaha* contracts constitute nearly 70% of all financing in Islamic banks.[i] Yet, despite its popularity and utility, *murabaha* remains controversial in Islamic financial circles because it appears to accord a money-value to time, which would be a form of the prohibited *riba* or, more precisely, *riba al-nasi'ah*. If the rationale for Islamic banking stems from the desire to make the services provided by banks available to practicing Muslims through banking practices that avoid *riba*, it follows that *murabaha* must be eliminated. This line of reasoning that has led many *Shari'ah* scholars, investors, and shareholders in Islamic banks to question the *murabaha* transaction. While some defend *murabaha* as a concession to modern banking exigencies, couching their defense in legal terms like *darura* or necessity, it may be possible to approach this matter through a study of its *'illa* or ratio legis.

I. INTRODUCTION

If the numbers indicate anything about Islamic banking, it is that an exciting chapter in the religious, cultural, and intellectual life of Muslims is opening.[ii] The relatively new field of Islamic economics and banking is particularly challenging for the reason that it brings together scholarship from jurists, economists and finance professionals. Realistically speaking, however, there is much about this novel interdisciplinary field that is not well understood, even at the conceptual level; and a great deal of groundwork still needs to be done. The problem at the present time, if we seek to reduce the matter to its lowest common denominator, is that scholars from both fields bring their own intellectual and disciplinary predilections to their understanding of the new phenomenon, and these are often at theoretical loggerheads.

For example, many Muslim jurists are reluctant to exercise any sort of independent thinking on economic issues, preferring instead to rely on the scholarship of past ages. Thus, their response to new questions is to locate in the classical legal literature questions of a similar nature, through the liberal use of what may at best be termed "rough" analogy, and then to graft the old solutions prescribed there to the questions at hand.[iii] In contrast to the literalist and traditionalist orientations of many Muslim jurists, our economists have suffered from a lack of Islamic contributions to their field. A former official of the State Bank of Pakistan asserts that Muslims writing on economics often apply western standards in proposing their "Islamic" models. "Let us admit that we Muslims are oriented in western theories of economics and are apt to believe them to be a fair standard of judging policies and decisions."[iv] Moreover, in their inability to appreciate *Shari'ah* principles and purposes, many Muslim economists appear in their thinking to assume that the only purpose of *fiqh* is to regulate and facilitate economic activity. At a very fundamental level, they would endow *homo Islamicus* with the same traits as the neoclassical *homo economicus* whose primary motivation is utility and precious little else.[v]

In modern times the appearance of serious thought, from an Islamic perspective, on the subject of economics coincided closely with the emergence of Muslim nation states following the colonial experience. This occurred at a time when Muslims sought not only to repair their ailing economies, but to reestablish their cultural and religious identities as well.[vi] Gradually, the ideas generated by this preliminary thinking led some Muslims to speak in terms of "Islamic economics," and a respectable body of literature on the subject (however tentative) appeared in several different languages, especially in Arabic, English, Persian, and Urdu, with significant contributions by both Muslim economists and jurists.[vii] Clearly, these works contributed to the establishment of Islamic banks as the most immediately achievable manifestation of the desire on the part of Muslims for working models of an "Islamic" economic system. The success of the first handful of Islamic banks, particularly in the decade of the seventies, led to the growth in the next decade of Islamic banks and banking all over the Muslim world. Today western economists are busy studying the potential impact of Islamic banking on economic

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relationships, as well as some of those aspects of Islamic banking which have met with success and show promise as profitable alternatives to established norms.[viii]

If I may venture a prediction of my own, the work of economic historians will become increasingly important as their studies begin to inform the thinking of Muslim economists, financiers, and jurists, further increasing the complexity of the interdisciplinary mix, and further emphasizing the inadequacy of present classifications to encompass this fascinating new field. No doubt, the economic history of Muslims is fraught with lacunae;[ix] and there is much in our past that may be of relevance to the economic activity of our future. In particular, the ways in which Muslim scholars, especially the jurists among them, wrestled with problems of credit, trade, and production in the centuries prior to the depredations of the colonial powers may have much to tell us about how these issues may be dealt with today. Until recently, this has been a subject that failed to gain the attention of Muslim jurists, owing perhaps to their preoccupation with the classical period and its texts, so that many legal scholars remain in the dark with regard to the practices and strategies developed in the recent legal past.[x] Indeed, the point has been made, and it seems a valid one, that we are dealing with an interrupted process. Between the "medieval" and "modern" forms of Islamic banking transactions, as described by Nicholas Ray in his work on Islamic banking, there lies a historical hiatus of as yet undetermined proportions and significance.[xi]

II. *MURABAHA*

One of the areas of chief concern in the operations of Islamic banks at present has been identified as trade financing or, in its particularly Islamic form, *murabaha*. In recent years *murabaha* has been challenged as suspect from an Islamic legal perspective by shareholders and *Shari'ah* boards alike. I should like, therefore, to make a few brief observations on the aspect of the *murabaha* transaction that has led to misgivings concerning this important transaction.

Murabaha, essentially a form of deferred payment sale, has been described as "interest-like" owing to its implied acceptance of the time value of money.[xii] Certainly, this is an engaging aspect of *murabaha* as an Islamic transaction, particularly in light of the well known prohibition in Islamic law of *riba*, or interest, for, as Abdullah Saeed points out, "accepting the time value of money logically leads to the acceptance of interest," or *riba al-nasi'ah*.[xiii] Thus, despite its utility and its popularity, many Muslim investors and shareholders view *murabaha* as a suspect operation. In order to clarify this matter, it will be necessary to review the jurists' classification of *murabaha* as a sale of trust, and their arguments for its legitimacy as an authentic and sound Islamic transaction.

III. SALES OF TRUST

Let us begin by looking at a specialized dictionary entry on the subject of *amana* sales, or sales of trust:

> "The classical jurists categorized sales, with regard to the way prices are determined, as either sales in which trust, *amana*, is the key element, or sales in which bargaining, *musawamah,* is the key element. Sales of bargaining are sales in which the seller does not disclose the amount of his investment in whatever he is offering for sale. In such a sale, both parties will agree to transact for a certain price, without the seller's disclosing to the buyer the price he originally paid for the goods or whatever it is he is offering for sale. Ibn Jazzi, the Maliki jurist, defined *musawamah* as "the buyer's negotiating with the seller over a price until they come to an agreement on it, without there ever being mention of how much the seller originally paid for the goods." In sales of trust, however, the price is specified as being the same as the seller's investment, or more, or less. Such sales are called sales of trust because the seller is to be taken at his word when he informs the buyer what he paid for the goods for sale."[xiv]

Let us continue by considering the meaning of trust, or *amana* in sales of this nature. According to Professor Shacht, "The main consideration in all such sales is the exclusion of dishonest, unjustified enrichment."[xv]

We may now turn to another encyclopedia entry for the purpose of furthering our understanding of *amana*.

> The lexical meaning of *amana* or trust is the opposite of betrayal, and it denotes any legal responsibility charged to a person, including acts of worship or entrusted property. The classical jurists, however, used the word in two ways; as a noun, and as an adjective. The meaning of trust, as a noun, is that which is kept with a trustee. As an adjective, the term is used to denote trust sales, like *murabaha*, in which the purchaser depends on the conscience of the seller and trusts his/her truthfulness. The Almighty stated in the Qur'an: *O you who believe! Do not be false to Allah and His Prophet, and do not knowingly be false to the trust that*

> *has been reposed in you* (8:27). Moreover, the Prophet, upon him be peace, said, "He is not one of us who attempts to cheat us." This *Hadith* was related by Muslim, Abu Dawud, and Ibn Majah, from Abu Hurayrah.
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> It is for this reason that if any sort of misrepresentation should be discovered in a *murabaha* sale, the buyer would have the option to retain the goods he/she purchased, or to return them. Some scholars have added that the buyer will have the further option to subtract from the price whatever extra amount was falsely reported as the original purchase price, and then to subtract a corresponding percentage from the agreed upon margin of profit. Details of the same may be seen in Kashani, 5/223, Ibn Qudamah 4/203, Dasuqi 3/164, and Nawawi, *al Muhadhdhab*, 1/295.[xvi]

To elaborate further, sales of trust are of three kinds, *murabaha*, *tawliyah*, and *wadi'ah*. *Tawliyah*, in the terminology of the jurists, refers to a sale in which the value of the goods as represented by the seller is itself set as their price, with no profit or loss. As such, *tawliyah* may also be understood as resale at the stated original cost. The classical jurists therefore define *Tawliyah* as the transfer of goods in their entirety from the seller to the entrusted by means of the words, "I entrust you," or the like, without increase or decrease. This is resale at the stated original cost. *Wadi'ah* refers to a sale in which the price is set at less than what the seller says is the value of the goods, or resale with a rebate on the stated original cost. *Murabaha* is resale with a stated surcharge that represents the profit.[xvii]

IV. The Rationale for *Murabaha*

But beyond this simple definition, *murabaha* sales perform a further function. Indeed, "*murabaha* is a form of commission sale, where a buyer who is usually unable to obtain the commodity he requires except through a middleman, or is not interested in the difficulties of obtaining it by himself, seeks the services of that middleman."[xviii] What must further be added, however, is the element of trust. The middleman performs a dual service, he facilitates the financing of a deal, and he does so in such a manner that even the most naive of consumers may rest easy with regard to the value he is receiving for his money.[xix]

This last point is an intriguing one, and one that deserves further consideration. The classical jurists were careful to trace every transaction they described and regulated to a clearly Islamic origin, thereby to establish the transaction as one that had the approval of the Almighty. Thus the manuals of *fiqh* and their glosses are sure to begin their discussions of every new form of transaction by establishing Islamic authenticity, or justifying licitness or otherwise, through reference to the Qur'an, the *Sunna*, consensus of the community, and/or the practice of the Caliphs or early Companions.[xx] In a very few cases, however, the only sort of recourse available was to the practical grounds of its economic function in society. Apparently, and despite the best efforts of the jurists to find a more sacred source for it, *murabaha* falls under this last category.

V. The Islamic Authenticity of *Murabaha*

In the main, the legal evidences or indicators variously adduced by the classical jurists for the legitimacy of the *murabaha* transaction are clearly general in nature and not at all specific to *murabaha*. Consider, for example, the following evidence cited for the legitimacy of the *murabaha* transaction, found in nearly all the *fiqh* manuals:

> And when the prayer is ended, disperse freely on earth and seek to obtain [something] of Allah's bounty (62:10).

In a very general manner, this verse establishes that it is lawful for people to go out in the world and earn their living. Such generalized permission may suffice as proof that trade and commerce are sanctioned by the Almighty; but there is clearly nothing there about the specifics of how one might, or should, go about seeking the bounty of Allah. There is certainly nothing in the verse about *murabaha*. The same is true of the other verses cited by the jurists in support of this transaction.

> He it is who has made the earth easy to live upon: go about, then, in all its regions, and partake of the sustenance that He provides (67:15)
>
> Allah has made buying and selling lawful (2:275)

The *Hadith* literature presented by the jurists for the same purpose is equally imprecise and inclusive. For example, the *Hadith* related by Tabarani: *Seeking the lawful is the duty of every Muslim.* Or the *Hadith* related by Muslim, Abu Dawud, Tirmidhi, Nasa'i, and Ibn Majah: *If the two [countervalues] are of different kinds, then sell as you like, provided that the deal is hand to hand.* Or, finally, the *Hadith* related by Ibn Hibban and Ibn Majah: *Verily, a sale is what takes place when there is mutual agreement.*

Several of the jurists appealed to *ijma'* as the justifying factor.[xxi] An interesting twist to the same was claimed by Badr al Din al 'Ayni, in his commentary on *al Hidayah*, in which he explained that *murabaha* is lawful:

> … because the item for sale is known, and so is the price. People deal in it without anyone's objecting to it. And when people deal in something without objecting to it, that is proof in itself of its validity because the Prophet, upon him be peace, said, 'What is considered becoming by the Muslims is considered becoming by Allah.'"[xxii]

In the classical Islamic hierarchy of evidence, the indicators, *adillah*, from the Qur'an, the *Sunna*, and the *ijma'* are the ones that carry the most weight. It should be clear from the foregoing, however, that the proofs adduced from those sources are hardly specific to *murabaha*, and thus quite open to challenge. Clearly, the jurists had to rely on other evidence from other sources in order to establish the lawfulness of this particular transaction. In other words, while the jurists did cite evidence from the Qur'an and the *Sunna* in support of *murabaha*, the evidence itself is in no way specific to *murabaha*. Moreover, while the root of the word *murabaha*, r-b-h, is used in the Qur'an,[xxiii] the transaction known as *murabaha* is nowhere mentioned in the Book of Allah. Likewise, no specific mention of the transaction is to be found in even the weaker *Hadith* literature. In other words, the most pertinent and substantial indicators for the legitimacy of the *murabaha* transaction are the ones accorded the least weight of all by the jurists.

VI. OTHER CONSIDERATIONS IN THE LEGITIMACY OF *MURABAHA*

Burhan al Din al Marghinani (d. 593AH), in his work *al Hidayah fi Sharh al Bidayah*, the mainstay of latter Hanafi *fiqh* scholarship, first has recourse to legal principle when explaining the legitimacy of *murabaha*: "It is lawful owing to its meeting all the conditions for validity," (*ja'iz li istijma`i shara'it al jawaz).* Thereafter, his commentator, Ibn al Humam noted,

> Since more than just the meeting of conditions is required to establish legitimacy, the author further mentioned the occasioning factor by saying, 'There is a great need for this sort of dealing because one inexperienced in the ways of business will have to depend on those more experienced, and be satisfied with paying as much as the more experienced one has paid, plus an additional amount of profit. This is why it is essential to term these sales lawful.' It should be clear that there is no need for proof of their legitimacy beyond the proof establishing the legitimacy of sales in general when there is mutual agreement and there is nothing to interfere with the conditions for a valid sale. Rather, the proof of the legitimacy of sales in general is the proof of the legitimacy of *murabaha* and *tawliyah*.[xxiv]

Here, what the commentator means when he refers to "meeting conditions" is that it is not enough for a transaction to fulfil the prescribed legal formula of there being a buyer, a seller, an object for sale, an offer by the seller, and an acceptance by the buyer. These are the elements of a transaction deemed essential by the classical jurists. However, just because these elements are present, it does not automatically follow that the transaction will be lawful. All of these elements, for example, are present in usury; and Allah has declared usury unlawful.

In addition, then, al Marghinani had to offer more convincing evidence for the legitimacy of this particular transaction, *murabaha*. That is why he mentioned the occasioning factor, or *'illa*. The classical jurists explained that while there are no occasioning factors in matters related to worship, *ibadat*, because these are related to the inscrutable will of the Almighty, there are always occasioning factors in transactions, *mu'amalat*, because these are related to the worldly interests of humans.[xxv] They further explained that the benefit of occasioning factors is that they facilitate an understanding of *Shari'ah* rulings and categorizations by clarifying cause and effect relationships in the law. If a feature can be shown to constitute the occasioning factor behind a ruling in a principal case, then it becomes relatively easy to establish the same ruling in a novel case with the same feature.

What al Marghinani and his commentators, both Ibn Human and Badr al Din al 'Ayni, appear to be attempting, however, is to provide a rationale for the transaction; thereby establishing its ethical and Islamic legitimacy. Not all jurists, however, held that a rationale, or *hikmah*, could function as an *'illa* or occasioning

factor.[xxvi] That they resorted to this sort of justification is indicative of the difficulties they had with the transaction and its apparent according of a money value to time.

VII. CONCLUSION: REVISITING THE SOURCES

These efforts on the part of the jurists were expended in the attempt to legitimize a transaction they recognized as essential to the success of the marketplace in their times. To my mind, the recourse by the classical jurists to a rationale for *murabaha* was essentially the same as recourse to *maslaha* or the public interest. Of course, not all the classical jurists held *maslaha* to be a valid indicator; and that may well explain the approaches taken by the Hanafi jurists mentioned here.

What may be deduced here, however, is that *murabaha*, in its protecting the innocent consumer, actually assigns a money value to trust rather than to time. The same is true of the other two sales of trust, *Tawliyah* and *wadi'ah*, where there is no increase, because there is a value to knowing, and to being able to trust that knowledge. Seen from this perspective, *murabaha* contains nothing that could be considered grounds for prohibition or legal disapproval, *karahah*. On the contrary, such an appreciation of the value of trust[xxvii] is key to the understanding of Islamic contractual justice in general.[xxviii] When dealing with the challenges of modern financial practice, it may be noted that consideration of such factors may well lead to a new appreciation for the *Shari'ah*.

[i] Nicholas Dylan Ray, *Arab Islamic Banking and the Renewal of Islamic Law* (Graham & Trotman: London, 1995) p. 37.

[ii] Today there are over 187 Islamic banks worldwide, with 271,000 employees in upwards of 21,000 branches. For an excellent overview of the current situation, see Samir Abid Shaikh, "Islamic Banks and Financial Institutions: A Survey" *Journal of Minority Affairs*, Vol. 17, no. 1, 1997 pp. 117-127

[iii] A few examples of such "grafting" may even be found in the pages of this work.

[iv] Hassanuzzaman, "Defining Islamic Economics" *Journal of Islamic Banking and Finance*, vol. 14, Jan-Mar 1997, no. 1, p. 13.

[v] Waleed El-Ansary, "The Spiritual Significance of Jihad in Economics," *The American Journal of Islamic Social Sciences*, Vol. 14, No. 2, Summer 1997, pp. 230-263. El-Ansary writes: "... Islamic economics should be seen as applied ethics, an examination of policies and institutions in terms of *homo Islamicus*' inner and outer jihad - his efforts to integrate the economic aspects of life around a Sacred Center."

[vi] See the entry on Banking by Rodney Wilson in *The Oxford Encyclopedia of the Modern Islamic World* edited by John Esposito (New York: Oxford University Press, 1995), vol. 1, pp. 191-195. See also Abdullah Saeed, *Islamic Banking and Interest: A Study of the Prohibition of Riba and its Contemporary Interpretation* (Leiden: E. J. Brill, 1995) pp. 8-16.

[vii] For one of the best surveys of literature on the subject, see M.N. Siddiqi, *Muslim Economic Thinking* (Leicester, UK: The Islamic Foundation, 1981).

[viii] See, by way of example, the study of financier remuneration embodied in *mudaraba* by John Presley and John Sessions, "Islamic Economics: The Emergence of a New Paradigm" *Economic Journal*, vol. 104, no. 424, May 1994, pp. 584-596.

[ix] Nicholas Dylan Ray, "The Medieval Islamic System of Credit and Banking: Legal and Historical Considerations," *Arab Law Quarterly*, Vol. 12, Part 1, 1997, p. 44.

[x] S. E. Rayner, *The Theory of Contracts in Islamic Law,* (UK: Graham & Trotman, 1994), pp. 274-276.

[xi] Nicholas Dylan Ray, *Arab Islamic Banking and the Renewal of Islamic Law* (UK: Graham & Trotman, 1995). I should further explain that there are two aspects to the hiatus I mention here. The first is in the record of Muslim legal thinking on economics and finance, and the second is in the suspension of Islamic financial practices when western commercial banks gained ascension in the Muslim world and replaced whatever institutions and practices had been prevalent there.

[xii] Abdullah Saeed, Op. Cit., p. 95.

[xiii] Ibid.

[xiv] Dr. Nazih Hammad, *Mu`jam al Mustalahat al Iqtisadiyah fi Lughat al Fuqaha* (Herndon: International Institute of Islamic Thought, 1995), p. 351.

[xv] Joseph Shacht, *Islamic Jurisprudence* (Oxford:), p. 154. Shacht completes the sentence by saying, "... but the exact part which these transactions played in the economic life of early Islamic society is not always clear." One wonders if Professor Shacht assumed that "early" Islamic society was the only Islamic society to use these transactions.

[xvi] *Kuwaiti* Fiqh *Encyclopedia*, (Kuwait: Ministry of Endowments and Islamic Affairs, 1988) vol. 6, pp. 236-239

[xvii] ibid.

[xviii] Udovitch*, Partnership and Profit in Medieval Islam* (Princeton: Princeton University Press, 1970)

[xix] Professor Udovitch goes on to say, "Al-Marghinani suggests that their [sales of trust] purpose, particularly of the *tawliyah* and *murabaha* sales, was the protection of the innocent general consumer lacking expertise in the various items of trade from the wiles and stratagems of sharp traders." Op. Cit. p. 220.

[xx] In this context it is interesting to note the comment of Franz Rosenthal, in his introduction to Charles Cutler Torrey's, *The Jewish Foundation of Islam* (New York, Ktav Publishing House, 1967) p. v. concerning Dr. Torrey's dissertation, *The Commercial Theological Terms in the Koran* (Leiden: E. J. Brill, 1892) "Its principal conclusion was that the commercial terminology of the Qur'an was characteristically Arabic and that it consisted almost entirely of native words, not acquired from other languages, in contrast to other terms of Arabic theology."

[xxi] See, for example, al Kashani, *Bada'i al Sana'i* (Beirut: Dar al Kutub, 1982) vol. 5, p. 220; and Ibn Rushd, *Bidayat al Mujtahid* (Cairo: Maktabat al Kulliyat al Azhariyah, 1389). Vol. 2, p. 321.

[xxii] Badr al Din al 'Ayni, *al Binayah fi Sharh al Hidayah* (Beirut: Dar al Fikr, 1982) vol. 6, p. 487.

[xxiii] At 2:16, and then only in a metaphorical sense.

[xxiv] Ibn al Humam, *Fath al Qadir* (Bulaq: al Matba`ah al Kubra al Amiriyah, 1316AH) vol. 5, p. 254.

[xxv] Kuwaiti *Fiqh* Encyclopedia, vol. 12, p. 319

[xxvi] Bernard Weiss, *The Search for God's Law* (Salt Lake City: University of Utah Press, 1992) pp. 555, 556, 564.

[xxvii] See the Qur'an at 8:27, 23:8 and 70:32.

[xxviii] Hideyuki Shimizu, *Philosophy of the Islamic Law of Contract* (Japan: Institute of Middle East Studies, 1989)