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مركز دراسات التشريع
الإسلامي والأخلاق
Research Center for Islamic
Legislation and Ethics
عضو في جامعة حمد بن خليفة
Member of Hamad Bin Khalifa University

ISLAM & APPLIED ETHICS

ETHICS AND FINANCE: AN ISLAMIC PERSPECTIVE IN THE LIGHT OF THE PURPOSES OF ISLAMIC SHARIA

MOHAMMAD FADEL

COMPILED AND EDITED BY: DR FETHI B JOMAA AHMED

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Introduction

In the name of God,
the Most Gracious,
the Most Merciful

The Research Center for Islamic Legislation and Ethics (CILE) is pleased to place into the hands of readers this series of booklets, which contain a collection of research papers that have been presented at events organized by the Center. Through these booklets, we are seeking to build a methodological platform that will contribute to the CILE's key objective, namely promoting radical reform. The type of radical reform that we are calling for is based on a fundamental concept: transformational renovation. This concept transcends traditional renovation and *a posteriori* diligence, which tends to maintain reality and adapt to it, assessing and judging its components through the system of the five categories of laws in Islam: *Wajeb* (required, obligatory); *Mandoob* (recommended); *Mubah* (permitted but morally indifferent); *Makrooh* (discouraged or abominable); and *Haram* (forbidden or prohibited); in other words, it is rather an evaluative type of jurisprudence. Transformational renovation goes beyond this intellectual space to create a kind of renovation and jurisprudence that addresses facts critically and explores reality intellectually so as to reform it, or even rebuild it if necessary. Moreover, this transformational renovation process puts forward alternative solutions for the shortcomings of the current reality, seeking to establish new means, models, and paradigms at all levels that would

achieve ethical objectives. Therefore, radical reform purports to go beyond superficial issues and directly into the crux of objectives and ethics, beyond minor details into theoretical foundations and frames of reference.

In order to implement radical reform by means of transformational renovation, religious scholars and scientists should share the responsibility. While religious scholars, in many cases, have been capable of judging reality based on specific facts provided by scientists, the task is different when it comes to diligence and transformational renovation. This is because an endeavor such as this requires an advanced and comprehensive understanding of both religion and reality. Being well-versed in Islamic Sharia sciences and being formally and partially aware of reality alone will not help bring about transformational reform unless it is accompanied with similar knowledge of our reality, and with today's scientific advancement, this is only possible by involving those specialist scientists and practitioners. The process of building reality on the foundation of proper Islamic ethics and values should be based on a deep and comprehensive understanding that will help analyze the reasons behind malice, which drive people to engage in substandard activities. This understanding may lead to the introduction of alternative solutions and new practices, which are more deeply founded on scientific knowledge. Not to dismiss the sound efforts and evaluative diligence of religious scholars, neither Islamic Sharia scholars nor scientists alone should monopolize knowledge or assume sole responsibility for undertaking reforms in society.

CILE activities are noteworthy for bringing together both religious scholars and scientists. We do not seek to address the evaluative process, which is limited to understanding reality through judgment and adaptation, drawing on permissions

or prohibitions. Rather, CILE events facilitate open dialogue between scholars and expert practitioners, who can collectively propose how best to undertake radical reforms and recommend solutions that are at once inspired by Islamic principles and supported by scientific knowledge.

While the combined work of religious scholars and scientists constitutes a fundamental methodological basis for transformational renovation, it should be coupled with many other elements pertaining to the methods, theories, and objectives of science. For instance, traditional Sharia scientific methods do not preclude the type of renovation desired. At the same time, modern science has failed to focus on ethics, as it has not addressed ethics as a fundamental issue. Rather, science relegates ethics to a secondary position. This raises the issue of the division of sciences into religious or secular sciences, and of their tendency to focus excessively on highly specialized topics without associating them with greater universal themes.

Undoubtedly, this undermines the communication between scientists from various disciplines and thwarts their efforts to work together to develop an epistemological approach that combines their knowledge to serve the important purpose of promoting ethics. Therefore, the challenge set before us is not to persuade scientists belonging to various disciplines and backgrounds to work together. Rather, it is to shake them in their scientific safe havens and drive them to push through the epistemological paradigms governing their own knowledge in order to set up a new system and outline methods toward achieving renovation.

Launching the first of its specialized research activities aimed at facilitating and exploring the communication between religious scholars and scientists, the CILE convened a three-day closed seminar in June 2014 in Education City, Doha, to

consider the contemporary challenges of and the relationship between Islamic ethics and economics.

The seminar participants, scientists and intellectuals with theological and practical experience from around the world, included Sheikh Dr Ali Mohyi Al-Din Al-Qaradaghi, Sheikh Dr Abdullah Bin Yousuf Al-Judai, Dr Hatem El-Karanshawy, Dr Abdelazeem Abozaid, Dr Philip Molyneux, Dr Muhammad Umer Chapra, Dr Asad Zaman, Dr Tariq Ramadan, Dr Catherine Samary, Dr Mohammad Fadel, Kavilash Chawla, and Chauki Lazhar. The seminar was moderated by Dr Abderahman Yousri.

The CILE requested the participants to focus the discussions on the following topics:

(A) What are the main objectives of financial institutions in the current neoliberal economic system in relation to the individual, society, state, and global economy?

(B) What are the main objectives of "Islamic Finance" from an Islamic perspective, in relation to the individual, society, state, and global economy?

This booklet includes a research paper presented in this seminar and is a part of CILE book series which we hope will contribute to our project of transformational renovation.

CHAUKI LAZHAR, *CILE Deputy Director*

About the Authors

MOHAMMAD H. FADEL is an Associate Professor at the University of Toronto Faculty of Law, which he joined in January 2006. Professor Fadel wrote his doctorate dissertation on legal process in medieval Islamic law while at the University of Chicago, with a focus on Maliki *fiqh*. Professor Fadel was admitted to the Bar of New York in 2000 and practiced law with the firm Sullivan & Cromwell LLP in New York, where he worked on a wide variety of corporate finance transactions and securities-related regulatory investigations. Professor Fadel also served as a law clerk to the Honorable Paul V. Niemeyer of the United States Court of Appeals for the 4th Circuit, and the Honorable Anthony A. Alaimo of the United States District Court for the Southern District of Georgia. Professor Fadel has published numerous articles in Islamic legal history and Islam and liberalism, and is the author of "Ribâ, Efficiency and Prudential Regulation: Preliminary Thoughts," *25 Wisconsin Journal of International Law* 655 (2008).

Ethics and Finance: An Islamic Perspective in the Light of the Purposes of Islamic Sharia

Mohammad Fadel

Introduction

I have written this paper in response to an invitation from the Research Center for Islamic Legislation and Ethics in Doha, Qatar, to participate in a seminar innocuously titled "Ethics and Economics." The organizers of the seminar asked me to address the following question: "From an Islamic perspective, what are the main objectives of 'Islamic Finance' in relation to the individual, society, state, and global economy?" They also asked me to address the following sub-questions: "What is your assessment of the Islamic finance journey so far (e.g. Islamic banks, Islamic Development Bank, Islamic Dow Jones)?" and "To what extent has Islamic finance introduced an alternative paradigm, or does it function within the boundaries of the current neo-liberal economic system?" All seminar participants circulated their papers in advance of the three-day meeting; and while this paper is, in broad outlines at least, unchanged from the pre-seminar version, I have revised it in the light of the questions and issues raised during the course of the often-lively exchanges that took place during the seminar, and added additional detailed citations from the *fiqh* and *hadith* literature for the benefit of the reader.

The paper will proceed as follows. I will begin with a discussion of what it means, from a methodological perspective,

to adopt a purposive approach (*maqasidi*) to understanding Islamic law (Sharia). After this methodological introduction, I will proceed to discuss my understanding of what a purposive approach to finance grounded in the norms of Islamic Sharia would mean. My analysis begins by identifying the extent to which the explicit textual sources of the Sharia broadly recognize the legitimacy of finance, and identifies the different kinds of finance that the Sharia explicitly recognizes, including, a for-profit financial sector and a charitable (or not-for-profit financial sector) and public finance. I then provide a substantive analysis of each sector, arguing that each sector is governed by its own particular purposes (*maqasid*), and that it would be inappropriate to import the concerns of one sector, for example, the for-profit sector, into analysis of another sector, for example, the not-for-profit sector, but that all sectors are united by a meta-Islamic ethic of a commitment to efficiency, or from an operational perspective, an anti-waste principle. I will then discuss specific problems related to contemporary Islamic finance: the failure of Islamic banks to guarantee the money of depositors by virtue of their use of the two-tiered *mudaraba* structure to finance their dealings; the difficulties raised by the current approach of Islamic equity indices, such as the Dow Jones Islamic Index; how to transform *zakat* into an effective tool for distributive justice due by overcoming the historical legacy of legal formalism in the jurisprudence of *zakat*; and, the role of general taxation in public finance in Islam and the achievement of social justice. The paper will then conclude on the state of the art in the theory and practice of Islamic finance across the various dimensions discussed in this paper.

The Methodology of Purposivism in Islamic Jurisprudence (*al-fiqh al-maqasidi*)

Before one can develop a purposive understanding of finance in the light of the Sharia, one must first begin with an understanding of the jurisprudential assumptions of purposivism (*al-fiqh al-maqasidi*) and how this method is to be applied for the purpose of deriving rules of Islamic law.

Purposivism is often understood to find its first explicit articulation in the writings of the great Shafiʿi jurist and Ashʿari theologian, Abu Hamid al-Ghazali. Al-Ghazali argued in his *al-Mustasfa fi Usul al-Fiqh* that the Sharia existed to serve five universal ends (*maqasid kulliyya*) of the preservation of religion (*din*), life (*hayat*), property (*mal*), progeny (*nasl*), and capacity/rationality (*ʿaql*). All rules of the Sharia, in turn, furthered one of these ends, but along three different levels of importance, which al-Ghazali identified as primary/necessary (*daruri*), secondary/convenient (*haji*) and tertiary/decorative (*tazyini*). Post-Ghazalian jurists further developed his theory of the *maqasid*, with such jurists as ʿAbd al-ʿAziz b. ʿAbd al-Salam, author of *Qawaʿid al-Ahkam fi Masalih al-Anam*, and Abu Ishaq al-Shatibi, author of *al-Muwafaqat fi Usul al-Shariʿa*, giving pride of place to *maqasid* in their jurisprudential theories of the Sharia.

It would be a mistake, however, to think that the purposive approach to understanding the Sharia was a relatively late development in the history of Islamic law. While the explicit formulation of the theory of the *maqasid* may have come at a later date, purposive interpretation characterized Sunni juristic activity from its earliest history. While traditional accounts of Islamic legal history tend to recognize Imam Malik as the early jurist who gave pride of place to *masalih mursala* (the

textually unattested public welfare) in his juristic system while his younger contemporary and critic, Imam al-Shafiʿi, is said to have rejected such analysis in favor of a stricter textualism; careful analysis of al-Shafiʿi's interpretation of revealed texts confirms his assumption that correct interpretation requires knowledge of the purposes of the revealed rule. This is clear in his treatment of the verse "and test the orphans when they reach the age of marriage, and if you find them to be of sound mind, deliver to them their property" (4:6, *al-Nisaʾ*), where he relied on the social distinctions in how minor boys and girls were raised to justify the different evidentiary presumptions that were to be used to determine when minor boys and girls, respectively, should obtain full ownership of their properties.[1]

Even before the explicit introduction of *maqasid al-shariʿa* as a technical jurisprudential concept, the general acceptance by Sunni jurists of analogy was dependent on the assumption that the rules of the Sharia existed to promote certain ends or goals (*maqasid*), and that human reason could reasonably infer what those goals were from the explicit rules of revelation. Accordingly, we could understand that revelation prohibited grape wine (*khamr*) not because of its color, taste, or texture, but because of its particular capacity to undermine the rational capacity (*izalat al-ʿaql*) of those who drank it. Of course, to be able to identify wine's capacity to cause inebriation as the legal cause (*ʿilla*) of its prohibition while excluding its other characteristics as the basis for the prohibition assumes that God's rules are purposive. The implicit assumption that God's revelation is purposive formed the basis for the *Zahiri* critique of analogy as an unwarranted assumption by human beings that they could understand divine purposes.

Although acceptance of the purposiveness of revelation is deep-rooted in Sunni jurisprudence, it is also a controversial

position, as evidenced not only by the *Zahiri* rejection of the entire justification of analogical reasoning, but also by the skepticism numerous jurists have expressed with regard to the capacity of human beings to discern the *true* purpose intended by divine revelation. More conservative jurists, such as the late Sheikh al-Buti, for example, have expressed doubts about our ability to apprehend the correct goal of revelation, and that instead, we should assume that the goal of the Lawgiver is perfectly assimilated into the textual rule itself, in which case, the best means to achieving the goal of the Lawgiver is through complete obedience to the rule without regard for the empirical consequences that result from conforming to the rule.[2]

I reject this approach, not because it is methodologically indefensible, but because as a practical matter it does violence to the entire enterprise of jurisprudence (*fiqh*), not only at the level of particular rules, but also at the level of the structure of jurisprudence, which implicitly assumes our capacity to understand the purposes of revelation as viewed from a *human* perspective, and thus apply the norms of revelation to an infinite set of *human* problems.[3] As Ibn Rushd the Grandson stated in defense of the obligation of *ijtihad*: texts are finite, but cases are infinite, and it is impossible for the finite to encompass the infinite.[4] Accordingly, the proper *maqasidi* approach to revelation is to begin with the texts of revelation; proceed to the empirical circumstances in which that rule originally operated; then propose the goal, that is, the *maqsud* or the *maslaha* which the rule furthers; and, finally, apply the textual rule to new circumstances while taking into account (*muraʿat*) what the jurist theorizes to be the original purpose of the rule. In other words, an interpretive dialectic, grounded largely in practical reason, must take place among our linguistic understanding of the texts of revelation, our own understanding of our empirical

(immanent) good in the light of our best understanding of the world at the time of the interpretation (*al-sunan al-ʿadiyya*), and our best understanding of the circumstances in which the rule will be applied. Finally, the *maqasidi* approach I adopt does not limit itself to regarding the texts of revelation discretely, but rather requires reading them together in an inductive fashion (*istiqraʾ*), along with the interpretations historically provided by the jurists, in order to best determine the Lawgiver's goal. This is essentially the method that the great Maliki jurist and scholar of *usul al-fiqh* Abu Ishaq al-Shatibi proposed in his magisterial work on *maqasid* and its relationship to theoretical jurisprudence, *al-Muwafqat fi Usul al-Fiqh*.

Finance, the Foundational Texts of Revelation and Finance's Status as an Essential Good (*Maslaha Daruriyya*)

To answer the principal question posed by this seminar – "what are the main objectives of 'Islamic Finance' in relation to the individual, society, state and global economy?" – we must begin with an inductive survey of the texts of revelation to identify the extent to which revelation addresses questions that are directly relevant to finance, whether in a legislative mode, that is, through direct commands, or in a confirmatory mode, that is, confirming social practices that are essentially financial. But we cannot begin the Islamic inquiry without first answering the question, "What is finance?" By finance, we mean the process by which surplus funds in the hands of savers – whether individuals, firms, or governments – are transferred to individuals and entities in need of those funds, whether for investment or for consumption. A financial system can be described as more or less efficient by measuring its success in transferring surplus, unused funds from savers to consumers and investors.

The need for a financial system stems not only from the fact of an unequal distribution of income and opportunities, but also from the reality of an unequal distribution of talent and desire: even if we imagined a world in which property was distributed in a perfectly equal fashion, so long as individuals have different desires in terms of consumption and saving, and talents with respect to how they wish to deploy their resources, there will exist a need to transfer property which is idle in the hands of its owner to another person who can make more productive use of it.

There is also a pressing need to transfer savings to debtors because of the reality of consumption patterns over a single lifetime: individuals' expenses and incomes vary depending on their age, for example, children and the aged, because they lack income, must draw on the surpluses generated by the working population, while persons in the prime of their career will generally generate income in excess of their present needs, which they need to save for future expenses. Accordingly, consumption patterns need to be adjusted to the natural rise and decline of actual incomes over a person's lifetime. Finance, therefore, entails more than the present transfer of surplus property from those who do not need it to those who need it immediately, something which could be accomplished simply by means of a present gift. Tt also refers to intertemporal exchange, whereby the person or entity with the surplus transfers it conditionally in the expectation of receiving its like in the future, oftentimes with an expectation of an increase, so that the saver will be able to meet their *future* needs, whether personal, for example, the cost of a child's wedding, or social, for example, the pensions of retired workers.

The only way to envision a society that lacks a financial system is to imagine one in which trade is absolutely prohib-

ited or to imagine a society in which all individuals have the same initial endowments and have the same tastes, in which case there would be no need for them to trade and in which current income is always sufficient to satisfy its members' current needs, regardless of age or circumstance. Because such a society has never existed, and as a matter of experience, is extremely unlikely (*mutaʿaddhir*) to exist, we can safely conclude that that existence of a financial system in human society is a fundamental interest (*maslaha daruriyya*) insofar as it is inconceivable for *any* human society to exist without some system for transferring surplus property to those who are in a deficit.

There is little doubt that the Qur'an and Sunna, as a general matter, recognize the role of finance, that is, the transfer of surpluses to those in deficit, in human society by encouraging the circulation of wealth. In so doing, the Qur'an recognizes both commercial (profit-seeking) and non-commercial (altruistic) means to effect these transfers of property. The following list includes some – but by no means all – texts of revelation that relate to finance: (a) the Qur'an condemns those who hoard wealth ("Those who hoard gold and silver and spend it not on the path of God . . .," *al-Tawba*, 34–5); (b) it instructs that public property (*fayʾ*) is to be spent on the needy so that "its circulation is not limited to the wealthy among you" (*al-Hashr*, 7); (c) it repeatedly commands the believers with means to pay a portion of their property as *zakat* in favor of the needy, as an obligation and not an act of charity (e.g. *al-Tawba*, 103, and *al-Maʿarij*, 24–5); (d) the Qur'an repeatedly encourages believers to extend "godly loans" (*qardan hasanan*) for the sake of God, (e.g. *Baqara*, 245); (e) the Qur'an not only recognized the permissibility of trade in the spot market (*tijara hadira*), it also recognized the validity of credit sales (*al-bayʿ ila ajal*),

as manifested by the fact that the single longest verse of the Qur'an, *Baqara*, 282, lays out the rules for documenting credit sales; (f) the *sunna* recognized the permissibility of commercial contracts (profit-seeking contracts) that include a credit term, such as *salam* (forward sale), *muzaraʿa* (share-cropping), and *musaqat* (a special kind of share-cropping arrangement); (g) the *sunna* recognized the validity of guaranty contracts (*ʿaqd al-daman* or *kafala*) as well as social insurance (*al-diya ʿaqila*); (h) the *sunna* recognized equity finance (*sharika*) with pure profit-and-loss sharing, and preferred equity finance (*qirad* or *mudaraba*) where only profits are shared; and (i) the *sunna* also recognized public borrowing, as set out in the Sunan of Abu Dawud in the report of ʿAbdallah b. ʿAmr b . al-ʿAs, concerting the provision of camels for the army.[5]

What this brief review of Qur'anic and Prophetic texts shows is that the foundational elements of both public and private (individual and business) finance, as well as commercial and noncommercial finance, both debt and equity, are found in the texts of revelation. It would be a mistake, then, in formulating a purposive interpretation of Islamic law's approach to finance to reduce the Sharia's teachings to one set of financial tools to the exclusion of the others. The Sharia endorses both profit-seeking modes of finance and altruistic modes of finance. It endorses voluntary acts of altruism – gifts (*hiba*) and charity (*sadaqa*) – as a means of transferring surpluses to those in deficits, and it also endorses coercive means of redistribution of surplus assets – *zakat* and *kharaj* – to those in need. Before formulating a general theory of the ethics of Islamic finance, therefore, it is crucial that we begin with understanding the purposes of each of the different financial tools that the Sharia has recognized, and then consider, from a macro-perspective, how these micro-financial tools are to work together. A closely

related question is whether Muslims are restricted to the tools explicitly endorsed by revelation,[6] or whether the presumption of permissibility (*al-asl fi'l-ashya ͗ al-ibaha*) should apply to financial transactions. Finally, there is also the larger, systemic question of the macroeconomic environment, in which these individual contracts ought to be deployed and the overall relationship between individuals' pursuit of their own ends, including, commercial for-profit ends, with the public good, question to which this essay will turn later.

We now turn to the more detailed question of analyzing the goals of each of the subareas of finance recognized in the basic texts of the Sharia: commercial contracts; altruistic finance; and coercive public finance (*zakat*).

Commercial Contracts, the Pursuit of Profit and *Maqasid al-Shari ͑a*

The jurists have recognized numerous contracts, the purpose of which is the realization of private gain for the contracting parties. The paradigmatic case of the profit-seeking contract in Islamic law is the sale (al-bay ͑). Jurists not only assume the parties to a sale contract, provided they enjoy full capacity and are entitled to maximize their private gains from a commercial contract, but that they ordinarily do seek to maximize their private gains, at least to the best of their ability. For this reason, Muslim jurists generally allowed parties to determine freely the terms on which they would trade, and in contrast to medieval Church doctrine, they rejected a just price theory. Even contracts that evidenced off-market prices (ghabn) were valid, or at a minimum, were not invalid solely because the price was off-market.[7] This presumption that traders seek to maximize their private returns is manifested in the juristic presumption

that contracts of sale and other commercial contracts are governed by a presumption of mutual covetousness, mushahha, which requires holding the parties strictly to their bargain in light of the presumption that each party demands performance of exactly what was in the contract, in contrast to other contracts, such as marriage, which is governed by a presumption of generosity – mukarama or musamaha – that results in a looser interpretation of contractual terms.[8] The assumption of profit maximization is also clearly manifested in the rules governing the obligations of an agent (wakil) who is entrusted with selling the goods of his principal[9] or the duties of an investment agent (al-ʿamil) in a qirad or mudaraba. The agent in a qirad, for example, is prohibited from making gifts (other than de minimis gifts, such as a loaf of bread or the like) out of the capital of the investment partnership on the theory that he is working solely for the interests of the investor.[10] A partner in a general partnership is also limited in his right to act out of generosity: while he is permitted, for example, to give discounts on debts owed to the partnership or make gifts, but only if such acts further the commercial interests of the partnership.[11]

The legitimacy of the private pursuit of profit is so ingrained in Islamic jurisprudence that the jurists over the centuries recognized numerous exceptions to their rules in order to facilitate the private pursuit of commercial gains. Indeed, the contract of the *qirad* is itself considered to be exceptional insofar as it entails a contract for hire for an indefinite wage (*al-ijara al-majhula*). Despite this otherwise grave contractual defect, Islamic law declared it to be permissible because of necessity in light of the fact that many people with surplus funds lack the ability or the opportunity to invest that property themselves.[12] A careful reader of the history of Islamic law will find numerous examples from the *fatwas* of the scholars that

evidence a principled willingness to recognize exceptions to various rules of *fiqh* in order to further the legitimate need of private parties to earn a profit. In addition to such exceptional contracts as *qirad*, *bay' al-salam*, *muzara'a*, *bay' al-'ariyya,* and *musaqat*, all of which have some textual basis, jurists also recognized exceptions to their own rules in numerous instances. In the Maliki school, for example, Andalusian jurists gave opinions permitting partnerships for the cultivation of silkworms (*tarbiyat al-dud*) despite the fact that the customary arrangements were not in accordance with Maliki teachings on labor partnerships.[13] Later Malikis, in an effort to enhance the rights of creditors, permitted the debtor to appoint the creditor his agent for the purpose of selling pledged property in the event the debtor defaulted in order to avoid the inconvenience of a judicial sale.[14] Maliki jurists also recognized an exception to their rule regarding the requirement of immediate payment or performance of a binding contract of hire (*ijara madmuna*) in the case of contracts for the advance hire of transportation for long distances, like the Pilgrimage, again on the grounds of necessity.[15] Muslim jurists also generally upheld the liability of artisans for the property of their customers (*tadmin al-sunna'*) despite the fact that the customers willingly gave them their property, and thus the artisans would ordinarily be deemed to be bailees (*amin*) and thus free of liability in the absence of proof of negligence.[16]

Another important example of the jurists relaxing the rules of *fiqh* in light of the need to pursue profit is found in an important opinion of the great Andalusian jurist al-Shatibi, in which he was asked about the legitimacy of another customary but controversial practice in Andalus that contradicted numerous rules of Maliki *fiqh*, but strict application of the rules of Maliki *fiqh* would have deprived average individuals of the opportu-

nity to earn a profit with their property.[17] Shatibi explained the controversial practice as follows: a group of urban dwellers who own livestock, for example, sheep or goats, contract with one or more shepherds, who then take the animals into the countryside to graze. While the animals are grazing, the shepherds milk the herd, and use the milk to manufacture cheese. When the shepherds return to the city, they distribute the cheese in proportion to the number of animals each partner contributed to the herd. He was also asked about the Andalusian practice of forming partnerships for the manufacture of cheese, with each partner contributing milk and the cheese being divided in proportion to the amount of milk contributed by each partner. Because the amount of cheese produced from milk is not uniform, that is, some milk yields more cheese than others, dividing the cheese in proportion to the milk contributed by each partner, for example, if A contributed 1/10th of the milk, he receives 1/10th of the cheese, does not result in a distribution of the cheese that in fact corresponds to the cheese produced by the partner's contribution of milk. Under standard principles of Maliki law, such a transaction amounts to *muzabana*, as well as *riba fadl* and *riba nasiʾa* insofar as it entails the unequal exchange of food combined with delay, that is, the exchange of milk for cheese on a deferred basis. Application of ordinary rules then would result in an invalidation of these two widespread customary transactions.

Nevertheless, al-Shatibi upheld this practice in reliance on an early opinion of Imam Malik recorded in the *ʿUtbiyya* and explicated by Ibn Rushd the Grandfather in *al-Bayan wa'l-Tahsil*. Malik is asked about a practice in his day, where people would meet at an oil press, and instead of each of them pressing his own seeds individually, they would combine their seeds together, press them together, and split the oil in proportion to

the amount of seeds that each person had contributed. Malik stated that in principle this was impermissible because there is no guarantee that each set of seeds produces oil in equal amounts, thus leading to uncertainty in exchange (*gharar*) and *riba fadl* in the exchange of food. Nevertheless, Imam Malik permitted the practice, saying:

"This is disliked because some of it will produce more than the rest, but when the people need this, I hope it is a trivial thing because they must have which is necessary to improve their condition. Accordingly, I hope that there is a dispensation for those things which they cannot avoid, God willing, and I see no harm in it."[18]

According to Ibn Rushd, Sahnun rejected Malik's view, and declared the practice forbidden on the basis of analogy, while Malik permitted it "on the grounds of *istihsan*, necessity compelling him to that conclusion, since it is impossible to press a small amount of seeds and in light of the opinion of some scholars that unequal exchange is permitted in those [commodities]."[19]

What is clear from the previous examples is that jurists, certainly in the Maliki school, were willing to make exceptions to rules that would normally apply by force of analogy in favor of reasoning based on doctrines such as *maslaha mursala* and *istihsan*, usually claiming necessity (*darura*) to justify abandoning the rule that analogy would require. Necessity in these cases, however, is a far cry from the necessity that would be required to permit, for example, a person to eat carrion (*akl al-mayta*); rather, the jurists in commercial contexts use necessity loosely, treating legitimate commercial need (*haja*) as the equivalent of necessity (*darura*) in other circumstances in order to justify a dispensation (*rukhsa*) from the ordinarily applicable rule. In other words, simple need (*haja*) is transformed into necessity

in the context of commercial dealings (*tunazzal al-haja manzilat al-darura*).

I am not aware of any explicit discussion among the jurists that explains this anomaly. After all, the Maliki jurists do not permit consumption of carrion except in circumstances where the person is starving. In the cases of the exceptions noted above, they did not require proof that the person seeking the dispensation was on the verge of starvation or poverty; it was sufficient that the transaction under consideration served a legitimate need, particularly the need for individuals to invest their property for a gain (*tanmiya*), or otherwise realize a profit. The different sense by which jurists use the term necessity (*darura*) in the two cases may be that the prohibition on eating carrion is owed to God exclusively (*haqq allah*), while property rights belong to human beings (*haqq adami*). All of the cases cited above involve exceptions to rules that regulate property rights, and thus belong primarily to the realm of the rights of human beings (*huquq al-adamiyyin*). Accordingly, and to the extent that they have consented to these practices, no violation is being committed against their property and so the lower standard for the *rukhsa* is justified.[20]

We can conclude then by noting that in private, commercial transactions, legitimate need (*haja*), not actual necessity (*darura*), is sufficient to justify an exception from a rule based on analogy. That is the inevitable conclusion that should be drawn from the various exceptions noted by the jurists to their own rules.

Altruistic Finance in the Sharia

In addition to utilizing the profit motive to encourage the transfer of surplus property to those who need it for immediate use,

the Sharia cultivates an ethic of generosity and altruism (*ithar*) among its followers to share whatever surplus they have with those who are in greater need. For example, the Qur'an praised the Ansar – the Arabs of Yathrib at the time of the Prophet's *hijra* (S) – for their altruistic sharing with the Emigrants their properties, even though the Ansar themselves were needy.[21] Altruistic contracts include the contract of gift (*hiba*) as well as the loan (*qard*). In each of these transactions, the person transferring the property to the other does so without any consideration, and indeed, in the case of a loan, the stipulation of a consideration nullifies the transaction's character as a loan and transforms it into a sale, which might or might not be valid depending on the terms of the sale.

The absolutely altruistic character of the loan is exemplified in the juristic rule invalidating self-interested loans, that is, *salaf jarra naf ʿan*, and is reflected in its definition among the Malikis as the transfer of property from the transferor to the transferee for the *exclusive* benefit of the transferee.[22] Even though this juristic rule rests on a weak report, it is rationally consistent with the notion that a loan should be solely for the benefit of the borrower in order for it to qualify as an act of altruism. We have seen previously that the Muslim jurists were keen to separate profit-seeking contracts such as sales, the governing presumption for which is covetousness (*mushahha*), from other contracts that were governed by a norm of generosity (*mukarama*). This distinction is reinforced through the juristic rule invalidating self-interested loans. It is also consistent with the Qur'anic ethic of altruism: individuals are not obliged to be altruistic (except in the limited circumstances of necessity), but where they choose to act altruistically, they may not then act toward the recipient in a way that contradicts the original intention:

"A kind word and a prayer of forgiveness are superior to charity followed by vexation."[23]

Likewise, the charitable nature of the loan, that is, the fact that the lender receives no benefit from the borrower in consideration for the loan, explains why, unlike a sale, it is an act of obedience (*mandub*) that entails divine reward.[24] A gift (*hiba* or *sadaqa*) is like a loan insofar that it is an uncompensated transfer of property, but with the important difference that the recipient is under no obligation to return the gift, unlike the case of a loan, but it shares with a loan the fact that it merits divine reward as a supererogatory duty (*mandub*).[25]

They also share the requirement that a prerequisite for the validity of the loan or the gift that the lender or the giver, as applicable, have the capacity to engage in a donation act (*ahliyyat al-tabarruʿ*) and be the owner of the property.[26] This means, for example, that agents lack the capacity to engage in donation acts without the consent of their principals. So, too, guardians are not allowed to engage in donative acts on behalf of their wards, and therefore, Malikis held that an orphan's guardian is not permitted to lend the orphan's property,[27] and a child is entitled to seek restitution from a parent who made gifts to others out of the minor child's property.[28]

Altruistic contracts also differ from commercial contracts in other important ways. For example, both contracts of loan (*qard*) and gift (*sadaqa*) are binding only after they have been performed by the lender or the donor, respectively.[29] By contrast, the contract of sale is immediately effective in transferring title of the sold good to the purchaser. This feature of altruistic contracts further weakens their obligatory character relative to commercial contracts. On the other hand, because these are altruistic contracts, they tolerate a degree of indefiniteness (*gharar*) that is not permitted in contracts of sale that

entail mutual compensation.[30]

To conclude, the Sharia encourages acts of generosity, and altruistic modes of finance are certainly part of the financial tools recognized by the Sharia. At the same time, however, it would be a mistake to limit finance in Islam to acts of altruism, which, according to the jurists themselves, are only recommended (*mandub*) and not obligatory (*wajib*). Finally, with respect to a purposive approach to donation contracts, Muslim jurists must be careful to preserve the wholly altruistic nature of contracts such as *qard* and *sadaqa* and not confuse them with profit-seeking contracts, or obligatory acts of transfer, namely *zakat*, the next topic to which I now turn.

***Zakat*, Distributive Justice and the Goal of a Universal Minimum Income**

So far, we have seen that Islamic law respects the private pursuit of profit, and that the jurists regularly made doctrinal concessions in furtherance of this goal in circumstances where it was clear that the concession (*rukhsa*) at stake was beneficial to both parties. We also saw that while the Sharia encourages an ethic of generosity, and rewards those who act altruistically toward those less fortunate, it does not compel generosity, but instead imposes it only as a supererogatory obligation (*mandub*). Indeed, in many contexts, where the property is managed by an agent or guardian, such agent or guardian, as applicable, is effectively prohibited from acting out of generosity on the theory that this is not in the best interest of the principal or the beneficiary. This might suggest that the Sharia is largely *laissez-faire* with respect to economics: it permits private parties to engage in commercial transactions and in so doing to maximize their returns from trade, provided

that they do so honestly, with no offsetting obligation to share their profits with others. This would be true but for the existence of the crucial institution of *zakat*, which acts coercively to redistribute surplus from those having property in excess of their current needs to those lacking sufficient property to meet their current needs.[31]

From the perspective of purposive jurisprudence, the fundamental goal of the law of *zakat* is to guarantee that each Muslim (or citizen, in the modern context) is guaranteed a minimum subsistence income. This is evidenced by the Maliki rule that anyone lacking a year's worth of food is entitled to receive *zakat* (*faqir la yamliku quta ʿamihi*).[32] Interestingly, there is no requirement that the able-bodied work in order to be eligible to receive *zakat*[33] nor must an individual prove his poverty: it is enough in the absence of contrary circumstantial evidence that he claims eligibility according to the Malikis.[34] *Zakat* funds were also to be used to free slaves and for debt relief,[35] with the general rule being that priority should be given to the neediest.[36]

I say that the fundamental purpose is to relieve the needy and *not* the moral improvement of *zakat* payers (although that is also an important goal of the Sharia) in light of the fact that it can be coercively enforced against wealthy individuals who refuse to pay and that even minors who are otherwise not morally obligated are required to pay *zakat* on their property if it exceeds the threshold amount (*nisab*).[37] This observation is also confirmed by the laws governing when it is obligatory to assist another in need. As a general rule, there is no duty to offer assistance to another (*muwasat*); however, if a person's need rises to that of dire and life-threatening necessity (*al-mudtarr*), a person who is able to help, but refuses is liable for his failure to offer assistance if the needy person dies.[38] Just as is the

case with *zakat*, although the Sharia desires to produce individuals who would voluntarily pay their obligations and offer assistance to those in desperate circumstances, where there is a conflict between the moral failures of the wealthy and the need of the poor or those under necessity, the latter are given legal priority, but only to the extent necessary to relieve their need, with *zakat* providing food for a year, and the obligation to provide a person facing a dire necessity enough to relieve the immediate need, but no more.[39]

The Sharia, viewed from a purposive perspective, endorses coercive redistribution based on need, with the goal of providing everyone in society a basic safety net, below which no one can fall. This is an absolute individual right, without proof that the person is morally worthy of our assistance, for example, has exerted sufficient diligence in feeding himself by working. At the same time, however, the Sharia appears to limit mandatory assistance to individuals' basic needs, and in so doing, it also appears to encourage voluntary transactions, whether commercial or altruistic, as the primary means by which individuals are expected to satisfy their economic goals.[40]

Efficiency and Human Dignity as a Meta-Islamic Ethics of Finance

In the discussion of *zakat*, we emphasized its aspiration to provide all persons a minimum income that guarantees their survival without regard to whether they are prepared to sell their labor in the marketplace. The willingness of the jurists to guarantee access to a minimum entitlement without demanding any contribution of labor suggests an ideal of free labor, namely labor that is given not out of necessity but out of genuine freedom.

One finds corroboration for this idea particularly in the writings of the Hanafi jurists who openly worry about the prospects that paid employment renders the employee vulnerable to degradation (*dhull*) and is one reason why hire-contracts are deemed exceptional (*khilaf al-asl*). For this reason, Hanafis prohibit a child from entering into a hire contract with either of his parents because it would put the child in a position to exploit his parents, something that is contrary to the parent–child relationship.[41] More generally, the great 19th century Damascene Hanafi jurist Ibn ʿAbidin explained in his *Radd al-Muhtar* that the Hanafi position that "self-effacement to other than God is sinful (*al-tawaduʿ li-ghayr allah haram*)," means "degradation of the self in order to receive a worldly benefit (*ay idhlal al-nafs li-nayl al-dunya*)."[42] He also quoted the prominent companion Ibn Masʿud as saying "Whoever humbles himself before a wealthy man and renders himself at his service to magnify him and out of covetousness for what he possesses loses two thirds of his manly self-respect and half of his religion."[43]

From the perspective of purposive jurisprudence, this value can be translated into an *anti-subordination* principle, meaning, that the Sharia strives to eliminate all manner of *avoidable* subordination of one person to another. We will return to this goal of the Sharia later in this essay when we discuss the principles of public finance in a modern context. Now, however, we must discuss the place of efficiency and its role in the Islamic ethics of finance and one of the goals of an Islamic financial system.

Before asking whether Islamic ethics incorporates ethics as a virtue, however, we first ought to ask what efficiency means. For economists, efficiency is a state of the world in which it is impossible to make one person better off without making another person worse off. This state, of course, is an ideal and is never actualized, but can only be approached.[44] Accordingly,

economists use the term efficiency and inefficiency to judge the relative ability of a society (or contract or institution) to produce a good without wasting resources. A financial system is more (less) efficient to the extent that it can produce the same amount of the good – the transfer of surpluses (savings) to those in deficit (users of savings, i.e., "borrowers" broadly understood) – at a lower cost. If the costs are lower, but the output of the good is reduced, or it produces greater misallocation of surpluses, it is not more efficient than a system with higher costs but produces better results. Likewise, a financial system that produces few losses, but also results in the hoarding of large amounts of surplus is not necessarily more efficient than an alternative financial system that produces more losses, but also produces more gains. In short, a system is efficient only when all resources available to it are optimally utilized. Essentially, maximizing efficiency is simply another way of saying minimizing waste, with waste including both realized losses arising from unwise uses of surpluses, for example, building too much private housing as was the case in the United States during the first decade of the 2000s, and unrealized losses arising from the failure to deploy surpluses to sectors of the economy that could use those resources productively, for example, as a result of hoarding.[45]

Fortunately, there is evidence in revelation that shows that efficiency, at least in this abstract sense, is indeed an important Islamic ethical value. God praises those who "When they spend, they are neither excessive nor are they miserly, and between these is prosperity." (*al-Furqan*, 67). The word *qawam* (also *qiwam*) includes the meaning of justice and stability, or to read the verse from the perspective of an economist, equilibrium. From this perspective, God praises those whose spending is neither more nor less than necessary, and is appropriate

for their needs, thus producing justice and stability. When all spending is directed to what is necessary and in the amount that is necessary, then a state of perfect efficiency is achieved, as it would be impossible to redirect spending without making someone worse off. By contrast, in an inefficient state, it is possible to redirect spending without making someone worse off.

This aversion to waste is affirmed in numerous verses of the Qur'an, where God makes clear that He does not impose obligations on humanity simply to burden them without a corresponding benefit. Thus, God negated the imposition of gratuitous difficulty (*haraj*) in numerous verses of the Qur'an, (e.g. *al-Maʾida*, 6 and *al-Hajj*, 78); He stated that He intends ease in religion and not hardship (e.g. *al-Baqara*, 185) and that He did not overburden us with useless commands (*al-Baqara*, 220). For these reasons, Imam Malik, may God be pleased with him, recognized "the removal of hardship" (*rafʿ al-haraj*) as one of the foundational principles of his legal school. This recognition of efficiency as a consideration in a jurist's legal determinations left many traces in Imam Malik's legal opinions, particularly with respect to monetary transactions, some of which were noted earlier in this essay.

The history of Islamic law no doubt provides other examples of cases where the jurists overrode the formal rules of *fiqh* in order to achieve the social goal of improved efficiency, and these examples are not limited to the Maliki School. The existence of cash *waqf*s (*waqf al-nuqud*) in the late Ottoman Empire, for example, is an important example of the jurists making exceptions to the formal rules of law in order to ensure that the law serves the goal of efficiency and does not result in waste. Indeed, one might make the argument that from a legal perspective, *haraj* ought simply to be understood as any kind of expenditure that is not necessary to achieve the goal of

the transacting parties and thus produces a dead-weight loss (*khusara safiya*) in economic terms.

In the Andalusian case of the partnership for the production of cheese, for example, the Maliki jurists might have relied on the famous hadith of Bilal, in which the Prophet (S) told him to sell one kind of dates in the market and use the proceeds from that sale to purchase the different kind of dates that he had originally traded for in order to avoid the unequal exchange of dates, which violates the prohibition against *riba al-fadl*.[46] Had they applied this hadith to that transaction, they would have told the people to sell their milk in the market for cash, form a partnership with the cash obtained from its sale, re-purchase milk from the partnership's capital, and *then* they could lawfully divide the cheese produced by the partnership in proportion to their respective cash contributions to the partnership's capital. By permitting them to avoid the intermediate steps of selling the milk and then repurchasing it, despite the formal violation of the rules against *riba al-fadl*, the jurists saved the partners the costs entailed in these two additional transactions. While that meant that the final distribution of the cheese would not be perfectly consistent with the actual productivity of the milk contributed by the various partners, the jurists recognized that the gains from forcing them to sell and then repurchase the milk with money were less than the costs such additional transactions would impose on them and thus represented dead-weight losses from the perspective of the parties.[47] This fact justified recognition of a *rukhsa*.

Based on the foregoing, it follows that an overriding purpose of Islamic finance is to minimize dead-weight social losses, even if they arise in connection with practices that are formally compliant with the rules of Islamic law. In fact, one might say that whenever adherence to formal rules of Islamic law leads

to dead-weight social losses, the higher principles of Islamic law, in this case – *raf' al-haraj* – dictate the recognition of an exception, a *rukhsa*, to the normally applicable rule, but only to the extent necessary to prevent the loss. This principle ought to be applied universally in the analysis of all contemporary private and public economic activity, and to the role of all financial institutions, whether for-profit or not-for-profit, with the goal of achieving a sustainable equilibrium that is reasonably stable – the state of *qiwam* that God praises in *Surat al-Furqan*, 67. We now turn to applying these principles in the light of the foregoing purposive analysis of finance in the Sharia to some contemporary problems.

Islamic Banks, Financial Intermediation and the Problem of the Guarantee of Deposits from the Perspective of Purposive *Fiqh*

While the texts of revelation and the historical *fiqh* developed in light of revelation clearly established the necessity of finance to the social life of the community, neither revelation nor the jurists had developed advanced institutional means for financial intermediation. Most pre-modern tools of Islamic law that could be used for finance assumed direct relationships between the transferor and the transferee, the major exception being the *qirad* or the *mudaraba*, where savers gave their surplus to an entrepreneur who, in certain circumstances, could then invest those funds in a second venture. As a result, banks, whether for profit or not-for-profit, did not develop indigenously in the Islamic world and were only introduced in the 19th century after contact with Europeans.[48]

Banks play a decisive role in modern financial systems by serving as efficient institutional intermediaries standing

between those persons with excess funds (savers) and those persons or entities in need of funds (borrowers). In the absence of a bank, any person with an excess of funds would have to expend substantial costs in order to find a person with whom he could invest his excess funds. At the same time, those persons needing funds also would have to expend substantial costs in identifying individuals with surplus funds that are available for investment. Banks, therefore, provide a convenient site for these two different social constituencies to meet: individuals with surpluses can place their money with the bank, and the bank can disburse those surplus funds to entrepreneurs and consumers who need the money immediately in exchange for repayment in the future. The bank also specializes in investigating the ability of the prospective borrowers to repay the funds borrowed from savers, resulting in further efficiency gains to society by reducing credit risk and thus lowering the risk of misallocated savings. Banks thus allow savings to be aggregated on a very wide scale and reallocated to productive uses throughout the economy, something that would be practically impossible if individual savers and individual borrowers had to find one another directly. Banks, therefore, perform tasks that would otherwise fall on savers and borrowers, respectively, but does so at a much lower aggregate (and in most cases, individual) cost than would be the case in their absence. Once the bank as an institution is developed, therefore, it would be socially wasteful to insist that the only permissible means of finance continue to be principal-to-principal contracting as had been largely assumed to be the case in pre-modern Islamic law.

Conventional, for-profit banking, however, poses at least two problems from the perspective of Islamic law. The first was that its profits were derived almost exclusively from interest income from loans. The second was that the bank guaran-

teed the deposits of savers even as they gave savers a return, an "interest," on the funds that they deposited with the banks. The first principle violated the charitable nature of loans in Islamic law, which, as previously noted, characterized loans as purely *altruistic* transactions. The second principle violated the distinction between a deposit (*amana*) and a debt (*dayn*): by guaranteeing the return of the deposit, the depositor's claim becomes transformed into a debt payable by the bank to the depositor, in which case it is prohibited for the depositor to receive a return in respect of that debt by virtue of the bank's guarantee of repayment. The depositor would only be entitled to the interest under classical juristic notions if the deposit was subject to loss, a possibility that was legally, if not practically, eliminated by virtue of the bank's guarantee of the deposit.[49]

In order to solve this problem, Muslim bankers and sympathetic jurists interested in creating an Islamic institution that acted like a conventional bank searched the Islamic tradition in order to find the closest analogue to financial intermediation that could function on a wide scale. They settled on the *mudaraba* or *qirad* for two principle reasons. First and unlike other kinds of Islamic partnerships, this contract contemplates passive investment on the part of individuals with surplus funds who invest the money with an entrepreneur pursuant to a pre-determined profit-sharing agreement between the entrepreneur and the investors. Because the entrepreneur could then invest the capital of the first *mudaraba* in a second *mudaraba*, known as *al-mudarib yudarib*, this structure allows for financial intermediation akin to the function of modern banks. It is not surprising, then, that when for-profit, commercial Islamic banks first made their appearance in the mid-70s, they used the *mudaraba* as the model for their operations.

Nevertheless, the so-called two-tiered *mudaraba* has not

proven to be an ideal structure for financial intermediation. First, and in contrast to a conventional bank, the entrepreneur, that is, the Islamic bank, cannot guarantee the capital of the depositors, at least according to the historical doctrines of Islamic law:[50] if he guarantees the deposits, then the depositors would not be entitled to a return, and so therefore, deposits must be liable for investment losses in order for the depositors to be entitled as a formal legal matter to a return on their investment. This, however, is contrary to the expectations of those who deposit money with Islamic banks, even if they are nominally deemed to be investors (*rabb al-mal*) rather than depositors. As a practical matter, depositors in Islamic banks do not expect that the funds which they place with Islamic banks should be exposed to greater risk of loss than funds placed on deposit with conventional banks. And, as a matter of politics, no government would allow a major Islamic bank to fail if that meant that the average depositor would lose his savings. In short, strict application of the doctrine of *mudaraba* to the deposits of Islamic banks would limit their effectiveness in mobilizing social savings, since they could only successfully attract funds which represent the risky portion of savers' portfolios. In practice, this risk is avoided using two strategies. The first is that the Islamic bank itself engages in a more conservative investment strategy in order to minimize the risk of loss – and thus the risk that depositors might lose their funds – and the second is reliance on either the existence of an explicit or implicit government guarantee of the bank's deposits.

These strategies to mitigate the problems inherent to the two-tiered *mudaraba* structure produces at least three problems. First, assuming strict application of traditional doctrines of *mudaraba*, investors would face a substantial risk of loss to their capital, which would mean that they would be willing to

give over to the Islamic bank only that portion of their savings that they are prepared to lose, and in the case of relatively poor individuals, they would be unwilling to give any of their meager savings to an Islamic bank. Since most Muslim countries are poor, it follows that a very small portion of societies' savings could be marshaled through Islamic accounts structured as *mudaraba*. Secondly, and on the assumption that Muslim scholars continue to prohibit Islamic banks from guaranteeing their customers' funds while allowing a third party to guarantee deposits, for example, the state, Islamic banks will likely choose to invest in excessively risky projects, secure in their knowledge that if the investments fail, the government will bail out their depositors, leading to a situation of "privatized gains, socialized losses." Such a policy will inevitably lead to poor use of social savings where the bank will finance many projects that do not deserve to be financed. Thirdly, an Islamic bank could adhere strictly to traditional Islamic norms, and in response become more *risk averse* than a conventional bank by maintaining higher ratios of cash reserves than conventional banks, investing in less risky projects, or both. This last strategy, which is in fact commonly adopted, inevitably results in substantial efficiency losses insofar as the Islamic bank will refuse to fund prospectively profitable, but relatively risky, ventures, in order to maintain sufficient cash reserves to pay the depositors. All things being equal, then, the conventional bank, operating with deposit insurance whose premiums are paid by the bank, would be more efficient in deploying savings than a similarly situated Islamic bank that cannot guarantee its deposits.[51]

If the case can be made that Islamic ethics commands us to minimize losses, then arguments contemplating the modification of traditional *mudaraba* doctrine in the context of financial intermediation to make it more effective in the deployment of

savings could be accepted. Because of the ubiquitous use of leverage in banking in privately owned banks, whether Islamic or conventional, for-profit banks have a structural incentive to pursue gains for their shareholders at the expense of the public that will implicitly guarantee the liquidity and the solvency of these institutions.[52] The two-tier *mudaraba* structure does nothing to solve the problem of moral hazard (*al-khatar al-akhlaqi*) that permeates commercial banking.

The most radical solution to this problem would be to abandon the two-tier *mudaraba* model in favor of a pure agency (*wikala*) model of investment pursuant to which the role of the Islamic bank is understood simply as the investment agent of the investors (depositors), and in that capacity, it agrees to guarantee the performance of the borrower whose loan it arranges.[53] Because the bank in this case is an agent and never owns the funds that will be provided to the borrower, the problem of guaranteeing the capital sum does not arise. Under this arrangement, the Islamic bank would earn its returns for its services in arranging the transaction, and not pursuant to a dubious claim that it is profiting from trade. A less radical solution from a practical perspective – although it would represent a substantial departure from existing doctrine – would be to require the bank, in its capacity as the investment agent in the first-tier *mudaraba* – to guarantee the deposits of the investors. This solution would be based on *istihsan* in light of the practical need to reduce the moral hazard involved in for-profit banking; it would also be fair to the bank insofar as the only economically valuable functions of Islamic banks is financial intermediation and evaluation of the creditworthiness of prospective borrowers, thus making the bank a better candidate for bearing the risk that the client defaults. Finally, a less drastic solution, at least in terms of doctrinal reform, would be to require the Islamic bank

to invest a certain amount of its own capital in the second-tier *mudaraba*, for example, 10%.

The need (*al-haja*) for an efficient system financial intermediation in the 21st century is just as legitimate as the need for 15th-century Andalusians to pool relatively small amounts of milk and small numbers of livestock in order to manufacture cheese efficiently. Likewise, applying the ordinary rule of *qirad/mudaraba* that would prohibit the entrepreneur from guaranteeing the funds would effectively prevent the benefits from financial intermediation from taking place, or it would require adoption of other solutions that themselves would substantially reduce the efficiency of the system of financial intermediation. The same problem faced the Andalusian Maliki jurists when they considered the legality of customary partnerships for the production of cheese: applying the rules of *riba* and *gharar* strictly would have prevented the achievement of efficient economies of scale and would have effectively prevented the people from pursuing their legitimate interest in realizing a gain from their own property, thus justifying a departure from the ordinary rules.

The same kind of reasoning ought to apply to the problem of guaranteeing the deposits of banks. Just as was the case for individuals who had small amounts of surplus milk, which they could not use to manufacture cheese except if they entered into partnerships with others, so too small-savers are not in a position to invest their surplus funds unless they are aggregated with the funds of others. However, they would be unwilling to invest those funds – given that they are rationally risk-averse given their liquidity constraints – except on terms that are guaranteed. While a third party could guarantee their investments, for example, the state, this solution, because of moral hazard, would be wasteful because it would lead to overinvestment

in risky projects. Accordingly, the entrepreneur – in this case, the bank – must be held liable for the loss in order to prevent wasteful investments in high-risk projects. Only by providing a guarantee to small depositors, and imposing liability on the entrepreneur, will the full benefits of financial intermediation be obtained, and in light of the principle of *rafʿ al-haraj*, an exception to the rule that the entrepreneur is not liable to the investor for losses in capital ought to be recognized in the case of banks.

Zakat, Distributive Justice and Islamic Public Finance in a Modern Setting

I now wish to turn to questions of distributive justice in Islamic ethics, and how this should impact a modern conception of *zakat* and public finance generally. As mentioned above, in principle, the law of *zakat* provides that each Muslim (or citizen, in the modern context), is guaranteed a minimum subsistence income. This is evidenced by the previously cited Maliki rule that anyone lacking a year's worth of food is entitled to receive *zakat* (*faqir la yamliku quta ʿamihi*). The insistence that each person should, in principle, be entitled to a year's worth of provisions without being forced to sell his labor is consistent with the principle of *anti-subordination* that is reflected in many rules of *fiqh* and clearly works to support Islam's commitment to non-subordination. People are much less likely to accept humiliating conditions of employment if they are guaranteed a minimum income that at least allows them to live independently of others.

The strong commitment to establishing a minimum entitlement to subsistence is in tension, however, with the formalistic nature of most of the rules of *zakat*, including, the rules establishing liability for *zakat*. For example, a person may

simultaneously be liable for *zakat* if he owns the minimum amount of property required (*nisab*) but nevertheless be eligible to receive *zakat* to the extent that he also does not own enough to provide him with a year's worth of food, a rule that indicates the failure of the jurists to index the *nisab* to prevailing inflation rates. In short, many of the classical fiqh rules were formulated without giving adequate regard to the general policies of *zakat* as an effective system of social justice.

The biggest obstacle to using *zakat* as an effective tool for social justice is the fact that far from being a unified system of taxation, it provides substantially different rules depending on the nature of the property, a feature that has substantially reduced the Islamic tax base. As is well known, the jurists recognized three different categories of property for purposes of *zakat*: livestock (*mawashi*); agricultural (*harth*); and cash money (*ʿayn*), meaning gold and silver, or money's worth (*qima*). The most important difference in the treatment of these various types of property is that agricultural products are liable for *zakat* immediately upon harvest (after deduction of the *nisab*), while in the case of money, it is assessed only on savings, not income. This leads to substantially unfair results. Consider the case of a wheat farmer. At the end of the season, he successfully harvests his crop; he is entitled to keep the *nisab* – five *awsuq*, a year's worth of wheat – for himself – but he must pay *zakat* on everything that exceeds this amount as of the day of the harvest. A person dealing in cash, however, whether a merchant or an employee, on the other hand, is only liable for *zakat* with respect to what he has saved, and then only if he has held on to that savings for one year, and if the savings are in excess of the *nisab*, which in the case of cash is either 20 gold dinars or 200 silver dirhams, or their value in cash substitutes, for example, *fulus* or goods held for sale (*ʿurud*). This

leads to dissimilar treatment of the farmer and the merchant/employee: the farmer pays *zakat* out of his income, while the merchant/employee pays his *zakat* out of savings. A person dealing in cash, therefore, can always minimize his *zakat* obligation simply by increasing his consumption! Such a perverse result hardly seems consistent with Islam's aspirations to achieve social justice; the Qur'an condemns excessive consumption as immoral and wasteful, but the rules of *zakat* as historically elaborated seem to encourage consumption among those who deal in cash, at least at the margins.

Historically, those who dealt in cash – largely, the people who lived in cities – were also privileged by the rules of *zakat* insofar as their property was deemed by many of the jurists to be *amwal batina* – hidden property – and accordingly, the state had no right to investigate the extent to which they held surplus cash. In other words, urban dwellers largely enjoyed the privilege of self-reporting their savings for purposes of liability for *zakat*. By contrast, agricultural output and grazing livestock were considered *amwal zahira* – manifest property – and accordingly, the state had the right to calculate and compel owners of livestock and agricultural property to pay amounts due as *zakat*.

From the perspective of modern tax theory, the treatment of cash in the rules of *zakat* represents "leakage" from the tax base: property that ought to be taxed is not being captured in the rules that define the tax base. No system of taxation captures the tax base perfectly, and it is not surprising that the classical rules of *fiqh* should have suffered from some leakage as well. The important point to note, however, is that in pre-modern age, such leakage was relatively small because agricultural production was by far the largest sector of the economy. For us in the modern world, however, the cash economy is the largest

sector of the economy, and we tend to consider the rules governing the treatment of cash in the law of *zakat* as the *asl*, the basic norm, and the other rules as secondary. Consider the case of Egypt: even though Egypt would hardly be considered an industrial powerhouse, the combined agricultural and livestock sectors represent only 14.5% of the country's annual economic output,[54] yet according to the rules of *zakat*, cultivators would be the only Egyptians subject to *zakat*-based liability on their income without first enjoying the right to satisfy their demands for consumption.

It is clear that a purposive approach to the rules of *zakat*, taking into account that the goal of *zakat* is to establish a minimally just distribution of the community's income, would require a radical revision in the rules of tax base to which *zakat* is applied, such that those who deal in cash are treated in line with those of agriculturalists: they should be allowed a deduction equivalent to a year's worth of subsistence level income, but they should then be liable for *zakat* based on the rest of the income they earn during that year, regardless of how much they save.[55] Such a departure from historical doctrine would be justified by analogy to the treatment of agriculturalists: insofar as *zakat* was an income tax and not a tax on savings with respect to agriculturalists, those who earn their living in cash ought to be subject to the same rules by virtue of the fact that they represent the largest portion of the tax base, just as agriculturalists represented the largest portion of the tax base in historical eras.

A reorientation of *zakat* to treat those who deal in cash similarly to agriculturalists would raise a substantial amount of revenue that could be used to fulfill the ambition of *zakat* to guarantee every person a minimum subsistence level income, something that is a condition for achieving human dignity and freedom, something that is required by Islam's commitment

to resist unnecessary subordination of one person to another. It would not, however, be enough on its own without increasing the rate of *zakat* that is payable. The historical rate of 2.5% should be adjusted in the light of the needs of current Muslim states to achieve the goal of *zakat*, namely a just distribution of the community's income while at the same time preserving incentives for private economic initiative. Unfortunately, the historical rules of *zakat*, because of the jurists' formalism, have been unable to countenance revising the rates of *zakat* that individuals must pay.[56] This is unfortunate, not only because it prevents *zakat* from achieving its goals, but also because there is no textual authority that limits Muslims to the historical rates discussed in the books of *fiqh*. In fact, the textual evidence used to establish the basic rates that apply to private property derives from actions and decisions of the companions rather than express Prophetic (S) precedent or Qur'anic text.[57] And even if we assumed that the companions and successors were acting on the basis of Prophetic practice that was not explicitly attributed to the Prophet (S), it would be more appropriate to interpret the relevant precedents in the light of the role of the Prophet as *Imam* of the community (*tasarruf bi'l-imama*) rather than in his role as messenger of God (*tasarruf bi'l-futya*),[58] especially in light of the fact that the relevant precedents show that different kinds of properties were subject to different rates, a fact that strongly suggests that these rules were originally developed to further the public good (*al-maslaha al-ʿamma*) and were not intended to be devotional rules (*taʿabbud*).

While *zakat* is intended to further distributive justice within an economy, it is not sufficient in the absence of macroeconomic policies that promote sustainable economic growth: one cannot achieve distributive justice if there is no surplus to redistribute. *Zakat* can only function, then, within an overall framework of

effective macroeconomic policy, an important pillar of which is public finance. The *fiqh*, however, provides very problematic limitations on the tools available for legitimate public finance, seemingly limiting permissible taxation to the taxes set forth in revelation, namely, *zakat* and *kharaj*. Indeed, one Maliki author claims a consensus for the proposition that levying taxes on a Muslim in excess of the textual rates is a matter of consensus, and whoever violates this consensus has abandoned Islam insofar as he has violated a cardinal Islamic principal.[59] When this rule is combined with the jurists' decision to fix the rates of *zakat* and *kharaj*, the state is deprived of the financial tools necessary to manage flexibly the legitimate needs of the public, especially with respect to financing badly needed investments in public goods, such as education, health, and public infrastructure.

By tying the hands of the state with respect to taxation, the jurists were forced, in certain circumstances, to adopt second-best solutions that were far from optimal from the perspective of a rational system of public finance. For example, the Shafiʿis adopted a doctrine of compelled loans, whereby the state could force the rich to lend money to the state in circumstances where the treasury lacked sufficient resources to meet its obligations.[60] While most Muslim states today have attempted to establish rational systems of taxation in spite of these doctrinal limitations, and many modern jurists have permitted taxation beyond that of *zakat* and *kharaj*, albeit reluctantly and on the assumption that they are exceptional measures,[61] it remains the case that many Muslims, scholars and laity, resent taxes, believe them to be inherently unjust and Islamic, and believe that it is Islamically permissible to engage in tax evasion, if such taxes are in excess of the obligations imposed by revelation.[62]

From the perspective of the Islamic objectives of public finance, however, the classical position rejecting the legitimacy of taxation in excess of what is imposed in the law of *zakat* and *kharaj* must be categorically rejected. What the Prophet (S) prohibited was *mukus*, taxes taken coercively from a tyrant to fulfill his own private ends, not money taken by a legitimate state used to further the legitimate ends of the public. Indeed, to the extent that the state is pursuing ends that are morally obligatory for it to pursue from the perspective of Islamic law because they are constitutive of the public good (*al-maslaha al-ʿamma*), that is, what the jurists call *furud kifaya*, then one might say it is obligatory on individual Muslims to obey rational rules of taxation that are intended to provide the state with the means to fulfill those obligations. This is consistent with the principle of *usul al-fiqh* that "what is an indispensable condition for the fulfillment of an obligation is itself an obligation" (*ma la yatimmu al-wajib illa bihi, fa-huwa wajib*). The pre-modern jurists recognized quite a wide scope for communal obligations. For example, pursuit of all the secular arts (*al-hiraf al-muhimma*) that are related to achieving the public good was historically recognized as a communal obligation, just as religious goods such as teaching religious sciences was a communal obligation.[63] It should be recognized that where the state chooses to provide these goods, then the citizens have an obligation to pay taxes levied to finance the provision of those goods.

This forces us to consider whether the state should have a role in fulfilling these collective duties, or whether it is permissible to leave the field open to private individual Muslims to discharge these obligations. After all, while the jurists identified various activities as being collective obligations, they did not say that it was the responsibility of the state to achieve them; indeed, they make it clear that as long as someone ful-

fills the obligation, then the community has fulfilled its duty. And given the broad class of actions that constitute collective obligations, for example, preparing the dead for prayer (*tajhiz al-mayyit*) and conducting funeral prayers (*salat al-janaza*), returning greetings of peace (*radd al-salam*), and praying for the one who sneezes (*tashmit al-ʿatis*), it would be inconceivable to conclude that it is always, or even presumptively, the state's responsibility to discharge all collective obligations. What is needed, then, is a principle that allows us to distinguish between which collective obligations ought to be fulfilled by the state in its capacity as representative of the Muslim community, and which collective duties can be left to individual Muslims to fulfill in their private capacities. Here, I would again suggest that Islamic ethics requires us to use considerations of efficiency, meaning, that those cases in which the state is in the best position to discharge the obligation at the lowest cost, responsibility should lie with the state, and the state can legitimately tax the population in order to fund the programs necessary to satisfy the obligation.

The provision of such basic tasks of modern government as universal education, universal health care, public infrastructure, for example, highways, bridges, railroads, and ports, constitute what most economists would call "public goods." Because they are public goods, the private market fails to produce them, or fails to produce them in an economically optimal quantity. To understand why, consider the case of education. If it were to be provided solely by the market, the only people who could acquire this good would be those who could afford it. The more wealth a person has, the more education he or she could buy. But unless it is the case that the cost of a minimally necessary education is less than the income of all the citizens of a particular state, the cost of education will have to

be subsidized to ensure that everyone in society receives a minimally adequate education. Otherwise, the law of supply and demand means that some people in society will be unable to pay the market-clearing price for education, and therefore they will be forced to forego education, causing a social loss. The public good, because it requires universal education, can only be achieved if the public subsidizes the cost of education for those lacking sufficient means to pay for it themselves. Taxes are the only reliable means to fund this public good.[64]

The same is true of health care: from a social perspective, it is always rational to treat a sick person when the benefits to be gained from curing, or even treating the sick person, exceed the costs of the treatment. Persons with chronic diseases, such as diabetes, high cholesterol, or high blood pressure, are good examples. Such persons gradually lose their ability to function as productive members of society if they are left untreated, and indeed, in some cases, their chronic conditions may develop into full-blown health crises that lead to substantial costs, for example, an untreated diabetic who may become blind or lose a limb, or a person with untreated high blood pressure or cholesterol may suffer a stroke or a heart attack. From a social perspective, it is rational to treat these individuals in order to prevent their conditions from deteriorating or leading to potentially catastrophic health consequences in the future for two reasons. The first is that as a result of the occurrence of a health catastrophe society loses the contributions such persons would have made to it. The second reason is the actual out-of-pocket costs that will have to be incurred by society as a result of the health catastrophe, including costs of medical care and post-event costs of recovery, such as increased monitoring and care, if the patient, for example, becomes bed-ridden or otherwise is incapable of taking care of himself or herself. Although it would

be rational for such persons to be treated to prevent these losses from occurring, it will inevitably be the case that many individuals will not be able to pay for the medication or other health care services necessary to treat their condition were it the case that such services or medications are provided exclusively by the private sector.

Because the private sector will only provide the service if it can do so for a profit, it will undersupply the required good of health care. The only solution is to have the government provide the care, as was the case for universal education. The government will only be able to do so; however, if it can collect revenue from the public in an efficient manner, and if the population believes that it is their duty to pay such taxes when the government demands them. Accordingly, whenever the government is reasonably viewed as the most efficient institution with respect to the discharge of a *fard kifaya*, Islamic ethics should be understood as requiring that this service be provided by the government and not the private sector; that the government be authorized to levy taxes in whatever amount necessary to allow it to discharge those obligations; and, that the citizenry is under a moral obligation to pay such taxes when they are levied.

Having established the legitimacy of taxation for the purpose of financing the legitimate collective goals of the community, the question then arises as to what methods of taxation and public finance should be used, and how to prioritize public spending. In this case, pre-modern Islamic law provides important principles in support of social justice. One of these is the legal principle of *darʾ al-mafasid qabla jalb al-masalih*, warding off harm is to be given priority to obtain additional benefits. While it is not completely clear how this principle can be applied in all cases, in general, I understand it as an Islamic version of

the American philosopher John Rawls' difference principle, namely, that inequality is to be justified by the extent, and only to the extent, that permitting inequality improves the welfare of the worst-off in society. One can find many statements from the jurists that support this proposition. Jalal al-Din al-Suyuti, for example, wrote in his *al-Ashbah wa'l-NaZa*ʾir that "It is not permissible for the Imam to prefer anyone over the most needy with respect to spending the treasury's funds."[65] The Hanafi author of *Ghamz ʿUyun al-Basaʾir Sharh al-Ashbah wa'l-NaZaʾir* quotes another Hanafi jurist for the proposition that the well-off have no claim to money from the treasury unless they are performing a specific task for the benefit of the community:

"Al-Razi was asked about the treasury, whether the rich have a claim to its revenue; he said, 'No, unless he is a scholar or a judge and the jurists (*fuqahaʾ*) have no claim except for a jurist who spends his days teaching law or the Qur'an.'"[66]

I take from this principle that a fundamental principle of Islamic public finance is that government spending must be targeted to prioritize the requirements of the neediest sectors of society. Failure to adhere to this principle in countries such as Egypt, where substantial amounts of public revenues are spent on subsidies that benefit the wealthy, for exampe, energy subsidies and subsidies for university education, disproportionately benefit those Egyptians who are already well-off, and have had the effect of substantially reducing the state's commitment to public investment in favor of financing private consumption by the well-off. It should not be surprising, then, to learn that only 12.5% of Egypt's gross domestic product goes to savings, ranking it 125th in the world in 2013, while Malaysia, a country whose per-capita income is almost three times greater than Egypt, devotes nearly a third of its GDP to investment, giving it an impressive ranking of 19th in the world in 2013.[67] It also

follows that in raising revenue, the government should focus on the relatively well-off and not the poor, and accordingly, should adopt progressive taxation policies.[68]

The Islamic Development Bank (IDB) could play an important role in this context by encouraging Muslim countries to rationalize their public finances so that public money is spent more rationally to develop the human capital of Muslim countries by providing financing to assist these countries seeking to transition from inefficient subsidies toward public policies that prioritize human development, as well as encouraging Muslim countries to adopt effective progressive taxation schemes rather than relying on regressive sales taxes. Unfortunately, the IDB for the most part has functioned primarily to assist Muslim countries finance international trade rather than finance the development of indigenous human capital or encourage Muslim countries to reform their spending priorities or public finances in a fashion more consistent with Islamic values of distributive justice and the needs of national development.

Evaluating the Performance of the For-Profit Islamic Financial Sector from the Perspective of Purposive Jurisprudence

Much of the practice of the for-profit Islamic financial sector, instead of seeking to avoid dead-weight losses, or to minimize transaction costs as a purposive approach to Islamic law would require, engages in meaningless transactions that *increase* dead-weight losses for the sole purpose of giving the appearance of complying with Islamic law (and earning additional profits). This problem of adherence to forms simply for the sake of compliance with forms is at its furthest extreme with the *tawarruq* transaction, but it is also present in the vast major-

ity of contemporary Islamic financial transactions where credit transactions are being consciously disguised as contracts of sale or lease in order to avoid the accusation of *riba*.

Such a strategy suffers from numerous defects, only one of which is that it generates dead-weight losses from a social perspective relative to their conventional, non-Islamic counterparts. More seriously, it risks undermining the public's confidence in Islam when they discover that the Islamic product is substantially no different from the conventional product, and in some cases, even more burdensome.[69] Islamic products, particularly in circumstances where the Islamic sector is small relative to the conventional sector, will generally be more expensive than the comparable conventional product by virtue of the lack of an economy of scale. Even where economies of scale exist, however, the Islamic product may be substantially worse in certain cases for the consumer than the conventional one, as the controversy around default under credit-sale financings (*bayʿ bi-thaman ajil*) have proven in Malaysia. Because the classical *fiqh* deems the credit price of a good to be fixed at the time of the contract, and because it views the discount of a debt in exchange for early payment to be a kind of *riba* (*daʿ wa taʿajjal*), a debtor who has purchased property using the credit sale structure is worse off than he would have been had he financed the transaction using a conventional loan: under the classical *fiqh*, if the bankrupt debtor defaults, the entire, undiscounted amount of the debt, which in the Islamic contract is denominated as the contract price for the good sold (*al-thaman*), becomes due and payable. In a conventional loan, by contrast, because the debtor's obligation is divided into principal and interest, the debtor is only under an obligation to pay interest when it accrues. Accordingly, he is only required to repay the outstanding amount of the loan at the time of the

default as well as any accrued, but unpaid, interest as of the date of default. In the Islamic contract, by contrast, the debtor is under a categorical obligation to pay the "price," even if he defaults one day after entering into a 25-year credit sale.

As a result, while the economic characteristics of an Islamic credit sale transaction and a conventional loan transaction are essentially the same, that is only true if the debtor performs the contract in full. If the debtor defaults and goes bankrupt, the debtor in the Islamic contract becomes liable for the entire amount of the contract, while the conventional debtor will only be liable for the principal plus interest accrued to the moment of default. The sooner the debtor defaults, moreover, the greater the loss will be. Accordingly, if the transaction entails a 25-year period of repayment, and the debtor defaults in year 3, the Islamic debtor's loss will be substantially magnified relative to the loss of a conventional creditor who also defaults in year 3, with the gap only gradually shrinking over the 25-year term.

This feature of Islamic credit law became extremely controversial in Malaysia when debtors discovered that upon default they were expected to pay the entire contract amount. The problem was only resolved when the Malaysian Central Bank intervened and forced Islamic banks to discount the debts owed by their debtors down to their present values.[70] Ironically, it was Malaysia's secular authorities that intervened to protect the Malaysian Muslim consumer, and not the *ulama* who continue, in too many cases, to adhere to the formal letter of historical doctrines without taking into account the real-world impact of those rules, and without taking into account advances in the sciences of finance, accounting, and risk modelling.

Islamic equity investing – the creation of Islamic equity indices such as the Dow Jones Islamic Index – poses fewer problems to the principle of reducing dead-weight losses than the

credit practices of Islamic banks, but it also is not free of difficulties. The biggest problem facing Islamic equity investing is the difficulty of constructing a reasonably diversified portfolio of shares using the various "Islamic" screens that scholars have stated must be met in order for an equity investment to be Islamically permissible. The first of these requirements, that the company be engaged in a permissible activity, is non-controversial and of course must be observed. What is more problematic are the financial screens that jurists insist on applying to any equity investment. The primary financial screens are those that test the leverage of a firm; the amount of income it receives from interest; and, the extent to which a firm's assets consist of accounts receivable rather than tangible assets.

The justification for the leverage screen is that a Muslim should not invest in a firm if it is substantially financed by debt, which for these purposes is defined as $1/3^{rd}$ (i.e. there should be $2 dollars of equity for every $1 dollar of debt in the firm's capital structure).[71] Presumably, for purposes of applying this leverage screen, it is irrelevant whether the debt is Islamic debt or conventional debt. While this rule has been criticized insofar as it is not clear why the jurists chose the $1/3^{rd}$ benchmark, a more fundamental criticism is that it is not at all clear how this screen can be meaningfully applied. Should it be applied to the book value of a firm's debt and equity, that is, paid-up capital plus retained earnings, or should it be applied to the market valuation of the firm's debt and equity? While it gives a relative objective measure of a firm's value, book value loses its value over time as an accurate presentation of a firm's value, or even of its balance sheet. In the case of a successful firm, using the book value of the firm's equity will substantially understate its true worth in the market as measured by the profitability of the firm, which ultimately supports both a higher sale price for the

company if it were to be sold to a third party, and an ability to support a relatively large amount of debt in light of its ability to earn substantial profits in a sustainable fashion. In the case of a failing firm, however, book value may *overstate* the value of the equity. This reflects the general inability of the firm to earn substantial or sustainable profits with its assets, thus justifying a low price for the company and an inability to support substantial debt, which may, in fact, be one reason why the firm may have a relatively small amount of debt. On the other hand, the use of market capitalization is also not free of difficulties: when market prices are high, that is, price-to-equity ratios are high, then the universe of firms which pass the leverage screen will increase. If, on the other hand, market prices are low, then the universe of firms which pass the leverage screen will shrink.[72]

It might make more sense to reconcile the goal of encouraging reduced reliance on debt with the goal of having a reasonably diversified investment portfolio by linking the two concerns such that Muslim equity investors are allowed, for example, to invest in the least leveraged companies from each of the sectors that make up a diversified portfolio. Such modification – instead of relying on one measure of excessive debt (1/3rd) – would be more sensitive to the financing characteristics of various sectors of the economy. Where one sector supports relatively high level of debt because of regular and predictable cash flows, such as real estate or public utilities, the permitted leverage ratio would exceed 1/3, while in other sectors which do not tolerate high levels of debt, for example, the hi-tech sector, the permitted leverage ratio might be less than 1/3.

It is crucial, then, that in discussing Islamic finance, we judge it not by its adherence to formal doctrinal labels (although it would be found wanting in that respect as well), but rather by

reference to its substantive successes or failures in achieving the various goals of an Islamic economy, one of which is its effectiveness in channeling savings into productive uses. And in this respect, Islamic finance, at least with respect to its credit instruments, for example, *sukuk*, *murabaha*, and *ijara-mutanaqisa* facilities, and *tawarruq* lines of credit, does little more than mimic conventional financial products but with added expense and complication; instead of avoiding or reducing dead-weight losses – what we have argued should be the definition of *haraj* for legal purposes – current Islamic finance products actually increase dead-weight losses relative to conventional products and thus produce an increase in *haraj*. The relative inefficiency of Islamic financial solutions, moreover, is not limited to Islamic credit instruments but also extends to Islamic equity strategies.

As long as Muslim jurists are unwilling to adopt a more functional approach to private, for-profit finance, however, the current practices of Islamic finance may nevertheless be defensible if they are successful in marshaling social savings to finance public and private investment and consumption. This would only be true if it could be shown that the creation of Islamic financial products – whether in the credit or the equity markets – have resulted in a net increase in banking deposits and equity investment in public companies, that is, it has convinced people who otherwise would not have deposited their surplus funds with conventional banks or to invest them in public equity markets, to place them with Islamic banks or Islamic investment funds, thus increasing the overall efficiency of the financial intermediation system. In the absence of such evidence, the existence of the Islamic financial system would simply divert resources from the conventional system to the Islamic system with no obvious efficiency gains to society, but raising the possibility of a decrease in overall efficiency in light

of the increased transaction costs associate with Islamic financial products.

Finally, we would be remiss if we smugly assumed that Islamic banks are exempt from the structural instability that plagues conventional for-profit banking. Conventional banks pursue high-risk, high-return investments because that is the optimal strategy for the maximization of their profits, insofar as they earn profits based on the "spread" – the difference between what they pay their depositors and what they receive from borrowers. For-profit, privately owned Islamic banks suffer from the same problem: they too earn their profit through the spread between what they pay investors in the first-tier *mudaraba* and what they receive as their share of the profits earned from the second-tier *mudaraba*. This structure not only poses structural risks to the safety and soundness of the banking system, but it also potentially distorts the allocation of savings away from socially desirable goals, such as public investment in favor of excessive private consumption. Particularly where there are few opportunities for private investment in profitable businesses, banks will gravitate toward consumer finance, which has very little positive impact on economic development. Muslim-majority states would be well-advised to consider strategies for bifurcating various institutions of financial intermediation, for example, by encouraging the spread of mutually owned banks or credit cooperatives for the purpose of financing private consumption, and limiting for-profit banking to the corporate or sovereign sectors.[73] By prohibiting for-profit ownership of consumer credit agencies, states can substantially reduce the risk that the profit-seeking incentive of banks will lead to a bubble in consumer credit.

Conclusion

I have tried to show in this essay that Islamic ethics provide a rich body of teachings that promote the efficient use of social resources and support a conception of distributive justice that favors the poor while at the same time preserving substantial freedom for private exchange. The sources of Islamic law, the Qur'an and Sunna, provide important precedents for public and private finance, and when properly interpreted in the light of the goals of promoting growth, human dignity and a just distribution of wealth, can and should contribute to the development of Muslim countries. At the same time, however, I would be remiss if I did not point out that if the failures of Muslim states in sustaining real human development is not a product of their religious values, then it is a failure of their politics: without the political will to implement rational public policy that promotes human development, it is unlikely (and indeed, unfair) to believe that private investment, whether supported by conventional or Islamic finance, will succeed in achieving sustainable development. In other words, it is impossible to avoid politics: unless Muslim governments begin to adopt rational economic policies, or are forced to adopt such policies, I suspect that Muslim countries will continue to be economic laggards, whether or not private finance develops along Islamic or conventional lines. Theoretical discussion of Islamic finance, such as that encouraged at this workshop, can play an important role, however, in educating the government and the public about the importance of adopting rational economic policies that support development and social justice as not only a crucial part of Islamic ethics, but also indispensable to promoting national development.

Notes

1 Muhammad b. Idris al-Shafiʿi, 3 *al-Umm* (*Dar al-Maʿrifa*: Beirut, 1990), p. 224.

2 Felicitas Opwitas, "*Maslaha* in Contemporary Islamic Legal Theory," 12,2 *Islamic Law and Society* (2005), pp. 215-20.

3 Indeed, at its extreme, the textualist approach to *maqasid* would obliterate the vital distinction between rules of devotion (*al-ʿibadat*) and transactional rules (*muʿamalat*).

4 Ibn Rushd *Bidayat al-Mujtahid*, ed. ʿAli Muhammad Muʿawwad and ʿAdil Ahmad ʿAbd al-Mawjud (Dar al-Kutub al-ʿIlmiyya: Beirut, 1996), p. 326.

5 According to this report, after ʿAbdallah informed the Prophet (S) that there were insufficient camels in the public treasury to equip a proposed military expedition, the Prophet (S) ordered him to purchase additional camels on credit, purchasing one camel for two to be delivered at the time *zakat* would be collected. Abu Dawud Sulayman b. al-Ashʿath al-Sijistani, 3 *Sunan Abi Dawud* (*al-Maktaba al-ʿAsriyya*: Beirut, n.d.), hadith no. 3357, p. 250. ʿAli b. ʿUmar al-Daraqutni, 4 *Sunan al-Daraqutni* (*Muʾassasat al-Risala*: Beirut, 2004), hadith no. 3055, p. 37. See also, Sulayman b. Ahmad al-Tabarani, 13 *al-Muʿjam al-Kabir* (*Maktabat Ibn Taymiyya*: Cairo, 1994), hadith no. 155, p. 63 (ʿAbdallah b. ʿAmr b. al-ʿAs was asked whether it was permitted to sell one camel for two, one cow for two, and one sheep for two, and he cited his experience equipping the Prophet's expedition). This report contradicts al-Tahawi's claim that the original ruling permitting this kind of sale was abrogated. See Abu Jaʿfar Ahmad b. Muhammad al-Tahawi, 4 *Sharh Maʿani al-Athar*, ed. Muhammad Zuhri al-Najjar and Muhammad Sayyid Jad al-Haqq (*ʿAlam al-Kutub*: Cairo, 1994), hadith no. 5737, p. 60.

6 For example, Maliki jurists believe certain contracts are exceptional, for example *bayʿ al-salam* or *qirad*, and accordingly, it is not permitted to derive new contractual forms by means of analogy to these contracts which are themselves deemed to be outside the operation of the ordinary principles of trade. See, for example, 3 *al-Sharh al-Saghir*, Abu al-Barakat Ahmad b. Muhammad b. Ahmad al-Dardir, ed. Mustafa Kamal Wasfi (*Dar al-Maʿarif*: Cairo, n.d.), p. 684 (rejecting the permissibility of using anything other than gold or silver coins as capital for a *qirad* on the grounds that "the *qirad* contract is a dispensation so its permissibility is restricted to what has been reported, and anything outside of that remains prohibited in accordance with the ordinary rule of prohibition [of a hire-contract for an indefinite wage]" (*li-ʾanna al-qirad rukhsa yuqtasar fiha ʿala ma warada wa yabqa ma ʿadahu ʿala al-asl min al-manʿ*)).

7 *Bulghat al-Salik,* p. 29 (*bayʿ al-ghabn jaʾiz*).

8 *Bulghat al-Salik,* p. 445 (explaining that it is impossible to include commercial contracts, such as sales, partnerships, and *qirad*, because the principles governing the two sets of contracts are incompatible, marriage being based on generosity and commercial contracts based on covetousness (*al-nikah mabni ʿala al-mukarama wa'l bayʿ wa ma maʿahu [al-qirad wa'l-qard wa'l-sharika wa'l-sarf wa'l-musaqat wa'l-jiʿala] mabni ʿala al-mushahha*)). Ibn Rushd the Grandfather illustrates the difference in the two kinds of contracts when he discusses the non-obligation of the guardian to disclose the moral defects of the bride, such as non-virginity, even if that would result in a reduction of the dower, while a seller is obliged to disclose any defects in the good if it would reduce the price of the good by noting that the marriage contract is governed by a presumption of generosity, *mukarama*, while a contract of sale reflects an adversarial relationship (*mukayasa*). See 4 *al-Bayan wa'l-Tahsil*, Ibn Rushd al-Jadd, p. 263.

9 *al-Sharh al- Saghir* p. 508 (an agent entrusted with selling or purchasing a good must act for the benefit of the principal (*was faʿala al-wakil al-maslaha wujuban . . . li-muwakkilihi*) and he may neither purchase for more, nor sell for less, than the market price (*thaman al-mithl*)).

10 *al-Sharh al- Saghir*, p. 710 (*wa laysa li-ʿamil ay yahrum ʿalayhi hiba . . . wa law li'stiʾlaf*).

11 *al-Sharh al- Saghir*, p. 464 (*wa lahu . . . al-tabarruʿ fi mal al-sharika bi-ghayri idhni sharikihi bi-shayʾ ka-hiba wa hatita li-baʿd thaman bi'l-maʿruf in istaʾlafa bihi . . . qulub al-nas li'l-tijara aw khaffa al-mutabarraʿ bihi . . . wa dafʿ kisra li-faqir*).

12 *Bulghat al-Salik* Ahmad b. Muhammad al-Sawi, ed. Mustafa Kamal Wasfi (Dar al-Maʿarif: Cairo, n.d.), p. 681. (*wa kana [al-qirad] fi'l-jahiliyya fa-aqarrahu al-mustafa ʿalayhi al-salat wa'l-salam fi al-islam li-ʾanna al-darura daʿat ilayhi li-hajat al-nas ila al-tasarruf fi amwalihim wa laysa kull ahad yaqdir ʿala al-tanmiya bi-nafsihi wa huwa mustathna li'l-darura min al-ijara al-majhula*).

13 *Al-Hadiqa al-Mustaqilla al-Nadra*, ed. Jalal ʿAli al-Qadhdhafi al-Jihani (*Dar Ibn Hazm*: Beirut,

2003). See fatwas nos. 157 (pp. 97–98), 168–71 (pp. 102–6). This was known as *sharikat al-ʿal-ufa*.

14 *Ibid*, fatwa no. 185 (p. 110). See also, 5 *al-Taj wa'l-Iklil* (*Dar al-Fikr*: Beirut, 1992), pp. 21–2 (discussing controversy regarding the bindingness of such a condition).

15 *al-Sharh al-Saghir*, p. 15 ("*taʿjil jamiʿ al-ujra fi mithli dhalika yuʾaddi ila dayaʿ amwal al-nas bi-sabab hurub al-jammalin idha qabadu al-ujra"*).

16 *al-Sharh al-Saghir*, p. 47.

17 *al-Hadiqa al-Mustaqilla al-Nadra*, fatwa no. 301 (pp. 170–73).

18 Ibn Rushd al-Jadd, *al-Bayan wa'l-Tahsil*, 12:16. ("*innama yukrah hadha liʾanna baʿdahu yukhrij akthar min baʿd fa-idha ihtaja al-nas ila dhalika fa-arju an yakuna khafifan li-ʾanna al-nasa la budda lahum mimma yuslihuhum wa'l-shayʾ alladhi la yajiduna ʿanhu ghina wa la budda fa-arju an yakuna lahum fi dhalika saʿa in shaʾ* a allahu wa l*a ara bihi baʾsan*").

19 Ibid. (*qawl Malik istihsan dafaʿahu li'l-darura ila dhalika idh la yataʾatta ʿasr al-yasir min al-jul-julan wa'l-fijl ʿala hidatihi [wa] muraʿatan li-qawl man yujiz al-tafadul fi dhalika min ahl al-ʿilm*).

20 See, for example, the 15th century Maliki jurist al-Mawwaq quoted Malik as saying that a starving person (*al-mudtarr*) may not only eat carrion, but that he also may take excess meat with him for his journey to be consumed in the future (*yatazawwad*); however, if he takes food belonging to someone on account of his hunger, he is only permitted to take enough to fill his stomach but he is not permitted to take more as provisions (*la yatazawwad*). This case arises in circumstances where the true owner of the food is not present to give the food to the starving person, something he is under an obligation to do. The narrowness of the exception in the case of another's property is on account of the need to respect the absent property's owner rights in that food. 3 al-Mawwaq, *al-Taj wa'l-Iklil* (*Dar al-Fikr*: Beirut, 1992), p. 233–34.

21 59:9, *al-Hashr*.

22 *al-Sharh al-Saghir*, p. 291. ("*al-qard iʿtaʾ mutamawwal fi ʿiwad mutamathil fi al-dhimma li-nafʿ al-muʿtafaqat*").

23 2:263, *al-Baqara*.

24 *al-Sharh al-Saghir*, p. 292.

25 Ibid., p. 139.

26 Ibid., p. 141.

27 Muhammad b. Muhammad b. ʿAbd al-Rahman al-Hattab, 6 *Mawahib al-Jalil* (*Dar al-Fikr*: Beirut, 1992), pp. 399–400. (Quoting several Maliki authorities who rejected lending out an orphan's property but encouraging the guardian to give it out as commercial investment, and sharply criticizing the Hanafi position allowing orphan's property to be lent out).

28 Shihab al-Din al-Qarafi, 6 *al-Dhakhira*, ed. Muhammad Hajji and Saʿid Aʿrab (*Dar al-Gharb al-Islami*: Beirut, 1994), p. 224.

29 *al-Sharh al-Saghir*, p. 143 (a gift is void if a legal obstacle arises preventing its completion prior to the donee taking possession (*hawz*)). Malikis consider both an unperformed gift and unperformed loan to be valid, meaning the donor or the borrower, as applicable, can sue the donor or the lender and compel his performance, but if something arises prior to performance, for example, the donor becomes bankrupt, then the obligation to perform the gift or lend the money lapses. Ibid. 3 *Bulghat al-Salik*, p. 295 (noting that every act of generosity, *maʿruf*, in the Maliki system transfers title by virtue of the contract except that the transfer is not complete until possession takes place, although there is a controversy within the school whether the requirement of possession also applies to loans). Shafiʿis and Hanafis, by contrast, hold that possession is a condition of the contract's validity, not its perfection, meaning that until the donor delivers the gift, the donee has no rights to the gift. 5 *Bidayat al-Mujtahid*, p. 363.

30 *al-Sharh al-Saghir*, p. 141 (an indefinite gift is valid). Likewise, a loan need not include a repayment date. 3 *al-Sharh al-Saghir*, pp. 295–96.

31 *al-Sharh al-Saghir*, pp. 670–71.

32 *al-Sharh al-Saghir*, p. 657.

33 Ibid., p. 665.

34 *Bulghat al-Salik*, p. 658 (*idha'ddaʿa shakhs al-faqr aw al-maskana li-yaʾkhudha min al-zakat fa-innahu yusaddaq bi-la yamin illa li-riba bi-an yakuna ẓahirahu yukhalifu ma yaddaʿih*).

35 *al-Sharh al-Saghir*, p. 661.

36 Ibid., p. 664.

37 The Hanafis reconcile the public assistance aspect of *zakat* (*muʾna*) with its status as a religious ritual (*ʿibada*) in the case of minors by holding that it accrues with respect to their property during their minority, but it only becomes due, for example, the obligation matures, when the minor reaches majority. 2 *al-Mabsut*, p. 162 and 3 *al-Mabsut*, p. 103. The Shafiʿis and Malikis, by contrast, impose the obligation to pay *zakat* on the property itself, so long as its owner is free (*hurr*), without regard to the owner's majority. 2 *al-Mabsut*, p. 162 (attributing this view to the Shafiʾis) and 1 *al-Sharh al-Saghir*, p. 589 (*zakat* is obligatory on all free persons owning sufficient property, even if they are not of majority or otherwise are not morally bound by the law (*ghayr mukallaf*)).

38 If he negligently fails to offer assistance and the person dies, thinking, for example, that he is not bound to help, then he is only monetarily liable, but if he knows that he is obliged to help, and refuses, then he is subject to *qisas*. 2 *Bulghat al-Salik,* pp. 169–70.

39 al-Mawwaq, p. 233 (*wa li'l-darura ma yasudd*).

40 This is consistent with several *hadith*s that reveal the Prophet (S) to have been reluctant to interfere in market transactions, for example, his reluctance to set prices for goods traded in the public market, and his statement prohibiting city-dwellers from acting as selling agents for itinerant Bedouin selling in the city.

41 Muhammad b. Ahmad al-Sarakhsi (*Dar al-Maʿrifa*: Beirut, 1993), 16 *al-Mabsut,* p. 56 (*wa in istaʾjara al-ibn abahu . . . li-khidmatihi lam yajuz li-ʾannahu manhi ʿan istikhdam haʾulaʾi li-ma fihi min al-idhlal*).

42 Muhammad Amin b. ʿUmar Ibn ʿAbidin, 6 *Radd al-Muhtar* (*Dar al-Fikr*: Beirut, 1992), p. 384.

43 Ibid. ("*man khadaʿa li-ghaniyy wa wadaʿa lahu nafsahu iʿẓaman lahu wa tamaʿan fi ma qibalahu dhahaba thulutha muruʾatuhu wa shatr dinihi*").

44 This is the ideal of *Pareto* efficiency. A state of the world is described as being *Pareto optimal* when it is impossible to make one person better off without making another person worse off. Under the Pareto conception of efficiency, a redistribution of entitlements is efficient only if it makes both (or all) of the parties involved better off, and therefore, a commitment to Pareto efficiency usually entails a commitment to private trade and a reluctance to permit coercive transfers. Another conception of efficiency, known as *Kaldor-Hicks efficiency*, permits coercive redistributions whenever the gains realized by those made better off from the transfer are sufficiently large that they could reimburse the losses suffered by those who suffered a loss from the redistribution of property or rights, as applicable. The criterion of Kaldor-Hicks efficiency is more realistic from a public policy perspective than that of Pareto efficiency.

45 For example, according to statistics maintained by the Federal Reserve Bank of the United States, banks in the United States held $2.578 *trillion* of excess reserves (reserves beyond that required by law) and United States corporations as of the end of 2013 held $1.64 trillion in cash on their balance sheets, figures that suggest that vast amounts of social resources are sitting idle, doing nothing productive for the economy.

46 Ahmad b. ʿAli b. Hajar al-ʿAsqalani, 4 *Fath al-Bari Sharh Sahih al-Bukhari* (*Dar al-Maʿrifa*: Beirut, 1959), hadith no. 2201, p. 400.

47 The Andalusian case of partnerships for the production of cheese from milk also suggests that the analysis provided by the economist Mahmoud el-Gamal regarding the mark-to-market justification for the rules of *riba al-fadl* exists only in the special case where no market for the goods exists, or is only coming into existence, something that was no doubt the case in the early Islamic period. In cases where flourishing markets already exist, and traders can be presumed to know market prices, as must have been the case in a sophisticated urban setting such as 15th-century Granada, the need to apply the rules of *riba al-fadl* strictly lapses. Mahmoud El-Gamal, *Islamic Finance: Law, Economics and Practice* (Cambridge University Press: New York, 2006), p. 53.

48 Cash *waqf*s which proliferated in the late Ottoman Empire were not full-fledged banks because the contributors of surplus could not retrieve their money invested in the *waqf* in the future. Instead of being depositors or investors, their capital took the form of a charitable contribution, which was permanently alienated to the *waqf*. In other words, they could only get their surplus back in the form of a loan in the future from the *waqf* itself.

49 This is a straightforward, even if mechanical, application of a bedrock principle of Islamic commercial law, namely that the right to profit is a function of the possibility of loss and is variously expressed as "*al-kharaj bi'l-daman*" or "*al-ghunm bi'l-ghurm*." Jurists have not deemed the con-

tinued existence of credit risk to be sufficient to satisfy this principle.

50 *al-Sharh al-Saghir*, pp. 687–88 (a *qirad* in which the entrepreneur guarantees the capital to the investor is invalid (*fasid*) and the condition is not enforced).

51 For a detailed explanation of the problems with the two-tiered *mudaraba* model for financial intermediation, see El-Gamal, pp. 165–69.

52 See, for example, the English language balance sheet of the 2013 Dubai Islamic Bank, p. 3 (listing its shareholder equity at approximately AED 16 billion and its liabilities at AED 96.9 billion, 79 billion of which is customer deposits). Note that the Arabic version of the same document appears to use different categories than that of the English language version, even though the totals are the same in both.

53 Mahmoud el-Gamal proposed this solution previously. See, El-Gamal, pp. 159–61.

54 Central Intelligence Agency, The World Factbook: Egypt: Economy (2013).

55 They would of course continue to be subject to *zakat* on their savings that exceed a minimum threshold and is held for more than one year.

56 Even a jurist as willing to revise historical rules of *zakat* such as Yusuf al-Qaradawi has been unwilling to consider changing the fixed-rate nature of *zakat*. See al-Nisbiyya wa'l-tasaʿud bayn al-Zakat wa'l-Dariba (*inna al-zakata bi'l-naẓar ila tabiʿatiha farida diniyya khalida khulud al-insan baqiya baqaʾ al-islam la tataghayyar bi-taghayyur al-ẓuruf wa'l-awdaʿ wa'l-hajat, bal yutalab bi-ha tadayyunan wa taʿabbudan kull muslim fi kull ʿasr wa fi kull biʾa wa fi kull hal*).

57 See, for example, 2 *Sharh al-Zurqani ʿala Muwattaʾ Imam Malik* (*Dar al-Maʿrifa*: Beirut, 1987), pp. 107-118 (mentioning the precedents of ʿUmar b. ʿAbd al-ʿAziz, Muʿadh b. Jabal and ʿUmar b. al-Khattab).

58 For the distinction between *al-tasarruf bi'l-imama* and *tasarruf bi'l-futya*, and their different effects in the Shariʿa, see Shihab al-Din al-Qarafi, *al-Ihkam fi Tamyiz al-Fatawa ʿan al-Ahkam wa Tasarrufat al-Qadi wa'l-Imam*, ed. ʿAbd al-Fattah Abu Ghudda (*Maktab al-Matbuʿat al-Islamiyya*: Aleppo, 1967), *al-Suʾal al-Khamis wa'l-ʿIshrun,* pp. 99-120.

59 *al-Sharh al-Saghir*, p. 322 (*wa'l-ijmaʿ* ʿal*a hurmat al-akhdhi min al-muslimin wa ʿala kufri mustahillihi li-annahu min al-maʿlum min al-din bi'l-darura*).

60 Zakariyya b. Muhammad al-Ansari, 5 *Asna al-Matalib Sharh Rawd al-Talib*, ed. Muhammad Tamir (*Dar al-Kutub al-ʿIlmiyya*: Beirut, 2001), p. 617 (*fa-idha ʿudima bayt al-mal . . . iqtarada ʿalayhi al-imam min aghniyaʾ baladihi . . . fa-in taʿadhdhara al-iqtirad qassataha ʿala al-aghniyaʾ qardan*).

61 See, for example, a variety of fatwas on the topic of the permissibility of modern taxes on the web site of Multaqa Ahl al-Hadith. For a detailed argument on the permissibility of collecting taxes in addition to the *zakat* and the *kharaj*, see Yusuf al-Qaradawi, al-Adilla ʿala Jawaz Fard al-Daraʾib Maʿ al-Zakat.

62 Bin Baz, for example, has given the opinion that it is permissible for a Muslim to circumvent payment of customs duties levied by a Muslim government so long as he does it secretly and without an intention to overthrow that government (*yajuz bi-shart an la yakuna fi dhalika munabadha li'l-hukuma*). See Fatawa al-ʿUlamaʾ fi Hukm al-Daraʾib wa'l-Jamarik al-Mukus Allati *ta*ʾkhudhuha al-Duwal al-Islamiyya al-Yawm.

63 *al-Taj wa'l-Iklil*, p. 348.

64 A state might have its disposal vast mineral wealth, like the states of the Arabian Gulf, but at some point in time that wealth will disappear, and the state will have to have access to other, recurring sources of revenue. Indeed, it would be healthier even for such states to invest their mineral wealth for the long-term benefit of their people and rely only on tax revenue for the state's ordinary expenses, such as education and health care.

65 Jalal al-Din al-Suyuti, 1 *al-Ashbah wa'l-Naẓa*ʾir, *al-Qa*ʿida al-Kh*amisa tasarruf al-Imam ʿala al-Raʿiyya Manut bi'l-Maslaha*, p. 121 (*la yajuz lahu an yuqaddima fi mal bayt al-mal ghayr al-ahwaj ʿala al-ahwaj*).

66 Shihab al-Din Ahmad b. Muhammad al-Hamawi, 1 *Ghamz ʿUyun al-Basaʾir Sharh al-Ashbah wa'l-Naẓaʾir li-Ibn Nujaym* (*Dar al-Kutub al-ʿIlmiyya*: Beirut, 1985), p. 372.

67 Central Intelligence Agency, The World Factbook: Country Comparison: Gross National Saving (2013).

68 Modern jurists who endorse a general power of taxation have also endorsed a progressive theory of taxation.

69 Edib Smolo, *Journal of Islamic Banking and Finance* (January–March 2010), "*al-Bay ʿ bi-Thaman Ajil* (BBA) As Practiced in Malaysia: A Critical Review," p. 69.

70 *Resolutions of Shariah Advisory Council of Bank Negara Malaysia*, BNM/RH/GL/012-2, pp. 89–92.

71 Note that if the corporation is taken to be a permissible form for doing business in analogy to the *qirad/mudaraba*, Maliki jurists did not allow *any* debt to be incurred in the name of the *qirad/mudaraba*, even with the permission of the investors. *al-Sharh al-Saghir* 698 (*wa la yashtari . . . bi-nasi ʾa . . . wa in adhina rabbuhu*).

72 See generally, El-Gamal, pp. 125–9.

73 Mahmoud Elgamal has discussed how mutual banking could help to revitalize Islamic banking and put it in the service of the needs of Muslim majority societies. El-Gamal, pp. 186–8.

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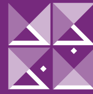

Research Centre for Islamic Legislation and Ethics (CILE)
P.O Box: 34110 Doha, Qatar | Phone (+974) 4454 2840 | Fax: (+974) 4454 6576
www. cilecentre.org