

The Fundamentals Of Islamic Banking and Finance:

A Prologue

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Abstract—The *raison d'être* of this article is to supply basic insights on the origin and characteristics of the Islamic Banking system, its distinguishing features, and related contentious issues that have remained the subject of on-going debates among *Sharia'* scholars and members of the academia. These were analyzed by referring to the principles of *Muammalat* (Islamic economic transaction), which are derived from the Holy Quran, *Sunnah* of Prophet Muhammad (p.b.u.h.), and *Ijma'* (consensus) of prominent *Sharia'* scholars. Contrary to the conventional banks, Islamic banks are required to operate according to the principles of *Muammalat*, which are identified as the avoidance of *Riba'*, *Gharar*, *Maysir*, *Hilah*, and the promotion of ethical business practices such as justice, fairness and transparency. The 2008 global financial meltdown has created a unique awareness among banking consumers on the need of an alternative to complement the conventional banking system, which was viewed by financial scholars as suffering from a crisis of failed morality as a result of greed, exploitation, and corruption. Likewise, many may viewed that the Islamic Banking system is merely another attempt to capitalize on the pulling power of religion towards people, yet there are a number of interestingly unique features that accentuate it from the other banking alternatives. In essence, it is aspired that this article may assist fellow readers, especially those who are still new to this alternative financial system, in understanding and appreciating its unique features, and further stimulate future research in this field. Insha'Allah (God's willing).

Keywords; *Islamic Banking; Maqasid As-Sharia'; Sharia' Compliance; Riba'; Gharar; Socially-responsible Investing*

I. INTRODUCTION

Prior to the devastating global financial crisis in early 2008, the inter-relationship between religion and finance was considered irrelevant [1], which partly owes to modern capitalism's separation of religion from politics, economics, and governmental administration. The crisis, however, has exposed the weakness of the current financial system and there has been "*public outrage over the excesses and support for more conservative and ethical finance*"[2, 3]. In reality, the concept of finance is very much closely related to religion, especially within the three Abrahamic faiths, *i.e.* Judaism, Christianity, and Islam, which share nearly identical

philosophies on finance. These bonds between the three *Samawireligions* are further illustrated as follows (see Figure 1):

JUDAISM	CHRISTIANITY	ISLAM
Exodus 22: 25-27 "25. When you lend money to any of my people, to the poor among you, you shall not be to him as a creditor, nor shall you impose upon him any interest. 26. If you take your neighbor's garment as a pledge (collateral), you shall return to him by nightfall. 27. For that is his only covering; it is his garment for his skin. In what shall he sleep? And it shall come to pass, that if he cries unto Me, I will hear it, for I am compassionate." Deuteronomy 23: 19-20 "19. You shall not charge interest on loans to your brother (Israelites); interest on money, interest on provisions, and interest on anything that is lent. 20. On loans to a foreigner you may charge interest, but on loans to your brother (Israelites) you may not charge interest."	Leviticus 25: 35-37 "35. And if your brother fall into difficulty and become dependent on you, then you should support him and take him to live with you although he may be a stranger. 36. Do not take interest in advance or make profit from him, but fear God; let your brother live with you. 37. You shall not lend him money at interest taken in advance, or provide him food at a profit."	Ali Imran 3: 130 "130. O ye who believe! Devour not usury, doubled and multiplied; but fear God; that ye may (really) prosper." Al-Nisa' 4: 161 "161. That they took usury, though they were forbidden; and that they devoured men's substance wrongfully; - We have prepared for those among them who reject faith a grievous punishment."

Figure 1: Prohibition of Interest in Judaism, Christianity and Islam [4]

In recent decade, the application of religious laws to finance is no longer an alien belief – as evidenced by the introduction of the DJ Dharma Index in 2008 for Hindu Banking, the launch of Stoxx Europe Christian Index in 2010

for Christian Banking, and investment companies such as the Roman Catholics Ave Maria Rising Dividend, or Aquinas Investment Company, to name a few[5-7]. However, out of these, one certainly exhibits promising global popularity; strengthened by its steady market growth of 15-20% per annum and current industry size of \$2 trillion that is further estimated to reach \$3.4 trillion in 2018 – Islamic Banking [8, 9].

Indeed, such a rapid progress has never been achieved by any other religion-associated financing, which causes one to wonder the uniqueness of Islamic Banking over the other systems. In fact, there were also speculations that it is the anecdote to the financial crisis problems, though there has yet to be any concrete evidences that justify its resilience towards the devastating 2008 financial crisis.

II. HISTORICAL PERSPECTIVE

It is generally believed that the modern concept of Islamic Banking was first introduced in 1963 by Egypt's MitGhamr Savings Banks, which initially started as a microlending finance operation[10, 11]. It has since continued to develop financial products that are based on the Islamic principles of profit-sharing and prohibition of interest. Since then, the push for Islamic Banking had gained both attention and momentum worldwide. Malaysia followed shortly after with the establishment of the Lembaga Urusan Tabung Haji (LUTH) in 1969; which was the first institution that utilized the *Sharia'* principles in its fund management operations for Muslims going on pilgrimage and was considered the first of its kind in the world[12]. By December 1973, the Islamic Development Bank ('IDB') was incorporated in Jeddah, Saudi Arabia pursuant to the Declaration of Intent issued by the Conference of Finance Ministers of Muslim Countries to further assist in fostering economic development and social progress of Muslim countries in adherence to the *Sharia'* law; which landmarks the first collective efforts by Muslim countries to promote Islamic Banking [13]. The following year, King Faisal of Saudi Arabia pledged to initiate a banking system that adheres to the tenets of *Sharia'* law and ethics in a bid to bridge the gap between the Islamic concept of banking with the 600-years-old conventional banking system. This saw a number of Islamic banks, both in letter and spirit, came into existence in the Middle East, *i.e.* the Dubai Islamic Bank in 1975, the Faisal Islamic Bank of Sudan and Egypt in 1977, the Bahrain Islamic Bank in 1979, and *etc.*, to name a few[14, 15]. Along with Malaysia, Indonesia, and Turkey, the Gulf Cooperation Council ('GCC'), which consists of Bahrain, Kuwait, Oman, Qatar, Saudi Arabia, and the United Arab Emirates, is now home to several renowned financial powerhouses, *inter alia*, the Deutsche Bank, Citi, UBS, and Barclays, which have already begun to offer their own *Sharia'*-compliant products and services[16]. With a combined banking customers' population of 252 million, it is suggested that these regions will be the main thrust for Islamic Banking expansion in many years to come.

It is without a doubt that since its emergence in the 1970's, the global Islamic Banking market is growing steadily at 15-20% per annum while global *Sharia'*-compliant assets are forecasted to grow from over US\$500 billion in 2009 to beyond the milestone of \$2 trillion by 2014[8] and is further expected to cross the US\$ 6.5 trillion mark by 2020[17] (see **Figure 2**).

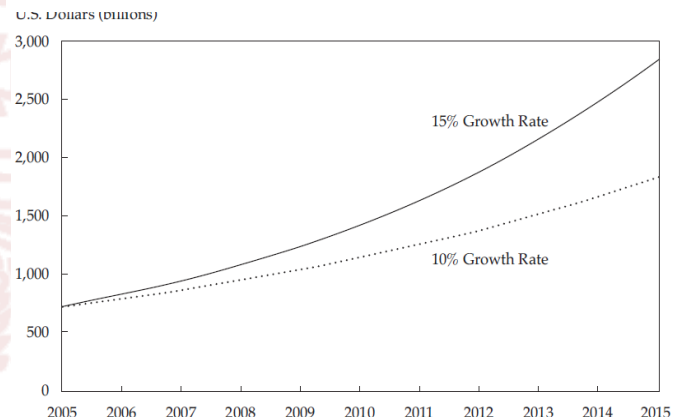


Figure 2: Projected Size of the Islamic Banking Industry 2005 – 2015[11]

Yet, despite all these remarkable figures, Islamic Banking faces mounting challenges to remain firm to true Islamic principles while expanding internationally. It is apparent that the role and responsibilities of IFIs are to serve the financial needs of their various stakeholders and to give proper consideration to the legitimacy of their operations from a *Sharia'* law point-of-view[18]. However, in recent years, the industry was heavily criticized for failure to ensure consistency, uniformity, and strict adherence of the products and services offered with the *Sharia'* law[19-21]. Furthermore, its authenticity and merit were even questioned by several Islamic Banking practitioners; citing them as mirroring the conventional banks'[15, 22-24].

III. THE CONCEPT OF BANKING IN ISLAM

Generally, banking institutions exist to fulfil the financial needs of the society. It is parable to a knife, which usufruct can either be used for permissible matters such as slaughtering an animal for its meat, or forbidden ones such as homicide. Prior to the introduction of Islamic Banking, Muslims around the world were restricted from making use of the conventional banking's products and services. It is in this regard that Islamic Banking began to offer a different concept from the conventional banking system in the sense that it is guided by the *Sharia'* law, which segregates between what is permissible and what is not. According to Ibn Al-Ukhuwwah, it is a banking concept that satisfies the divine law in both form and spirit[25]. Once a taboo practice, the Islamic Banking concept has started to serve as a gateway for Muslims to finally enter the formal world of finance.

In definition, an Islamic bank is a financial institution that officially and practically abides by the precepts of *Sharia'* law, which prescribes guidelines for moral economic transactions[26]. It encapsulates a banking practice that transcends the doctrine of separation of powers between religion and the state[10]. In other words, its objective, mission and vision are all dictated by the *Sharia'* law, which encompasses the Holy Quran, and the *Sunnah* (the doings and sayings of Prophet Muhammad (p.b.u.h.)).

IV. THE MAIN THEME OF ISLAMIC BANKING – SHARIA' COMPLIANCE

In essence, Islamic Banking is a financial practice that places similar regards in enforcing the rule of God on *Muamalat* (financial transactions). This is executed by deriving *Sharia'* rulings from the various sources of Islamic law; which are primarily the Holy Quran and the *Sunnah*, and ensuring strict compliance of any financial products and services with the said rulings – which is commonly termed as *Sharia'* compliance. For this purpose, those who are responsible for the interpretation of the *Sharia'* rules; known by many names - the *Ulama'*, the *Ustadz* or *Ustadzah*, the *Mufti*, the *Imam*, and many others, are seen to hold the decisive key in determining what is permissible and what is not, and are subsequently held accountable under the *Sharia'* law for their decisions in the hereafter.

Abdullah Bin Umar narrated that:

Prophet Muhammad (p.b.u.h.) said, "Surely! Every one of you is a guardian and is responsible for his charges; the Imam (ruler) of the people is a guardian and is responsible for his subjects; a man is the guardian of his family (household) and is responsible for his subjects; a woman is the guardian of her husband's home and of the children and is responsible for them; and the slave of a man is a guardian of his master's property and is responsible for it. Surely, every one of you is a guardian and responsible for his charges."[27]

In matters relevant to business and financial transaction, Islam imposes a high degree of accountability towards the *Sharia'* boards of IFIs, particularly the *Sharia'* scholars because they are the gatekeepers to the *Sharia'*-compliant accreditation of IFIs' financial products and services; which are vastly unique due to their compliance with the *Sharia'* law. As a result, any *Fatwas* (*Sharia'* rulings) issued by the *Sharia'* board must strictly adhere to the Holy Quran and the *Sunnah*. However, this is easier said than done since it involves prioritising the rule of God over the financial institution's interest. Without strong regulatory and corporate governance frameworks, this conflict can potentially marred the image of IFIs as a working embodiment of the rule of God in finance.

V. FIRST PRINCIPLE: PROHIBITION OF RIBA' (RECEIPT OR PAYMENT OF INTEREST)

The first principle of Islamic Banking demands for the financial transaction to comply with the *Sharia'* prohibition of *Riba'*. Terminologically, *Riba'* is an Arabic word that implies excess, expand, extra or addition[28]. Technically, it can be defined as any unjustified excess above and over the capital that occurs either in a loan transaction or an exchange of commodity.

Contrary to the conventional banking system that regards money as tradable as any other commodity, the Islamic Banking system considers money only as a medium of exchange and nothing more. Comparatively, Islam also views money as having no intrinsic value since it cannot be directly utilised to satisfy human's need; which is in contrast with commodity that can rather be consumed directly[29-31]. In Christianity, this view was also corroborated by St Thomas Aquinas, who justified the prohibition of interest in his famous *Summa Theologica*[32]. Surprisingly, the ban on interest has even its own footings in secularism teachings as emphasized by Aristotle and Plato, who regarded money as sterile[30, 33] and that the 'making of money from money' as unnatural and problematic[34, 35].

For this reason, the *Sharia'* law prohibits the utilization of money as a medium of profit from money-lending practices such as an ordinary interest-based loan since it causes the borrower to pay more than the amount initially borrowed. The amount can also continue to increase if the payment is made beyond the specified date in the loan agreement due to the presence of a late payment interest clause, which is common in all standard loan documentation.

Practically, it implies that customers with either an Islamic savings account or current account are not to expect to be paid interest or dividends on their deposits. This also applies to borrowers with an Islamic mortgage who are not to pay interest on their debt[36]. Accordingly, the IFI must only engage in non-interest bearing business activities to ensure mutual adherence of such prohibition[37]. The prohibition of interest had also garnered significant backing by Maurice Allais, the 1988 Nobel Prize winner of economic science, who argued that one of the structural reforms that can be undertaken to address future economic crisis is, *inter alia*, the adjustment of the rate of interest to 0 per cent; which incidentally coincides with the express prohibition of *Riba'* in Islam [3, 38].

VI. THE DIVERGENT VIEWS ON THE PROHIBITION OF RIBA'

There are divided opinions as to the rulings of *Riba'* under the *Sharia'* law. Traditional *Sharia'* scholars have concluded that the *Sharia'* law injunctions over *Riba'* demand for the total prohibition over the receipt and payment of interest regardless of its amount[39-41]. This coincides with the following provisions of the Holy Quran and *Hadith* of Prophet Muhammad (p.b.u.h.):

“Those who devour usury will not stand except as stand one whom the Evil One by his touch hath driven to madness. That is because they say: “Trade is like usury,” but Allah hath permitted trade and forbidden usury. Those who after receiving direction from their Lord, desist, shall be pardoned for the past; their case is for Allah (to judge); but those who repeat (the offence) are companions of the Fire: they will abide therein (forever).”

(Surah Al-Baqarah 2: 275)

“O ye who believe! Devour not usury, doubled and multiplied; but fear God; that ye may (really) prosper.”

(Surah Ali Imran 3: 130)

“That they took usury, though they were forbidden; and that they devoured men's substance wrongfully; - We have prepared for those among them who reject faith a grievous punishment.”

(Surah An-Nisa' 4: 161)

Ibn Mas'ud narrated that:

“The Messenger of God p.b.u.h. cursed the one who consumed Riba', and the one who charged it, those who witnessed it, and the one who recorded it.”[42-44]

Accordingly, this strict interpretation of *Riba'* is influenced by the fact that such practice is causing the circulation of wealth to be only in the hands of a few[45]. Consequently, this widens the gap between the rich and the poor. In addition, the *Sharia'* law views that the financier in a particular transaction has no right to be guaranteed profit, unless it shares the same risk of potential losses as the borrower does[46]. This reiterated the stance taken by previous *Sharia'* scholars such as Imam Razi, who viewed that the payment of something definite such as interest against something uncertain such as the borrower's ability to make profit and repay the loan is *Haram* according to the *Sharia'* law:

“While the earning of profit is uncertain, the payment of interest is predetermined and certain. The profit may or may not be realized. Hence, there is no doubt that the payment of something definite in return for something uncertain inflicts a wrong (Haram).”[39]

Contemporary scholars, on the other hand, preferred to view interest or usury in the context of ‘excessive interest’ and reckoned the consumption of a small amount as admissible[37, 47-49]. This is evident from the practice of *Murabahah* (mark-up sale contract) in Islamic Banking, which is viewed by scholars as a permissible financial instrument, and the mark-up amount is deemed as a fair profit towards the financier[20, 50].

Nevertheless, the ban on interest does not infer that profit maximization was never on the agenda of IFIs for Islamic Banking is just as any legitimate business activities that attempt to maximize the value of its shareholders[18]. In fact,

the concept of time value for money is indeed recognized by the *Sharia'* law. However, it can only be realized as part of a real transaction instead of a loan contract. For instance, the bank is prohibited from profiting out of loans, but it may do so from other alternatives such as a lease or hire purchase contract, in which the return increases as the lease prolongs. Alternately, the bank may also opt to apply safekeeping charges as a replacement to interest paid to savings account. This practice was implemented by Qasr Al-Haj, an ancient Islamic bank in Libya that was frequently used by pilgrims during the 13th century to store valuable goods whilst they were away for the *Hajj*. Uniquely, the bank did not charge any interest apart from taking one-fourth of the value of goods stored as a safekeeping fee, which was subsequently donated to Islamic education institutions around the area. Although this method is perhaps impractical in modern banking practices due to the number of employees involved and complexities of financial products and services, it highlights the original banking operation from *Sharia'* law perspective.

On the other hand, low or zero interest rates do not necessarily render a bank as unprofitable. This has been recently exemplified in a recent report that Gulf banks have been experiencing healthy earnings growth over the last fiscal year despite their low interest rates, and is expected to remain so over the next few years[51]. Accordingly, this may prove the contention that the *Sharia'* law prohibition on *Riba'* will not automatically inflict losses to the banks.

Above all, the wisdom behind the prohibition of *Riba'* is rather to eliminate any form of exploitation and the practice of unjust enrichment. Under the *Sharia'* law, in order for a contract to be valid, three elements must exist, *i.e.* risk (*Ghurm*), work and effort (*Ikhtiar*) and liability (*Daman*)[46]. In a *Riba'*-based financing, one or more of these elements are missing, rendering such a contract to be invalid under the *Sharia'* law. To illustrate, in an ordinary loan contract, the bank is guaranteed a return on capital and profit without the need to share any risk. In addition, the bank possesses the right to sell the collateral or hold the guarantor liable in the event of default by the borrower. On the other hand, the borrower does not enjoy such a guarantee. Yet, he is required to pay an extra amount in addition to the loan. Therefore, the Islamic Banking system aspires to rectify this injustice by requiring all parties to equally share the risks in order to create a win-win situation between the bank and the customers.

VII. SECOND PRINCIPLE: PROHIBITION OF GHARAR (UNCERTAINTY)

The prohibition of *Riba'* has indeed counterparts in other religions, but the second principle is solely exclusive to Islam, *i.e.* the prohibition of *Gharar*. It is an Arabic word that connotes “*uncertainty over the existence of the subject matter of sale*”[52]. *Sharia'* jurists such as Al-Babarti defined it as “*...when the subject matter is unknown*”[53], whereas Ibn Taymiyyah and Al-Sarakhsi viewed it as “*...unknown consequences*”[21] and “*...when the consequences are concealed*”[54] respectively. In simple words, the ban on

Gharar implies that the parties to a contract must be aware of the counter-value offered in the transaction.

In practice, it requires for the important terms and conditions of contract such as, the price, deliverability, quantity, quality, and existence of the goods and services[55, 56], to be fixed and reduced to writing in order to minimize the risk of uncertainty. This is in line with the following provisions of the Holy Quran and the *Sunnah*:

“O ye who believe! When ye deal with each other, in transactions involving future obligations in a fixed period of time, reduce them to writing, let a scribe write down faithfully as between the parties: let not the scribe refuse to write: as God has taught him, so let him write. Let him who incurs the liability dictate, but let him fear his Lord God, and not diminish aught of what he owes. If the party liable is mentally deficient, or weak, or unable himself to dictate, let his guardian dictate faithfully, and get two witnesses, out of your own men, and if there are not two men, then a man and two women, such as ye choose, for witnesses, so that if one of them errs, the other can remind her. The witnesses should not refuse when they are called on (for evidence). Disdain not to reduce to writing (your contract) for a future period, whether it be small or big: it is more just In the sight of God, more suitable as evidence, and more convenient to prevent doubts among yourselves but if it be a transaction which ye carry out on the spot among yourselves, there is no blame on you if ye reduce it not to writing. But take witness whenever ye make a commercial contract; and let neither scribe nor witness suffer harm. If ye do (such harm), it would be wickedness in you. So fear God; for it is God that teaches you. And God is well acquainted with all things.”

(Surah Al-Baqarah 2: 282)

Abu Hurairah narrated that:

“Prophet Muhammad (p.b.u.h.) prohibited sale that is based on Hasah (throwing of pebbles) and Gharar (uncertain sale).”[43, 57]

However, in order to minimize injustice and potential dispute, the mere writings of the terms and conditions of contract will not suffice, for they must also be comprehensible to average customers. One with legal or business astute may be able to understand the documents with ease, but it may not be the case for average customers considering the lengthy nature of modern contracts, in addition to numerous business and juristic jargons, and small prints[58].

In principal, there are two forms of *Gharar*, i.e. *Gharar Fahish* (major *Gharar*) and *Gharar Yasir* (minor *Gharar*). According to Ibn Rushd, *Gharar Fahish* refers to excessive uncertainty and exists in the following situations:

- (a) Uncertainty over the subject matter of the contract;
- (b) Uncertainty as to the sale or purchase price;
- (c) Uncertainty as to the existence of the subject matter of the contract or ability of the seller to deliver it; and

- (d) Uncertainty as to the condition of the subject matter of the contract[59].

Examples of *Gharar Fahish* are the sale of fruits before ripening (*Mukhabarah*), buying on the basis of touching a commodity (*Mulasamah*), sale by throwing a commodity towards a buyer (*Munabazah*), conditional sale, sale of goods before obtaining possession, and sale of non-existent matters such as a genie in the bottle[59]. On the other hand, *Gharar Yasir* refers to the uncertainty of slight nature. For example, the monthly lease of a house, of which the days can either be thirty or thirty one; or the sale and purchase of wrapped items, or simply a restaurant menu with no price stated.

Admittedly, *Gharar* is difficult to be completely avoided, or as Al-Shatibi had put it, *“to remove all Gharar from contracts is difficult to achieve, besides, it narrows the scope of transactions”*[60]. However, *Sharia'* jurists agreed that only *Gharar Fahish* is prohibited due to its inherent uncertainty and impairment on the validity of contract as compared to *Gharar Yasir*, which impacts are too minimal and difficult to be assessed in quantitative value[48, 60-63].

VIII. THIRD PRINCIPLE: PROHIBITION OF MAYSIR (GAMBLING OR SPECULATION)

The third principle of Islamic Banking necessitates the avoidance of *Maysir*, i.e. gambling or the speculative nature of transaction. This can be understood as an attempt to predict the future outcome of an event or simply conceding to a game of chance. Algaoud viewed *Maysir* as *“... to undertake a venture blindly without sufficient knowledge or to undertake an excessively risky transaction”*[48]. The *Sharia'* law prohibits such practices as they are often not backed by any analysis or interpretation of relevant information[64]. In one *Hadiith*, Prophet Muhammad (p.b.u.h.) stressed on the importance of proactive reasoning before leaving nature to its work:

It was narrated that Prophet Muhammad (p.b.u.h.) once asked a Bedouin, who left his camel untied, “Why don't you tie your camel?” the Bedouin answered, “I put my trust in God”. The Prophet then said, “Tie up your camel first then put your trust in God.”[42]

In theory, there is a resemblance between *Gharar* and *Maysir* in the sense that the latter can be deemed as an active act upon the prohibited *GhararFahish* or excessive uncertainty. For instance, the pre-Islamic practice of *Bai Al-Munabazah* (sale by throwing a commodity towards a buyer) involved a high degree of uncertainty since the buyer could not properly assess the quality of commodities thrown to him. Also, the contract is deemed to be concluded once the buyer touches the commodity. Yet again, the pre-Islamic society was willing to gamble on such a risky transaction due to the hope of acquiring valuable commodity from the other party. Likewise, this would also apply to investments such as trading in futures on the stock market, or FOREX (foreign exchange).

Albeit the risk in these transactions may possibly be mitigated by utilizing modern financial softwares, the unpredictable nature of world economics such as the notable 1997 and 2008 global economic crisis have only proven that the two prohibited elements remain the biggest obstacles to the financial community.

Nevertheless, this does not imply that the *Sharia'* law proscribes the taking of risk in investment. In fact, investment is very much encouraged in Islam, provided the risk environment is properly studied beforehand. For example, the *Sharia'* allows risk-taking in entrepreneurship and those that naturally occur as a result of natural disasters and calamities, which are reflected in several Islamic Banking products such as *Mudarabah* (profit-sharing contract), *Musharakah* (partnership contract), and *Takaful* (Islamic insurance). By the same token, Islamic financial units such as IFIs are required to properly assess the variant risks in banking, which do not only include generic risks such as credit, market, liquidity and operational, but also those that are specifically unique to IFIs risk profile such as rate of return, *Sharia'* non-compliance, displaced commercial, and equity investment risk (see **Figure 3**).



Figure 3: Risk Profile of IFI

In addition, each financial transaction by IFIs must be tied to a tangible underlying asset in ensuring that IFIs remain connected to the real economy[61, 65]. In an Islamic Banking transaction, the return on investment is obtained as a result of the investment process or the leasing process of a tangible asset, which further justifies the return on such investment as the real measure of the value of the investment activities[10]. An immediate example is *Sukuk* – a certificate of equal value representing undivided shares related to the ownership (not debt) of tangible assets, usufruct and services or to the ownership of the assets of particular projects or a special investment activity, extending even to contractual rights, which are held in trust for the *Sukuk*-holders[61]. It is akin to the conventional asset-backed securities transaction, which includes the sale of tangible assets and generates returns and risk associated therewith[66].

IX. FOURTH PRINCIPLE: SOCIALLY RESPONSIBLE INVESTMENT ('SRI')

Fourthly, the principle of Islamic Banking emphasizes on the socio-economic aspects of economic activities that benefit the society at large (*Tahqiq al-khidmah al-ijtima'iyah*); which is similar to the conventional concept of Socially Responsible Investment ('SRI')[67]. Inspired by the *Sharia'* law injunction

of 'human accountability before God', individual or financial investors such as an IFI must seek for suitable avenues for money as a medium to generate social value and ease the burden of the needy via its economic activities[68]. By all means, Islam regards the overall interest of the society as of equal importance as generating high profits for corporations.

“What God has bestowed on His Messenger (and taken away) from the people of the townships, - belongs to God, - to His Messenger and to kindred and orphans, the needy and the wayfarer; in order that it may not (merely) make a circuit between the wealthy among you. So take what the Messenger assigns to you, and deny yourselves that which he withholds from you. And fear God; for God is strict in punishment.”
(Surah Al-Hasyr 59: 7)

To this end, the *Sharia'* law ordains for Islamic funds to be invested in industries that benefit the public such as, *inter alia*, telecommunication, technology, engineering, health care, construction, transportation, and education, whilst it prohibits the involvement in industries of questionable ethics such as alcohol, pork processing, gambling, prostitution, pornography, firearms, entertainment, music, and weapons of mass destruction[69, 70].

“They ask thee concerning wine and gambling. Say: "In them is great sin, and some profit, for men; but the sin is greater than the profit.”
(Surah Al-Baqarah 2: 219)

“O ye who believe! Intoxicants and gambling, (dedication of) stones, and (divination by) arrows, are an abomination, - of Satan's handwork: eschew such (abomination), that ye may prosper. Satan's plan is (but) to excite enmity and hatred between you, with intoxicants and gambling, and hinder you from the remembrance of God, and from prayer: will ye not then abstain?”
(Surah Al-Ma'idah 5: 90 – 91)

The realizations of the above notion have been displayed by several Islamic banks, notably Bank Al-Bilad of Saudi Arabia, which has recently opened a new branch in Riyadh that provides banking facilities to people with sight, hearing and other physical disabilities[71]. More recently, the Abu Dhabi Islamic Bank ('ADIB') has donated a new mosque to the local Fujairah community as part of its CSR activities, which also provides residences for the Imam and *Muazzin* (the caller of prayer)[72]. The same can also be said of Noor Islamic Bank of the United Arab Emirates, which offered bank services through post office to capture the 50 per cent of the country's population and low-paid workers who have no access to formal banking account[11]. Likewise, the Bangladeshi Grameen Bank's microfinance project that had witnessed Islamic Banking's effectiveness as a working tool in alleviating poverty was also another commendable initiatives

by IFIs around the world in blending social welfare with banking services[58, 73-75].

X. FIFTH PRINCIPLE: AVOIDANCE OF HILAH (TRICKS) IN TRADE

Fifthly, the principles of Islamic Banking prohibits the practices *Hilah* (tricks or deceptions), e.g. fraud, misrepresentation, juristic ruse, etc. For example, a simple sale and purchase transaction over fisheries is permissible, while a similar transaction over ‘fish in the ocean’ is not, due to uncertainty over the type, weight, quality and quantity of the subject matter. The same can also be said over a she-camel, which is again permissible, but not the sale and purchase over the she-camel and her unborn calf[60, 76, 77]. In essence, the *Sharia’* law ordains that profits can only be attained in business “...so long as it stays within the rules of the game, and engage in open and free competition without deception or fraud”[78].

In one *Hadith*, Abdullah reported that Prophet Muhammad (p.b.u.h.) mentioned:

“It is obligatory for you to tell the truth, for truth leads to virtue and virtue leads to Paradise, and the man who continues to speak the truth and endeavours to tell the truth is eventually recorded as truthful with God, and beware of telling of a lie for telling of a lie leads to obscenity and obscenity leads to Hell-Fire, and the person who keeps telling lies and endeavours to tell a lie is recorded as a liar with God.”[42, 79]

In another *Hadith*, the Holy Prophet (p.b.u.h.) was also narrated saying:

“When two people trade, they have the choice (to proceed with or cancel the transaction), so if they are honest and clarify (e.g. the defects in their merchandise) their trade will be blessed, but if they lie and conceal (defects) there will be no blessing in their trade.”[27]

In general, there is a mixture of views among Islam’s four major schools of thought with regards to the issue of *Hilah*. The *Maliki* and *Hanbali*’s schools opined that all *Hilah* are impermissible, while the *Hanafi* and *Shafie* maintained that *Hilah* is allowed as long as there is no fraudulent intention to neither deprive the rights of the society, nor demean the reputation of Islam [80]. However, some scholars have expressed their concerns over the application of *Hilah* in Islamic Banking. For instance, the issue of *Hilah* is evident in *Bay Al-Inah* (sale and buy back contract), an Islamic financial instrument that has so far been permitted in two countries, i.e. Malaysia and Brunei[81]. In this instrument, the bank would purchase an asset from the client on a cash basis and then immediately resell the asset to the customer at a marked up price on a deferred payment basis. The *Hanafi*, *Maliki*, and *Hanbali*’s school of thought regarded it as a legal device to circumvent the prohibition of *Riba*’-based financing by providing IFIs with a ‘back door’ to *Riba*’ since the main

intention is to obtain cash rather than the commodity itself[82-84]. Moreover, this instrument can also be misused by the banks to take advantage of the customers’ plea for cash and subsequently subjugate them to debt[19, 20]. However, this view was rebutted by countries that subscribed to the *Shafie*’s school such as Malaysia and Brunei, which opined that the customer’s motive is an irrelevant factor in declaring *Bai Al-Inah* as impermissible[21, 62].

Admittedly, these conflicting views on *Hilah* are confusing to customers, who are looking towards Islamic Banking as a unique financial service provider over its conventional counterparts. With the permissibility of *Bai Al-Inah* and several other controversial instruments, there are probabilities for the public, especially those who are religious-averse, to re-evaluate their selection of Islamic banks as their banking institution of choice. More importantly, it is academically fascinating to see whether the permissibility of these instruments, coupled with a number of other pressing issues the industry is currently facing, will have any adversarial effect towards the reputation of Islamic Banking in the years to come.

XI. SIXTH PRINCIPLE: JUSTICE AND FAIRNESS IN TRADE

Finally, the practice of Islamic Banking must always uphold the notion of justice, balance and fairness in trade (*Al-adluwa at-tawazun*). *Sharia’* scholar such as Ibn Taymiyyah considered justice as an integral outcome of the Islamic monotheism that integrates both the Muslims and non-Muslims.

“Justice towards everything and everyone is imperative for everyone and injustice is prohibited to everything and everyone. Injustice is absolutely not permissible irrespective of whether it is to a Muslim or a non-Muslim or even to an unjust person.”

Ibn Taymiyyah[21]

Islam recognizes that to God belongs the dominion of heaven and earth, and whatever mankind possesses, is none but only a trust from God. As the vicegerent of God on this earth, mankind are repeatedly reminded in the Holy Quran to administer justice at all times, even if it may jeopardise the life, financial status or reputation of the parties involved. In Islamic jurisprudence, this exercise of justice is known as *suisti’malal-haq*. According to Al-Khafif, a renowned *Hanafi* scholar, the administration of justice or the exercise of one’s right may by itself be valid and lawful, but it may also cause harm or damage to others[85, 86]. Undoubtedly, Islamic views the concept of justice as not a matter of choice, but rather a divine obligation that has been deeply rooted in the Holy Quran and Prophet Muhammad (p.b.u.h.) teachings.

“Say: “My Lord hath commanded justice; and that ye set your whole selves (to Him) at every time and place of prayer, and

call upon Him, making your devotion sincere as in His sight: such as He created you in the beginning, so shall ye return.”
(Surah Al-A'raf 7: 29)

“God commands justice, the doing of good, and liberality to kith and kin, and He forbids all shameful deeds, and injustice and rebellion: He instructs you, that ye may receive admonition.”

(Surah An-Nahl 16: 90)

“O ye who believe! stand out firmly for God, as witnesses to fair dealing, and let not the hatred of others to you make you swerve to wrong and depart from justice. Be just: that is next to piety: and fear God. For God is well-acquainted with all that ye do.”

(Surah Al-Ma'idah 5: 8)

As far as commercial trade is concerned, the manifestations of justice are exemplified in practices such as, *inter alia*, transparency in terms of measurement, price, and quality of the commodities; mutual consensus in trade agreement; free-will; impartiality, and generosity towards the customers. These can further be illustrated in the following provisions of the Holy Quran and the *Hadith*, which highlighted Prophet Muhammad (p.b.u.h.)'s advices on the issue of generosity in trade and the prohibition of meeting merchants from neighboring village and towns[87]. In the latter, the Prophet denounced such a practice in order to guarantee a fair and transparent economic dealing. However, the transaction is allowed if the seller is given an option to terminate the contract if he finds that he has been unfairly treated after knowing the real market value of his goods.

“O ye who believe! Eat not up your property among yourselves in vanities: but let there be amongst you traffic and trade by mutual good-will: nor kill (or destroy) yourselves: for verily God hath been to you Most Merciful!”

(Surah An-Nisa' 4: 29)

Jabir bin Abdullah reported that Prophet Muhammad (p.b.u.h.) mentioned:

“May God have mercy on the person who is lenient when he sells, lenient when he buys, and lenient when he demands his payment (debt).”[57]

Uthman bin 'Affan narrated that Prophet Muhammad (p.b.u.h.) said:

“God will admit to Paradise a man who was lenient when he sold and when he bought.”[57]

Abdullah bin Tawus narrated from Ibn Abbas that Prophet Muhammad (p.b.u.h.) said:

“Do not go to meet the caravans on the way (for buying their goods without letting them know the market price); a town dweller should not sell the goods of a desert dweller on behalf of the latter.” I asked Ibn Abbas, ‘What does he mean by not

selling the goods of a desert dweller by a town dweller?’ He said, ‘He should not become his broker.’”[43, 79, 88, 89]

Above all, the application of justice in modern Islamic Banking context can be seen in the various Islamic financial contracts such as *Mudarabah* and *Musharakah*, which, *inter alia*, emphasise on the concept of profit-and-loss sharing and the mandatory disclosure of information in such contracts such as profit-and-loss margin, contribution ratio of each party, risk management policies, and other aspects[90]. Since disclosure of information and transparency are among the most vital characteristics of Islamic Banking, it is necessary for all of the staff in IFIs' division, from CEO to even the security guards, to have adequate knowledge on the tenets of IFIs' financial products and services in ensuring that the customers are well-informed of everything that they are about to subscribe to[5, 91].

XII. CONCLUSION

To summarize, this article has attempted to explain the conceptual dimension and theoretical framework of Islamic Banking from the *Sharia'* law perspectives, which are imperative in enlightening fellow readers on the overall concept of Islamic Banking. Contrary to the conventional banks, IFIs' operations must be based on the *Maqasid As-Sharia'* (*Sharia'* objectives), which are identified as the prohibition of *Riba'*, *Gharar*, *Maysir*, *Hilah*, and the promotion of ethical business practices such as justice, fairness and transparency. The 2008 global financial meltdown has created a unique awareness among banking consumers on the need of an alternative to complement the conventional banking system, which was viewed by financial scholars as suffering from a crisis of failed morality[3, 16, 47, 92-95]. Meanwhile, the Islamic Banking system, which was identified as a viable banking alternative, have long preached on the concept of banking institution as a medium that generates not only profit, but also a tool that integrates and prioritizes the *Maslahah* (public interest) and ethical values in banking practices[96]. Nonetheless, it remains whether Islamic Banking is truly deserving of such an accolade – at least amidst the presence of revolving issues that necessitate further clarification and understanding such as, *inter alia*, the independence of the *Sharia'* board, conflict of laws and schools of thought, education and qualification of the *Sharia'* board members, non-standardized *Sharia'* rulings and guidelines, conflict of interest, etc. God knows best.

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