Investigation of Compliance of the Prevailing Import Murabah'a to Sharia

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Abstract**—**One of prevailing modes of finance in emerging Islamic banking system is Murabah'a. It means a financial dealing or transaction in which seller tells cost of the goods to be sold to buyer. Otherwise, the transaction would become invalid. In this mainstream, import Murabah'a transaction is divergent in such a way that the cost is not recognized and identified due to execution of import transaction in foreign currency i.e. US Dollar and the next transaction of Murabaha'a with the client is executed in local currency. Since this transaction is executed in dual currency i.e. bank pays supplier in foreign currency and executes Murabah'a with its client in local currency and it is not allowed in according to Islamic Injunctions as mentioned in hadith narrated by Hazrat Ibn-e-Umar (May Allah be pleased with them) used to sell his camels with Dirhams and take dinars instead and vice versa. Upon revealing before the Prophet (Peace be upon him), he was advised that it must not be contingent in the agreement and the ready rate would be applied and possession of one of the consideration is compulsory. The solution in this regard is that the import Murabah'a transaction should be in single currency However, other currency can be paid in payment at the time of payment in a very indispensable situation provided that ready rate would be applied. Moreover, some of other solutions have also been given in this regard.

Keywords**—**Shariah compliance, import murabaha, islamic banking, product development.

I. Introduction

MOST of the Islamic banks and financial institutions are using murabah'a as an Islamic mode of financing, and most of their financing operations are based on murabah'a. That is why this term has been taken in the economic circles today as a method of Islamic banking operations, while the original concept of murabah'a is different from this assumption.

"Murabah'a" is, in fact, a term of Islamic Jurisprudence (Fiqh) and it refers to a particular kind of sale having nothing to do with financing in its original sense. If a seller agrees with his purchaser to provide him a specific commodity on a certain profit added to his cost, it is called a murabah'a transaction. The basic ingredient of murabah'a is that the seller discloses the actual cost he has incurred in acquiring the commodity, and then adds some profit thereon. This profit may be in lump sum or may be based on a percentage.

The payment in the case of murabah'a may be at spot, and may be on a subsequent date agreed upon by the parties. Therefore, murabah'a does not necessarily imply the concept of deferred payment, as generally believed by some people who are not acquainted with the Islamic jurisprudence and who have heard about murabah'a only in relation with the banking transactions.

Murabah'a, in its original Islamic connotation, is simply a sale. The only feature distinguishing it from other kinds of sale is that the seller in murabah'a expressly tells the purchaser how much cost he has incurred and how much profit he is going to charge in addition to the cost.

If a person sells a commodity for a lump sum price without any reference to the cost, this is not a murabah'a, even though he is earning some profit on his cost because the sale is not based on a "cost-plus" concept. In this case, the sale is called "musawamah." This is the actual sense of the term "murabah'a" which is a sale, pure and simple. However, this kind of sale is being used by the Islamic banks and financial institutions by adding some other concepts to it as a mode of finance. However, the validity of such transactions depends on some conditions which should be duly observed to make them acceptable in Shari'ah. In order to understand these conditions correctly, one should, in the first instance, appreciate that murabah'a is a sale with all its implications, and that all the basic ingredients of a valid sale should be present in murabah'a also [1].

Originally, murabah'a is a particular type of sale and not a mode of financing. The ideal mode of financing according to Shari'ah is mudarabah or musharakah. However, in the perspective of the current economic set up, there are certain practical difficulties in using mudarabah and musharakah instruments in some areas of financing. Therefore, the contemporary Shari'ah experts have allowed, subject to certain conditions, the use of the murabah'a on deferred payment basis as a mode of finance

II. Methodology

This paper is a type of Qualitative descriptive research, researcher uses legions of eruditions accessible from distinctive books on Islamic legislation and Historical evolution, past research papers, data from available resources including online libraries, blogs and articles from websites, public libraries etc.

III. Data Description

A. Basic Features of Murabah'a Financing

1. Murabah'a is not a loan given on interest. It is the sale of a commodity for a deferred price which includes an agreed profit added to the cost.

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2. Being a sale, and not a loan, the murabah'a should fulfill all the conditions necessary for a valid sale, especially those enumerated earlier in this chapter.
3. Murabah'a cannot be used as a mode of finance except where the client needs funds to actually purchase some commodities. For example, if he wants funds to purchase cotton as a raw material for his ginning factory, the Bank can sell him the cotton on the basis of murabah'a. But where the funds are required for some other purposes, like paying the price of commodities already purchased by him, or the bills of electricity or other utilities or for paying the salaries of his staff, murabah'a cannot be effected, because murabah'a requires a real sale of some commodities, and not merely advancing a loan.
4. The financier must have owned the commodity before he sells it to his client.
5. The commodity must come into the possession of the financier, whether physical or constructive, in the sense that the commodity must be in his risk, though for a short period.
6. The best way for murabah'a, according to Shari'ah, is that the financier himself purchases the commodity and keeps it in his own possession, or purchases the commodity through a third person appointed by him as agent, before he sells it to the customer. However, in exceptional cases, where direct purchase from the supplier is not practicable for some reason, it is also allowed that he makes the customer himself his agent to buy the commodity on his behalf. In this case, the client first purchases the commodity on behalf of his financier and takes its possession as such. Thereafter, he purchases the commodity from the financier for a deferred price. His possession over the commodity in the first instance is in the capacity of an agent of his financier. In this capacity he is only a trustee, while the ownership vests in the financier and the risk of the commodity is also borne by him as a logical consequence of the ownership. But when the client purchases the commodity from his financier, the ownership, as well as the risk, is transferred to the client [2], [3].
7. As mentioned earlier, the sale cannot take place unless the commodity comes into the possession of the seller, but the seller can promise to sell even when the commodity is not in his possession. The same rule is applicable to murabah'a.
8. It is also a necessary condition for the validity of murabah'a that the commodity is purchased from a third party. The purchase of the commodity from the client himself on 'buy back' agreement is not allowed in Shari'ah. Thus, murabah'a based on 'buy back' agreement is nothing more than an interest based transaction.
9. The above-mentioned procedure of the murabah'a financing is a complex transaction where the parties involved have different capacities at different stages.

- At the first stage, the institution and the client promise to sell and purchase a commodity in future. This is not an actual sale. It is just a promise to effect a sale in future on murabah'a basis. Thus at this stage the relation between the institution and the client is that of a promisor and a promise.
- At the second stage, the relation between the parties is that of a principal and an agent.
- At the third stage, the relation between the institution and the supplier is that of a buyer and seller.
- At the fourth and fifth stage, the relation of buyer and seller comes into operation between the institution and the client, and since the sale is effected on deferred payment basis, the relation of a debtor and creditor also emerges between them simultaneously [1], [4].

All these capacities must be kept in mind and must come into operation with all their consequential effects, each at its relevant stage, and these different capacities should never be mixed up or confused with each other.

10. The institution may ask the client to furnish a security to its satisfaction for the prompt payment of the deferred price. He may also ask him to sign a promissory note or a bill of exchange, but it must be after the actual sale takes place, i.e. at the fifth stage mentioned above. The reason is that the promissory note is signed by a debtor in favour of his creditor, but the relation of debtor and creditor between the institution and the client begins only at the fifth stage, whereupon the actual sale takes place between them.
11. In the case of default by the buyer in the payment of price at the due date, the price cannot be increased. However, if he has undertaken, in the agreement to pay an amount for a charitable purpose, as mentioned in para 7 of the rules of Bai' Mu'ajjal, he shall be liable to pay the amount undertaken by him. However, the amount so recovered from the buyer shall not form part of the income of the seller/the financier. He is bound to spend it for a charitable purpose on behalf of the buyer.

In the light of the aforementioned principles, a financial institution can use the murabah'a as a mode of finance by adopting the following procedure:

B. Step by Step of the Procedure

Firstly: The client and the institution sign an over-all agreement whereby the institution promises to sell and the client promises to buy the commodities from time to time on an agreed ratio of profit added to the cost. This agreement may specify the limit up to which the facility may be availed.

Secondly: When a specific commodity is required by the customer, the institution appoints the client as his agent for purchasing the commodity on its behalf, and an agreement of agency is signed by both the parties.

Thirdly: The client purchases the commodity on behalf of the institution and takes its possession as an agent of the institution.

Fourthly: The client informs the institution that he has purchased the commodity on his behalf, and at the same time, makes an offer to purchase it from the institution.

Fifthly: The institution accepts the offer and the sale is concluded whereby the ownership as well as the risk of the commodity is transferred to the client.

All these five stages are necessary to affect a valid murabah'a. If the institution purchases the commodity directly from the supplier (which is preferable) it does not need any agency agreement. In this case, the second phase will be dropped and at the third stage the institution itself will purchase the commodity from the supplier, and the fourth phase will be restricted to making an offer by the client.

The most essential element of the transaction is that the commodity must remain in the risk of the institution during the period between the third and the fifth stage. This is the only feature of murabah'a which can distinguish it from an interest-based transaction. Therefore, it must be observed with due diligence at all costs, otherwise the murabah'a transaction becomes invalid according to Shari'ah.

C. Determination of Murabaha Cost

It is already mentioned that the transaction of murabah'a contemplates the concept of cost-plus sale; therefore, it can be effected only where the seller can ascertain the exact cost he has incurred in acquiring the commodity he wants to sell. If the exact cost cannot be ascertained, no murabah'a can be possible. In this case, the sale must be affected on the basis of musawamah (i.e. sale without reference to cost) [4]. This principle leads to another rule: the murabah'a transaction should be based on the same currency in which the seller has purchased the commodity from the original supplier. If the seller has purchased it for Pakistani rupees, the onward sale to the ultimate purchaser should also be based on Pakistani rupees, and if the first purchase has occurred in U.S. dollars, the price of murabah'a should be based on dollars as well, so that the exact cost may be ascertained.

IV. Conclusion

A. Murabah'a in Islamic Trade Finance

In the case of international trade, it may be difficult to base both purchases on the same currency. If the commodity intended to be sold to the customer is imported from a foreign country, while the ultimate purchaser is in Pakistan, the price of the original sale has to be paid in a foreign currency and the price of the second sale will be determined in PKR. This situation may be met with in two ways. Firstly, if the ultimate purchaser agrees and the laws of the country allow, the price of the second sale may also be determined in dollars. Secondly, if the seller has purchased the commodity by converting Pakistani Rupees into dollars, the exact amount of Pak rupees paid by the seller to convert them into dollars can be taken as the cost price and the profit of murabah'a can be added thereon.

In some cases, the bank purchases the commodity from abroad at a price payable after three months or in different instalments, and sells the commodity to his client before he pays the full price to the supplier. Since he pays the price in dollars, its equivalent in Pakistani Rupees is not known at the time when the commodity is sold to the client. Due to fluctuation in the price of dollars in PKR, the bank may have to pay more than it anticipated at the time of murabah'a sale. For example, the rate of U.S. dollars at the time of murabah'a was Rs. 40/- for one dollar. The price of murabah'a was settled according to this rate, but when the bank paid the price to the supplier, the dollar rate increased to Rs. 41/- for one dollar, meaning thereby that the cost of the bank increased by 2.5%. In order to meet this situation, some financial institutions put a condition in the murabah'a agreement that in case of such fluctuation in currency rates, the client shall bear the additional cost. According to the classical Muslim jurists, murabah'a based on this condition is not valid because it leads to uncertainty of the price at the time of sale. Such uncertainty continues up to a date after three months when the buyer actually pays the price to the supplier. Such uncertainty renders the transaction invalid.

V. Recommendations

In the light of aforementioned details, there are following recommendations open to the bank to fix the issue:

a) The bank should purchase that commodity on the basis of L/C at sight and should pay the price to the supplier before effecting sale with the customer. In this case no question of fluctuation in currency rates will be involved. The murabah'a price can be determined on the basis of the market rate of dollars on the date when the bank has paid the price to the supplier.
b) The bank determines the murabah'a price in US dollars rather than in Pak rupees, so that the deferred murabah'a price is paid by the customer in dollars. In this case the bank will be entitled to receive dollars from the customer and the risk of the fluctuation in dollar's price will be borne by the purchaser [5].
c) Instead of murabah'a, the deal may be on the basis of musawamah (a sale without reference to the cost of the seller) and the price may be fixed as to cover the anticipated fluctuation in the currency rates.
d) Despite all of the above situations, if the price is paid by the bank in dollar and is ascertained and then both parties (bank and its customer) agree to pay the murabah'a price in PKR, then this transaction may be rendered as valid provided to:

- Conversion from dollar to local currency is not contingent. It means that the condition of conversion from dollar to PKR is not contingent at the time of execution of the agreement [6].
- The rate of conversion must be of the day of payment of murabah'a price (ready rate)
- Conversion price must be paid, delivered and possessed on spot, neither fully nor partially should remain on deferred basis. For example: if the cost price is \$110 and the conversion of those dollars are 5500 PKR (\$1=50 ~ 110 at 50=5500) in according to ready rate, the full payment must be affected on the spot and none of this remains unpaid for future date. However, if the full price is not intended to be converted into PKR but the portion

of dollars is being converted into PKR on ready rate basis, then whatever the amount being converted into PKR must be on spot and the rest of the amount i.e. not converted may be on deferred basis [7].

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