Elimination of Riba (Interest) In Financial Transactions

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INTRODUCTION

With financial turmoil of 2007 to 2009, the collapse of Wall Street on 28th October 1929 known as "Black Monday", economic disaster also known as "Great Depression" shook the capitalist economy brutally and compelled many economists as well as societal intellectuals to find solution and reconcile carefully the soundness of the economic system. Consequently, the world experienced several severe economic disasters, which stimulated serious thinking on economic matters (ul Hassan, 2005).

With the failure of communism, capitalism had spread, many people think that capitalism in which interest plays a very important role, is the best economic system for the present world. These include banking, finance houses, business, industry and agriculture. Modern society think capitalist economic system cannot exist without paying or charging of interest and no economy of the present world can survive with strict prohibition on the interest (ul Hassan, 2005).

Bergstra and Middelburg (2011), emphasized several different policies for dealing with interest. Interest can be defined as one of the forms of income from dividends, property, rent and profit. The price of rental for the use of money or as the percentage of excess of a money contracted for forward units of time over the spot or cash price of the sum thus contracted for forward delivery is referred interest. These include interest moderation is applied in all systems of conventional finance involving the imposition of higher bounds to rates of interest and to the size of loans, it essentially prevents people devastate their lives by accepting huge amount overdue. The upper bounds to interest rates are relative to the financial capabilities of the borrower, interest prevention which involves redesign of financial methods so that loans play a lesser role.

Debt prevention is the key means for achieving prevention of interest. The debts which are necessary, can occur within the system and will still carry interest if the needs of parties cannot be satisfied in other technique and finally interest party comes on top of interest prevention. The party that deal interest must adhere to the interest prohibition policy and party who adheres to it will either pay or receive interest. Islamic finance has been designed in such a way that it implements both interest prevention and interest prohibition, and it does so to the extent that there is no need left for interest moderation.

Islam is a religion presenting a system for the welfare of the society and prohibits a system where people earn income without putting work or efforts. Islam encourages a business of commodities and does not allow an exchange of precious goods with inferior goods of same goods with excess. This paper examines the meaning and types of riba, to explore verses of the Quran and their interpretations towards riba and to identify rational prohibition of riba.

DEFINITION OF RIBA

In particular, all forms of interest to denoting interest rates are termed interest and interest has become standard practice in the Western world (Bergstra & Middelburg, 2011). There is a consensus among Muslims that all forms of riba which lead to exploitation of the poor by means of usurious consumption loans, are prohibited by the Shariah and that banking should be in conformity with it (Nomani, 2003). The word “Interest” derived from the Medieval Latin word interesse and became usura means an increase on principal. Interest means the way in which the intention of the lender to obtain more money in return from a loan than the principal amount. Both interest and usury are riba and have the meanings of “increase or excess” above the principle amount (ul Hassan, 2005).

Riba is an Arabic word, derived from the verb riba that literally means ‘to grow’ or ‘expand’ or ‘increase’ or ‘inflate’ or ‘excess’. Technically, Riba refers to the ‘premium’ that must be paid by the borrower to the lender along with the principal amount as a condition for the loan or for an extension in its maturity. In terminology of fish, riba means an increase in one of two homogeneous equivalents being exchanged without this increase which is being accompanied by a return.

Riba is the payment or receipt of interest for the use of money.
perverse and harmful that falls in the category of gravest sins. Profit is a justified increase which is usually generated through exchange of two goods while, riba occurs either in the same thing or commodity to be returned with an increase (Nur, 2008).

There is a consensus of opinion among Muslim jurisprudence of all schools that riba al-nasihah as well as riba al-fadli are prohibited on the light of Quran and Sunnah respectively. The nature of the prohibition is strict, clear-cut and absolute. However, if the positive or negative return on principal depends on the final outcome of the business, it is allowed and it is in accordance with the principles of justice laid down in the Shariah (Chapara, 2006; Jammeh, 2010).

**Prohibition Of Riba**

Quranic Verses On Riba

There are 12 verses in the Quran dealing with Riba.

<table>
<thead>
<tr>
<th>The Name of Surah</th>
<th>Surah Number</th>
<th>Verse Number</th>
<th>Total Verses</th>
</tr>
</thead>
<tbody>
<tr>
<td>Suratul Rum</td>
<td>30</td>
<td>39</td>
<td>1</td>
</tr>
<tr>
<td>Suratul Nisa</td>
<td>4</td>
<td>161</td>
<td>1</td>
</tr>
<tr>
<td>Suratul Al-Baqarah</td>
<td>2</td>
<td>275-281</td>
<td>7</td>
</tr>
<tr>
<td>Total</td>
<td></td>
<td></td>
<td>12</td>
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</table>

The word riba itself is cited eight times in the Quran, three times in 2:275 and one time in 2:276; 3:130; 4:161 and 30:39 (Siddiqi, 2005).

The injunctions of riba in the Holy Quran were revealed in a period spread over a number of years. Surah Al Baqarah Verses 275-81 were summarized as followings: first and foremost interest is firmly prohibited, secondly, interest is defined what is an excess over the amount of money borrowed; thirdly interest is unjust, it is destined to destruction and lastly it degrades and trims down persons who indulge in it taking. Riba generates various evils like moral evils, social evils and economic evils (Siddiqi, 2005).

**Some Selected Ahadith On Prohibition Of Riba**

1. From Jabir: The Prophet, may peace be on him, cursed the receiver and the payer of interest, the one who records the transaction and the two witnesses to the transaction and said: “They are all aike [in guilt]” (Muslim, Kitab al-Musaaqat, Bab la’ana aki al-riba wa mu’kilahu; also in Tirmidhi and Musnad Ahmad).

2. From Anas ibn Malik: The Prophet, peace be on him, said: “When one of you grants a loan and the borrower offers him a dish, he should not accept it; and if the borrower offers a ride on an animal, he should not ride, unless the two of them have

**The Rationale Prohibition of Riba**

Both Quran and Sunnah showed strong evidences for prohibition of riba. The researcher attempts to express some reasons for its prohibition to better appreciate the wisdom behind the injunctions. These are provided as the following:

**Disparities of Income**

- Lack of collateral and established economic standing, poorer segments of the economy are at an economic disadvantage when competing for credit to finance economic activities.
- As a result, wealth and income disparities increase among the society members, which generates envy and hatred among the society.

**Injustice and Exploitation**

- It guarantees lenders’ return without involvement in risk.
- It takes advantage of a man’s inferior economic position, which kills the spirit of cooperation in the society and discourages people from doing mercy to each other.

**Creation of Materialistic Society**

- Riba nurtures a materialistic society and people must work harder and harder and may exercise unethical business practices in order to repair their bank debt.

**Impediment of Healthy Economic Development**

- Riba discourages innovation since potential entrepreneurs without security to pledge are denied credit (Alessa, u.d).

**Discourse of Entrepreneurship**

- Riba encourages the creation of wealth with no effort from its provider at the cost of borrower.

**Elimination of Interest in Islamic Financial Institutions**

The Islamic financial institutions innovated and developed numerous financial instruments which are free from riba. The most frequently used instruments are wadiah (safekeeping), mudharabah (profit sharing), murabahah (cost plus), ijarah (leasing), qardh al-hassan (benevolent loan) and musharakah (joint venture).

<table>
<thead>
<tr>
<th>Types of Concept</th>
<th>Description</th>
</tr>
</thead>
<tbody>
<tr>
<td>Wadiah</td>
<td>Is a non-interest-bearing demand deposit (checking account) similar to the current account offered by conventional commercial banks. It is also a non-interest bearing savings deposit account, but with a promise of giving hiba (gift) whenever the bank has “profits” to share.</td>
</tr>
<tr>
<td>Mudharabah</td>
<td>Account is a form of time deposit that cannot be withdrawn before the contractual time has elapsed. The bank as the intermediary (mudharab) gets profit on the basis of profit sharing—less bearing principle. Murabahah (cost plus) is financing facility in which Islamic bank buys the merchandise, adds an amount for “profit” and sells it to the borrower, to be paid back in equal installments or lump sum.</td>
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<tr>
<td>Ijarah</td>
<td>Is another way of enriching the Islamic bank at the cost of the borrower. The Lessee cannot renounce or change the contract in view of changes in the market conditions. Any break in the contract goes in favor of the Islamic bank.</td>
</tr>
<tr>
<td>Qardh al-hassan</td>
<td>Is given in good faith—the borrower is obliged to pay back the amount lent only, without any obligation to pay anything extra. It is quite obvious that not many loans would be given by a financial institution that is open for business of making money.</td>
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<tr>
<td>Musharakah</td>
<td>In which an Islamic bank and clients jointly finance a venture by issuing participation certificates that can be bought and sold in the market. This type of joint venture is commonly known as sukuk, and the ‘participation certificates’ are traded like bond.</td>
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</table>

Islam is a religion that ensures complete success of human life in here and the hereafter. The Holy Quran and Sunnah clearly declared an interest comprising riba al-nasihah and riba al-fadli as Haram and people are prohibited to practice it. Prohibition of interest in financial transactions is not unique to Islam but also other revealed books. The wisdom behind prohibition of riba includes unjust, destruction, creation of various evils like moral, economic and social evils.