

S. M. Imam-ud-Din

A HISTORICAL BACKGROUND OF MODERN ISLAMIC BANKING

Bayt-al-Mal

To discuss the development of banking in Muslim countries one is to start with the time of the Prophet of Islam who introduced the system of *Bayt al-Mal* for the collection and disbursement of revenues among the displaced *muhajirs* and needy *ansars*. The *Bayt al-Mal* which was a welfare agency functioned as the central or State Bank of Muslims from the early days of Islam. Actually Prophet Muḥammad (be peace of God upon him) did not need a treasury house. Whatever came as *jizyah*, *zakat* or *al-ghanimah* (booty) were distributed then and there by him. In the second year of the *Khilāfat* Ḥaḍrat Abū Bakr Ṣiddiq (*Radia Allahu anhu*) had his treasury box at the Masjid al-Nabawai of Madīnah but there was only one dirham left in it on his death. Following the Prophet Ḥaḍrat Abū Bakr Ṣiddiq (*Radia Allah anhu*) had distributed all what he received, ten dirhams to every one in the first year and twenty in the second year of his *khilāfat* (13-14H/632-34 A.D.). The first caliph had a separate building for the *Bayt al-Mal* but according to Ibn Saʿad it remained empty and unused throughout his reign.

Ḥaḍrat 'Umar al-Fāruq, the second caliph (14-24H/634-44 A.D.), took census of the Muslims and established *Diwan*, a Persian institution, to register the names of the recipients of pensions. He was the first man in history to take the responsibility of feeding the people living within the Islamic State. It has justly been described by Maulana Shibli Nuʿmani as an early form of socialism. Ḥaḍrat 'A'ishah (*Radi Allah anha*) topped the list of pensions and received 12,000 dirhams annually. According to the gradations, the *ahl-i-bayt*, emigrants and helpers, received 4,000 to 5,000 dirhams annually. An ordinary soldier received 500 to 600 dirhams while women, children and clients (*Mawalis*) were given 200 to 500 dirhams a year. The treasury was reorganised and sub-treasuries were set up in provincial headquarters. When Abu Huraira came from Bahrain with an annual revenue of 500,000 dirhams and *al-ghanimah* and revenue from *al-Fai* land increased unprecedently. 'Umar al-Faruq's proposal of founding a permanent treasury

at Madinah and its branches in the provinces was approved by the *Majlis al-Shura* in about 15H/636-7 A.D. and the Hijra era was introduced in the following year, the 15th century of which is being celebrated this year throughout the Muslim World. Walid b. Hisham, who had the knowledge of the administration of public treasury under the Byzantine kings of Syria, pleaded for the separation of the executive and treasury officials. To manage the collective wealth of the community the treasury officials were appointed and guards were posted by the second caliph. 'Abd Allah b. al-Arqām was appointed in-charge of *Bayt al-Māl* and 'Abd al-Rahman b. 'Ubayd al-Qārī and Mu'ayyib as his assistants. The treasury officers were generally independent of the governor and held an important position in the Muslim Society. Khālīd b. Ḥārith and 'Abd Allāh b. Mas'ūd were appointed treasurers in Isfahān and Kūfah respectively. After covering the expenditure of the provincial governments the governors despatched the balance to the central *Bayt al-Māl* located at Madinah which spent 3,00,000 dirhams on the salaries and pensions of the Madinites alone.

The Bayt al-Māl, the state bank of the Muslims, was a special department of the Central Secretariat supervised and directed by a special government officer called *Khāzin al-Māl* or *Ṣāhib al-Makhāzin* and provincial treasurer *Khāzin* or *amīn* and considered among the elites of the Muslims. Many people served under him as his assistants and accountants. Ahmad 'Ali, the author of *al-Tanzimāt al-Ijtamā'iyah wal Iqtasādiyāt fil Baṣrah*, is of the opinion that the staff was mostly consist of non-Arabs and a good number of them might have been Jews. The supreme head of the provincial *Bayt al-Māl* was the *Amīr* and that of the centre the *Khalīfah* himself and both were responsible for the smooth running of the departments of the government. The very nearness of the *Bayt al-Māl* to the residence of the *Amīr* indicates the close control of the *Amīr* over the *Bayt al-Māl*. The French writer Tyan's opinion that it was closely connected with the chief *Qāḍī* is contradicted by Ahmad Ali.¹ The *Qāḍī* was in-charge of a treasury which came to be known as *Bayt al-Māl Muslimīn* and was located in the mosque. This treasury was different from the general public treasury.

In Spain and elsewhere, there were two kinds of treasuries one called *Khazīnat al-Māl* or *Bayt al-Māl* and another *Bayt al-Māl al-Muslimīn*. There was also a third treasury called *Bayt al-Māl al-Khās* which had been introduced by the Umayyad caliphs of Damascus to deal with their personal income and expenditure.

The *Bayt al-Māl* was not only the property of the Muslims alone

but of non-Muslims also, Out of the funds of the *Bayt al-Māl* the State was obliged to support needy *dhimms*¹ as well as indigent Muslims. The terms of the treaty entered between Khālid b. Walīd and the people of Hira was that the old *dhimms*² and their dependents would not only be exempt from the payment of *Jizyah* but would be given regular financial support as long as they would reside within the boundary of the Islamic State. While explaining *sadaqah*, Maulana Shibli Nu'mani, the author of '*Umar al-Faruq*, says that it was meant for the Muslim beggars and the needy *dhimms*.³ The *Bayt al-Māl al-Khās* was the personal treasury of the Umayyad, Abbasid and other caliphs, their princes and harems.

According to a Mez, the learned German author of the *Renaissance of Islam*, the State Chest was kept at Fustat in front of the pulpit of Amr's Mosque and it had wooden steps and iron doors with a lock.⁴ As early as 97 and 99 H/715 A.D. 'Uthamah b. Zaid (who had led the Syrian expedition under caliph Abū Bakr (R) in 632 A. D.) while posted as the director of finance in al-Fuṣṭāṭ built a *qubbah* on pillars in front of the minbar (pulpit) of the Mosque of 'Amr for the *Bayt al-Māl* of Egypt.⁵ The treasury stood in a Syrian Mosque at Barda on nine columns and had iron doors and a leaden roof.⁶ The caliph al-Mu'taḍid of Baghdad (270-89 H/892-902 A.D.) built a house for his private treasures and got its joints filled with lead. He kept the money in purses with the seal of the treasurers. The Ikhshid rulers of Egypt kept the money in sacks made of nets of steel wire inside the armoury. While other Muslim rulers of the 10th century kept it in the chest. Maqqari says that the treasures were always kept in sealed jars within the palace of the caliph at Cordova. But when Sultanah Subh, the widow of Hakam II, was found laying hands on it, Hajib al-Mansur, the Prime Minister of Hisham II (366-403H/976-1012 A.D.), was the first man to remove it from the palace of Hisham II to his newly constructed palace at Zahirah in a newly built capital city al-Zahirah⁷ which was different from al-Zahra palace city of 'Abd al-Raḥmān al-Nāṣir III (301-350H/912-961 A.D.) both were located in the neighbourhood of Cordova.

Bayt al-Māl dealt with the income and expenditure of the State. Some slight changes were introduced in the Byzantine dinar and Persian dirham which were retained in circulation by Ḥaḍrat 'Umar to be Arabicised fully later under the Umayyad caliph 'Abd al-Malik (43-63 H/685-705 A.D.) and registers were maintained in Persian in Iraq and Persia, Syriac in Syria and Coptic in Egypt for recording revenues and expenditures, these were also Arabicized by 'Abd al-

Malik, the builder of *Qubbat al-Sakhara* (Dome of the Rock) at Jerusalem, the second sanctuary of the Muslims.

Among the sources of revenue were the *zakāt* (poor rate), *al-sadaqah* (alms), *jizyah* (pool-tax), *'ushr* and *kharāj* (land tax), *al-'ushūr* (tithes, customs and market duties), taxes on mines, *khums* (one-fifth of the booty), *al-Fayy* (income from State lands). The income from the *zakāt* the religio-State duty paid by the Muslims formed the part of revenue resources of *Bayt al-Māl al-Muslimīn* and was spent on the needy and indigent Muslims, collectors of *zakāt*, the emancipation of slaves, military enterprises, debtors, thieves and women of suspected characters etc. The *jizyah* being a military tax was collected from able and earning adult members of the *Dhimmis* only when the Muslims were sure of giving protection to the life and property of the protected non-Muslims. On failure of giving protection the *jizyah* was returned to the people of Ḥims, Damascus and other advance posts before the battle of Yarmuk and the Cypriots were exempt from the payment of *jizyah* for sometimes even after surrender till Ḥaḍrat 'Uḥmān, the third caliph, became sure of their security and protection. The income from *jizyah*, *kharāj* and *ghanimah* etc. went to the general treasury and was spent on the maintenance of soldiers and other administrative purposes.

The earliest *al-Fayy* land was the Fadak, the income from which was spent on the Prophet's relatives, the orphans, the indigents, the way-farers and on the general welfare of the Muslim community. A good portion of *al-Fayy* lands was assigned to the soldiers and converted to *'Ushrī* lands later on and some were acquired by the caliphs under the Umayyads and the revenue from such lands went to their personal treasury, the *Bayt al-Māl al-Khās*. The income from the state lands which formed the source of the general treasury was spent on public works like digging of canals, construction of dams, dykes, tanks and roads and maintenance of postal service.

The *Bayt al-Māl al-Muslimīn*, as discussed above, was located in the chief mosque under the custody of the chief Qāḍī. Ibn 'Abdun, the author of *al-Hisbah*, commenting on this opines: "The treasury of the pious foundation should be kept in a mosque well guarded and locked. Its keys should be in the possession of the Qāḍī. If sufficient amount of money was not found available in the general treasury and the rulers liked to spend a necessary sum for the undertakings of some meritorious works, like that of organising a campaign, repairing some fortresses or for defending the Muslims against the attacks of enemies,

the Qādī was entitled to give him the necessary amount which he deemed essential for the improvement of the conditions of the Muslims from the treasury but would not give him any more since after all he was responsible for the administration of the funds".⁸

The *Bayt al-Māl al-Muslimīn*, functioned as the centre of deposits. While writing the biographies of Qādīs of Spain in the 9th and 10th centuries, the famous writer al-Khushanī mentions a number of cases of embezzlement of *awqāf* funds and orphans' money by qādīs like Yūsuf b. Baṣīl of Sidonia, Naḍar b. Salmah al-Kalbī of Cabra, Mūsā b. Muḥammad and 'Amr b. 'Abdullah and the Cordovans demonstrated against the appointment of greedy Abi al-Ghamar b. Fahd as the chief Qādī of Cordova during the time of 'Abd Allāh, Amīr of Spain (852-86 A.D.). Documents have been found of depositing money by dying father for his children and 10,000 dinars by Ibn al-Qusaybi, a merchant, about 260 H/873 A.D. and 263 H/876 A.D. and another document of the time of Qādī al-Habīb (d. 312/924-5 A.D.). The chief Qādī Mundhir b. Sa'īd b. 'Abd al-Ballūti was the in-charge of the house of the orphan children of Zakariya, the brother of Najda, and refused to sell the house to 'Abd al-Rahmān III saying, "the property of an orphan cannot be sold except for three reasons: necessity, impending ruins, or the offer of more advantageous terms than those on which it was at first obtained". Al-Mu'taṣim b. Samadīh, ruler of Almeria, could not complete his palace till he bought an orphan's orchard by paying the price fixed by the orphan and his guardian. There are many other cases of orphans' deposits in the *Bayt al-Māl al-Muslimīn* (Mosque) which was under the custody of Qādīs both in the East and West. In the absence of legal guardians the Qādīs (courts) are still guardians of orphan's property, a tradition which has been followed by the Muslims with some modifications throughout the ages.

The public treasury of *Bayt al-Māl* played the role of an agricultural credit bank and also a commercial bank from the early days of the Umayyads. During the time of Ḥajjāj b. Yūsuf (d. 73 H/714 A.D.), according to the Muslim geographer Ibn Khurdābih (d. 229-33H/844-848 A.D.), it lent to the peasants two million dirhams. Aḥmad 'Alī says that we have no details about the conditions of this loan but surmises that no interest was charged for it.⁹

Apart from this function of giving money on loan *Bayt al-Māl* used to finance many commercial transactions. It was a sort of clearing house among merchants in the different provinces thus facilitating their trade in the medieval period. Merchants used to borrow money from

this public treasury to buy rare and variable goods and by selling them in another province used to repay the debt to the nearest *Bayt al-Māl* where the amount was credited to the account of the province from where the money had been drawn. During the time of Abū Mūsā al-Ash'arī, the governor of Kūfah, 'Ubayd Allāh ibn 'Umar borrowed money from the public treasury of Baṣrah, bought goods and sold in the Ḥijāz and paid to the *Bayt al-Māl* of Ḥijāz at Madinah what he owed to that of Baṣrah (Um, Vol. III, p. 258). Ahmad 'Ali suggests that there might have been some other cases of this nature in the East but the sources are silent. To invest in trade Qāḍī Sulaymān b. Aswad advanced 5,000 dinars to al-Ḥabīb Aḥmad b. Muhammad b. Zayyād al-Lakhmī, before the latter was appointed Qaḍī of Cordova in 291 H/903-4 A.D. This money might have been given to him from the *Bayt al-Māl al-Muslimīn* of Cordova.

Mudarabah

Money lending was an old custom in Muslim society approved by the pious Khalifah 'Umar b. al-Khaṭāb. His two sons, 'Abd Allāh and 'Ubayd Allāh, carried on trade on credit basis and Ḥaḍrat 'Uḥmān b. 'Affān, who later became Khalifah, lent money to Ya'qūb, a Jew of Madinah, the owner of al-Ḥarqah, to carry on business at Madinah with his money during the Khalīfat of Ḥaḍrat 'Umar when the Jews had an expulsion order from the Caliph.¹⁰ Muḥammad ibn Aḥmad al-Sarakhsi writes :"

"The word *Mudāraba* is derived from *darb* on Earth. It has been so named because the *mudārib* (user of other's capital) qualifies to get profit's share on account of his endeavour and work. He thus participates in the profit as well as he gets the right to use capital and strive according to his discretion. People of Madinah call this contract *Muqārada*. This has been related on the authority of 'Uḥmān ibn 'Affān that he handed over to a person some capital on *muqārada* which is derived from the word *qard*, meaning a severed part. The owner of capital thus severs his right of disposal over the portion of capital and gives it to an *'amil* (user of capital). This is how it has been so named, we have, however, chosen the former name as it conforms to what occurs in the Book of Allāh saying and others strive on earth seeking the gift of God . . ."

A more explicit explanation of *Mudāraba* is given by another jurist Burhānuddin Abū Bakr Marghinānī in the *Hidāyah* thus¹² :—

"*Mudāraba* is derived from the word *Ḍarb* (endeavouring and journeying on earth). It has been so named because the *Mudārib*

(investor of capital) deserves the profit on account of his efforts and work. It has been allowed (in *shari'at*) because of necessity, as there are so many kinds of people. There are some, rich in wealth but without talents to use it, and others capable of using it but empty-handed. There accrues thus, a necessity for this kind of utilization which can reconcile the interests of both the incapable and the resourceful, the poor and the rich. People practised it in the days of Prophet (peace be upon him); he confirmed its legality. The companions of the Prophet too entered into similar contracts. The capital, then is a trust in the hands of the user and he is authorised to use it (with his own discretion) as he gets the possession with the sanction of actual owners, not on account of exchange or pawn. He is an agent as he uses it with the sanction of the owners. He shares the profit when it accrues on account of his authority over it, and because of his work. If the contract is violated on account of the owner it will be treated as employment on wages till the investor violates any of the condition to become a usurper on account of misuse of another's wealth".

Partnership business is allowed in Islam. Ahmad b. Mughith al-Sadafi, yet a great jurist, writes in his *Kitāb al-Wathā'iq*: "The Muslim should associate himself in trade with persons of religion and integrity, but not with one who practices *riba* (usury) and treason".¹³ According to the custom approved by theologians, there should be equal shares in the partnership business, however, trade was permitted even if the capitals invested were not equal provided the profit and loss were shared in proportion to the capital invested and the labour put in¹⁴.

A partnership business was also constituted between men and women and a slave with the permission of his master could also enter into such contract.

In *shirkat anām* (society for supplying material) it was allowed to trade with merchandise only without investing money provided these were evaluated before entering into contracts which had to be based on the value of the merchandise. The association for sale and purchase based on an expected capital or on credit was not permissible. It was, however, permitted that one bought merchandise on credit with the guarantee of another and it was also permitted to form a society of two persons by virtue of which one lent money to another for investment in trade on condition that the profit would be provided equally between the two and the loss would be borne by the capitalist and the worker (user of capital, entrepreneur) was to get his remunera-

tion which was calculated on the basis of local wages. Trade on credit was not allowed and one who took articles, other than coins, on loan and traded in them was entitled to a remuneration like a servant.¹⁵

Institution of Credit

Credit is derived from the Latin word '*Credo*'. It is a belief in the ability of a person to pay. The principal credit instruments are promissory notes, cheques, bills of exchange and the like.

The Jews had their colonies in all the commercial centres and participated in the economic life of the towns and villages and held key positions in Muslim States. Ibn Taghri Birdi, the author of *al-Nujūm al-Zāhira*, writes that in 296 H/908 A.D. Muqtadir bi'llah (296-320 H/908-32 A.D.), the Abbasid caliph, made the enrolment of Jews (and Christians in the State service) as bankers (and physicians.) According to Maqdisi, a renowned historian and geographer, most of the bankers and money-changers in Syria and Egypt were Jews (and most of the physicians were Christians).¹⁶ Joseph ben Phineas and Aaron ben Amran who had been merchants and money-changers, were appointed as court bankers by the Abbassids. They had formed a limited firm staffed by their sons and relatives. Once they charged from an Abbasid *wazir* interest at the rate of 30% on a loan of 10,000 dinars.¹⁷

There was a colony of 'Irāqī Jews in Egypt, some of whom worked as agents of 'Irāqī merchants. The Jews and the Christians were patronised by all the Fatimid caliphs except al-Hākim (386-411 H/996-1020 A. D.). They took special part in the economic life of Cairo as they did in that of Baghdad and their most important figure was Abul Faraj Ya'qub b. Yusuf b. Killis (d. 380H/991 A. D.). A Jewish bank with the name of Sahl Brothers migrated from Tustar (Persia) to Cairo and joined the 'Irāqī Jews already settled there. They served the Fatimid caliphs, al-Zāhir and al-Mustansir, from 412-438 H/1020-1047 A.D. Abū Sa'd Ibrāhīm and Abū Naṣr Hārūn, the two sons of Sahl according to Maqrīzī, received the goods of the merchants, who died in distant lands, and reported the same to their heirs.¹⁸ Abū Sa'd Ibrāhīm was the royal merchant and travelled far and wide to purchase precious stones, valuable and luxurious goods and slave girls for his master Zāhir (412-26H/1021-35 A. D.). His brother Abū Naṣr Hārūn was engaged in money transactions. Difference of exchange in the various countries and the fluctuating values of dirhams and dinars necessitated an exact knowledge of the local and international money markets in the interest of correct computation. Payment took the form of cheques or orders on other accounts. Abū Naṣr procured,

at the shortest possible notices, the means of financing the commercial undertakings and journeying of his brother Abū Sa'd. The Irāqī Jews and the Sa'd brothers were the intermediaries of all the trade goods and wares exchanged between 'Irāq and Egypt. The agents of a large Baghdād firm, as we learn from Maqrīzī, "placed large deposits of goods, and perhaps of money too, with them"¹⁹. There was another colony of Irāqī merchants from Baṣrah, Kūfah and Baghdād in Sijilmāsah (Morocco). A large number of the Jews carried on trade at Gabes (Qabis in Ifriqiyah) and 'Aydḥāb and elsewhere, the Abyssinian ports of the Red Sea, Pechina (Almeria) and other ports of Spain, Cologne, Aix Magdeburg and Narbonne in France, Merseburg and Sajonia and they devoted themselves to the traffic in Christian slaves. Notker Balbulus in his *Tales of Charlemagne* speaks of Jewish boats sailing in the Mediterranean in the 9th century²⁰ to regularize the weights and letters of exchange. Torres Balbas says that inside al-Qaysariyah of Muslim Spain the money-changers functioned.²¹ In the beginning of the 13th century the Jews had some money-changers shops in al-Qaysariyah of Clatayud.²²

The Jewish bankers had their offices at Sijilmāsah, Gabes and 'Aydḥāb to encash the *suftaja* (draft) issued by them and to do other indenting business. They had their trade centres also at Verdun, Narbonne, Marseilles, Naples, Venice and other towns in Europe. Ephraim ben Jacob, a merchant from Denia (Spain), appointed one Abun as his attorney to claim whatever his late father might have left for him in Egypt and to sue against one Abū Naṣr Musāfir in 493 H/1098 A.D. A Spanish merchant in Jerusalem requested Abū Naṣr Faḍl ben Sahl al-Tustari to send an account sheet and the resulting balance.

The appearance of *Jahbadh*, derived from a Persian word *Kahbadh* meaning money-changer, banker or tax-collector goes back to the time of the Sasanids. Their famous ruler Jamshid was its founder. It was well known during the time of the Umayyads from the *Khilāfat* of Mu'āwiyah. The Abbasids enlarged and intensified the functions of *Jahbadh*, who worked also as tax-collector and accountant in some provinces.²³

In the 8th and 9th centuries the revenue were collected in dirhams from the Eastern provinces of the Abbasid Empire and in dinars from the Western ones and in the 4th/10th century only in dinars. The ratio between dirham and dinar fluctuated very much in the market. In this connection, the *Jahbadh* has been frequently used. The duty of the *Jahbadh* was to convert silver coin into gold and *vice-versa*. In 326/

938 A.D. a separate department of *Jahbadh* was created by the Abbasids under the headship of a Christian named Ibrahim b. Ayyub. The *diwan al-amwal* equipped with a numbr of *Jahābidha* was located in the palace of Ya'qub b. Killis, the prime minister of the Fatimid caliph al-'Aziz (d. 996 A.D.) of Egypt.

The history of the word *al-sayrfah* (dealers in money), another economic term, goes back to the Babylonian time. During the time of the Sasanids there lived a Christian minority in Mada'in. Their mediation between the Persian silver coins and the Byzantine gold ones facilitated trade. On their migration to Kufah in the early years of Islam they converted dinar into dirham and dirham into dinar and solved the problem of the difference between the quality and weight of the same coin. They played an importact role in the development of the banking system in 'Iraq. In the exchange of dirham and dinar the discount was made at the rate of one dirham per dinar and one *dāniq* per dirham: but sometimes the discount rate was very high. The unscrupulous money-changers made some unfair gains due to the constant fluctuations in the values of coins and prices of articles.

This system of exchange of money drained away gold and silver in the form of bullion or coin from the importing countries to the exporting ones. The trade balance of Europe in her Dark Ages was always in her favour, because their export of raw materials and slaves to Muslim countries brought in gold in large quantity e.g. flow of gold from Asia to Europe and this helped later in the economic development of Europe in the period of Renaissance. To facilitate large transactions and to solve the risk of transfer of huge amounts they introduced an instrument of credit operation in the name of *suftajah*.

Suftajah is the Arabicized form of the Persian word *saftah* meaning paper money or letter of credit. This letter of credit, or draft as we now call it, was issued by a money-changer on receiving a certain amount as deposit instructing his agent in a distant town or country where the traveller or merchant wanted delivery of the sum to make payment on receipt of this letter. This was, in short, a pay order from one man on another for the payment of a specified sum by a certain date. References to such payments are there in the contemporary literature of the Muslim countries. Commercial, government and private transactions were made through some international money-changers like the companies of Joseph ben Phineas and Aaron ben Amran of Baghdad and the Sahl Brothers of Cairo²⁴ already mentioned above. A house wife received 200 dinars through a *suftajah* from her husband. In the year 313 H/925 A.D.

The caliph of Baghdad namely al-Muqtadir (296-320/908-32 A.D.) received a *suftajah* of 147,000 dinars sent by the Governor of Egypt and Syria through a Jewish banker of Egypt. The public treasury in Baghdad contained *amwāl safātij* sent from Faris, Isfahān and other eastern provinces and the bearer of these *safātij* was a special messenger called *fij*. A certain traveller from the East on his journey to Spain carried with him a letter of exchange and 5,000 dirhams in cash for his travelling and other expenses and to make certain purchases on the way.²⁵ This was encashed most probably.

Generally *suftajah* became payable forty days after its drawal. The owner of the *suftajah* was entitled to receive the entire amount if it was cashed in due time or by instalments if he so pleased. A certain deduction was made if it was cashed before the stipulated time²⁶. In 301 H/913 A.D. one 'Ali bin 'Isa paid in the East one and a half *dāniq* (one *dirham* = 6 *dāniq*) or one-sixtieth *dīnār* per *dīnār*, because he cashed his draft before the fixed time. By the 4th/10th century merchants of Basrah had become so much commercial and bank minded that they always kept their accounts in the banks and used cheques (*khatt-i-saraf*) even in the local transactions. A man of Sijilmasah drew a cheque of 42,000 dinars on another man of the same city, ratified officially.²⁷ *Suftajah* and *Khatt-i-saraf* were also used commonly in Fairs, weekly or monthly, national or international.

In the introduction and use of credit the Arabs and the Byzantines were the fore-runners of the nations of the West. From the beginning of the Middle Ages Byzantine gold coins, usually of fixed value, were accepted in the international markets. But the developments of trade in Byzantine territory led the Greeks to introduce a credit system. In spite of the disagreement of the church, lending of money was very much common there and money was easily raised at the moderate rate of 6 to 12% interest and in the 4th/10th century the rate of interest was even lower.

Henri Pirenne says that in important negotiations the general rate of interest was 10% but at times it rose to 50 per cent or 100 per cent or even higher. In 712/1311 A. D. the French king Philip of Valois allowed money lenders to charge 20 per cent interest in the fair of Champagne. To compensate their frequent losses caused by dishonest borrowers, the Jewish money-lenders of Europe sometimes charged very high interest rising to 80 per cent. This created hatred against them which was taken advantage of by their rivals, the Christian money lenders, to incite their expulsion from Europe.

In short it may be mentioned that all the main functions of

the modern banks were performed by the *Bayt al-Māl* in cooperation with the *Jahābidbah* office of the government, private *Mudarabah* and 'anan systems, e.g. the sharing system (of the joint stock companies) and the *sayrfah* system of the Jews. Bank cheques, *Khatt-i-Saraf*, *softah* or *saftajah* were issued and accepted in local and foreign transactions and discount was allowed as service charges in the exchange of coins and encashment of *suftajah* and interest was charged by the Jewish banks and not by the *Bayt al-Māl*. Now in the light of these a study of modern interest-free Islamic banking may be made here.

Modern banking is expanding and becoming sophisticated because of growing industry, technology and commerce. This is true in the case of all non-Muslim or Muslim countries but the latter are faced with the problem how to earn profit out of this system without having interest which is the crux of the problem and which can be solved by establishing banks on the basis of *Mudaraba* or 'anan systems.

Economic needs of Islamic Society have grown in bulk and we are to keep pace with the economic development in non-Muslim countries having capitalistic, socialistic or communistic pattern of living. Muslim countries though politically independent they are very much dependent economically on others as they need interest carrying loans of the World Bank and of other organisations for their development nay for their subsistence. It cannot be denied that our key problem is economic development to which the banks' contribution is the most important factor. Keeping our requirements in view, we are to orientate a system of banks without violating the fundamentals of Islam and to prevent the shattering of the economy of the country this should be introduced very cautiously and gradually phasewise by providing incentives and moulding the habits more of the depositors than of the borrowers.

Modern Central or State Bank is the agent of the Government. It is empowered to issue currency and regulate credit and other banks are profit making concerns performing some or other functions of the bank which brings into a common pool the idle money of the general public, makes advances to others and thereby gains a return in the form of interest or dividend.

The origin of bank may be found in the Italian word '*banco*' but the system was known to the Jews and Muslims and even to the Babylonians (c. 2,500 B.C.) much before the Italians came to know of it. The evolution of commerce and banking started with the civilization itself. Engraved clay-tablets discovered in Arabian desert

prove that in ancient Babylonia, a money and credit economy had developed to such an extent that it required the services of banks and they used deeds, promisory notes, mortgage and other business forms.

Interest has been prohibited in the Holy Scriptures of the Jews as well as of Christians. Lending of money on interest was prohibited by the Greeks and the Romans. Catholic Church prohibited interest as long as it remained in power. Private lenders started money lending on interest to the feudal lords in European countries when one needed money to raise an army against another. Modern banking is the result of the commercial revolution of the 16th century. The '*Banco di Rialto*' was the first public bank started in Venice in 979H/1584 A. D. The gold-smiths were the first bankers in England during the civil war (1642-45) the people in England deposited with the gold-smiths their valuables. They charged a commission on these for safe-keeping. This gave growth to banking system in England.

Institution of interest which developed as a matter of accident encourages savings and attracts idle money of the community. To bring the most remote countries into frequent contact with other parts of the world modern banks gear up transportation and communication system and thus multiply the effective use of accumulated wealth through credit institutions. A banking system, if badly constructed or badly handled, is capable of upsetting the whole economy of a country.

Interest-free Banking

To eliminate interest from society banks and certain other institutions may be established on the basis of *Muḍārabah* where capital and labour can be combined together as partners in an enterprise and can share the profit and bear the loss equitably. This will serve as a good device for the mobilization of capital and labour and will provide employment in the country and with increase of the exchequer's return on income tax, development of the country will take place. The *Qurān* eliminates and condemns *riba* (interest) but justifies and retains *bai* (normal business). Gains without risking capital is interest and after exposing it becomes profit. Interest-free economy practised in early Islam was neither capitalistic nor communistic, yet it has good features of both. If Islamic banking is based on *Muḍārabah* system, which is, however, very much risky in a society like ours, the profit-sharing principle will provide an incentive to the depositors to invest money in the bank which will run business like joint stock company and

distribute profits among the share holders as dividends. The consumer loans may be granted easily by the *Bayt al-Māl* or Banks as they do not pay interest or dividend on current deposits. To run Islamic banks certain social reforms besides changes in the economic system are required. Some aspects of this problem will be discussed under different heads by some of our experts in modern and Islamic banking system in their valuable papers. As interest includes reward for risk and profit constitutes reward for in uncertainty, it is not difficult to substitute the prevalent system of banking, but never to supplement it, if the Muslim Society in an Islamic State becomes genuinely and sincerely interested in eliminating *riba* and introducing the interest-free banking system and is prepared to bear the inconveniences or the difficulties that are unavoidable in a transitory phase of change-over. Similarly it will not be difficult for a bank to shift from interest earning bodies to profit sharing or dividend receiving bodies.

The *Qurān* says اهل الله البيع و حرم الربوا 11 : 275.

God hath permitted trade and forbidden usury. This is primarily a directive prohibiting commercial interest with which prohibition of consumption and personal interest is appended. The Holy Prophet (be peace of God upon him) on the occasion of the last 'Haj called 'Hujjatul Wida' prohibited commercial and trading interest and waived all interest due to Hadrat 'Abbaṣ from the Banu Thaḳif of Ta'if. This was substantially a large amount to be had out of the commercial transactions. The Banu Thaḳif were great capitalists and merchants and had not borrowed money due to their poverty to purchase food and clothes for their personal use.

This clarifies that interest of all types be commercial, consumption and personal loans is prohibited; so there is no scope of accepting interest from bank as share in the profit made by the banks.

It is a happy occasion to learn from some experts and specialists of modern banking system that interest is not something necessary and that economic system can do without it. We have ruled as Muslims for centuries, participated in business, agriculture and industry and our trade vessels have operated between the Mediterranean and Chinese seas and throughout we have organised our economic system without interest and managed it well.

The prohibition of interest has been ordained in the 2nd chapter of the Holy *Quran* five times in the following words: (1) Madness *Takhabbut*, (2) Thing God wants to destroy (*Mahq*), (3) Thing which deserves a war

(*Harb*) from God, (4) Thing which is anti-thesis of Faith (*Iman*) or is infidelity (*Kufr*), and (5) a Thing if persisted leads to Hell permanently (*Khulud fi'nmar*). Here interest is prohibited in strong words for all purposes and in all its forms.

Conceptually speaking interest on lending money and profit by investing money in trade have some resemblance, one suffers from risk and another from uncertainty, but *riba* (usury) is prohibited and *bai* (trade) is allowed in Islam.

Bai (trade) teaches just distribution of profit between two persons engaged in trade but the unjust division is in *riba* (usury). Justice demands that if two persons join to do a work, they must be similarly affected by both, the profit and the loss. It is inequitable otherwise. In the case of *riba*, if there is a profit, a nominal share is given to the capitalist who has contributed the money by depositing in the bank and the rest is appropriated by the other party (bank). And if there is a loss the man (party or bank) who has made the money available takes back his money and also the agreed fixed return, while the other man (borrower or enterpriser) sustains loss and loses even his capital in the case of heavy loss. In this case, it is injustice to the enterprising person. Therefore Islamic *shari'ah* permitted *bai* and prohibited *riba*. Besides in the case of *bai* the whole *millat* (nation) is benefited and her standard of living is raised but in *riba* the capital of the entire *millat* is appropriated by a few persons and the rich becomes richer and the poor, poorer.

As interest is prohibited in strong words for all purposes and in all its forms the system of banking which may be in consonance with Islam is the institution of *muḍaraba*, *qirad* or *muqarada* or *anan* which has been explained by theologians like al-Sarakhsi (d. 483 H/1090 A. D.), Marghinani (d.) and Ahmad b. Mughith al-Sadafi (d. Safar 459/Jan. 1067). This type of partnership business is allowed in Islam.

Imam Malik bin Anas asserts that the Quranic phrase *darb fi'l ard* (endeavour in the world) is sanctioned by the Prophet and recognised by the pious caliphs, 'Umar and 'Uthman, and practised by Hadrat Ayishah and 'Uthman²⁹.

This type of partnership business, one supplying money and another labour, is recognised by jurists like 'Alauddin Mas'ud al-Kasani, the author of *Bada'i al-Sana'i fi Tartib al-Shari'ah* and others. Ibn Rushd al-Qurtubi (d. Dec. 10, 1191) writes "And there is no difference of opinion among the Muslims about the legality of *qirad*. It was an institution in pre-Islamic period and Islam confirmed it. They all agree that its form is that a person gives to another person some capital that he uses it in

business. The user gets, according to conditions, some specified proportion of the profit may be one-fourth, one-third, or even one-half."²⁹

If the bank is run on the basis of partnership it will link the consumption and production and will stand a guarantee and security between the two and for this bank will have its own share in the profit or loss as the case may be. Thus there will be triangular relationship between depositor and bank, and borrower and through bank the lender and actual user of the fund or entrepreneur.

The banks may encash the bills of exchange receiving discounts as service charges. Discount at the rate of one *daniq* per dirham and one dirham or one-sixtieth dinar per dinar in the exchange of currency was allowed by the *Bayt al-Mal* under the Abbasids and charged by the Jewish bankers if the *suftajah* was encashed before the expiry of time (40 days) discussed above.

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NOTES

1. Ahmad Ali, *Al-Tanzimāt al-Ijtamā‘īyah wal Iqtisādīyāt fil Basrah*, Baghdad, 1953, pp. 250-1.
2. Quoted by the author in *The Economic History of Spain*, Dacca, 1963, pp. 297, n. 9.
3. *Al-Farooq*, p. 72; Syed Ayzada Hanafi, *Islam ka Iqtisadi Nizam*, p. 131 quoted by Siddiqi, p. 132, n. 2 & 3.
4. Quoted in the *Economic History of Spain*, p. 397, n. 1.
5. Cf. Author's paper on “Mosque as a Centre of Education”; Cf. S. M.” Imamuddin, *A Political History of the Muslims*, Vol. II, Pt. I, Dacca 1970, p. XVI.
6. *The Economic History of Spain*, p. 397.

7. *Ibid.*, p. 397, n. 4
8. Quoted by the author in the *Economic History of Spain*, p. 398, n. 3 & 4.
9. *Al-Masālik*, p. 15 quoted by Ahmad Ali, p. 254, n. 2.
10. Cf. Author's article "Bayt al-Mal and Banking" in *Islamic Culture*, Hyderabad, 1961, p. 18.
11. *Al-Mabsut*, Vol. XXII, Cairo, pp. 18, 71 quoted by Uzair, *Interest Free Banking*, Karachi, 1978, pp. 115-6.
12. *Hidāyah*, Vol. III, p. 241 quoted by Uzair, pp. 116-7, 205-6.
13. Quoted by author in *Economic History of Spain*, Dacca 1963, p. 293.
14. *Ibid.*, p. 294.
15. Cf. *Economic History of Spain*, pp. 295-96.
16. *Al-Nujūm al-Zāhira*, ed. T. G. Juynboll, Vol. II, p. 174.
17. Maqdisi (ed. de Goeje), p. 183.
18. Mez, p. 483.
19. Maqrizi, I, 424 quoted by Fischel, p. 72 & n. 1.
20. Mez, *Renaissance of Islam*, 471, n. 2
21. *Al-Andalus*, XIV, p. 454.
22. *Ibid.*, p. 453, n. 1
23. Al-Qumi, *Ta'rikh-i-Qum*, Tehran, 1353 H, p. 119 quoted by Duri, p. 161.
24. Fischel, pp. 75-6; Mez, 483; *The Economic History of Spain*, pp. 441 nos. 1 & 2.
25. *The Economic History of Spain*, p. 447, n. 1.
26. *Ibid.*, p. 441, n. 11.
27. Ibn Hawqal, pp. 42, 70 quoted by Mez, 476, n. 8.
28. Cf. Imam Malik, *Muwattah : Kitabul Qirad*.
29. Cf. *Bidayat al-Mujtahid wa Nihayat al-Muqtasid*, Cairo, 1389/1969, vol. II, p. 256 quoted by Uzair, p. 22, n. 6.