AN ENHANCED STRUCTURE OF TAWARRUQ AND RAHN: A WAY OUT OF CURRENT PROBLEMATIC STRUCTURE OF AR-RAHN PRODUCT

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Abstract

This work examines the challenges experienced by the institution on the principles of *sharī‘ah* with regards to product structure. It does not necessarily mean that the *sharī‘ah* principles that are applied with the existing product are wrongly casted, though it may happen, but this effort is to look for a better alternative. Therefore, it may avoid the need for total amendments that ultimately affects the reluctant costs borne by the institution. Consequently, the improved principles need to be reviewed from time to time, either by finding the best alternative or slight modification in the framework of the existing structure. By using discourse analysis, this paper aims to examine the current structure and to suggest the new structure of *ar-rahn* product that is constructed using the principle of *tawarruq* and *rahn*. Through this method, certain feature in the structure will be enhanced in order to suit the needs of the industry. While the structure was initially introduced by earlier researchers, the interviews adopted from the key players of the industry were crucial to be dicoursed and examined for better enhancement. As a result, the enhanced structure of *tawarruq* and *rahn* was suggested.

Keywords: *Tawarruq, Ar-rahn, Structure, Ar-Rahn Product*

INTRODUCTION

Although *ar-rahn* has vibrant evidences in *al-Qur'ān* and *Ḥadīth*, its application needs some adherence to the principles of *mu‘āmalat* that were outlined by the jurists through their consensus, analogy and debate. If the application does not provide a clear understanding towards the evidence, this would lead to the violation of Islamic objectives. For instance, the objective of *ar-rahn* is merely securing the debt issued by the creditor, and thus, any ill-intention of profit generation from the transaction will cause its objective to be inappropriate. One of the probable misleading structure in *ar-rahn* can be shown in the digram below:
In understanding the scholars’ view related to the appropriateness of *ujrah* that is based on *wadīʿah*, the basic concepts related to these two terms are to be described as above. The diagram describes the flow and the implication of *Ujrah-Wadīʿah*’s connection when it is applied through current *ar-rahn* product. The flow starts with the engagement of loan contract before an institution keeps the collateral under their custody. The safekeeping of collateral is applied based on the principle of *wadīʿah* where they impose a fee for the service that is rendered. This kind of fee is charged under the principle of *ujrah*. However, this connection gives rise to the indirect implications of *bayʿ wa salaf* and *qard jara manfaʿah*, that are prohibited in *sharīʿah*. In this regard, a deeper debate involving these two principles (*ujrah* and *wadīʿah*) is therefore explained and analyzed. The review on the application of *Sharīʿah* principles in the existing product structure is significantly important to identify its weaknesses, so that it may be improved. However, if it has fulfilled the Islamic principles, the application of the current structure may be continued.

**LITERATURE REVIEW**

The previous studies consistently agrees on the findings of unnecessary concept of *ujrah* to be embedded in *ar-rahn* contract, as Mohamad (2008) and Khir (2012) stated that *ar-rahn* is only served for securing the debts, and is not a method for generating the profits. In fact, Khir (2012) analyzed that the concept of *ujrah* is a part of sale contract under *bayʿ manfaʿah* (sale of usufruct) and thus, it is prohibited to be applied with the *qard* (loan) contract. This is understandable why the concept of *ujrah* is wrongly used in *ar-rahn* product, as there is a
hadīth that prohibits such practice. Meanwhile, Naim (2004) concluded that some practices adopted by the Islamic system are not truly in compliance with the teaching of the Islamic law. Naim (2004) also found that ar-rahn scheme still contains elements of usury in its transaction; hence Naim (2004) proposed a "good loan", which must be backed by the pawned item, and maintained that it is the responsibility of the government and the riches to prevent the public from continuously getting trapped in this financial system.

**METHODOLOGY**

According to Cook (1989), discourse can be defined as a stretch of language consisting of several sentences which are perceived as being related, not only in terms of ideas, but also in terms of the jobs that they perform. This paper adapts the discourse analysis technique as suggested by Cook (1989). With regards to this, the data from the existing structure, the classical text of Islamic jurisprudence and the interviews of the industry players will be reviewed in constituting a coherent unit. It allows the enhanced structure for not focusing only to the Shari'ah compliance, but also be suited to the industrial framework and policy. To comprehend how the interview session was conducted, it should be understood that not only the language used by the respondents, but the context is also to be given much attention. In this paper, the respondent’s words and statements will be analyzed based on his position and experience. The same approach will be repeated several times to different people. The process will then end up with a conclusion. The issue of ujrah that outlawed by the academician is then discussed among practitioners in the industry to get a balanced consideration. Finally, the existing problematic structure found in the institution's product, data derived from the opinions of Islamic jurists and the interviews conducted are then discussed together in considering the new structure.

![Figure 2 : Cook’s Discourse Analysis Flows on Ar-rahn Product Structure](image-url)
RESULTS AND DISCUSSION

The need for changes

In discussing the appropriateness of *ujrah* based on *wadīʿah yad ḍamānah*, which is currently applied by most *ar-rahn* institutions, there are two sects of scholars’ views. The first sect is the one that suggests the improvement of *ujrah* application, and the second sect is the one that opposes such improvement as they would rather prefer to replace it. Generally, the sects of scholars that support the application of *ujrah* application to be improved are the scholars from the *sharīʿah* division or department from respective financial institutions, particularly the banking institution. They supported such effort as they believed that the total rejection of *ar-rahn* scheme that using the principle of *wadīʿah* is impractical. They suggested that the structure does not need to be replaced, but enhanced. It is as shown as below:

"The existing *sharīʿah* structure of *ar-rahn* is still acceptable as the structure is widely accepted among the players in the Islamic banking and cooperative institution that conducts *ar-rahn* scheme. If the structure fails to suit the requirement of *sharīʿah* compliance, the *Sharīʿah* committee of the institution has to stop the operation of the product immediately".

(Hamid, H. A, personal communication, June 21, 2013)

Meanwhile, it also supported by the statement that the terminology of the contract was not really an issue as it is shown as below:

"The term *ujrah* leads to a controversial issue among the Islamic researchers as it is not really the case, and that he concerns more on the substance. If the imposition of *ujrah* fee in *ar-rahn* contract is considered inappropriate, another term can be suggested."

(Chik, M. N, personal communication, May 24, 2013)

However, Chik (2013) did not mention the appropriate terms that should be adopted to replace the term of *ujrah*, or otherwise it shall fulfill certain requirement such as the details of job scope as it is mentioned:

"The cost of holding the collateral by the institution must be written in details so that a safekeeping fee (*ujrah*) imposed upon the item can be justified"

(Borhan, J. T, personal communication, May 8, 2013)

The detail of the *ujrah* job scope is also suggested by introducing the size of the storage box. It mentioned:

"The storage box of collateral can be categorized into several classifications such as small, medium or big size."

(Masri, M. F, personal communication, June 13, 2013)
However, these types of charges can only be imposed on three types of fees, and such practice appears unattractive for the institution, despite the fact that it has been implemented in the Middle East countries.

Meanwhile, the second sect is the opponents of the *ujrah* application. The scholars of this sect are mainly the academicians and researchers, who see it as misleading the *shari‘ah* principle in the contract. The criticisms over this concept have been widely discussed and written. Mohamad (2008) and Khir (2012) consistently agreed about the findings in their research in 2008 and 2012 are still valid about the unnecessary concept of *ujrah* to be embedded in *ar-rahn* contract, as they stated that *ar-rahn* is only served for securing the debt, and is not a method for generating the profits. It mentioned:

"The concept of *ujrah* is a part of sale contract under *bay‘ manfa‘ah* (sale of usufruct) and thus, it is prohibited to be applied with the *qard* (loan) contract."

(Khir, M. F. A, personal communication, May 22, 2013)

It is understandable that the concept of *ujrah* is claimed to be wrongly used in *ar-rahn* product, as there is a *hadith* that prohibits such practice.

"Do not allow a loan (in combination with) and a sale, do not have prerequisites to sell, do not gain a profit if it is guaranteed, and do not sell what you do not have”

(Sunnan Abī Dawūd, n.d.)

In addition, Khir (2013) also argued:

"The safekeeping fee imposed by the institution exceeds the reasonable rate of that safe deposit box, hence it corroborates the presence of *ribā* elements"

(Khir, M. F. A, personal communication, May 22, 2013)

This higher rate of fee can be seen through the calculation of annual fee against the loan that is given at 13% in banking institutions, and 11.9% as the average charge in a whole *ar-rahn* shop owned by the cooperative societies. Even though the rate seems higher, the product is widely engaged by the small middle income group, and makes it relatively expensive for them.

Khir (2013) also stressed:

"Because the product has unique and attractive elements such as a quick approval, rollover functionality, and a guarantee of getting back the pawned jewelry, the situation however reveals the real motives of customers who are willing to pay more on safekeeping fees than they really should, and that they subscribe to *ar-rahn* scheme merely for the purpose of obtaining the financing facility."

(Khir, M. F. A, personal communication, May 22, 2013)
These two contradicting views can simply be understood as their points of differences. Both come from a different circumstantial ground and thus, affluence their perspectives on ar-rahn scheme to differ from one another. The scholars who supported the improving efforts are more indulgent in placing the juristic analysis of a transaction, while the others are firmer in their stance. In case of this issue, the scholars from the industrial background who are directly involved in the operation are unwilling to eradicate the entire principles used and replace them with the sale contracts. In the financial institutions, particularly from a banking point of view, the complete amendment from a loan that is backed by collateral to a sale contract will distress their main activities, such as the operational system, the risks’ management, and the costs of operation. Though not impossible to implement, the unnecessary contract of wadi‘ah, as what some scholars have claimed, has yet to reach a level where the authority is agreeable on stopping their product’s operation.

In addition, the claim on the indirect connection between the safekeeping fee (ujrah) and the loan amount is somehow established in industries for quite a long time; the situation is always being analogized to an issue of the sale’s arrangement contract through the method of tawarruq and ‘inah. As the principle of tawarruq and ‘inah is still permissible in the financing products of Islamic financial institutions, a claim of the indirect connection between ujrah and qardh cannot be considered as a form of prohibited contract, hence, a total rejection is not a priority issue for ar-rahn product. Unless a solid alternative for the current mechanism of tawarruq through Šūq al-Sila‘ could be sought, any further ideas will bring about the irrelevant pace in the perspective of the industries.

Accordingly, several proposals have been considered to improve the existing concept and researcher has finally proposed several improvements in some areas through the implementation of combining the concepts of ar-rahn and tawarruq. The concept was once revealed by Khir (2012) as it can free itself from the element of riba and thus, the operators are freed from the issue of determining the profit rate. However, several adjustments have been made to suit the requirements of the banking institutions and the needs of customers.

Sharī‘ah improvement

This paper proposes the Sharī‘ah improvement that replaces the existing concept that has an issue on riba. With regards to this, the principle of tawarruq is proposed to be adopted by ar-rahn institutions. A tawarruq can be defined as purchasing an asset with deferred price,
either based on *musāwamah* or *murābaḥah*, then selling it to a third party to obtain cash. (BNM, 2010:224) Based on analysis that was made on the arguments of both sides, the best option is to change the structure of *qard - wadī‘ah - rahn* to *tawarruq – rahn*, if the amount of financing is more than RM50,000. The flow of structure can be shown based on the following figure:

![Diagram of the suggested structure](image)

**Figure 3: A suggested structure: An enhanced structure of *tawarruq* and *rahn***

1. At the first stage, the customer approaches the institution for cash financing. The institution then assesses customer's ability of engaging in such contract. This stage is practically critical because most *ar-rahn* institutions do not assess customer's credit ability in repaying the debt. The absence of customer's credit assessment is a great turning point for the success of this suggested structure. Thus, a quick exemption or very minimal assessment is mandatory.

2. The institution buys a commodity from Broker A; normally, this process of buying a commodity is done through *Sūq al-Sila‘* or Commodity *Murābaḥah* House. This trading platform that uses commodity such as crude palm oil as the underlying commodity is introduced by Bursa Malaysia in 2009 to facilitate Islamic financial transactions, particularly the application of commodity *murābaḥah* which is based on the principle of *tawarruq*. Usually, this process will include buying and selling transactions in ten minutes, since it is applied through the system in the computer (Johari, M. S. M, personal communication, June 26, 2013).
3. The institution sells the commodity to the customer at a mark-up price, and the customer pays the price in deferred payment basis, based on six months or above according to agreed terms and conditions of the contract.

4. The customer's jewelry is pawned to the bank based on rahn contract in lieu of a debt, which he/she pays in the deferred time.

5. The customer appoints the institution as his/her agent to sell the commodity to a third party to get cash. This process is also conducted through the mechanism of Sūq al-Sila’, or Commodity Murābahah House. Once again, at this stage, the institution must find a way for the exemption of wakālah fee that is resulted from the appointment of bank as the customer's agent. This fee may discourage the customers as the institution is already making a profit from the marked-up price.

6. As an agent, the institution sells the commodity to the third party, who is known as broker B. But this time, the selling price is based on the current market price. This makes a difference on what the customer should pay to the institution.

7. The difference that creates the cash will then be given directly to the customer, or credited into the customer's account depending on the agreed financing.

This structure suggestively allows the institution to generate legitimate profit, as it does not involve qard as the underlying contract for profit generating and thus avoiding the unnecessary embedded principle of ujrah.

CONCLUSION

In conclusion, this structure has manifested gains over other structures that have been earlier debated. The use of rahn in this structure consistently meets the purpose for which the rahn contract was constituted by the Sharī‘ah, i.e. as an assurance contract. In this structure, profit generation is placed appropriately, which is a trading contract, while ar-rahn remains a trust-based security contract. Thus, this structure does not try to employ rahn for a purpose that contravenes the very nature of the rahn contract, and its objectiveness. As a result, this structure is ultimately safe from the prohibited elements of bay’ wa salaf or qard jarra manfa’ah, which regularly arise from the structures such as that of ijārah (additional exchange contracts), and ar-rahn contract. In addition, there is no conflict of muqtaḍa al-‘aqd
between *wadī’ah* and *rahn*. This structure significantly enables the bank to generate a legitimate profit, since it does not involve *qard* as the underlying contract for profit generating. In fact, the profit is purely generated from a marked-up sale via *tawarruq* arrangement that the parties enter into.

**REFERENCES**


