

Discussions /Dialogues – Islamic Economic Forum  
Topic: Commodity Murabaha  
Compiled by: M. Khalid Hasani  
Date: 10/15/2016

Summary of the Discussions on  
Commodity Murabaha held in  
Islamic Economic Forum  
Started on 15<sup>th</sup> Oct, 2016

Brief Introduction of Islamic Economic Forum:

The Group with title of “Islamic Economic Forum” is for Islamic Economic Professionals – Sharia Scholars, Economists, Professors/Researchers and IF Practitioners for the purpose of positive discussions on various issues and challenges, facing the Islamic Economic Industry in order to explore ideas and solutions, pertaining to Islamic Economic from an economic as well as Sharia perspective. Since there are already various forums devoted to Islamic Economic, this forum is expected to have more emphasis on critical analysis as well as to make ensure you're up to date with the latest market movements, analysis, and research. The ideas generated will be for the benefit of the Islamic Economic Industry globally.

Administrative Committee of the Forum:

Dr. Abdul Bari Mashal (Head of Committee)

Dr. M. Burhan Arbouna

Sheikh Ashraf Gomma Ali

Dr. Yousuf Azim Siddiqi

Dr. M. Iman Sastra

Sheikh Ibrahim Musa Tijani

M. Khalid Hasani (Founder of the Forum)

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Preface: The discussion on the topic “Commodity Murabaha” initiated by Ahmed Ali Siddiqi

What is Commodity Murabaha?

Commodity Murabaha (CM) is a product to facilitate cash advances and liquidity management. In this transaction one person /party sell the commodities to second person /party on deferred payment basis. Subsequently the second party sells those commodities on spot basis to receive cash.

Without dealing with Riba (which is strictly prohibited by Shariah), Commodity Murabaha /Tawarruq is so far the permissible option to facilitate the bank’s liquidity management as well as to assist individuals in obtaining cash via trading of commodity.

Ahmed Ali Siddiqui: Assalam o Alaikum Dear Respected Members I would like to hear views about following:

Can we issue a Ijarah based Sukuk say on a Highway where the road is under a BOT /concessional agreement for say 10 years to a company. Now Govt issued a Sukuk based on Ijarah on this Motorway without canceling the BOT arrangement. Is there any Shariah issue as the highway is sold and taken back on lease in the international market? Secondly what would be the Status of the Sukuk if the Govt, Advising banks and Legal council remain silent on this BOT arrangement ?

Another query on Commodity Murabaha transaction, which platform is better for it LME Brokers, Souq al Sila or Dubai one ?

Mufti Irshad Ahmed Aijaz: I think it depends on nature of consession agreement. If it is mere a grant or permission to use government's land then this would not mean a contract for sale/ contract of transfer of ownership. Also, if it has novation clause then novation is also possible.

Ahmed Ali Siddiqui: If the contract is of BOT nature where the govt has asked the Company to upgrade the road and make some bridges etc and as a compensation you of this BOT you have the right to collect toll for next 10-15 years.

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Sheikh Ashraf Gomma Ali: Souk al sila hands down, in my opinion. I have studied the documentation of all of the provided (LME / bursa Malaysia / dmcc). All are good but it is clear that the sharia governance of bursa is far beyond everyone else. Although some of the UK brokers may be able to offer better technical solutions such as STP (for a fee of course). They may also be able to handle larger volumes than bursa. As far as cost, I believe that all of them have competitive costs. Biltowfiq.

Ahmed Ali Siddiqui: Jazakallah for the reply. Also I need some thoughts when we buy commodity from one broker A on spot and sell to Customer on Credit and then Customer sells to Broker B on spot. The broker A gives the amount to Broker B (some say as a loan and some say that the Broker B sells something of same amount). This inter Broker deals - Is it Ok or is it a buy back thing among brokers

Ashraf Gomma Ali: When the bank buys from broker a, it receives a holding certificate evidencing its ownership of the commodities. Then the bank sells to its customer on credit. The broker system generates a holding certificate to evidence this transaction and to show the bank's customer as the legal owner (with the bank acting as the customer's agent). Finally, the customer sells to broker b with proper offer and acceptance with reference to holding certificate number. All of the ownership transfers are legally binding and the contacts all ensure that the goods are owned by the seller and are not pledged to any other parties. Of course, all of this should be subject to regular sharia audits and under the supervision of a sharia board. There is no loan between broker a and b. There is be an arrangement between broker a and it's supplier which broker b may be a party to ask well, but this does not affect the bank's relationship with the brokers as long as broker a owns the commodities that it sells to the bank. (And Allah knows best)

Habib Mohtashim: What's the interest of broker B undertaking to buy commodities from bank's customer for the same price on which bank has purchased from broker A even though commodity market fluctuates quickly....?

And has it ever been sold to a third party (other than broker B) so we can see the validity?

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In DMCC, it's confirmed by the organizers that commodity usually goes back to the first owner after customer sold to a third party from which d first owner buys back..

Ahmed Ali Siddiqui: What I understand that in some cases the commodity is bought back from Broker B by Broker A. But since these broker are not operating in a Shariah complaint manner so the scholars may have considered to remain silent on this leg as this is out of the scope of Commodity Murabaha but a separate arrangement between brokers

Dr. Humayon Dar: From broker's viewpoint it makes better sense to facilitate a commodity Murabaha transaction by itself (i.e., a one-broker facilitated commodity Murabaha). However, on the insistence of many Shari'a boards two-broker facilitate commodity Murabaha is preferred, which in many cases is done through an undisclosed agency between the two brokers. For example, brokers B owns the commodity to start with and appoints Broker A to sell it on its behalf. The Bank 1 buys the commodity from Bank A on spot and appoints it to sell the same commodity to Bank 2 through its agent Broker B. So There is no movement of commodity at all. The commodity remains in the possession of Broker B throughout. Answer to the question above. What is the incentive for Broker B? Both Broker A and B benefit from the agency fees that are contributed by the participating banks.

Ahmed Ali Siddiqui: Shukran Dr Dar, but does this creates a buy back issue if Broker B owns the commodity from the start.

Dr. M. Masum Billa: If it's formalised in a single agreement, does this not involve the element of "Buy al-Ina' (buy back sale)? For the validity, it's recommended that, the deal shall be formalised in 2 different agreement, so to avoid buy al-ina'. Allah (swt) knows the best

Sheikh Ashraf Gomma Ali: Personally, when I do due diligence on brokers to decide to deal with them I put a condition that there is no common ownership between broker a and broker b, to ensure there is no ina. Also, broker a represents that he owns the commodities therefore if he is acting as agent for broker b, this would be misrepresentation. I don't believe this is the case.

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Habib Mohtashim: When I discussed with one of the brokers and asked about the relationship they have with another broker, they clearly confessed that broker A shares the fee (which broker A charges to the buying bank) with broker B. That's how they have set up the process.

Siraj Yasini: I agree with Sheikh Ashraf. At least in case where I was involved, Broker A represents that it owns the commodity. If Broker B owns the commodity from inception and Broker A acts as agent of Broker B (as Prof. Dar described), in cases I worked on, it will be a misrepresentation by Broker A.

Separately, I have seen a case where only one broker has been used. The logic behind selling back to the same broker was that it is allowed because documentation does not stipulation to sell back to the same broker.

Ahmed Ali Siddiqui: So do most scholars agree this way

Siraj Yasini: Ok. And I ensured to read the documentation which was not stipulating to sell back to the broker.

Ahmed Ali Siddiqui: Reference to the Commodity Murabaha discussion, what are the views of majority of the Shariah Scholars where if the Commodity is going back in almost majority or may be in all cases to the same seller (although not stipulated in the agreements) and it is a public knowledge that no buying bank or client has an intention of taking delivery in any case (true for 99.9% cases). So can we ignore these facts or despite of this we can say that these does not impact the transaction because these are not serious violations or not even a violation at all.

Can we also say that although commodity is going back to same seller but as it is happening at the same price at which Seller One has started the sale. Hence although implicitly agreed but this is not buy back or Innah due to no increase is paid the seller one in the end sale and also due to it being spot. So no Innah in Spot and also no Innah at the same price. So it is allowed Would appreciate some thoughts and guidance on above from the respected members

Almir Collan: Reality of these commodity murabaha transactions is that we have 1 piece of metal that is sold and resold millions of times without ever becoming anything. Only economic

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output of these fictional sales activities is creation of cash loans at profit. This can lead to our own bubble economy that has nothing to do with real economy. Even if banks don't have any other way of doing anything about it - we should not be blind to think this is actual financing. This is just normal borrowing and lending but dressed as trade financing. I have raised this here many times and frankly I am bit concerned that much of transactions in our industry are slowly losing the spirits of Islamic finance and with that link with real economic activities that actually provide real benefit to society.

Result of commodity murabaha is that metal is doing nothing and never leaving warehouse. We have end result where customer ends up with cash in pocket and higher debt as a result of this transaction - what happens with commodity ? Nothing. Nobody needs it. It goes back to warehouse to create another loan.

End result is 0 economic activity and creation of a cash loan for party involved. Exactly what Islam wants to prohibit ie commercialisation of loans.

Dr. Humayon Dar: I tend to take a similar view on commodity Murabaha as Almir Colan. This is one of the weakest products on the menu of Shari'a compliant products. Commodity Murabaha transactions in the whole wide world have similar problems, whether in Malaysia, Dubai or London. In countries where there has been historic resistance to commodity Murabaha, it is fast creeping into the practice and the irony is that this is being intellectually fed by those who have argued against it previously. We had to live with this " bride" of Islamic banking and finance because we couldn't come up with a better one, and I think it is the time that we give it the status of a respected first wife and bring a new bride. 35 years is a long time! This is a good discussion point and we should analyse this product with open heart and try to suggest something that is more practical and of course more beautiful. As a teacher of Islamic banking and finance, I always find a strange taste in my mouth when covering commodity Murabaha, especially in front of non-Muslim students whose unspoken sarcasm stabs my body language when explaining commodity Murabaha.

Almir Collan: I understand they (Bursa) are trying to make it better in terms of taking ownership, at least in theory. Reality is however that people who engage in these transaction are not commodity traders but liquidity seekers. And this should not be seen as financing and

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profit making arrangement as it creates cash & debt with same person. On the other hand I understand that if there is emergency for bank I understand why some might see it as necessary to go for it when there is specific need (although even for this purpose banks they could create emergency pool between them for liquidity purposes that they share that is used as qard hasan between them on basis similar to takaful and/or waqf). But it is far from desirable transaction.

Siraj Yasini: @almir, this is more a discussion about the commercial banking model rather than a particular banking instrument. The impact that a commodity Murabaha has is the same impact an Ijara, Salam, or even Musharaka and Mudaraba based banking instruments have. The outcome of all is meant to be debt instruments in a commercial bank model. As long as a bank is an intermediary to borrow and lend in the current regulatory environment , the economic impact will remain the same. You need to focus more on an alternative banking or even an economic model to achieve different results.

Almir Colin: Difference is one where with other transactions financed assets end up being used... goal is not to get cash loan... when goal is to purchase asset it is much different transaction even if sometimes transaction itself is not fully as we wish in terms of movement of asset ( this excludes buy and sale/lease back transactions that also only create loans as commodity murabaha)

Siraj Yasini: The fact is that commodity Murabaha is not only used for cash financing. It is used for financing services, goods, and assets as well. Circumstances or customer/bank position may not allow to do other types of transactions; they end up with commodity Murabaha. Commodity Murabaha is not an even after all. It is a wonderful solution in many cases.

I therefore believe your argument of cash and debt accumulation is more a debate related to the banking model, not a particular banking instrument.

Almir Collan: You did not understand my point. I am not talking what they use cash for but that end result is cash loan. It is symthetic financing to create loan and charge profit from that loan.

Siraj Yasini: How is it different than other Islamic banking instruments? All end up with obligation to pay principle + profit.

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Almir Colin: One is profit from real sale of asset that ends up being used in real life eg customer actually buys or leases home or machine. Other one, asset is only used on paper to get cash loan. Islam does not want to see profit from cash loans but economic and genuine sale only. Hence difference between sale and riba.

So always question is what are we doing? Financing and buying things or giving cash loans?

Dr. Humayon Dar: I shall not like to use a strong language to call commodity Murabaha and even bai' al-ina as riba, as they are Shari'a approved concepts. These remain Shari'a compliant products. However, we have to come up with better products to replace these seemingly weak links in value proposition of Islamic banking and finance.

Siraj Yasini: @Almir, Commodity Murabaha fulfills that requirement. Profit derives from sale, not from cash. Your argument was economic output, now you drag it towards Shariah authenticity. According to all Fiqhi Institutions and scholars I know, Tawarruq is an acceptable method (They may vary on execution).

@Prof.Dar, we so far were discussing economic output. I agree with you on Shariah authenticity. It is fully Shariah compliant. If we are not happy with the economic output (which in my view is a valid point), I suggest we come up with alternative banking model or focus more on investment banking/private equity model for Islamic banking.

Dr. Humayon Dar: Honestly, it is not just about economic output rather it is about a mindset. Islamic bankers and their hawariyyoon (I am being one of them) have failed to come out of a "money management mode" although they talk about trading. They need to switch from money management to actual trading. Islamic banking on many fronts have failed to switch to a "trading mode". Islamic bankers offer their customers panini but try to convince them that it is biryani. While pressed by my desire to eat any thing, I am OK with eating panini in the name of biryani but there are people who would like to insist on calling something what it is actually. Commodity Murabaha is definitely a panini and I would like to eat it as such.

Dr. Yousuf Azim Siddiqui: If we compare In'ah and Tawarruq sale so it's evident that lack of contractual liberty makes any sale transaction either a synthetic one or a real one.

Although most of the Sharia scholars agree on Shares Tawarruq where the customer takes complete risk of identified assets and has the right to hold or sell them, the same is lacking in most of the Commodity Murabaha solutions where forceful liquidation and exclusive agency are integral parts of the structure.

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In case the Murabaha buyer holds the commodity then the loop isn't closed and entire transaction falls apart.

This besides suspicion of existence of physical commodities in such large quantities. Sharia audits on intervals do not serve the purpose of Sharia accuracy. Also these trades are happening in OTC and not in LME.

Almir Colin: Best structure is to use different method to solve liquidity problem... eg banks create fund for all of them based on idea similar to takaful or Waqf basis where purpose of fund is to give qard loans without charging if anyone needs it, and then return in the fund... mutually helping each other and sharing resource like in taqaful insurance concept... rest can be negotiated

Siraj Yasini: I like the ideas about alternatives. I echo Prof. Dar suggestion to write about it. It will enable us to see how practical it is and how it could be improved further.

IKRAM THOWFEEK: Prof. Dar and Almir great discussions nailing it down. If we don't change or move from this product soon we will replace loans in conventional banks to Tawarruk/commodity Murabaha (to get cash) for all your financing needs. Then IFIs can shelve the other products.

Yerlan A. Bidaulet: Dear Br. Ikram, you wrote: "we will replace loans in conventional loans..." Whom do you mean here? How do you see this process of replacement? Could we influence any conventional institution?

How could we move from this most popular product in current Islamic banking practice (more than 80% among other IB products)? Just discussions cannot help. Here we should jointly come to more effective models and help the industry. We should push collective bodies like AAAOIFI or IFSB.

\*instead of "loans" put "banks" (as written in original text)

Ahmed Ali Siddiqui : Dear Dr Dar why only for Pakistan and why not for the rest of the world? If it allowed then we need to do it correctly and if not then first the name of the all the banks and markets needs to be highlighted that are doing it wrongly. (In terms of practice).

IKRAM THOWFEEK: What I meant you captured brother. More than 80% or majority of it on commodity murabaha/Tawarruk and will not have any impact if we continue with this product but have to move to Products that impacts individuals, corporates and economy at large.

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Dr. Humayon Dar: @Ahmed Ali Siddiqui Pakistan shouldn't be forgiven for adopting Commodity Murabaha because the scholars in Pakistan have had an attitude of "Commodity Murabaha in Pakistan? On our dead body." While we have accepted and used commodity Murabaha in other parts of the world, the Muslim communities have never felt comfortable with it. Pakistan shouldn't be entrapped. In Pakistan and elsewhere, there is a need to develop an alternative model of Islamic banking and finance, which shouldn't develop Islamic banks as mere deposit collection boxes to invest in government securities and investing in products similar to commodity Murabaha.

Ahmed Ali Siddiqui : I understand the objection is always on the process/implementation and also when using it without necessity in all areas.

Dr. Humayon Dar: The necessity of using CM all over the world is to earn some bps on un-utilised money by banks. "It is like I have no use of this money but I still want to earn some return on it, so let me "lend" it to someone." Is this a dhururah?

Ahmed Ali Siddiqui: Dear Dr Dar there are other usages as well like

- 1) Govt want to pay off its interest based debt and does not have assets available for Sukuk issuance and still wants to raise Islamic financing
- 2) A company working in a service sector needs to convert its entire balance sheet from Riba based lending to Islamic and no other options seems workable to them
- 3) Central bank wants to extend financing at a fixed concessional rates for promotion of export to the clients and for agriculture sector but does not want to take risk of asset or business like in lease or Musharakah and customer wants only Islamic mode of financing.

And many others where it is not to only for liquidity

Khalid Hasani: Commodity Murabaha /Tawarruq is so far permissible option to facilitate the bank's liquidity management as well as to assist individual in obtaining cash via trading of commodity and fulfilling the economic need under Sharia.

Sharia scholars have to follow Sharia streamline

We should also do not ignore the fact if the huge liquidity kept uninvested, what would be the end result

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@dr. Dar This question arise only if the sharia scholars allow impermissible solution while in the said case, they never allowed an impermissible transaction

Tawarruq is permissible in all four thought of Islamic fiqh

Even imam abu yusuf ra said,

العينة جائزة مأجور من عمل بها

While the contemporary scholars allow tawarruq not inah

the view, I stated earlier regarding Tawarruq /Commodity Murabaha, was the consensus among the four schools of thought /Madhahib.

And Our Malaysian brother's view on Einah is based on Shawafi' Madhhab, as they are followers of Imam Shaafi RA, and according to Shaawafi, not only Tawarruq is permissible but Einah too.

However BNM does not promote any new product using al-inah..

industry has moved to tawarruq for new products since 2013, however still have some inah assets related to home financing.

I Guess some senior members despite not capable in fiqh, but rather than economic perspective. They touch the sensitive issue which is debatable among sharia scholars. And mixing between economic perspective and sharia perspective. They should understand that

not adding value from economic point of view, is not sharia compliance

Ahmed Ali Siddiqui: The issue of CM is not in the concept but sometime from its implementation.