THE APPLICATION OF *HAWALAH* IN MODERN TRANSACTIONS

Submitted to:
PROF. DR. ZIA-UL-HAQ
DR. OBAIDULLAH KHAN

Submitted by:
ASIF RAZA
Reg # 9-FSL/LLMICL/F07

FACULTY OF SHARIAH & LAW

INTERNATIONAL ISLAMIC UNIVERSITY, ISLAMABAD

M. Shil
M.d

1. Finance - Religious aspects - Islam.

Acceptance

By the Viva-Voce Committee

Title: The Application of *Hawalah* in Modern Transactions

Name: Asif Raza

Reg No# 9FSL/LLMICL/F07

Supervisors:

Prof.Dr.Zia-ul-Haq

Dr.Obaidullah Khan

External Examinor:

Maulana Muhammad Zahid

Internal Examinor:

Prof.Dr. Muhammd Tahir Mansoori

Table of Contents

Dedicated

to my elder brothers

who always remained to me very kind

and inculcated in me the spirit of long learning.

Acknowledgment

First of all I must thank Allah Almighty that I have been blessed to complete this thesis. I am grateful to the faculty of *Shari'ah* and Law which gave me the opportunity to complete my higher studies. I must appreciate my worthy teachers Prof. Imran Ahsan Nyazee and Prof. Dr. Tahir Mansoori, who helped me while choosing this study for LLM research thesis. They are great for me as encouraged me and gave me moral support. I am thankful to my worthy supervisors, the Honorable Prof. Dr. Ziaul Haq (Dean of the faculty of *Shari'ah* and Law IIUI) and Prof. Dr. Obaidurehman. They have great honor for me as they who took the responsibility of the supervision of the study and guided me in a proper way of research. They are also respectable for me for the reason that they always gave me moral support. They gave me great moral and academic support during the studies. I must not forget the help and cooperation of my elder brother Dr. Khurshid Iqbal (Additional District & Sessions Judge), whose guidance inculcated in me the spirit to do research. He supported me both morally and financially while completing the current study. I must mention the support and help of two of my class fellows Muhammad Israr and Gohar Ali. They helped me while discussing different issues related to my thesis. Their criticism on my arguments during discussions proved helpful in my study.

ASIF RAZA

Summary

The underlying objective of this study is to see whether the doctrine of *hawalah* is applied in real sense in different transactions and laws. The study describes the jurisprudence of the doctrine of *hawalah* which was given by the classical Islamic Jurists. It proceeds further to critically analyze *hawalah* based transactions and the related laws in the domain of its basic jurisprudence. It traces back the doctrine of *hawalah* to the early history of Islamic law. Historically speaking, the concept was used for the first time by Muslim trades in the form of *Suftaja* (bill of exchange) during their trades. It was used in order to avoid risks of way and carrying huge and heavy currencies from one place to another. As *hawalah* stands for transfer of debt liability, it is therefore, required that the element of debt must be there. Debt is only created when some commercial activity takes place which involve some real assets and material goods.

The study looks the legal framework by taking different sets of laws based upon the doctrine of *hawalah*. While examining the legal status of *hawalah* it is argued that different sets of laws are equated to the doctrine of *hawalah* on the principle of analogy. It is to argue that different laws are subjected to be deleted others to be amended and some to be added with explanations. One set of laws i.e. constituted by *al-Majallah al Ahkam al-Adalia,* is worth of appreciation and worth of appropriation to its basic jurisprudence.

It further argues that both the transactions and laws based upon the doctrine of *hawalah* suffer the element of interest (*Riba*). They violate other rules of Islamic commercial law as well. The argument is supported by the fact that the two distinct concepts viz., debt and loan are dealt with one and same yardstick while applying in *hawalah* based transactions and laws. The study focuses on this very point during analysis. It also takes the general principles of Islamic commercial law as well. It critically examines that any kind of transaction to be based upon the doctrine of *hawalah*, should be applied in strict inclination to its jurisprudence, given by the classical Islamic Jurist. The study discusses that *hawalah* can not be used exclusively for commercial purposes. It can, rather, be used as for the facilitation of the commercial activities.

INTRODUCTORY CHAPTER

1. Introduction and Significance

Hawalah is one of a well-known doctrine in Islamic commercial law. It is a contract through which the liability of payment of a debt is transferred by a debtor to a third person against his creditor. It provides basis for many commercial transactions, such as *hundi* (bill of exchange), negotiable instrument and bank cheques. As a concept of classical Islamic law, *hawalah* has been of great importance in trade and commerce since the early age of Islam.[1] As Islamic jurisprudence developed with the passage of time, *hawalah* received considerable attention of the early Muslim *fuqaha* (jurists).[2] Hawalah is applied in different modern transactions on the theory of permissibility and necessity.[3] In addition to jurisprudential questions, *hawalah* has also become a controversial commercial practice since 9/11 as the United States (US) government suspected its use as a tool of transfer of money for financing terrorism.[4] While such a suspicion has not been confirmed

---

[1] For a *hawala* transaction during the early years of Islam, Ibn Zubayr, a companion of the Holy Prophet Muhammad (May God's blessings be upon him), used to take money from some persons in Mecca and would give them a letter addressed to Mus'ab ibn Zubayar in Iraq, instructing him to pay that money to those persons in Iraq. It may be mentioned here that during the early days of Islam, *hawala* was not used a legally recognized tool of commercial transaction. It was a trade method.

[2] Al- Kasani, *Bida'i' al-Sana'i' fi Tartib al-Shara'i'*, Karachi, Education Press, 1979, p.15.

[3] Muhammad Tahir Mansoori, *Islamic Law of Contracts and Business Transactions*, Islamabad, Shariah Academy International Islamic University, 2nd Edition. 2004. p. 314.

[4] Edwina A. Thompson, *'Misplaced Blame: Islam, Terrorism and the Origins of Hawala'* in A. von Bogdandy and R. Wolfrum (Ed.), *Max Planck Year Book of United Nations Law*, Vol. 11, 2007, pp 279-305. BBC, 08 Nov., 2001. Available at http://news.bbc.co.uk/2/hi/business/1643995.stm (Last accessed: 01 Sept., 2009). In 2001, the US launched a campaign to blacklist *hawalah* companies. Part of that campaign, Al-Barakt, a Somali hawala company was blacklisted and its assets were frozen. It was in 2006, the said company was struck off the list of the blacklisted companies. See details at BBC, 28 August, 2006. Available at http://news.bbc.co.uk/2/hi/business/1643995.stm (Last accessed: 01 Sept., 2009).

by the 9/11 Commission,[5] the apprehension still persists. Thus it appears that there is a potential need of research on such an important concept of Islamic Commercial Law.

Hawalah can be traced back to an era prior to Islam. The concept was found in Europe and India in the form of credit instruments and hundi respectively. However, it got a proper jurisprudential status when it was introduced by Islamic law. It provided basis for many other contracts like *Salam* and Credit sales. Muslim traders were using instruments in their credit sales in order to avoid risks of way and carrying cash money. In other words, Islamic law gave an encouragement to traders for continuing their commercial activities irrespective of taking risks of way or carrying cash payments. It was due to its importance in trades that laws regarding *hawalah* were made in *Majallah* in order to give a legal protection to the doctrine of *hawalah*. However, after colonization the practice of *hawalah* was based upon a new law i.e., the Negotiable Instruments Act, 1881. The similarity was based upon the doctrine of analogy of Islamic law. However, the principles of *hawalah* were not followed in the true sense. It was also wrongly criticized after 9/11 for holding responsible for the promotion of terrorism. The Audit and Accounting Organizations for Islamic Financial Institutions (AAOIFI) also included *hawalah* in it *Shari'ah* Standard No 7.

The study has a great significance. It can be said that the concept of Islamic banking emerged as a new concept in the contemporary banking system. Most of the products, practiced in Islamic banks are considered as permissible (*halal*). Most of the transactions are justified as Islamic on the rule of permissibility in (*mua'milaat*). However, the rule is subject to the condition that the basic principles of Islamic law should not be violated. The doctrine of *Hawalah* has a distinct jurisprudence in Islamic commercial law.

---

[5] 9/11 Commission Final Report.

It was justified in order to facilitate the traders in avoiding the risk of way and carrying large amount of money in the form of cash. Instead, instruments had to perform the purpose of cash. It was, however, allowed subject to the condition that some credit sale must have occurred between the traders.

2. Background and Statement of the Research Problem

This study seeks to focus on the questions surrounding the application of *hawalah* in modern transactions. The question of this study is that whether different transactions based upon the doctrine of *hawalah*; follow the doctrine in the real sense. The significance of this question is that if *hawalah* is the transfer of loan rather than the transfer of debt, it will amount to interest (*riba*), which is, strictly forbidden in Islam. The study argues that *hawalah* is a transfer of debt and the rules relating to the creation of debt must be followed. The principle rule of the creation of debt, the study argues, is that a credit sale is a must. The credit sale here means a kind of sale in which (*ajal*) a period has been fixed. Loan means to give some cash money to a needy person, while debt is a credit sale in which the price is deferred.[6] The study seeks to answer the question from the perspective of finding the element of debt in the current practice of *hawalah* in different transactions. It will critically analyze those transactions from the perspective of the general principles of Islamic commercial law. The study will further look the legal frame work regarding *hawalah*. It will critically analyze different sections of relevant laws and will point out how the element of interest (*Riba*) is found in such laws. It will further argue as the two

---

[6] Muhammad Ayub, *Understanding Islamic Finance,* John Wiley & Sons Ltd, 2007, p. 155.

distinct principles of Islamic commercial law, i.e. loan and debt have been mixed up. It is due to this reason that Islamic jurists critically criticized the *hawalah* based transactions.

The study will further take into consideration two concepts in order to answer the question, i.e., *Suftajah*[7] and *Hundi*[8]. *Suftajah* was a commercial practice based on *hawalah* in 10th century in *Abassid's* era. *Hundi*, on the other hand, was practiced in sub-continent and is still prevalent in the region. The main difference between *Sujtajah* and *Hundi* was that the former was conditioned with use of credit notes, actual possession of the money, the risk of way and was based on trust and reputation while the latter was devoid of such conditions. Since *suftajah* was found hard to implement in the contemporary practice, so could not got appreciation in the contemporary world. *Hundi* was further appreciated as it was found in consonance the Negotiable Instruments Act, 1881. A critical analysis of these two will further clear the concept. This will further the broader perspective of *Hawalah* which will prove helpful to overcome the current economic recession and terrorism, being international issues in these days.

The current study focuses on the elaboration of the concept of *hawalah*. It is argued that the application of hawalah in different modern transactions is not based upon the true principles of hawalah doctrine. Most of transactions are based upon loans instead of debt. While Islamic law strictly prohibits loans for commercial purposes. The study supports this argument. It looks its application in modern transactions, coupled with its legal frame work. Each transaction is analyzed and looked. It is be justified why a

---

7 (Orig. Persian) A debt transfer transaction, practiced in Islamic societies since the *Abbasid* period in which A, a debtor authorizes his agent (*wakil*) or someone who owes him a debt, to pay a given amount to C to whom A owes a debt. *Suftajah* is related to and may be considered a special case of the standard Islamic debt transfer transaction known as *hawalah*. http://www.islamicbanker.com/glossory.html.

8 The word came from *Sanskrit* root meaning collect, it means bill of exchange or promissory note. A presentation given by Harjit Sandhu on the topic: *Terrorism-Criminal Nexus, Non banking conduits, Vienna, March 2004,* available on: http://www.osce.org/documents/sg/2004/03/2514_en.pdf. (Last accessed: 14, January, 2010).

transaction is incompatible with Islamic law. It also looks the relevant laws and their compatibility with Islamic law. It is argued that the *hawalah* may become an established principle if it is followed in its true sense.

3. Scope of Study

It is to further add that there is a considerable scope for research and analysis of *hawalah*. The study focuses to point out how the element of interest (*Riba*) is founding in different transactions based upon *hawalah*. It clarifies the concept in the sense that it is only transfer of debt or debt related liability and right. In this way, they will be accepted by the Islamic jurists as well. The study will also look the legal frame work of *hawalah*. It will examine and analyze different laws constituted on the basis of *hawalah* by taking *Shari'ah* appraisal. This will further enhance the scope the study as the legal status can be amended and improved for the purpose of using it in the large perspective. The main focus of the study is to examine the transactions both inside and outside banks which are justified on the basis of *hawalah*.

4. Approach of Study

The approach of the study is analytical and appraisal from the perspective of Islamic commercial law. The Holy Quran, the Traditions of the Holy Prophet (SAW), the Negotiable Instruments Act, 1881, the *Majallah*, the AAOIFI *Shari'ah* Standards and the Money Laundering Act, 1960 is used as the Primary sources in the study. It relies on the original sources. Books, Journals and Articles is be used as secondary sources. The Holy

Quran is cited in the manner that the first number denotes chapter (*sura*), the second denotes the number of verse, for example, 01: 88. All the four Sunni schools of Islamic jurisprudence, i.e. Hanafi, Maliki, Shafi and Hanbali are cited wherever is necessary.

5. Structure of the Thesis

The whole thesis is divided into three Chapters. Chapter 1 addresses the conceptual issues like definitions, historical controversies with regard to origin, validity, essentials, effect and termination of *hawalah*. It further focuses on the jurisprudential controversies, such as whether the concept is transfer of debt or loan. Chapter 2 proceeds to the core issues of the application of *hawalah* in modern transactions. The doctrine of *hawalah* in different transactions has been analyzed. Chapter 3 uses the legal framework of *hawalah* to investigate whether the laws have been properly constituted in accordance with the main concept of *hawalah*. It analyzes different laws from the perspective of Islamic commercial law. Chapter 4 sums up and draws a conclusion of the arguments along with some suggestions.

CHAPTER 1

JURISPRUDENECE OF *HAWALAH*

1.1 Introduction

Hawalah is one of the important concepts of Islamic Commercial Law. It has been found in practice in other commercial legal systems as well. However, much more recognition has been given to the concept by Islamic Law, particularly with regard to its Jurisprudence. It is, therefore, necessary to describe the concept in the light of classical Islamic Jurisprudence. This chapter highlights the basic concept of *Hawalah*. It discusses different concepts related to *hawalah* like its literal meanings, definitions, controversies with regard to its historical background, validity, nature, elements, parties and their respective qualification along with differences of opinion among the four schools of thoughts, essentials, kinds, effect and termination. It analyses the different definitions given by the prominent Islamic jurists.

It further describes the origin of *hawalah*, particularly, in the perspective of other economic systems, besides Islam. It focuses how the concept can be linked with other economic systems, particularly with Europe and India. It also describes the two concepts, i.e., and *Dayn*, collaterals to *Hawalah*. The said concepts have their distinct principles in Islamic commercial law and they can not be confused and can not be dealt in the same yard-stick. The main differences have been pointed out between the two concepts. It is argued that *hawalah* is the transfer of debt only and it can not be justified as transfer of

loan in any way. The chapter focuses on how the doctrine of *hawalah* is considered in contemporary economics. It is further followed by view which has been changed after the event of 9/11 regarding transactions based upon *Hawalah*. A brief conclusion of the chapter is given at the end.

1.2 Literal Meaning

The word *Hawalah* is purely an Arabic term. Some jurists translated it with the word *Tahwil* or *Intiqal*[9], i.e., shifting of a thing from one place to another. Others jurists translated it with its proper definition, *as al-Naqal mutlaqan li dayn au ayan*[10]"

النقل المطلق لدين أو العين

i.e., transferring/shifting a liability exclusively for *Dayn*/Debt or *Ayan*. Most of the classical Islamic Jurists recognized the concept as *Hawlah tu-Dayn/Debt* instead with single word *Hawalah*.

1.3 Definitions

A simple definition of *Hawalah* is the transfer of liability/debt of debtor from the principal debtor to a third person/new debtor in favor of the creditor. It is pertinent to refer to some definitions given by prominent Islamic Jurists:

The famous classical jurists Kasa'ni has defined *hawalah* in the following words:

---

[9]Wahbatul Zuhaili, *al-Fiqh ul-Islami wa Adilatuhu,* Darul Fiqr al-Muasir, Beirut, v.6, p.4187.
[10] Tehmaz, *al-Fiqh ul-Hanafi fi Saubil Jadeed,* v.3, p.422.

"Hawalah is the transfer of debt to a third person as a result of which the liability of the original debtor is terminated."[11]

al-Majallah al-Ahkaam al-Adalia has defined *hawalah* in the following way:

"Al-hawalah is naqlu-dayn min zima ila zima ukhra,"[12] i.e., Transfer of Debt (*Dayn*) from one person to another person or Transfer of responsibility of paying Debt/Dayn from one person to another.

According the famous contemporary Islamic jurist Wahbatul Zuhaili hawalah is:

"*naqlul mutalaba min zimatul madeen ila ziamatul multazim*[13]"

نقل المطالبة من ذمة المدين إلى ذمة الملتزم

Another famous jurist Dasooki defines *hawalah* as:

"Naqlul dayn min zimatul Ukhra bisabab ujood Mislahu fil Ukhra[14]":

نقل الدين من ذمة الأخرى بسبب وجود المصلحة في الأخرى.

It is the transfer of debt from one shoulder to another by the previous responsibility in the same manner.

The Audit and Accounting Organization of Islamic Financial Institutions (AAOIFI) gave the following definition of hawalah:

"*Hawalah* of debt is the transfer of debt from the transferor (*Muhil*) محيل to the bayer (*Muhal Alaihi*)محال عليه . The transfer of right, on the other hand, is a replacement of a creditor with another creditor. The transfer of debt differs from the transfer of right in the

---

[11] Al- Kasani, *Bidai al-Sanai,* vol.6.p.17
[12] *Al-Majallah al-Ahkaam al-Adalia, Article* 673.
[13] Zuhailai, , *al-Fiqh ul-Islami wa Adilatuhu,* op.cit., p.4188.
[14] Dasooki, *Hashia ul-Dasooki ala al-Sharhul Kabir*, Cairo, Isa al-Badi al-Halabi, 1350 H, vol.3, p. 325.

sense that in transfer of debt a debtor is replaced by another, whereas in a transfer of right a creditor is replaced by another creditor".[15]

The word debt has been used in the sense of liability/right (Arabic: *Dhimmah/Mutalaba/Haq*)ذمة . Debt is a credit sale in which the price is deferred.[16]

1.4 Historical Overview: Controversies with regard to Origin of *Hawalah*

It is argued that it was, *Kasani,* who wrote on the subject of *Hawalah* for the first time in 1327 A.D.[17] Prior to *Kasani*, *hawalah* was in commercial practice based upon the famous saying of the Holy Prophet (May God's blessings be upon him), narrated by *Abu Huraira*, a well known companion of the Prophet. The Prophet said,

عن أبي هريرة رضي الله عنه أن رسول الله صلى الله عليه وسلم قال مطل الغني ظلم فإذا أتبع أحدكم على ملي فليتبع.

Narrated Abu Huraira: The Prophet said, "Procrastination (delay) in paying debts by a wealthy man is injustice. So, if your debt is transferred from your debtor to a rich debtor, you should agree." [18]

There are many views with regard to the origin of debt negotiability. Some claim that it had been practiced in India with the name of *Hundi* hundreds of years before Islam.[19]

---

[15] AAOIFI, *Shariah Standard* No.7 Article, 2, Madina al-Munawwara, 2002.
[16] Muhammad Ayub, *Understanding Islamic Finance*, West Sussex, John Wiley & Sons Ltd, 2007, p:2009.
[17] *Evolution and institutional foundation of the hawala financial system,* an article published by M. Schramm and M. Taube, International Review of Financial Analysis, Volume, 12, Issue, 4, 2003, pp. 405-420. See for details: http://www.elsevier.com/wps/find/journaldescription.cws_home/620166/bibliographic (Last Accessed: 13, Nov, 2009).
[18] Sahib al-Bukhari, , *Kitab-al-Hawalaat, Hadith No: 2287.*
[19] Divya Sharma, *Historical Traces of Hundi, Sociocultural Understanding, and Criminal Abuses of Hawala,* an article published in International Criminal Justice Review—A quarterly journal issued by the

Hundi is almost seventy eight hundreds years old and is originally spread in Hindustan as villages were settled.[20] It is claimed that the Islamic doctrine of negotiability (*hawalah)* is an offshoot of *hundi*; the latter had been prevalent earlier than Islamic *hawalah.*[21] Others say the ancient Chinese were the pioneers of such doctrine by using debt transfer under the name of *fei qian* (or flying money).[22] The transfer of debt was a commercial practice in Europe before the rise of Islam.[23]

The Islamic law recognized debt transferability with a distinct name known as *hawalah.* A review of some of the earlier literature on *hawalah* reveals that it is purely an Islamic concept. The etymology of *hawalah* recognizes the fact.[24] Islamic jurists claim that Muslims were the first to use promissory notes and assignment, or transfer of debts via bills of exchange ("*Hawalah*").[25] In Islamic legal and religious texts the *hawalah* kind of value transfer mechanism is analogous to a financial instrument called *suftaja.* سفتجه [26]. In the 10th century A.D., the '*Abbāsid* financial administration made full use of the *suftaja*

Department of Criminal Justice, Georgia State University, Georgia. See for more details: http://icj.sagepub.com/cgi/content/abstract/16/2/99 (Last Accessed: 01, May, 2010).

[20] Galina Glushchenko, *Hawala—A Vestige of the Past in the Service of Globalization*, an Article published in a Russian Politics and Law journal, vol. 43, no. 5, September–October 2005, pp. 28–44. © 2005 M.E. Sharpe, Inc. (Last accessed: 01, May, 2010).

[21] Ibid.

[22] Sam Vaknin, *Hawala, or the Bank that Never Was" Global Politician Magazine-* an article published in the Online International Political News Journal, Storobin & Associates Corporate Offices, 14 Wall Street, 20 Floor New York, N.Y. 10005 Details available on: http://www.globalpolitician.com/2882-crime (Last accessed: Thursday, December 17, 2009).

[23] See Edwina A. Thompson, 'Misplaced Blame: Islam, Terrorism and the Origins of Hawala' in A. von Bogdandy and R. Wolfrum (Ed.), *Max Planck Year Book of United Nations Law*, Vol. 11, 2007, pp 279-305. BBC, 08 Nov., 2001. Available at http://news.bbc.co.uk/2/hi/business/1643995.stm (Last accessed: 01 Sept., 2009). In 2001, the US launched a campaign to blacklist hawalah companies. Part of that campaign, *Al-Barakt*, a Somali hawalah company was blacklisted and its assets were frozen. It was in 2006, the said company was struck off the list of the blacklisted companies. See details at BBC, 28 August, 2006. Available at http://news.bbc.co.uk/2/hi/business/1643995.stm (Last accessed: 01.05.2010).

[24] Ibid.

[25] S.Vaknin, "*Hawala, or the Bank that Never Was*", op.cit., 20.

[26] (Orig. Persian) A debt transfer transaction, practiced in Islamic societies since the *Abbasid* period in which A, a debtor authorizes his agent (*wakil*) or someone who owes him a debt, to pay a given amount to C to whom A owes a debt. *Suftajah* is related to and may be considered a special case of the standard Islamic debt transfer transaction known as *hawalah*. Details available on: http://www.islamicbanker.com/glossory.html. (Last accessed: 09, Oct, 2009).

in transferring its funds between the provincial treasuries of Baghdad based on the principle of *hawalah*.[27] The practice of *Hawalah* made it recognized as a legal concept in the *Majallah al-Ahkam* al-*Adalia* (hereafter as *Majallah*), a body of legal concepts codified by the Ottoman Empire[28].

The Negotiable Instruments Act, 1881 gave a legal coverage to the doctrine of Negotiability in different transactions. After the fall of *Ottomon* Empire, in 1924, issues related to transactions based upon *Hawalah* were dealt under the Negotiable Instruments Act, 1881[29]. In the contemporary Islamic laws, *Hawalah* has been recognized as Standard No. 7 in the *Shara'iah* Standards, codified by Audit and Accounting Organizations for Islamic Financial Institutions, in 2003.

1.5 Validity

Every doctrine recognized by Islamic law is required to be followed and recognized by some primary or secondary source. The word *hawalah* has not been mentioned in the Holy Quran. However, there are number of Traditions of the Holy Prophet (P.B.U.H) from which the concept has been inferred. The famous saying of the Holy Prophet (May God's blessings be upon him), narrated:

عن أبي هريرة رضي الله عنه أن رسول الله صلى الله عليه وسلم قال مطل الغني ظلم فإذا أتبع أحدكم على ملي فليتبع.

[27] A.E. Lieber, *Eastern Business Practices and Medieval European Commerce*", an article published in the Economic History Review 21(2) (August) (1968). Ref given by Thompson, *An Introduction to the Concept and Origins of Hawala.*

[28] Ottoman empire was a Muslim empire, lasted from 1299 to Nov.1, 1922 and was spread over three continents, controlling much of Southeastern Europe, Western Asia and South Africa. See for more details: http://en.wikipedia.org/wiki/Ottoman_Empire#cite_note-3 (Last Accessed: 11, Nov, 2009).

[29] The Act of laws constituted by British Parliament in 1881.

Narrated Abu Huraira: The Prophet said, "Procrastination (delay) in paying debts by a wealthy man is injustice. So, if your debt is transferred from your debtor to a rich debtor, you should agree." [30]

All the Islamic Jurists have Ijma- consensus of opinions on the validity of *Hawalah*. Even the doctrine of necessity and logic also supports the doctrine as well.

1.6 Nature of *Hawalah*

Hawalah is a secondary contract in which the rights of one party are transferred to a third party. In other words, it is an exception to the rule of privity[31] of contract.[32] The contract is required to be confined only to assignment/transfer of debt. It is required to be issued for a pre-existing claim based on a trade transaction.[33] It should, however, not be confused with the sale of debt or loan or even transfer of commercial/business loans, which depict Riba. In other words, *Hawalah* must be free of Riba. It has also been further elaborated that *Hawalah* is the assignment/transfer of liability or debt and not the right of creditor in the debt due from the debtor to a new party.[34]

---

[30] Sahib al-Bukhari, , *Kitab-al-Hawalaat, Hadith No: 2287.*
[31] The exclusive relationship of rights and duties between parties of a contract
[32] Nyazee, *Outlines of Islamic Jurisprudence,* op.cit., p. 246.
[33] Ibid. p. 293.
[34] Muhammad Tahir Mansoori, *Islamic Law of Contracts and Business Transactions*, Islamabad, Shariah Academy, International Islamic University Islamabad, p.305.

1.7 Transfer of Right

It refers to the transfer of right from one creditor to another. While in transfer of debt one debtor replaces another in transfer of right one creditor replaces another. For instance, a particular seller refers a purchaser to pay the price of the sold item to his (the seller's) creditor. It may also happen when a pledgee wants the pledgor to pay the debt to another person.

1.8 Elements/Ingredients

There are differences of opinions regarding elements of *Hawalah* among the Jurists.

Imam Abu-Hanifa considers only one element for the formation of contract of *Hawalah*[35] i.e., Offer and Acceptance. An offer made by the original debtor (*al-Muhil*) to the creditor (*al-Muhal lahu*) by saying I have transferred your liability to the particular person. The second part of the element is Acceptance (*al-Qabool*) but that must be both by the original creditor and the third person i.e., *al-Muhal alaihi.* In other words, offer made by the original debtor and an acceptance made simultaneously by the creditor and the third person will conclude the contract of *Hawalah.*

Imam Shafi enumerates six elements for the conclusion of the contract:

- *Muhil* i.e., Origional debtor.
- *Muhal alaihi* i.e., Third person/ New debtor.
- *Muhal lahu* i.e., The creditor.

[35] Zuhaili, *al-Fiqh ul-Islami wa Adilatuhu,* op.cit. p. 4189.

- *Dayn lil-Muhal ala al-Muhil* i.e., Debt of creditor on the original debtor
- *Dayn lil-Muhil ala al-Muhal alaihi* i.e.,Debt of the original debtor on the third person/new debtor
- *al-Ijab wal Qabool* Offer and Acceptance.

According to Imam Shafi there must be a pre-exiting debt of the original debtor on the third person. It means if this element is missing, it will not amount to *Hawalah.*

Malikis consider three ingredients in this regard.

- *Muhil*
- *Muhal bihi*
- *Sigha* i.e., Offer and Acceptance.

According to Imam Hanbal there are four ingredients in the contract of *Hawalah.*

- *Muhil*
- *Muhal bihi*
- *Muhal alaihi*
- *Sigha* i.e., Offer and Acceptance.

The conclusion which can be drawn from the above discussion is there must be an offer usually from some one who is called *Muhil* and that must be accepted by some one but that acceptance should be from two persons i.e., *Muhal alaihi* and *Muhal lahu.* Moreover, there must exist a debt i.e., the new debtor must be debtor of the original debtor.

1.9.1 Parties

Three parties involved in the contract of *Hawalah*:

- Debtor i.e., *al-Maduoon called Muhil.*
- Creditor i.e., *al-Dayin/assignee called Muhal Lahu.*
- Third person i.e., *transferee called Muhal alaihi.*

Those parties can be best understood by the following illustration.

Illustration:

A has debt owing to him from B and owes debt to C. C, instead of realizing from A and A his debt from B, can realize it from B through the contract of *Hawalah*. In this example debtor B is substituted for debtor A with the agreement of C. A is discharged. The debtor who transfers debt is *Muhil* (debtor-assigner), the creditor *Muhal* (creditor-assingnee) and. new debtor to whom transfer is made, *Muhal alaihi* (Transferee).

1.9.2 Qualification of Parties

The Hanafi Jurists have assigned different qualification for the parties involved in *Hawalah.*

i. Qualification for the Transferee (*Muhal alayh* محال عليه):

He should be sane and has attained majority of age. Even a discerning minor (*sabi mumayaiz*) is not legally competent to accept *Hawalah*, for the reason, not to put the minor in financial loss. If he accepts with or without order or consent of the transferor, it will amount to a gratuitous act or gift which is not permissible for a minor. Even

guardian of a minor can not accept *Hawalah* on behalf of a minor. However, the condition of sanity and puberty is not necessary according to some jurists in case of restricted Hawalah where the transferee has a debt due from the transferor.

ii. Qualification for the creditor (*Muhal Lahu*) and the debtor *(Muhil*):

They should have the capacity of understanding (*Aaqil*) and discretion. However, the contract will remain suspended until approved by the guardian of the minor. The condition of attaining the age majority is impliedly included for the reason that a minor has no understanding.

The qualification for the parties has been bifurcated on the basis of validation of the nature of the contract and its execution in *Majallah al-Ahkam al-' Adliyyah,*. It has postulated the condition for the formation of the contract, both the creditor (*Muhal Lahu*) and debtor (*Muhil*) are required be worth of understanding while the transferee (*Muhal alay*) must be major and having capacity of understanding (*Aaqil*).

On the other hand, for the execution of the contract, both debtor (*muhil*) and creditor. (*Muhu*) must be major, while the contract made by discerning minor (*sabi mumayaiz*).[36]

1.11 Effect of *Hawalah*

The main effect of *Hawalah* is to discharge the principal debtor/Muhil from the debt. If the liability remains for the payment of debt upon the shoulders of the principal debtor, then the arrangement will not amount to *Hawalah*. It will amount to another kind contract called the contract of Guarantee. In such situation the creditor/assignee has the

[36] *al-Majallah al-Ahkam al-' Adliyyah*, Sections: 684-685.

option either to claim from the principal debtor or from new debtor. It has been described that the creditor/assignee has a right to recourse to the principal debtor.

1.12 Rights and Duties of Parties

Hawalah creates the following rights and duties for the parties:

i. The new debtor/transferee, in case of absolute *Hawalah* steps into the shoes of the creditor after making payment to the creditor. The transferee is entitled to claim the amount of the debt assigned to him through *Hawalah* from the payer. The payer, on the other hand, is obliged to pay him and has no right to refuse payment.[37] The new debtor/transferee takes the place of the transferor in respect to all rights, legal protections and obligations.[38]

ii. While in case of conditional *Hawalah*, the right of the principal debtor to the property or debt in possession of transferee ceases.[39]

iii. In case of death of the new debtor/assignee before the payment of Hawalah debt in his hand, both the principal debtor and the creditor have equal rights over the disputed debt.

iv. The transferee/new debtor is also liable to honor his commitment even if his obligation ceases to exist. This is what happens in case some credit sale gets revoked either by the destruction of the subject matter or exercising option of inspection or defect.[40]

---

[37] Ibid, Article 9
[38] Ibid.
[39] Mansoori, *Islamic Law of Contracts and Business Transactions,* op.cit., pp: 306-307.
[40] Mansoori, *Islamic Law of Contracts and Business Transactions,* po.cit. p.306.

v. The transferee will have no right of recourse against the transferor for payment. In other words, the transferor is discharged from both the debt liability and any claims related to such debt. However, the former has the right to recourse if it has been conditioned that the payer must be solvent.[41]

vi. Besides, the transferee is entitled to have a right of recourse against the transferor in situations of (a) death of the payer in bankruptcy, (b) liquidation of an institution that is the payer in the case of bankruptcy before payment of the debt, (c) the payer is declared bankrupt in his lifetime, or he denies concluding the *Hawalah* contract and has taken a judicial oath to this effect and there is no evidence to prove otherwise and (d) the institution that in the payer is declared bankrupt by a court.[42]

vii. The transferee has the right over an amount paid to him during debt settlement. In other words, the transferor is no longer entitled to reclaim from the transferee any amount transferred to the payer in such debt settlement because the right to receive this amount has now passed to the transferee.[43]

1.13 Conditions of *Hawalah*

a. The validity of *Hawalah* requires the consent of all the parties.

b. The validity of a *Hawalah* requires that the transferor be a debtor to the transferee. A transaction in which a non-debtor transfers another is an agency contract for collection of the debt and not a transfer of debt.

[41] AAOIFI, *Shariah Standard* No.7 Article, 7.
[42] Ibid.
[43] Ibid, Article 8

c. It is not a condition in a *Hawalah* that a payer is a debtor to the transferor. If the payer is not a debtor to the transferor, the *Hawalah* will be an unrestricted *Hawalah.*

d. It is a condition that all *Hawalah* parties, be legally competent to act independently.

e. It is a condition in *Hawalah* that both the transferred debt and the debt to be used for settlement be known and transferable.

f. It is a condition for concluding restricted *Hawalah* that the transferred debt or the transferred portion of the debt be equal to the debt owed to the transferee in terms of kind, type, quality, and amount. However, the transferor may transfer a lesser amount of a debt owed to the transferee to be settled from a larger amount owed by the transferor on condition that the transferee be entitled only to the equivalent amount of his debt.[44]

g. *Hawalah* by agreement of the creditor and the new debtor: The original debtor does not participate in this sort of *Hawalah,* which is not of common occurrence but can still be encountered. This is lawful according to Hanafi jurists.[45]

h. *Hawalah* by agreement of debtor/assignor (*Muhil*) and the creditor/assignee (*Muhal lahu*): For Hanafis this is contingent upon the new debtor's agreement. To others his consent is not necessary, especially when he is solvent.

i. *Hawalah* by agreement of the debor/assignor (*Muhil*) and the new debtor (*Muhal alayh*): This *Hawalah* is contingent upon the creditor's agreement according to

[44] Ibid.
[45] Mansoori, *Islamic Law of Contracts and Business Transactions,* op.cit., p.307.

Hanafi, Shafi'I and Maliki jurists. Hanbali jurists hold that when the new debtor is solvent his consent is not necessary.[46]

1.14.1 Termination of *Hawalah*

A *Hawalah* liability will come to an end by settlement of the debt or by a mutual agreement to terminate it or by the debt being written-off by the transferee.[47]
There have been enumerated other circumstances as well. Some of them are related to absolute *Hawalah* and others to restricted *Hawalah.*

1.14.2 Termination of absolute *Hawalah*

According to Imam *Abu Hanifah,* contract of *Hawalah* is terminated and debt reverts to the principal debtor in the following circumstances:

a. Where the transferee denies the existence of the contract upon oath, and the creditor can not produce witnesses to prove it.
b. Where the transferee denies poor and insolvent. In either case the debt is destroyed, since in either case is it practicable for the creditor to receive payment from the transferee.[48]

1. *Hawalah* is terminated less than one of the three circumstances. Of these, two are the same as those above cited above and the third is a

[46] Nabil Salih, *Unlawful Gain and Legitimate Profit in Islam,* pp. 103, 104. Quoted by Mansoori, *Islamic Law of Contracts and Business Transactions*, p.307.
[47] AAOIFI, *Shariah Standard* No.7 Article, 11.
[48] Marginani, *al-Hidayah*, vol. 3, p.99.

declaration by the court of poverty and insolvency of the_transferee during his lifetime. This third circumstance is not admitted by Abu Hanifah because according to him, poverty and insolvency can not be established by the decree of court, since property comes in the morning and goes in the evening. But according to the two disciples the_decree of the court can also establish poverty. Before this declaration the creditor is not entitled to make any claim against the transferor.

2. The creditor has no right to make any claim for his due upon the transferor, although his right is destroyed. It is because in consequence of the transfer that the transferor becomes exempted from the debt and this exemption is absolute and not restricted to the condition of payment from the transferee. Hence the debt can not revert to the transferor, except on account of some new cause and no such cause is to be found in this case.

1.14.3 Termination of restricted *Hawalah*

1. If *Hawalah* was with condition that payment is to be made from property of the debtor-assignor in possession of the transferee, and then a person who was the rightful owner of that property turned up took its possession. The *Hawalah* is void and the debt is returned to the debtor who made the *Hawalah.* In other words, restricted *Hawalah* is terminated when the property in the hand of the transferee does not belong to the assignor and is taken possession of by its owner.

2. It is terminated, if the property held by the transferee in fiduciary capacity is destroyed without any negligence on part of transferee.

It is not terminated in the following two cases:

a. If the property was held in trust and destroyed by negligence.

b. It was a property of assignor usurped by transferee.

1.15.1 Dayn (Debt) in *Shari'ah*

Dayn means debt. It is something in which payment is delayed.[49] According to Majallah dayn means the thing or liability due.[50] It can either by monetary or a commodity, i.e., food or metal.[51] Its technical meaning can be understood in comparison with the term '*Ayn*' rather 'cash loan' as has been viewed by some modern writers.[52] *Ayn* is any commodity that has been ascertained or determined at the time of contract with respect to its quantity and valuation so that ownership it can be passed on to the buyer. The process is known as *Ta'yin*. *Dirhams* and *Dinars* which are referred to as dayn are not subjected to the process of *Ta'yin* through weight and measure at the time of contract. In other words, they are considered as Dayn as they are always associated as liability.

Thus Dayn (debt) is created when a commercial activity takes place on credit. It does not apply to cash loans.[53] In other words, it usually comes into existence when any

---

[49] Nyazee, *Outlines of Islamic Jurisprudence* op.cit., p. 289.
[50] *al-Majallah al-Ahkam al-Adalia,* section: 158.
[51] Ust Hj Zaharuddin Hj Abd Rahman, *Rulings On Debt Trading In Shariah.* This article was published by Business Times, NST, Malaysia on 21st June 2006. Details available on: www.zaharuddin.com. http://www.kantakji.com/fiqh/Files/Finance/169.txt 27/07/09.
[52] Nyazee, *Outlines of Islamic Jurisprudence* op.cit., p.289.
[53] Ibid.

other contract or credit transaction is involved. It can be incurred either by way of sale or rent or purchase or in any other way which leaves it as a debt to another. It has been described that *Duyun* (Debts) are required to be returned without any profit since they are advanced to help the needy and meet their demands and, therefore, the lender should not impose on the borrower more than what he had given on credit.[54]

1.15.2 *Bai-al-Dayn* (the sale of debt)

There is found consensus of opinions among all schools of Islamic Jurists that there is no concept of sale of debts. It rules out that there should be no benefit to the purchaser in order to avoid deferred payment in different transactions which amounts to Riba. It can only be ensured if debt is paid back equivalent in quantity. However, Malikis and some Hanafis and Shafis permit selling

There are found differences of selling to a non debtor or a third party. According to most Hanafis, Hanbalis and Shafie jurists, it is not allowed at all. However Malikis, and some Hanafis and Shafie jurist permitted selling of debt to third party subject to some conditions which are:

- The seller must be in a position to deliver debts.
- The debt must be *mustaqir* or confirmed and the contract must be performed on the spot.
- The debt cannot be created from the sale of currency (gold and silver) to be delivered in the future and the payment is not of the same type as debt, and if it is so, the rate should be the same to avoid Riba.

[54] See for more details: http://www.zaharuddin.net/content/view. (Last visited: 08, Nov, 2007).

- The debt should be goods that are saleable, even before they are received. This is to ensure that the debt is not of the food type which cannot be traded to the debtor.[55]

The ruling regarding selling of a confirmed debt, backed by non ribawi goods at discounted price is that it is permitted subject to the condition that it must be at face value. Subject to this rule, when a bank buys an instrument of debt (shahada-al-dayn) from the original buyer, it is not entitled to any discount. There should be no difference between what is paid and what is received. However, some Islamic banks have been offering Islamic bill discounting products by giving the reason as they treat debt as any other physical asset that can be traded at a negotiated price.

It is quite logical that Bay'-al-dayn mostly involves a debt receivable in terms of money. The rule of exchanging the price at par value is hardly followed. Resultantly, there is quite possibility that some increase or decrease is involved which amounts to interest (*Riba*).

The proponents allow the contract of *Bay'ad-Dayn* in two cases. One, when a debt is created through a sale of commodity. Dayn in this case gets the status of securitized debt differentiating from currency, hence is permitted to be sold with discount.

Second, a debt is created by the sale of goods and services through the sale based on modes of Islamic Finance, particularly Murabahah. The price which is got, as a result of debt, is the profit on transaction and not interest. This is permitted by the Shariah Scholars. So, the selling of debt instrument at a discount is permissible and not a share in the profit rather interest.

---

[55] Dusuqi *Hasyiah ala al-Sharh al-Kabir,* Cairo, Isa al-Babi al-Halabi, 1350, vol 3, p: 63.

It further added that commercial papers such as cheques, promissory notes and bill of exchange cannot be sold at a discount as because there is found the element of Riba. It is not allowed to deal, issue, distribute or trade with Riba based Bonds because the element of Riba is present. Furthermore, dealing with debt notes in the secondary market as it involves discounts and sale of debts to third parties is also prohibited because has Riba elements.[56]

1.16 Qard in *Shari'ah*

In Islamic law stands for loan. Literally, it means 'to cut', i.e., to cut a property from the usage of one person when it is given to another. Legally, it stands for to give a valuable thing in the ownership of another person so that the latter can use it for his benefit and the same thing or similar amount of that thing will be paid back either on demand or at the settled time, without interest or profit sharing. [57] It is given for a good cause, benevolent, gratuitous, or charity, in hopes of repayment or reward in the Hereafter.[58]

In Islamic Law only a special kind of *Qarz*, i.e., *Qarz Hassan* has been recognized. The Holy Quran has recognized Qarz in the context of charity. It has also been ratified by the Tradition of the Holy Prophet (SAW), "Every Qarz is Charity (Sadaqah)". It is also very relevant to mention here that the permitted type of Loan does not accept

---

[56] 16th convention, held at Mekka on 5-10th January 2002. See for more details: http://in.answers.yahoo.com/question/index?qid=20081118224650AAdnm8X.29/07/09 (Last visited: 29, Nov, 2009).

[58] Ibid.

AGENCY as it is like to begging for charity and one can not appoint an agent for begging.[59]

It has been dealt with from another aspect as well. Loans under Islamic Law have been classified into *Salaf* and , the former being loan for a fixed time and the latter payable on demand.[60] Similarly, there is no concept of time value[61] of Qarz/Loans/Money because it will amount to Riba. So no time value can be added to a loan's or a debt's principal after it has been created or the purchaser's liability has been stipulated.[62] It is held to be for this reason that the commercial bank deposits or other lending transactions are strictly prohibited by majority of contemporary Islamic Jurists.

1.17 Differences between *Dayn* and Loan

From the above discussion, it can be inferred that the whole jurisprudence of Dayn and Loan are different. The main points of differences can be summarized as:

- Dayn is created only in case of a credit sale[63], in which the claim for the price is attached to the *dhimmah* of the buyer.[64] *Qarz*, on the other hand, is when some cash is given in the form of loan.
- No ownership is transferred in Dayn. In other words, ownership in the commodity continues to remain with the owner. On the other hand, Qarz is something that is consumed with use and ownership gets transferred.

---

[59] Nyazee, *Outlines of Islamic Law*, op.cit., p. 290.
[60] For more details see: http://www.islamic-world.net/economics/debt_trading.htm, last visited: 05, Dec, 2009.
[61] Abu Umar Faruq Ahmad and M. Kabir Hassan, *The Time Value of Money Concept in Islamic Finance*, details available: *http://i-epistemology.net/economics-a-business/899-the-time-value-of-money-concept-in-islamic-finance.html* last visited: 10/09/09
[62] Ibid.
[63] Sale in which the *ajal* (period) for the payment of price is fixed.
[64] Nyazee, *Outlines of Islamic Law*, op.cit., pp: 275-276.

- Dayn accepts Agency, Guarantee or *Wakalah*. Qarz, on the hand, being a charitable act, does not accept agency, *Hawalah*, Agency, *Wakalah* etc. is the lending of something that is consumed with use.
- Dayn ascertained by the rule of *Tayin*, i.e., measurement and weight. While such ruling is not found in Qarz.

1.18 How a modern *Hawalah* works

Hawalah is used as an easy and cheap way of money transfer, particularly by the migrants. A migrant who wishes to send money to his home, approaches a *Hawalah* broker by giving him the money to hand over to a recipient at the specified place. The *Hawalah* broker gives the details to another *Hawalah* broker in the recipient's city and settle the debt. The *Hawalah* broker takes his commission from the money to be transferred. Such arrangement is mostly based on honor, trust and good will of the *hawalah* companies. In most of cases there are no material records available for such transactions and hence claims can not be asked through legal or juridical form. The laws on which such transactions are regulated are vague and insufficient due to which these practices have been reported as misused on broader scale. That is why such transactions have adopted different forms and modes and many times have been misused. The fact can be illustrated by the recent money laundering crimes committed by Khanania and Kalia *Hawalah*/Hundi companies. It is to further state that most of the *Hawalah*/Hundi companies do not follow the official exchange rates, thus makes open back doors for illegal and unlawful profits. However, customers get attracation to adope such mode for the reason that it is a fast and convenient mode of transfe of funds and a lower commission

is charged. It further gets deep rooted where there are distortive exchange rate regulations and where banking system is much more complex one. They also get exempted from paying tax to the government and any currency control. It for this reason that governments do not favor the system and are also unable to defend the very mode from the accusation that terrorists activities are getting multiplied in this way.

But Islamic law has recognized the above arrangement in the form a separate concept called the concept of *Sarf* (remittance) which will be discussed in the next chapter in details along with its rules and limitations. *Hawalah* has only been recognized in the form of *Suftajah* (bill of exchange). *Suftajah* is one of the convenient way among traders for transferring money in order to avoid risks of way and handling cash amounts.

1.19 Hawala after September 11, 2001

Hawalah became a controversial commercial practice since 9/11 as the United States (US) government suspected its use as a tool of transfer of money for financing terrorism.[65] It was held responsible for the incident of 9/11. Though, such suspicion was held fictitious and was not confirmed by the 9/11 Commission Report.[66] Some *Hawalah* brokers were held responsible for the incident of 9/11, stating that they might have helped

[65] See Edwina A. Thompson, *'Misplaced Blame: Islam, Terrorism and the Origins of Hawala'* in A. von Bogdandy and R. Wolfrum (Ed.), *Max Planck Year Book of United Nations Law*, Vol. 11, 2007, pp 279-305. BBC, 08 Nov., 2001. Available at http://news.bbc.co.uk/2/hi/business/1643995.stm (Last accessed: 01 Sept., 2009). In 2001, the US launched a campaign to blacklist hawala companies. Part of that campaign, Al-Barakt, a Somali hawala company was blacklisted and its assets were frozen. It was in 2006, the said company was struck off the list of the blacklisted companies. See details at BBC, 28 August, 2006. Available at http://news.bbc.co.uk/2/hi/business/1643995.stm (Last accessed: 10, Dec, 2009).

[66] 9/11 Commission Final Report http://en.wikipedia.org/wiki/Bank_account last visited: 11, Dec, 2009.

the terrorists to transfer money to their activities. For example, it stated that funds were sent by an inter-bank wire transfer to a SunTrunk Bank in Florida.

A big pressure was put world-widely by the US government to curb the activities of those involved in financing terrorism through *Hawalah/Hundi* mode of transactions and number of *Hawalah/Hundi* networds was closed down and their masters/hawaladars were prosecuted. US also declared *Hawalah* as illegal and a form of money laundering.

1.20 Conclusion

It can be concluded from the current chapter that the doctrine of *hawalah* has it distinct jurisprudence in Islamic commercial law. It has been found that the concept is deep rooted in different other economic systems as well. It has also been found that there is consensus of opinion among the four schools of Islamic law on the justification of *hawalah*. It has also been noticed from the discussion in the chapter that Traders had to have some convenience and courtesy during their trades in order to have a way out for the risks of way and carrying cashes. However, the doctrine of *hawalah* was used in different transactions. In other words, different transactions were justified as Islamic on the basis of *hawalah*. However, such transactions contain the element of interest *(Riba)* and violate other principles of Islamic commercial law as well.

What are those transactions and how they are subject to criticism? This will be discussed in the next chapter. Different transactions will be looked from the perspective of Islamic commercial law. Some commentators have argued that Islamic law has taken the doctrine from other economic systems, particularly, Europe and India. Hence, it has been recognized in the academic discussion regarding transfer of liability in trades and

businesses. It has been discussed that after 9/11, *hawalah* was held responsible for the promotion of terrorism. In other words, it was considered as one of the key sources for providing financial aid to terrorists, particularly, in Pakistan and Afghanistan. Although, this was a misconception which was even proved as wrong by the UN annual commission, however, it has opened a new discussion as how the doctrine of *hawalah* is promoting terrorism while using in practical transactions. The application of *hawalah* principles in different transactions are going to be taken in the next chapter.

CHAPTER 2

THE APPLICATION OF *HAWALAH* IN MODERN TRANSACTIONS

2.1 Introduction

The previous chapter discussed the conceptual elements of *Hawalah.* It necessitated looking whether the concept is applied in its practical form in the real sense? In other words, the application of *hawalah* in different transactions is needed to be analyzed from the perspective of Islamic commercial law. Different transactions are said to be permissible as they are as based upon the doctrine of *hawalah.* They are justified on the doctrines of permissibility, *hiyal* and analogy. They also justify the use of loans for commercial purposes, delay payments and uncertainty in commercial transactions. Islamic commercial law has strictly prohibited all these elements to be used in commercial activities. It is argued different hawalah based transactions are devoid of one of the important elements of *hawalah* i.e. the creation of debt in the form of credit sale or involving some commercial activity. It is further argued that some of such transactions involve sales of debts which are strictly prohibited in Islam.

What are the elements of interest (*Riba*) involved in *hawalah* based transactions and how they can be critically analyzed, how they are devoid of commercial activity and how they contain uncertainty? This chapter addresses all these issues. The scheme of discussion is in such a way that each transaction is described with its short jurisprudence

and usage in commercial activities. It is then critically analyzed from the perspective of Islamic commercial law under the heading *Shari'ah Appraisal*. The rules described in Chapter 1 will be taken into consideration in the analysis.

2.2 Remittances

Remittance is the system of sending money from one place to another.[67] It may be either in the form of payment of a demand or account, or draft.[68] As globalization has led to ever higher levels of labour mobility, the volume of funds remitted to their families by workers employed in countries far distant from their homes has increased by leaps and bounds. The total volume of such transfers currently amounts to over $100 billion per annum, the greater part of which flows from economically advanced regions in the West and North to developing countries in the East and South. Delivering those funds swiftly, reliably and cheaply to relatively remote destinations opens up new opportunities for the financial services industry, but also represents a major logistical challenge.[69] Money is sent either through banks or through non-bank channels. Each of such modes is going to be discussed separately.

---

[67] Merriam-Webster online dictionary available on: http://mw4.m-w.com/dictionary/remittance.
[68] Marie,Hawala remittance system and moneyLaundering, published in ChêneU4 Helpdesk Transparency International,Date:23,May,2008 *http://www.google.com.pk/search?hl=en&q=remittance&start=20&sa=N* Accessed: 17, May, 2010. (Please see: http://www.fatf-gafi.org/dataoecd/16/8/35003256.pdf).
[69] Roger Ballard, *Delivering Migrant Remittances: the logistical challenge*, available on: http://www.casas.org.uk/papers/hawala.html Last accessed: (20, Dec, 2009).

2.2.1 Remittances through Banks

Apart from accepting deposits and lending money, banks also carry out, on behalf of their customers, the act of transfer of money from one place to another, both domestically and on foreign level. Banks issue Demand Drafts, Banker's Cheques, and Money Orders etc. for transferring the money.

In Remittance transactions, Bank 'A' at a place 'a' accepts money from customer 'C' and makes arrangement for payment of the same amount of money to either the customer 'C' or his "order" i.e. a person or entity, designated by 'C' as the recipient, through either a Branch of Bank 'A' or any other entity at place 'b'. In return for having rendered this service, the Bank charges a pre-decided sum known as exchange or commission or service charge. This sum can differ from bank to bank. This also differs depending upon the mode of transfer and the time available for affecting the transfer of money. If the transfer is in faster mode, higher charges are taken.

The transfer is made in another way as well. Suppose Mr. A, a Pakistani working in Dubai, wants to send money to his family in Islamabad; he goes to a bank, opens an account and puts money in that account. The bank makes a demand draft and sends to Islamabad to the account of the wife of Mr. A. among the pre-requisites for making such transactions, Mr. A is required to have a bank account and has to fill out elaborate forms or show a government ID number. He is also needed to deal with an artificial exchange rate set by the Pakistani central bank — a rate of exchange intended to cut tax.

2.2.2 *Shariah* Appraisal

The transfer of money (remittances) is said to be based upon the doctrine of *Hawalah*. It has been described in the *Shari'ah* Standards in the following words,

"The request of a customer for the institution to transfer a certain amount of money in the same currency from his current account to a particular beneficiary is a transfer of debt if the applicant is a debtor to such a beneficiary. The fee that the institution gains from this transaction is consideration for the delivery of the money and it is not an additional amount gained by the institution over the amount transferred. However, if a remittance is to take place in a currency different from that presented by the applicant for the transfer, then the transaction consists of a combination of currency exchange and a transfer of money that is permissible."[70]

The above ruling permits transfer of money through a bank with the condition that the principal debtor is the debtor of the beneficiary. In other words, there must have been created debt between the principal debtor and the benefiary. Debt as we know is created through some commercial activity or credit sale. It is to argue that such kind of tranaction is impracticable in the contemporary transactions. It has also justified the fee taken by an institution/bank for the transfer of money on the basis of service charges. It is again to argue that no institution can just rely upon the true service charges. Service charges are charged only when the actual cost of the transfer of money is shown and acknolwedged by the customer but in the practice such activities are hardly noticed.

The standard has described remittance in another way as well. It says:

---

[70] AAOIFI, Shari'ah Standards7 Section 12/6.

"It is permissible to execute a financial transfer of money (remittances) in a currency different from that presented by the applicant for the transfer. This transaction consists of a currency exchange affected through actual or constructive possession by delivering an amount of currency that is evidenced by a bank draft, followed by the transfer of the amount using currency that is bought by the applicant for the transfer of money. It is permissible for the institution to charge a fee for the transfer."[71]

However, in Islamic law the concept of remittance is somewhat different. It should not based upon the doctrine of *hawalah*. Islamic law has recgonized the transfer of money in its distinct system called *sarf*. On the other hand, the tranfer of debt is recognized in the form of *suftaja*. In countries like Pakistan, India and Afghanistan the system of sending of money is usually known as *hawalah*. It is to argue that this is not hawalah as understood in Islamic law. This is, in other words, sarf, which has its own rules. There is great difference between *sarf* and *hawalah*. The former stands for sending of money, rather, selling of money, while the latter, means transfer of liability of payment of debt to a third party. Both the doctrines are going to be discussed in details to support the argument.

2.2.3 *Sarf*

The literal meaning of the word *sarf* is excess. The supererogatory worship *(nafl)* is called *sarf* because it is an additional thing. Technically, it is the sale of a monetary value for another monetary value of the same genus or of another genus.[72] In other words, it is the sale of absolute price for absolute price. The main conditions of *sarf* contract are as follows:

---

[71] Ibid, Standard No.1 p.8.
[72] Nyazee, *Outlines of Islamic Law*, op.cit., p. 279.

1. The counter-values must be delivered and taken possession of within the session of the contract. This is one of a conditions which is specific to the contact of *sarf* and distinguishes it from all the other contracts.[73] In other words, the condition of delay should not be stipulated.
2. The counter-values must be exchanged in the same quantity if the same currencies are exchanged. In other words, there must be equality or sameness in weight if gold is exchanged for gold. If the currencies are different then equality in weight is not the requirement. However, the counter-values must be exchaged within the same session. There must not be delay and the values must be exchanged in the same meeting of the contract. In this way, gold can be exchanged for silver with different quantity or weight but without suffering any delay.
3. No option can be stipulated in this contract. The reason is that an option delays the transfer of ownership and this violates the condition of spot delivery and possession.
4. Good and bad quality of exchanged counter-values is not relevant in contract.

It has been viewed that the rules mentioned earlier are not specific with gold and silver or dinar and dirham alone, but are applicable to every commodity or thing that performs the functions of money namely; a medium or exchange, unit of value, and

[73] Ibid. p.80.

standard of deferred payment.[74] Any institution or medium through which money is sent or which deals with *sarf*, must fullfill the above mentioned conditions.

Islamic commercial law has the basic rule that nothing can be charged on consumables including money. What can be charged is rent on tangibles like property or any asset only. What is required is that money should be converted into asset and then sell the asset on a profit or give the asset on rental basis to earn profit.[75] If it is not followed, it will be clear violation of the rules of Islamic commercial law. The same rule is applied to *hawalah* contract as well. The contract is based upon the existence of debt and debt involves some trade activity of some asset or tangible property. While it has been noticed from the rules of *sarf* that it is not based upon debt which involves some commercial activity. It is to further add that bank remittance can not be equated to transfer of debt. Bank always acts in as a commercial entity. It does not involve credit sales and debt-related transactions in its practice. It rather sells the money in the form of loans. In other words, it sells loans. Even if it involves debts then the way in which it makes transactions may amount to the sale of debt.

2.2.4 *Suftaja* سفتجه

Suftaja (bills of exchange) is one the important credit instruments employed in Islamic world. Historically speaking, it was a written obligation, issued by and drawn upon well-

[74] Mansoori, *Islamic Law of Contracts and Business Transactions,* op.cit., p.197.

[75] Salman Ahmed Sheikh Accounting, *Critical Analysis of the Current Islamic Banking System*, Published on 11/8/2007. For more details see: http://www.accountancy.com.pk/articles.asp?id=178 (Last accessed: 06, Jan, 2010).

known merchant for repayment in the same type of currency paid to the issuing agent.[76] In other words, it is one of the applications of *hawalah*. It is found in the form of *suftaja* (a credit instrument employed in Islamic world which must not involve currency exchange and payment must be made in the same currency).. The concept had been extraced from the folllwing event, reported in *Daaim al-Islam* composed by *al-Qadi al-nauman* in roughly 960 A.D one of Muhammad's companions is reported to have said,

"He gave a certain sum of money in a particular town (min madinat) and received it in another place (bi-ard ukhra). He permitted the use of bill of credit (suftajah), and this means that a man obtains a loan at one place and recieves it at another place."[77]

It can further be understood from the following example:

Suppose *A* lends a sum of money to *B* in return for a *suftaja*, which he gives to *C*, who resides elsewhere and pays *A* the same sum in the same currency. It was typically written as: "Ali asked me to take from him Rs.2000, which I did and for which I wrote him a bill drawn on you."

In the *Abbāsid* period it had been used for fund transfers between provincial treasuries and Baghdad. Besides, it had also been used for trade, tax farmers and bribes.[78] Although, it was useful in the sense that it had to extend credit and helped merchants avoid risk in transport, however, it did not involve a currency exchange – the bill merely permitted merchants in one region to make payments in the same currency in another

---

[76] Ibid.

[77] *"Book of Business Transactions and Rules Concerning Them"*, " in: *the Pillars of Islam Da A Im al-Islam of Al-Qadi al Nu'Man,* Vol II, translated by AAA Fayzee, revised and annotated by I.K.H, Poonawala, 2004, 47. Reference by Thompson p.13.

[78] Ibid.

region.[79] It was neither transferable nor negotiable and was immediately redeemable upon presentation. The issuer (borrower) usually used to charge a fee. If the agent upon delayed payment, he would be sued by suftaja holder in an Islamic court.[80]

The bill of exchange was an important financial instrument that had positive legal standing in both the medieval Islamic and Christian worlds but remained relegated to personal networks only in the former.[81] Like in the Europe, numerous credit instruments were employed in the Islamic world.

Suftaja was made analogous to European bills of exchange, however, the additional element of currency exchange associated with the latter allowed opened a back door for the wealthy European lenders to profit in addition to the exchange transaction. This profit had been derived from two transactions which exploited variations in exchange rates. The lenders who purchased bills of exchange were necessarily involved in inter-regional (and hence inter-currency) commerce with multiple agents. Resultantly, the practice shifted to institutional finance and organizational forms.

The practice shifted to another form. The *Medici* and *Datini* banks emerged in the fifteenth century, in Europe, dealing to some extent in interregional finance and bills of

---

[79] Jared Rubin, *"Bills of Exchange, Interest Bans and Impersonal Exchange in Islam and Christianity"*, p.8, available on: http://www.google.com.pk/url?sa=t&source=web&cd=5&ved=0CCkQFjAE&url=http%3A%2F%2Feconomics.stanford.edu%2Ffiles%2FRubinApr01.pdf&rct=j&q=Bills%20of%20Exchange%2C%20Interest%20Bans%20and%20Impersonal%20Exchange%20in&ei=nATXTNjPEcSecM7P1K4L&usg=AFQjCNE3a4MyobJfRePWDybJYzJ5aWAidQ (Last accessed: 27, Feb, 2010).

[80] The enforceability of such late penalties are exemplified in a case noted by S.D. Goitein (1967, p.243): The bill arrived on the holiday [and, therefore, was not paid; it was payable it seems, to a government office]. Immediately mounted police were sent out carrying an order for a fine of 6 dirham per day." By J. Rubin, p8.

[81] Jarad Rubin, *Bills of Exchange, Interest Bans and Impersonal Exchange in Islam and Christianity*. For more details visit the web site: http://www.google.com.pk/search?hl=en&source=hp&q=Bills+of+Exchange%2C+Interest+Bans+and+Impersonal+Exchange+in+Islam+and+Christianity*&btnG=Google+Search&meta=&aq=f&aqi=&aql=&oq=&gs_rfai= (Last accessed: 02, March, 2010).

exchange. They acted as principals and agents and had to keep themselves about exchange rate fluctuations, capital market and the money market. They conducted transactions primarily with semi-personal relations and extension of the credit network for less personal credit relations to arise from the primary capital holders. Most of financial activities were conducted with unknown relations.

On the other hand, nothing resembling these organizational forms emerged in the Islamic world – instead, *suftaja* was employed only where permanent and direct business connections existed between well-known, closely-knit groups of merchants and bankers. The large, enforceable fees imposed on late repayment of *suftaja* (along with their convertibility upon delivery) made most bankers from issuing large *suftaja* discouraged – if the issuer did not have complete confidence that his partner could pay the debt, he risked incurring such fees (charged to his partner) upon delivery. The dealers were reluctant in the sense that in a world of their personal business relations dependent on repeated interaction, entering into such a contract without assurance that the bill could be paid was a risky job. For this reason, those documents reflect numerous instances of merchants unable to procure *suftaja* and banker were unwilling to issue *suftaja*, encouraging them to instead carry purses of gold specie in order to conduct their business.

The profit which was permissible in *suftaja* business practice borrowers could charge a fee for writing a bill, payable in a distant land. Without the element of currency exchange, there was little incentive for the dealers to employ *suftaja* as an instrument of finance. Instead, investors remained the primary lenders (purchasers), and *suftaja* remained relegated to facilitating trade.

2.2.5 Modern bill of exchange (*Suftaja*)

A bill of exchange is a form of hawalah if the beneficiary is a creditor to the drawer. The drawer is, in this case, the transferor who gives orders for the paying bank to pay a certain sum of money at a specified date to the defined beneficiary. The party executing payment of such amount of money is the payer whereas the beneficiary, i.e. the holder of the bill, is the transferee. If the beneficiary is not a creditor of the drawer, then the issuance of the bill of exchange becomes an agency contract to recover or collect the amount of the bill of exchange on behalf of the drawer.In the absence of a debt obligation between the drawer and the paying bank, the issuance of a bill of exchange becomes an unrestricted *hawalah.*

A bill of exchange is endorsed in a manner that transfers title to its value to the beneficiary is a form of hawalah if the beneficiary is a creditor to the endorser. If the beneficiary is not a creditor to the endorser, the endorsement becomes one of agency contract for collection of the amount of the debt. However, an endorsement on behalf of a client who requires the institution to transfer, after collection, the amount of the instrument into his account does not amount to *hawalah.* This is, however, a contract of agency that is permissible with or without consideration.

It is permissible for the first beneficiary from a bill of exchange to endorse it in favor of any other party. The second beneficiary may also endorse such a bill of exchange in favor of a third party and so on; in such case the revolving of endorsement is a form of successive *hawalah* which is not objectionable in *Shariah.* It is to further add that it is not permissible to disccount bills of exchange by transferring the ownership of their values, before their due date, to an istitution or others for a discounted immediate payment.

The modern *hawalah* based transactions departs somewhat from the earlier practice in that the debt settlement occurs only among *hawaldars* while the liquidity is supplied by other groups, such as labour migrants and refugees, foreign traders and humanitarian agencies. But that is very complex and not applicable in present day while the present day *hawalah* partially fulfills debt negotiation. It can be said that customers operate at the level of the *suftaja* while dealers at *hawalah* based system. In back office terms the *suftaja* thus becomes far more complex than a straight forward transfer of funds through bills of exchange. Its execution entails a long standing relationship between the *hawaladar* who honours the payments instruction and his distant partner who issued the instrument in the first place, in addition to linkages with additional *hawaldars* with whom it is propitous to do business. It can be said that the modern *hawalah* based transactions deviate from fullfilling both the conditions of debt and *suftaja.*

Thus it can be extracted from the above discussion that bank remittances are not based upon the doctrine of *hawalah.* Similarly, they do not fulfill the conditions of *suftaja.* They involve currency exchange, delay in handling money and absence of credit sale. However, as mentioned above *suftaja* did not involve a currency exchange. It was merely permitted to be exchanged in one region to make payments in the same currency in another region. It is one of the possible applications to be based upon *hawalah.* There must be among the traders involving some commercial activity. It can further be added that in *Suftaja* there is the interest of both the lender and the borrower without harm being caused to either one of them. The lender is secured against the danger of the way in carrying the amount in cash. Similarly, the borrower benefits from the loan and is also secure against the dangers of the highway being under an obligation to pay in the said town.

2.2.6 Difference between *Hawalah* and *Suftaja*سفتجه

In *Hawalah* a debtor makes payments in another place through his agent or a second person. On the other hand, *Suftaja* is a loan of money in order to avoid the risk of transport. A lends an amount to B in order that he may pay it to him or C in another place. In *hawalah* the obligation of B to A is already in existence. In *Suftaja*, the obligation of B to A is created on purpose by a payment which A makes to B. However, both have the same effect. Similarly, *Hawalah* is a doctrine upon which transactions will be based. It provides a jurisprudential status to the delegation of debt instead of a concret application. While *suftaja* refers to a bill of exchange as one of the possible commercial instruments based upon *hawalah*.[82]

2.2.7 Remittances through non-banks institutions

Money which is sent through non-banks institutions is also one the known mode sending money. Expatriates of many countries send money to their homes through non-banks institutions. Those who deal such business are called *hawaladars*. If an expatriate wants to send money to his home, he will go to a *hawaladar* instead of going to a bank. The *hawaladar* sends the information to another *hawaladar* in the home town of the customer. The customer tells some secret code to the sender. The sender goes to a local *hawaladar* and collects money by telling the secret code. In this case neither the sender nor the receiver needs a bank account nor fills any lengthy forms. This arrangement is

[82] Goiten also suggests that payment through a third party in another city fell under the general category of transfer of debt; S.D Goitein, A Mediterrarian society: the Jewish communities of the Arab World as Portrayed by the documents of the Cairo Ganiza, 1967-1993, 242. Ref given by p. 16.

called hawalah in most countries like Pakistan and Afghanistan. It is used widely because it a faster and more reliable mode of sending money than banks. This transaction however, is based upon trustworthiness.

2.2.8 *Shar'iah* Appraisal

Whether remittance is through banks or non-banks institutions, it comes under the doctirne of *sarf*. This is not hawalah from the perspective of Islamic law. It is a sale of currency. The hawalah which is found in Islamic law is that it is a convenient arrangement among the traders for payment of debts. Debts are transferred to third persons in order to avoid risk of way and carring huge amounts of currencies. Islamic law has laid down the rule for dealing with debts and their negotiabilities. It says that debts should be goods that are saleable and it should not be created from the sale of currency to be delivered in the future. In other words, Debt should be created throgh the sale of a commodity. Islam prohibits sale of debt to a third party or non-debtor. It further puts restriction that any sale of debt or transfer of debt must be piad at face-value. It, however, permits the selling of debt by its equivalent in quantity and time of maturity or debt trasfer. It is also one of the important rules of Islamic law that the financial transactions involving debt should not be allowed on deferred payment as this would be regarded as interest (*riba*).

It is argued that the transactions become hawalah if the contract of agency is involved.[83] Agency (*Wakalah*) is the appointment of an agent (*wakil*) in place of the principal (*muwakkal*) for the performace of an act authorized by the principal. The *hawaldar* steps into the shoes of an agent while sending money on the customer to his home country through his counter-part *hawaldar* in the home-country of the customer.

[83] Nyazee, *Outlines of Islamic Law*, op.cit., p.259.

What he charges is the service charges which are allowed in Islamic law. The relationship between the customer and the *hawaladar* is that of laoner and loanee. If the transfer is going to be made in the same currency then there is no problem and the *hawaladar* can take his service charges. On the other hand, if a remittance is to take place in a currency different from the presented by the applicant for the transfer, then the transaction consists of a combination of currency exchange and a transfer of money that is permissible subject to the following *Shariah* rules.[84]

a. Both parties must take possession of the countervalues before dispersing, such possession being either acutal or constructive.
b. The countervalues of the same currency must be of equal amount, even if one of them is in paper money and the other is in coin of the same country, like a note of one pound for a coin of one pound.
c. The contract shall not contain any condtional option or deferment clause regarding the delivery of one or both courntervalues.
d. The dealing in currencies shall not aim at establishing a monopoly position, nor should it entail any evil consequences to the interest of individuals or societies.
e. Currency transations shall not be carried out on the forward or future market.[85]

The above rules are required to be followed strictly and violation of any of such rule will amount to interest (*Riba*).

To sum up the above discussion it can be said that working in money exchange to transfer money from place to place and charging for that is permissible. One can also

[84] AAOIFI, *Shariah Standard* No.7 Article, 12/6.
[85] AAOIFI, *Shariah Standard* No.1 Article, 2/1.

work as an agent for this transaction. The condition that the ownership of the money should not be delayed, should be strictly followed because any delay between giving or receiving the money amounts to interest (*Riba*) which is forbidden. This is the ruling of "hand-to-hand" transactions. However, it can not be based upon the doctrine of *hawalah*. There is no harm in earning from *hawalah* in a country where it is banned; however, it must be regulated by the *Shari'ah* limits. Violation of some of the regulatory laws in this regard does not prohibit benefiting from the profits a man gains thereof although abidance by the laws, even those of foreign countries, is obligatory in some cases in order to save the person from danger and accountability. Also, many of these laws were laid in order to achieve public interest, so it is necessary to abide by them.

2.3.1 Cheque

Cheque is derived from *Arabic* word, *Sakk* which means a piece of paper on which some amount of money is specified. Cheque can be traced back to the 9th century when Muslim businessmen/traders used to issue letter or note or document of credit in their tradings. The letter would be a proof of guartenee that the amount specified over it would be paid on specified time. It was appreciated and accepted by most of the traders throughout the world for the reason was that they got rid of carrying large quantitites of currency to far areas. It also minimized the risk of loss in the way for carrying cash currencies.

It was particularly witnessed durinng the trade between Baghdad and China. Cheque was further developed with the development of banking system. However, a stage came when it was confined only to banks. It got its proper legal status when it was included the Negotiable Instruments Act, 1881. In this way it has got legal cover as well

and any dispute related to cheque can be settled through courts. The Act defines cheque as:

"A cheque is a drawn on a specified banker and not expressed to be payable otherwise than on deman".[86]

The law further guides that bank is bound to pay either to the customer or other than customer himself, being bearer of cheque. However, the bearer must be a natural or legal person in due course. The jurisprudence of Cheque further reveals that a cheque may be an ordered or bearer one. Another classification is it will either be open or crossed. It must bear the name and date of the issuer and its validity is for six months.

2.3.2 *Shari'ah* Appraisal

Cheque is considered as based upon the doctrine of hawalah. The legal validity of a cheque drawn by the client upon a bank, contains the elements of *hawalah*. The *muhil* (transferor) is the account holder, the *muhal* is the beneficiary and the *muhal alayh* (transferee) is the drawee bank. In other words, it contains the elements of bill of exchange (*suftaja*). Its history can be traced back to the Companions (God be pleased with them) of the Holy Prophet (SAW). They used to deal in the instruments in the form of bill of exchange, i.e. Cheque.

A cheque can be used for a commercial activity. It will amount to a price for ascerained goods in the form of sale of a debt. The sale will be made to a person other than the one who owes the debt. This is permitted according to the Maliki school if it takes place after possession so that it does not turn into the delaying of the two counter-values.

[86] The Negotiable Instruments Act, 1881, S.6.

However, the Islamic Fiqh Academy did not permitted the use of any kind of commercial papers incluing cheque on discount.[87] It is argued that in reality the discounting of commercial paper amounts to a loan with interest (*Riba*). It affirms that the interest (*Riba*) charged through discounting varies according to the value of the commercial paper and its date of maturity. Such kind of arrangement is strictly prohibited in Islamic law.

Cheques are used for paper money and are sold by banks. But using paper money requires the actual worth of paper must be in existance, particularly in its weight. If the worth is not available, it will amount as based upon uncertainity which is prohibited in Islamic commercial law. It is to further add that banks must have entered in some commercial activity in the real sense agianst which cheques are issued. There must have occurred some give and take of the commodities or assests being the subject matters of different contracts between bank and the customer. It has, however, been noticed that bank is hardly invloved in such activities. This creates the confusion that why a cheque is then issued by bank if some commercial activity has not taken place? Banks have involved itself into many different businesses, it can not be certified as the account holder has been enterered into which of such businesses and why it is not in a position to give money to the account holder.

It is also argued that an issuance of a cheque against a current account is a form of *hawalah* if the beneficiary is a creditor of the issuer or the account holer for the amount of the cheque, in which case the issuer, the bank and the beneficiary are the tranferor, the payer and the transferee respectively. If the beneficiary is not a creditor to the issuer of the cheque, then this is not a *hawalah* transaction because there can be no *hawalah* transaction

---

[87] In its 16th session held in Mecca on 21-26 Shawwal 1422 H. quoted by AAOIFI p.290.

without an existing debt. In the absence of a debt, the transaction becomes an agency contract for recovery of the amount of the debt on behalf of the transferor, which is lawful in *Shari'a*.[88]

If it is considered as loan, by saying, one has loaned the bank Rs.100 from a third party who is also a current account holder at the bank. The first person writes a cheque in the amount of Rs. 100 and gives it to the third party who pays into his current account. The cheque instructs the bank to transfer to the third party the debt that it presently owes to the first person. By transferring ownership of this debt to the third party, the bank has not placed the money in the ownership of the third party. In this way payment for the purchase has been made with a debt, not with money. But such a situation is the clear violation of the Shariah rule, i.e., it is widely prohibited for a debt to be used when paying the capital in a *salam* or *mudarabah* or *sarf* is made. It further worsens the situation as the person receives some benefit in return for giving the bank a loan of Rs. 100 which amounts to interest (*Riba*).[89]

On the other hand, if the transaction between the bank and the depositor is considered as deposit, then the substance of the contract is that the bank is being entrusted to hold the money in a place of safekeeping. Because the bank represents that it is available for immediate withdrawal whenever is desired, it should not be used for other purposes during the period of the deposit. For example, it should not invest one's money without seeking permission. This is would violation of trust. By considering the current account as a genuine deposit of trust then, when something paid by cheque, that cheque

---

[88] AAOIFI Shariah Standard No.7 Section, 12/1.
[89] A discussion on current account available on: http://www.islamic-finance.com/item150_f.htm, (Last accessed: 25, March, 2010).

acts as an instruction requesting that the bank transfers the money held in my name to the name of the third party. In this case, payment is made by transferring money, not by transferring debt.

Another argument made by the bank by considering current account as debt in the sense that the bank has borrowed the money, which has been placed by customers in its current accounts, and that the bank is therefore the owner of such money. If the bank owns the money, it has the right to lend it to others for a commercial gain. But it is impossible for money to be in two places at the same time. It cannot be available for withdrawal by depositors and loaned out to the bank's borrowers. In such a situation, the element of *gharar* is sensed in commercial banking.

Cheques are sold by banks in the forms of traveller's cheques or postal order. These are cheques drawn by in varying values by institutions upon their foreign branches or correspondent institutions in the interest of a traveller who will receive their value by merely presenting them for payment to a party that will accept them. The holder's of a traveller's cheque, the value which has been paid by him to the issuing institution, is a creditor to such an institution. If the holder of the traveller's cheque endorses the cheque in favor of his creditor, it becomes a transfer of debt in favor of a thid party against the issuing institution that is a debtor to the holder of traveller's cheque. This is a restricted transfer of debt and the amount of debt is the value of the cheque for which the institution received payment. It is permissible for the institution issuing it to take commission in lieu of intermediation in such issuance or at the time of its payment provided this does not include interest (*riba*).

It can be argued that cheques are treated as paper money. Islamic commercial law has fixed certain rules for using paper money. One of such rules is that it must be based on quantity of price, say in the form of gold and silver. Since, no actual weight of such price is involved, so it can not be treated as a paper money. If it is supposed that if has some value, then which sale transaction has taken place, for which bank issues cheques for payment to be made later on.

If the beneficiary of the amount of a cheque is a creditor to the issuer, then issuing a cheque against the account of the issuer without a balance is unrestricted transfer of debt if the bank accepts the overdraft. If the bank rejects the overdraft, then this is not considered a transfer of debt, in which case the potential may have recouse to the issuer.

Bank becomes principal debtor, when a person keeps his money with bank and as creditor, if lends. In former case, he must transer his liability, i.e., payment of money by a third person which it does hardly in practice. In latter case, it can not transfer but can be transferred to it. The concept again creates confusion as if the nature of transaction is sale, where is the actual sale, subject matter. In other words, it is based on a thing very uncertain which is strongly prohibited by the Holy Prophet (SAW).

The basis for the permissibibilty of dealing in cheques for banks transfers, when the intention is to transfer the same currency in which payment is to be made, is that it belongs to the category of *suftajah*, which is permissible.

This view is held by the opponents for the validity of *hawalah* that the transferee is indebted to the *muhal* (transferor) with *hawalah* (transfer) being valid for a person who does not owe a prior debt. The second view is that it is an agency for borrowing. Banks

will not accept cheques drawn upon them by clients with no balance except by charging riba-bearing profits that are due from the client along with the value of the cheque. Consequently, if the cheque drawn by the client upon the bank, where he does not have a balance, includes riba-bearing profits it is prohibited; it is not permissible to write such a cheque nor to undertake transactions in it.

The collection of the amount of commercial papers is considered an agency with the client appointing the institution as an agent to collect the value of the paper on his behalf. The institution is entitled to commission that is agreed upon between the client and the institution. In the absence of an agreement between them, the practice prevalent among institutions is to be acted upon.

2.4.1 Paper money and the doctorine of Negotiability (*hawalah)*

Paper money (fiat paper currency) is an alternative form of coin metals made up of precious metals i.e., gold and silver. The replacement was made for the reason that the latter had to face the risk of loss and was too heavy to carry out from one place to another. The worth of a bank note its equivalency to the quantity of gold and precious metals available. so that the worth of the bank note in the form of gold or silver must be available at any time, whenever, it was asked by any one. It got appreciation and the need of issuing notes in greater numbe was felt.

The task of issuing notes was given to the state treasury of a state which assigned the responsibility to state banks. Banks started printing notes in great numbers/quantities with the increased demand but without caring for the quantity of gold or precious metals available. Resultantly, the physical inconvertibility of a note with its worth, i.e., gold or

silver has almost ceased. If a person wishes to get the worth of Rs.100 note from bank, he will get a worth of similar nature, i.e., a paper of Rs.100 from bank. It was also felt that if banks are asked to redeem notes with their actual worth which they can not, the whole banking system will collapse. Bank notes were given legal status by the Negotiable Instruments Act, 1881 by declaring it is a kind of negotiable instruments.[90]

2.4.2 *Shari'ah* Appraisal

Whether bank notes (fiat paper money) can be justified by Islamic point of view is itself a debatable issue. One view is that, paper money can be treated a medium of exchange and measure of value and substitution for dinars and dirhams.[91]

The fiqh academy of Makkah in its meeting held in October, 1986 maintained that paper money has all the chararacteristics of gold and silver. It is thaman from the point of view of Shariah pertaining to riba, zakat, salam and other contracts which are applicable to gold and silver.[92]

The workshop held under the auspices of the Islamic Development Bank in Jeddah in April, 1987 on indexation also concluded that: "Paper money assumes the functions of gold and silver money from the point of view of the applicability of the rules of riba and zakat as well as being the principle of salam contracts, capital of mudarabah or investment in a partnership".[93]

---

[90] The Negotiable Instruments Act, 1881, S.13.
[91] Mansoori, *Islamic Law of Contracts and Business Transactions*, op.cit., p.199.
[92] Rabitah al-Alam al-Islami, Qararat Majlis al-Majma', al-Fiqh al-Islami, pp.96,97.
[93] Recommendations of the Workshop on Shariah position on Indexation (25-26 April 1987) organized by Islamic Development Bank, Jeddah.

The other opinion is that paper money cannot be put in the framework of Islamic law. If the strict legal position of Islamic law is adopted, all transactions in paper currency become invalid. Here is to consider the following definition while critically analyzing the status of paper money.

"A standard of deferred payment on exchange agreements extending into the future."[94]

If paper money is considered as debt from the above definition,[95] then it is a promise or acknowledgment to pay some debt liability. In other words, it is a promise to pay to an unknown person some worth and potentially carries the power of ensuring. The contract is considered as *Hawalah* (endorsement) with the difference that endorsement in the case of money is effective through possession. The claim can be passed on to another person merely by passing on the note; no express endorsement is needed. In this way it shall be subject to the contract of *hawalah.*[96] However, while analyzing critically this concept, any kind of trade in such currencies will amount to exchange of debt (dayn) for a debt (dayn).

In other words, if paper money is considered a debt, then, sarf in such a debt will not be permitted.It is the transfer of the liability to repay a debt from the debtor to the assignee specified in the contract. In this transaction the transfer of liability to repay the debt takes place from the Assigner to Assignee. The assignment of debt is allowed in

---

[94] Ruffin & Gregory, Glenview, Illinois, *Principles of Economics,*: Scot, Foresman and Company, 1983, p.115.
[95] Wills, Primack, Vass & Holmes, Redding, Explorations *in Macroeconomics*, California: CAT Publishing Company, 1989, p.317.
[96] Imran Ahsan Nyaee, *The Concept of Riba and Islamic Banking,* Publishing House 332 Sawan Road, G-10-1, Islamabad, First Edition, p.83.

respect of original amount of debt only, creation of debt due to credit sale among three parties.

2.5.1 Islamic Accepted Bill

The Islamic Accepted Bills were introduced in Malaysia in 1991.[97] They are the Islamic Financial Instruments which are traded in Islamic Inter-bank Money Market.[98] The main arrangement of the transaction is such that bank buys some goods from a customer and sells him/her or a third party those goods for a greater price on a deferred payment basis. In other words, it is an order made by a customer to bank to pay certain amount to the holder of the Bill. The bank pays money in lump sum. It sells the goods for which the money has been paid to the customer on deferred payment basis.

The proponents justify IAB to be Islamic for certain reasons. There is involved a commercial activity in the form of *Murabaha. Murabaha* is a sale of goods at a price based on cost plus profit margin basis which is permissible by Islamic commercial law. It is a form of negotiable instrument which is acknowledged in the form of *Hawalah.*

---

[97] Professor Mohd Ma'sum Billah, Operational Mechanisms of Islamic Accepted Bill. For more details see: http://www.takaful.coop/doc_store/takaful/Islamic%20Accepted%20Bill.doc. (Last accessed: 12, August, 2009).

[98] Nor Mohamed Yakob, *Money Market in Islamic Banking: The Problems of Thin Trading,* Paper presented in the conference on SPTF and Islamic Banking Products, December 1995.

2.5.2 *Shari'ah* Appraisal:

It is analogous to a controversial kind of transaction which is called *baiul in'ah* (buy back transaction).[99] It also contains the element of *Gharar* (uncertainty) as the buyer is incapable of possession of what is bought.

The Holy Prophet (SAW) said:

لَا تَبِعْ مَا لَيْسَ عِنْدَكَ.

"Do not sell what you do not possess".[100]

It is also argued that first debt is created as bank gives money to the customer and bank gets its profit as service charges. With regard to IAB as accepting the status of negotiable instrument, is worth of appreciation. However, it involves the sale of debt as the bank sells the commodity for a greater price and earns the money. But any kind of sale of debt is strictly prohibited by Islamic law.

2.6.1 Letter of Credit

A letter of credit (LC) is a document issued by a financial institution during trades.[101]It is a contract between a buyer and a seller in such a way that a buyer's bank issues a letter of credit to a seller. Seller consigns the goods to a carrier in exchange for a bill of lading. Seller provides bill of lading to bank in exchange for payment. Seller's bank exchanges bill of lading for payment from buyer's bank. Buyer's bank exchanges bill of

---

[99] Sale in which one buys something and then re-sales to the same seller on deferred payment with an increased amount.

[100] Sahib al-Bukhari, , *Kitab-al-Hawalaat, Hadith No: 2281*

[101] See for more details: http://en.wikipedia.org/wiki/Bank_account. (Last accessed: 15th, August, 2009).

lading for payment from the buyer. Buyer provides bill of lading to carrier and takes delivery of goods.

The parties to a letter of credit are usually a beneficiary who is to receive the money, the issuing bank of whom the applicant is a client, and the advising bank of whom the beneficiary is a client. There are other examples of documents which serve as letter of credit like transport document, Insurance certificate, bill of lading, truck reciept etc.

The LC can also be the source of payment for a transaction, meaning that redeeming the letter of credit will pay an exporter. Letters of credit are used primarily in international trade transactions of significant value, for deals between a supplier in one country and a customer in another. They are also used in the land development process to ensure that approved public facilities. Almost all letters of credit are irrevocable, i.e., cannot be amended or canceled without prior agreement of the beneficiary, the issuing bank and the confirming bank, if any. In executing a transaction, letters of credit incorporate functions common to Traveler's cheques.

Typically, the documents a beneficiary has to present in order to receive payment include bill of lading and documents proving the shipment was insured against loss or damage in transit. However, the list and form of documents is open to imagination and negotiation and might contain requirements to present documents issued by a neutral third party evidencing the quality of the goods shipped, or their place of origin.

If the Credit provides for negotiation by another bank – by payment without recourse to drawers and/or bona fide holders, Draft(s) drawn by the Beneficiary and/or document(s) presented under the Credit, (and so negotiated by the nominated bank)Negotiation means the giving of value for Draft(s) and/or document(s) by the bank authorized to negotiate, viz the nominated bank. Mere examination of the documents and

forwarding the same to LC issuing bank for reimbursement, without giving of value / agreed to give, does not constitute a negotiation.

The documentary credit is that the payment obligation is abstract and independent from the underlying contract of sale or any other contract in the transaction. Thus the bank's obligation is defined by the terms of the credit alone, and the sale contract is irrelevant. The defences of the buyer arising out of the sale contract do not concern the bank and in no way affect its liability. Accordingly, if the documents tendered by the beneficiary, or his or her agent, appear to be in order, then in general the bank is obliged to pay without further qualifications.All the charges for issuance of Letter of Credit, negotiation of documents, reimbursements and other charges like courier are to the account of applicant or as per the terms and conditions of the Letter of credit. If the LC is silent on charges, then they are to the account of the Applicant.

2.6.2 *Shariah* Appraisal

Guarantee is a pure donation and must have a zero charge. In other words, any charge on a guarantee is considered in the category of Riba (in Riba you give money as a loan and charge interest, whereas in a letter of guarantee you give only words, a pledge, and it is natural that any charge for these words is even worse than interest because you do not give money). The letter of guarantee as a new contract necessitated by the contemporary and financial situation. It is not similar to the classical guarantees that are

contributory based. It is also permissible for banks to charge customers for issuing letters of guarantee. Most Islamic banks follow the this kind of concept.[102]

Letter of guarantee is justified on the basis of suftaja as well. It is argued that when someone takes a loan from someone else and asks his representative/agent the lender to pay him from his money; this constitutes the suftaja based transaction which is permissible by a group of scholars. In the same way a letter of credit is a kind of guarantee issued by the bank that it pays a sum of money to another party upon the request one of its clients in case of entering in a tender or implementing a project. The beneficiary of this guarantee takes his rights in full in case of any delay or failure on the part of the client to fulfill his obligations. It is further added that the credit letter issued by banks is lawful, because it is either a guarantee or authorization, which are both lawful unless they involve anything which invalidates them (makes them prohibited). Hence, not all cases can be ruled as lawful or unlawful; rather, each case has its own ruling in light of its conditions.

In other words, issuing a letter of credit is a kind of favor and kindness, charging on a favor or a kind act is not permissible in Shari'ah. Moreover, sometimes charging against a guarantee becomes Riba when the guaranteed person does not settle his due, because a bank pays on behalf of his guaranteed client and then takes back from him by force. This procedure is the same as if the bank has lent him the money in advance and charged extra money against the guarantee letter.

---

[102] An answer given by Dr. Monzer Kahf to a question regarding permissibility of bank guarantees, for more details: http://www.islamonline.net/servlet/Satellite?pagename=IslamOnline-English-Ask_Scholar/FatwaE/FatwaE&cid=1119503545328#ixzz0uXR60Psr (Last accessed: 28, March, 2010).

2.7 Conclusion

The chapter argued that most of the transactions are based upon loans instead of debt. The doctrine of *hawalah* is not followed in its real jurisprudence. Some of the transactions like remittances are not even the subject matter of *hawalah*. It can be extracted from the discussion of the chapter that *hawalah* was not a commercial entity. It was rather a courtesy and convenience for traders. Traders had to face the risk of way and carrying cash amounts. The Islamic law gave a convenient way by using instruments as guarantee of payment to them.

It further argued that involving banks in *hawalah* based transactions remained the main bone of contention between the proponents and opponents for the justification of modern application of *hawalah* in different transactions. The proponents gave their justification that what extra amount bank charges is the service charges for the facility it provide to the customers. They further added that the doctrine of *hiyal*, permissibility and analogy could be used for the justification of *hawalah* based transactions by banks. The opponents, on the other hand, questioned as in which capacity bank involve it in *hawalah* based transactions. It does not step into the shoes of real traders nor involving any credit sale for a commercial activity. They further added that the real form of *hawalah*, i.e. *Suftajah* has been rejected by the modern economists. The chapter further discussed that most of the transactions are based upon the doctrine of agency. Agency contracts are permissible in Islam but they can not be mixed up with *hawalah* contracts. The former is stands for the recovery of the amount of debt while the latter means the transfer of liability of payment of debt from the principal debtor against the creditor.

Most of transactions, particularly those involving banks, are directly based upon the laws constituted exclusively on the doctrine of *hawalah*. It can be argued that the legal frame work of *hawalah* is required to be critically examined. In other words, the non-Islamic elements, the *hawalah* based transactions contain, can be extracted if the legal basis provided to the transactions is made according to the injunctions of Islamic law. What are laws made on the basis of *hawalah* and how those laws can be critically examined from the perspective of *Shari'ah* law; this will be discussed in the next chapter.

CHAPTER 3

LEGAL FRAME WORK OF *HAWALAH*

3.1 Introduction

Chapter 2 analyzed the practical application of *hawalah* in different transactions. It was found from most of the transactions had got the legal cover. In other words, the transactions described were such, most of which have been discussed in different laws and have been permitted by some Islamic jurists as according to Islam. While most of the transactions have been found as violating the principles of Islamic commercial law, there is a need to critically examine the laws upon which the transactions are based. It is worth to mention that due to the importance of the doctrine of *hawalah*, laws have been constituted by both Islamic and English legal systems. Historically speaking, the laws related to *Majallah tul-Ahkam al-Adalia*, were constituted in chapter 4. In the same, the Negotiable Instruments Act, 1881 have been related to the principle of *hawalah* on the basis of analogy. It was in 1960, that the Money Laundering Ordinance, 1960, was constituted in Pakistan and was declared to be containing the laws based upon *hawalah*. Recently, the Audit and Accounting Organization for Islamic Institutions (AAOIFI), made mentioned laws for *hawalah* based transactions in its *Shari'ah* Standard No, 7. The main purpose of Majallah and AAOIFI was that the concept should be taken in technical terms while applying in different transactions. It is to argue that there is a need of providing a legal cover to the doctrine of *hawalah* which may be strictly in accordance with the basic principles of *hawalah* and Islamic commercial laws.

Chapter 3 uses the legal framework of hawalah to investigate whether the laws have been properly constituted in accordance with the main concept of *hawalah*. It analyzes different laws from the perspective of Islamic commercial law. It discusses sections of different sections of laws which are needed to be completely deleted or amended or to be described in the form of giving explanations to the respective laws. It further mentions some of the laws, though are worth of appreciation and according to Islamic law; however, they seem to be impracticable in the contemporary economic activities. They have been inappropriately mentioned under the caption of *hawalah*.

3.2.1 Rules drawn by the Negotiable Instruments Act, 1881

The Negotiable Instruments Act, 1881 was constituted by the British Parliament. Prior to the Act, the English Common Law was applied to issues related to negotiable instruments.[103] The Laws were based upon customs prevalent among Anglo-American and European merchants. This was usually known as law-merchant.[104] The economic activities extended to the whole world, particularly, during colonization period. It necessitated the constitution of a uniform law which could for the regularization of the practice of the negotiable instruments. Issues were solved by Indian Courts by the Common Law of British, while between Muslims or Hindus, by their respective personal laws. Resultantly, the Negotiable Instruments Act, 1881 was constituted by the British Parliament. It was constituted with the aim to lay down some law regarding negotiable securities in common

[103] A.M.Choudhry, P.L.D Publishers, The Negotiable Instruments Act, 1881, p.1.
[104] The Negotiable Instruments Act, 1881 details available at http://photographerinme.blogspot.com/2009/03/law-negotiable-instruments-act-1881.html (Last accessed: 02 April, 2010).

use. In this regard, three classes of instruments were specifically included in the law, i.e., negotiation of bills, notes and cheques.[105]

The law was successfully practiced in India, because courts used to decide issues related to instruments on the basis of customs or general local laws of Muslims and Hindus. One misconception had also been developed that the respective personal laws of Muslims and Hindus were devoid of having laws related to instruments. It was further argued that if there had been any such laws, they could be used to decide issues related to instruments cited by the courts.[106] Such cases could be cited as case laws for interpretation their interpretation. After the departure of Britishers, both Pakistan and India, adopted the existing legal system. The Negotiable Instruments Act, 1881 was declared fertile enough to solve instruments related issues. It was argued that the said Act would be amended with the passage of time. In this regard, The Negotiable Instruments (Amendments) Ordinance, XLIX of 1962 was entrusted by the President of Pakistan to amend some provisions.

Negotiable instrument has not been properly defined by the definition class of the Act. It has only mentioned its different kinds i.e., a promissory note, bill of exchange or cheques.[107] It will be very difficult to quote each and every section of the Act and to appraise them through *Shariah* perspective because the sections of the Act are lying scattered. It will be convenient if only the Act is dealt with in a descriptive manner along with relevant section wherever is needed.

The Act has recognized three negotiable instruments, i.e., promissory note, bill of exchange and cheques.[108] The said instruments have been defined in the respective sections, i.e., 3, 4 and 5. Each instrument has a distinct definition. It says a promissory

---

[105] A.M.Choudhry, P.L.D Publishers, The Negotiable Instruments Act, 1881, p.1
[106] See for details: http://photographerinme.blogspot.com/2009/03/law-negotiable-instruments-act-1881.htm, (Last accessed: 05. April, 2010).
[107] The Negotiable Instruments Act, 1881, S. 13.
[108] Ibid.

note is a written promise to pay a certain sum of money unconditionally. He who makes promise is called the maker and to whom the promise is made is called the payee. A bill of exchange is a written order for the payment of a certain sum of money unconditionally. He who makes this order is called the drawer; he to whom it is addressed, the drawer and if he accepts it, the acceptor; he in whose favor it is made, the payee. The signature of the maker or drawer is essential to the making of instrument. A cheques is a species of bills of exchange drawn on a specified banker and always payable on demand. It is intended for immediate payment and needs no acceptance. The drawee of cheques is always a banker and he must pay the cheques if he has sufficient funds. He becomes the principal debtor after acceptance of the cheques.

Each of these instruments must be in writing, with a certain amount of money to a certain person with a certain date, having been properly stamped and the proper designations of the parties. The promise of payment or demand which is made must be unconditional. With regard to date, it is not an essential part of the instrument, however, it becomes a material part in three cases, i.e., where amount is payable at certain time after date; where calculation of interest is involved and where unauthorized alteration in date has been occurred. Payment of stamped duty makes the instrument worth for evidence.

After fulfilling the above requirements of an instrument, the instrument does not said to be negotiated. There is another part of the contract which must be properly fulfilled. It is related to the negotiation of the instrument. It has been defined as, "when a promissory note, bill of exchange or cheques is transferred to any person, so as to constitute that person the holder thereof, the instrument is said to be negotiated.[109]" It means that when such an instrument is physically transferred to any person so as to constitute that person

[109] Ibid, S.14.

the holder thereof, the instrument is said to be negotiated. Negotiability is open until payment is satisfied. Such a transfer has been ruled as of two types, i.e., delivery and Indorsement. Delivery means mere handing over the instrument to be paid to its bearer. It may be actual or constructive but in either case, it must be with the intension to pass the property in instrument. Indorsement on the other hand means when the instrument is indorsed by specified the transferor's name. It may be either in full or in blank; a full Indorsement is the one in which the name of the party is mentioned; Indorsement in blank is the one where the name of the party is not mentioned. Indorsement may be made by the signature of the maker either on the instrument or issuing a separate slip of paper. In either of the case it must contain the purpose of negotiation. It can also be made restrictive Indorsement if it is explicitly worded to restrain the negotiability.

After describing ingredients of a negotiable instrument and delivery to the payee, next step, the Act has ruled out, is the effect of the instrument in the hands of the holder. It has ruled out that all the titles get transfer to the payee if he fulfills the characteristics of a holder in due course. They have been enumerated as a holder in due course is the one who has sufficient cause to believe that the instrument has any defect of title of the maker. In other words, a holder in due course would not be held liable to any kind of offence like fraud or lost or unlawful consideration or incomplete or blank instrument. The payee after getting the status of the holder in due course has to present the instrument to the drawee. The drawee's liability does not arise until he has accepted the instrument. An acceptance is either done by the written acknowledgment on instrument, even it can be written by a single word, 'accepted'. Once the drawee acknowledges the liability, he becomes bound to

make payment. The payment, however, should be made only to the person in possession of the instrument and should be made in good faith and without negligence.

There are special provisions regarding bank-cheques. It divides a cheque into two kinds. It may be either open or crossed; the former is the one which is paid t the counter of the concerned bank while the latter is the one which is paid through another bank. The Act provides some procedure for bankers while making payments to the cheques. They are bound to check the signature of the drawers and make the payment with bonafide intension. It talks about dishonoring of an instrument when drawer or drawee makes default in payment of the instrument. The payee can be compensated along with interest and expenses if he has properly given a notice to the defaulting party within a reasonable time and has made noting of such dishonoring.

3.2.2 *Shari'ah* Appraisal

It is viewed that negotiable instruments are based upon the doctrine of *hawalah*. In both kinds of transactions payment of loan is guaranteed and the transfer is made to a third person.[110] Accpetance of liability of debt is made voluntarilly in *Hawalah* while in that of negotiable instruments, it is made for honor.[111] *Hawalah* has been declared as a doctrine which involves assignment of debt concept and which itself has relaxed the harsh rules for commerical transactions Islamic law which has been further justified on the doctorine of necessity and growing needs of the changed circumstances.

---

[110] Mansoori,' *Islamic Law of Contracts and Business Transactions*. Op.cit., p.310.
[111] The Negotiable Instruments Act, 1881, S.108.

It is a known fact that the present Banking system, even the one introduced in the form of Islamic banking is subject to great criticism as contains the element of interest *(Riba)*. It can be argued that banks do not enter into businesses with their respective account holder with whom debt is going to be transferred. It must have some business and trade with its account holder against which cheques are issued. The analogy of bank draft can be justified when bank gets service charges for providing the facility of sending money to another place. But bank must not mix up the sending money with money which it has invested in other businesses. While, most of the transactions involving Negotiable instruments take place with or within banks.

As it has been discussed that there is great difference between debt and loan which can not be confused while applying *Hawalah* in different transactions. It application is only restricted to *Hawalah* of debt. However, such sort of technicality has not been highlighted in negotiable instrument. The analogy can also be criticised for the reason that there in *Hawalah*, there must be three parties. However, a promissory note – a negotiable instrument involves only two parties. One of a pre-requisite of a negotiable instrument is that it must be based upon a written proof, however, a *hawalah* based transaction must not necessarily be based a written proof, instead, the element of trusworthiness must be taken into consideration which, on the other hand, is not necessitated in negotiable instruments. *Hawalah* transactions are mainly for security, guarantee and interest free businesses purposes but negotiable instrument is used in trasactions which are based on interest and elements like uncertainity, lust for more and more profit and back door transactions which is clear violation of the Hadiths of the Holy Prophet (SAW). It has been narrated,

The Holy Prophet (SAW) said:

لَا تَبِعْ مَا لَيْسَ عِنْدَكَ.

"Do not sell what you do not possess".[112]

Both the transactions contain the element of consideration. In the opinion of majority of Jurists *Hawalah* must be with consideration. The same is the position in the negotiable instruments. It is presumed that every negotiable instrument when it has been accepted, endorsed, drawn, or made was accepted, endorsed, drawn or made for consideration.[113] It is to further add that according to *Hanafis* it is not necessary that the transferee must be the debtor of the original debtor. He may accept his liability voluntarily. In the same way, the same sense is conveyed when an acceptance is made in negotiable instrument for honor.[114]

Similarly, the drawing of a bill or instrument by one bank to another for the benefit of a third person is based upon the doctrine of *Hawalah*. In the same way the *Hanafis* are of the view that it is immaterial whether the drawee is a debtor of the drawer or not because for them it is not a condition that the transferee should be debtor of the transferor but the acceptance by a drawee is a condition precedent for implementation of *Hawalah*. In other words, majority of the jurists do not treat acceptance by the drawee as essential if he is indebted to the transferor or drawer in the same amount. It becomes the transaction of *Hawalah* only if the person in whose name the negotiable instrument is made payable, is a creditor of the drawer. In case he is not a creditor, the instrument creates an agency in which the drawer shall be the principal and the payee shall be his agent. In this case it will be possible to call the instrument as a bill of

[112] Sahib al-Bukhari, , *Kitab-al-Hawalaat, Hadith No: 2281.*
[113] Abd al-Latif Amir, *al-Duyun wa Tawthiquha fi al-Fiqh al-Islamic*, Cairo: pp. 160.161: Reference given by Mansoori.
[114] The Negotiable Instruments Act, 1881, section: 108(a): reference given by Mansoori.

exchange. If the obligation of the drawer towards the first payee terminates or becomes void and the payee endorses the negotiable instrument in favor of the holder in due course and the latter demands its payment from the drawer, the drawer is stopped from pleading termination of his liability as the right of the third person has accrued in this case. The doctrine can be exemplified as if A draws a bill on C. Later on the obligation of the A towards C becomes void, and C then endorses it in favor of D, who is holder in due course. A's liability towards D is not terminated.[115] Such rule has been recognized in Islamic Law as well when the transferee of the liability of the debtor is not competent to defend against claim of the creditor by pleas with which he could defend the action of the debtor unless the debt of the debtor due against him be factually non-existent.[116] The doctrine of *hawalah* was developed in order to cover the other rights and liabilities.[117]The *Hawalah* was followed not only as a guarantee for the payment of debt to the creditor but also as a medium of commercial transactions.

However, it is argued that there is difference between *Hawalah* and the negotiable instrument. The modern negotiable instrument is issued in return for a new cash loan, while in *Hawalah* transactions an instrument must be issued for a pre-existing claim which must be based on a trade transaction.[118] The argument is justified on the basis that a debt under Islamic law can not arise from a business cash loan, because it is only the charitable loan (Qarz hassan) that is permitted which is created only from a commercial transaction of some other type, like a credit sale or (Advance payment)*salam*. It has been further added that Qarz can not arise from a sarf

[115] The Negotiable Instruments Act, 1881, section: 9: reference given by Mansoori.
[116] Mansoori *Islamic Law of Contracts and Business Transactions,* op.cit., p. 312.
[117] Mansoori, *Islamic Law of Contracts and Business Transactions*, op.cit., p. 314.
[118] Nyazee, *" Outlines of Islamic Jurisprudence"*, op.cit., p.293.

transaction. The transfer is, however, permitted without difference of opinion when a debt is created in permissible transactions. In other words, *Hawalah* can be based on what is called a trade acceptance in modern law. A trade acceptance is a bill of exchange or draft drawn by the seller of goods on the purchaser and accepted by the purchaser's written promise on the draft. Once accepted, the purchaser becomes primarily liable to pay the draft.[119] It has been further argued that in modern law there is a distinction between the assignment of rights under a contract and negotiation. In case of assignment the rights belonging to one party may be assigned to another, however, a better title can not be established for the assignee. On the other hand, in negotiation, a better title may be established for the assignee and such a person is usually is called as a holder in due course. This term has been the Negotiable Instruments Act, 1881 and company law.[120] While in Islamic law, the distinction is based upon a better title but the general term used for both assignment and negotiation is *Hawalah.*[121]

3.3.1 Rules constituted by AAOIFI *Shari'ah* Standards

The Audit and Accounting Organizations for Islamic Financial Institutions has made rules regarding in Standard No 7 constituted in 2003. It defines *Hawalah* as A contact of *Hawalah* which is concluded by an offer from the transferor and acceptance from transferee *(Muhaal)* and the payer in a manner that clearly indicate the intention of the parties to conclude a *Hawalah* contract and the transfer of liability or obligation in

[119] Ibid. pp.292,293.
[120] Ibid. p.292.
[121] Ibid.

respect of a debt or right from one party to another party. The transfer of debt must take effect immediately and be concluded on the spot. It must not to be suspended for a period of time and not to be concluded on a temporary basis or contingent on future events. However, it is permissible to defer payment of the transferred debt until a future specified date.[122] The standard has discussed and permitted both the kinds of *hawalah*, i.e., restricted *Hawalah* and unrestricted *hawalah*. It describes a restricted *hawalah* as a transaction where the payer is restricted to settling the amount of the transferred debt from the amount of a financial or tangible asset that belongs to the transferor and is the possession of the prayer while unrestricted *Hawalah* is defined as a kind of transferred debt in which the transferor is not a creditor to the payer and the prayer undertakes to pay the amount of the debt owed by the transferor for settlement, provided that the transfer for payment was made on the order of the transferor. It is permitted to conclude a *Hawalah* on a spot payment basis. This is a *Hawalah* in which the debt transferred to the payer becomes payable on the spot, whether the debt has already fallen due and the obligation is then transferred to the payer for immediate settlement, or the transferred debt is yet to fall due and the transferee has required, as a condition for accepting the transfer, that it be paid immediately by virtue of transfer.

The standard further describes the validity of *Hawalah*. It says the contract must full fill the condition of taking the consent of all parties, namely the transferor, the transferee and the payer. The transferor must be a debtor to the transferee. If in a transaction in which a non-debtor transfers debt to another, the transaction becomes an agency contract instead of *hawalah*. The transaction is said to be a contract for collection of the debt and not a transfer of debt. It is not a condition in a *Hawalah* that the payer must

[122] AAOIFI, *Shariah Standard* No.7 Article, 4.

be a debtor to the transferor. If the payer is not a debtor to the transferor the *Hawalah* will be an unrestricted *Hawalah*. All the parties must be legally competent to act independently. Both the transferred debt and the debt to be used for settlement must be known and transferable. It is a condition for concluding restricted *Hawalah* that the transferred debt or the transferred portion of the debt must be equal to the debt owed to the transferee in terms of kind, type, quality and amount. However, the transferor may transfer a lesser amount of a debt owed to the transferee to be settled from a larger amount owed by the transferor on a condition that the transferee be entitled only to the equivalent amount of his debt.[123]

The Standard has also discussed the application of the doctrine of *Hawalah* in modern transactions i.e., withdrawal from Current account, cheque etc which have been discussed in detail in the previous chapter. Here is to discuss and look analytically the legal position of the related sections. It says an issuance of a cheque against a current account is a form of *Hawalah* if the beneficiary is a creditor of the issuer or the account holder for the amount of the cheque, in which case the issuer, the bank and the beneficiary are transferor, the payer and the transferee respectively. If the beneficiary is not a creditor the issuer of the cheque, then this is not a *Hawalah* transaction because there can be no *Hawalah* transaction without an existing debt. In the absence of a debt, the transaction becomes an agency contract for recovery of amount of the debt on behalf of the transferor, which is lawful in *Shari'ah*.[124]

The holder of a traveler's cheque, the value of which has been paid by him to the issuing institution, is a creditor to such an institution. If the holder of a traveler's cheque endorses the cheque in favor of his creditor, it becomes a transfer of debt in favor of a

[123] AAOIFI, *Shariah Standard* No.7 Article, 6.
[124] AAOIFI, *Shariah Standard* No.7 Article, 12/1.

third party against the issuing institution that is a debtor to the holder of the traveler's cheque. This is a restricted transfer of debt and the amount of debt is the value of the cheque for which the institution received payment.[125]In this transaction only restricted kind of *Hawalah* has been described. Here is to raise the question as what status have been given or should be given to a traveler's cheque from the perspective of Islamic Law if the current practice is not Islamic one and having some reservations either in practice or theory or both?

A bill of exchange is a form of *Hawalah* if the beneficiary is a creditor to the drawer. The drawer is, in this case, who gives orders for the paying bank to pay a certain sum of money at a specified date to the defined beneficiary. The party executing payment of such amount of money is the payer whereas the beneficiary, i.e., the holder of the bill, is the transferee. If the beneficiary is not a creditor of the drawer, then the issuance of the bill of exchange becomes an agency contract to recover of collect the amount of the bill of exchange on behalf of the drawer. In the absence of a debt obligation between the drawer and the paying bank, the issuance of a bill of exchange becomes an unrestricted *Hawalah.*[126] An endorsement of a negotiable instrument in a manner that transfers titles to its value to the beneficiary is a form of *Hawalah* if the beneficiary is a creditor to the endorser. If the beneficiary is not a creditor to the endorser, the endorsement becomes one of agency contract for collection of the amount of the debt. An endorsement of a bill of exchange on behalf of a client who requires the institution to transfer, after collection, the amount of the instrument into his account is not a *Hawalah.* This is a contract of agency that is permissible with or without consideration.

---

[125] AAOIFI, *Shariah Standard* No.7 Article, 12/3.
[126] AAOIFI, *Shariah Standard* No.7 Article, 12/4.

It is also permissible for the first beneficiary from a bill of exchange to endorse it in favor of any other party. The second beneficiary may also endorse such a bill of exchange in favor of a third party and so on, in which case the revolving of endorsements is a form of successive *Hawalah* which is not objectionable in Shari'ah. It is not permissible to discount bills of exchange by transferring the ownership of their value, before their due date, to an institution or others for a discounted immediate payment. This is because the transaction in this manner is a form of Riba.[127] The request of a customer for the institution to transfer a certain amount on money in the same currency from his current account to a particular beneficiary is a transfer of debt if the applicant is a debtor to such a beneficiary. The fee that the institution gains from the transaction is consideration for the delivery of the money and it is not an additional amount gained by the institution over the amount transferred. However, if a remittance is to take place in a currency different from that presented by the applicant for the transfer, then the transaction consists of a combination of currency exchange and a transfer of money that is permissible.[128]

3.3.2 *Shariah* Appraisal

The Standard has mostly discussed the jurisprudence of *Hawalah* irrespective of its modern application in the true sense. The modern applications which have been described are impracticable and most of them are related to Agency contract in which debt is recovered instead of transfer. It is to further argue that only those transactions have been included which are related to banks. It has not talked about *Hundi* and

[127] AAOIFI, *Shariah Standard* No.7 Article, 12/5.
[128] AAOIFI, *Shariah Standard* No.7 Article, 12/6.

Suftajah which are very much related to the doctrine of *Hawalah*. It has neither talked about whether *Hundi* without government permission is permissible or not.

Most of the sections of the Standard are according to the injunctions of Islam, particularly, those sections which are related to the jurisprudence of *Hawalah*. However, some of the sections are subject to deletion, some edited and some require to be explained:

Section No1 states as:

The standard deals with hawalah transactions that involve a change of debtor, i.e. transfer of debt. The scope of this section shall not include banking remittances except the remittances that take the form of hawalah (transfer of debt).

In this section, the scope of *hawalah* has been confined to banking remittances which involve transfer of debt. It means a credit sale should be involved which takes place when some commercial activity occurs. But most of transactions in banks do not take the form of *hawalah*. It has rather, narrowed down the scope of *hawalah* transactions in banks. As it is known transfer of debt is recognized in the doctrine of *hawalah* which is an adjustment for convenience among the traders. Involving banking institutions which do not step into the shoes of traders, in *hawalah* transactions creates a back-door for interest (Riba). It has been witnessed that the concepts of loan and debt have been mixed up. The *hawalah* transactions have been relied on loan basis which is repugnant to the concept of hawlah.

Section No2 states as:

"Hawalah of debt is the transfer of debt from the transferee (Muheel) to the payer (Muhal Alaihi). The transfer of right, on the other hand, is a replacement of a creditor with another creditor. The transfer of debt differs from transfer of right in that

in transfer of debt a debtor is replaced by another debtor, whereas in a transfer of right a creditor is replaced by another creditor."

In this section two concepts have been described. They are concept of transfer of debt and the concept of transfer of right. The concept of debt is self explanatory. However, the transfer of right is subject to explanation. The concept of right is a vast concept. In this section, it has not been mentioned that right should mean the right of the principal debtor against the new debtor and that right must be related to debt. In other words, some debt transaction must have taken place. There can no right except the right of debt.

Section 4/3, states as,

"It is a requirement that a transfer of debt take effect immediately, not to be suspended for a period of time and not to be concluded on a temporary basis or contingent on future events. However, it is permissible to defer payment of the transferred debt until a future specified date."

In the later part of the above section, i.e., '...however....until future date', should be deleted from the section. It has permitted a defer payment for a future date which is against the rule of *hawalah* that the payment can not be permitted for a future date. In other words, the section is self contradictory.

Section 5/1/4 has also allowed a *hawalah* transaction, on 'deferred payment basis'. It can be argued that 'deferred payment basis', has not be explained any where in the said standard. The section can be criticised for two reasons. One, the section has permitted a *hawalah* transaction on deferred payment which is against the doctrine of *hawalah*. So the section should be deleted. Two, an explanation of the words, 'deferred.

payment basis', must be added to the section in order to remove the confusion regarding the words.

Section 12/1 is related to withdrawal from a current account. It is stated as:

"An issuance of a cheque against a current account is a form of hawalah if the beneficiary is a creditor of the issuer or the account holder for the amount of the cheque, in which case the issuer, the bank and the beneficiary are the transferor, the payer and the transferee respectively. If the beneficiary is not a creditor t to the issuer of the cheque, then this is not a hawalah transaction because there can be no hawala transaction without an existing debt. In the absence of a debt, the transaction becomes an agency contract for the amount of the debt on behalf of a transferor, which is lawful in Shari'ah."

The section can also be criticized for the reason that it has related the contract of *hawalah* with a current account in a bank. But current accounts of banks are worth of controversies. The doctrine of *hawalah* is mostly related with credit sales and credit instruments in which parties must be involved in some trade and exchange of commodities. The practical form of such transactions, however, is not found in current accounts of banks. It has included banks which step into the shoes of transferee. But what is the status of a bank. If bank takes the responsibility of payment of debt, then is it allowed for bank to take the extra charges? If the extra charges are considered as service charges then it is to again clear whether bank takes the risk of loss and is it not mixing up the money in other commercial activities and shares its gain with the account holder of the extra amount it gets from such commercial activities?

The analogy of withdrawal from a current account with *hawalah* has been conditioned with the beneficiary to be creditor for to the issuer of the cheque. The

section says withdrawal from a current account is a form of hawalah. But it has not been mentioned which form of *hawalah* as no different forms have been mentioned in the Standard. It is to further argue that such fulfilling such condition is not practicable, particularly in trade activities. In the same section it has pointed out there can be no *hawalah* without an existing debt and the beneficiary must be creditor to the issuer of a cheque. But contradicts section 5/1/2 of the Standard which permits an unrestricted *hawalah* in which the transferor is not a creditor to the payer and the payer undertakes to pay the amount of the debt. A transaction without an existing debt becomes an agency contract. It can be said that the practicable form of withdrawal from a current account is agency instead of *hawalah*. The latter part of the section should be deleted and should be described in a separate Standard to be based upon Agency.

Section 12/2 is related to overdrawing from an account or overdraft. It is stated as:

If the beneficiary of the amount of a cheque is a creditor to the issuer, then issuing a cheque against the account of the issuer without a balance is unrestricted transfer of debt if the bank accepts the overdraft. If the bank rejects the overdraft, then this is not considered a transfer of debt, in which case the potential beneficiary may have recourse to the issuer."

This section also describes an impracticable situation. It is to argue that firstly, cheques are dishonored if there is no balance in the account of an account holder. If the bank even agrees in principle then it can be further argued that it is not an unrestricted transfer of debt as no credit sale and commercial activity has taken place between the bank and the account holder. It has been further ruled that if the bank rejects the overdraft, then this is not considered a transfer of debt, in which case the potential beneficiary may recourse to the issuer. But such situation will open a series of disputes

and litigation which will result in inconvenience. In other words, a potential risk is involved which are mostly not encouraged in commercial activities by traders.

Section 12/4/1 is related to overdrawing from an account or overdraft. It is stated as:

"A bill of exchange is a form of hawalah if the beneficiary is a creditor to the drawer. The drawer is, in this case, the transferor who gives orders for the paying bank to pay a certain sum of money at a specified date t the defined beneficiary. The party executing payment of such amount of money is the payer whereas the beneficiary, i.e. the holder of the bill, is the transferee. If the beneficiary is not a creditor of the drawer, then the issuance of the bill of exchange becomes an agency contract to recover or collect the amount of the bill of exchange on behalf of the drawer."

In this section again it has bee conditioned that the beneficiary must be creditor to the drawer. It to again argue that fulfilling such condition is impracticable. Most of transactions in banks take place irrespective of the condition that the beneficiary should be creditor to the drawer. A bill of exchange is one the most appropriate and suitable application of *hawalah*. However, involving banks institutions in *hawalah* transactions will narrow down the scope of *hawalah*. Banks transactions involve interest (Riba) which can not be trusted al least for *hawalah* based transactions. On the other hand, the Standard has confined the concept only to banks. Similar is the case with sections 12/5 which can be objected for the reasons described above.

Section No 12/6 states as:

"The request of a customer for the institution to transfer a certain amount on money in the same currency from his current account to a particular beneficiary is a transfer of debt if the applicant is a debtor to such a beneficiary. The fee threat the

institution gains from this transaction is consideration for the delivery of the money and it is not an additional amount gained by the institution over the amount transferred. However, if a remittance is to take in a currency different from the presented by the applicant for the transfer, then the transaction consists of a combination of currency exchange and a transfer on money that is permissible."

This section is based upon the rules of remittance (*Sarf*) and its rules must be followed which have been discussed in the previous chapter in details. Here is to point out that the transaction of remittance (*sarf)* is not based upon debt. In this section remittance (*sarf)* has been confused with debt. It is to further add that in case of a remittance *(sarf)* between the same currencies, the transfer of the payment must be on the spot and in the same meeting. But this has not been mentioned in the section. It is required to be included as this is one of the pre-requisites of remittance *(sarf)* transactions. In other words, it has left a loop-hole for encouraging transactions which may involve delay in payment. The very word 'debt' should be deleted from this section. The section has further justified taking additional amount over the remittance as service charge. But here is to argue that money which is involved in remittance *(sarf)* must not be used in other trades and should not be mixed other activities in banks. If the money is even used in other trades, the profit should be shared with the customers. It is to further argue that remittances best fit in Standard No2 of AAOIFI. Here its relation with *hawalah* has been described in such a way which is impracticable in modern transactions. If remittance *(sarf)* is related with *hawalah*, it will create doubts and confusion for other principles of Islamic commercial law, particularly, debt and loan concepts.

3.4.1 The West Pakistan Money-Laundering Ordinance, 1960

The law relating to money laundering constituted in the form of 'The West Pakistan Money-Lenders Ordinance, 1960'. The Ordinance made mandatory the registration and getting license to be issued from the government of Pakistan for dealing in money-lending business. It says that no money-lender shall carry on or continue to carry on the business of money-lending unless he holds an effective license under this Ordinance.[129] It further says that whoever carries on the business of money-lending without possessing of an effective license under the law shall be punished with imprisonment for a term which may extend to six months, or with fine or with both.[130] In this regard it is further made mandatory that every money-lender shall regularly keep record and maintain an account for each debtor separately, of all transactions relating to any loan advanced to that debtor.[131]

3.4.2 *Shari'ah* Appraisal

It is to argue that two concepts, i.e., loan and debt have been mixed up. The two concepts, on the other hand, have distinct jurisprudences. The former has been strictly prohibited, particularly, in trade transactions. The Ordinance has used the word, 'loan', in most of the sections. The word, 'loan', must be deleted from the sections and instead, the word, 'debt', should be written. In its definition class it has defined money-lender as money-lender is the person carrying on the business of advancing loans.[132] Any one trading in advance loans amount to interest *(Riba)*. Similarly, in the definition clause, sub-

---

[129] The West Pakistan, Money Laundering Ordinance, 1960, Section 3 (1)1960.
[130] Ibid. S.19.
[131] Ibid. S.14.
[132] S.1 (m).

sections, debtor has not been defined in proper way; it should be, defined as, 'a person to a debt is advanced.' Sub-section 'k' and 'l', should be completely deleted. Section 16 is related to computation of interest on loans is also confusing as it involves loan for trading purposes so it should be deleted. The Ordinance can be appreciated for the reason that it has given some basis for the trade of money-lending. It must be controlled by the state treasury. It can be analogized to *Hawalah* based transactions if it is properly modified and based upon the footings of Islamic commercial law.

3.5.1 Rules made by *Majallah*

The *Majallah al-Ahkam al-Adalia* constituted rules regarding for the doctrine of *Hawalah* in Chapter No.4 comprising relevant sections i.e., 663-700. *Hawalah* has been defined as a transfer of debt from one liability to another.[133] The liability is created only when some activity has taken place. Here the activity of credit trade should have taken place. Both kinds of restricted and unrestricted *hawalah* have been recognized by *Majallah.* It has defined restricted *hawalah* as transaction in which the principal debtor is the creditor of the new debtor while in an unrestricted *hawalah* the new debtor may not necessarily be debtor of the principal debtor and he can shift the responsibility on the basis of courtesy.[134] *Majallah* has also described elements of *hawalah.* It says there must be shown the intention of the parties entering in the contract of hawalah and such intention must be acknowledged by the parities.

The contract of *hawalah* is contingent upon the consent of the creditor if it is concluded in his absence.[135] All the parties are required to be major and of sound mind.

---

[133] The word *'Dhimah'* has been translated as liability.
[134] *al-Majallah al-Ahkam al-Adalia*, Sections: 678 and 679.
[135] Ibid. 673.

3.5.2 *Shari'ah* Appraisal

The rules made by *Majallah* for *hawalah* can be appreciated for many reasons. This codification recognized the doctrine of *hawalah* in its true jurisprudential spirit. It remained in practice and most of cases/disputes were decided by courts while relying upon its laws. It has confined the rules to the transfer of debt only which is the main requisite of *hawalah*. Only debt principles are to be used while dealing with *hawalah* transactions. The codification of *Majallah* was accepted by Islamic Jurists with consensus. It is to further add that the doctrine has been broken upon into different sections. The sections are convenient way for courts to decide disputes in a shorter span of time. They are also described in such a way that can easily be interpreted with reference to the Classical literature related to the principles of *hawalah*. It is also to view that the rules made by *Majallah* for *hawalah* are worth of application on different transactions in the present times. This will remove the element of interest (*Riba*) from the *hawalah* based transactions. It will confine the concept to debt only. In other words, the justification for the loans transactions to be based upon *hawalah* will be removed. It will keep debt and loan principles at par and confusion regarding nature of different transactions as whether based upon debt or loan, will also be removed.

3.6 Conclusion

Chapter 3 examined the legal frame work regarding hawalah. It discussed different laws based upon the principle of hawalah. In this regard, different sets of laws, viz., i.e. the Negotiable Instruments Act, 1881, the AAOIFI *Shari'ah* Standard No 7, the

Majallah and the Money Laundering Ordinance, 1960 were examined. They were analyzed from the perspective of Islamic commercial principles. The perception that the laws constituted in the Negotiable Instruments Act, 1960 are in compatible with Islamic law on the basis of hawalah is incorrect. In the said Act, the two distinct terms, i.e., loans and debt have been mixed up. Some of the sections in the Negotiable Instruments Act, 1960 containing the element of interest (*Riba*) are to be deleted. Some sections are not clear in the true sense and therefore, needed to be amended or described with explanations. The chapter discussed the laws constituted by *AAOIFI* regarding hawalah. The sections related to the very jurisprudence of hawalah were appreciated up to great extent. However, those related to the application of hawalah in modern transactions have been found as they were subject of agency contracts. The two contracts, viz., hawalah and agency, though, are permissible by Islamic commercial law; however, they have their own distinct jurisprudences were mixed up. The latter stands for the payment of money and the former means the transfer of debt. It has also discussed the Money Laundering Ordinance, 1960. The need of mentioning these laws was that it is to support the argument that the said Ordinance is constituted for remittances. It has no relation with hawalah as remittances are analogous to *sarf* which has been described in details in Chapter 2. The Ordinance can be compared with the rules of *sarf* in a separate study.

The laws of the Majallah related to hawalah were also mentioned. It is has been found that the concept of hawalah has been described in Majallah in the true sense. Such laws can be used for the practical application of different hawalah based transactions. Such laws can be interpreted according to the injunctions of Islamic laws by the Islamic jurists. It will be accepted to the Islamic jurists as well. The rules of Majallah can play a

vital role in the promotion of Islamic banking system as well. It can actively involve Islamic banks in commercial activities in the true sense.

CONCLUSION

The purpose of this study was to examine the application of hawalah in modern transactions. In this respect the main issues, discussed were the jurisprudence of hawalah; its application in different transactions and the legal frame work related to the doctrine of hawalah.

There has been discussed issues like different concepts related to *hawalah* like its literal meanings, definitions, controversies with regard to its historical background, validity, nature, elements, parties and their respective qualification of the parties, essentials, kinds, effect and termination. It analyses the different definitions given by the prominent Islamic jurists. It was found that in whole jurisprudence of hawalah, discussed by classical Islamic jurists, the concept was confined to the transfer of debt only. None of them described the concept as the transfer of loan.

It was further discussed that the concept had even been found and acknowledged in other financial systems as well. It was traced back to the era prior to Islam where it was found that the concept was there in Europe and India.

Two concepts, viz., *qarz* and *dayn* which are distinct principles in Islamic commercial law were also discussed in details. It was necessary for the reason that the main focus of the study is that hawalah is the transfer of debt rather than the transfer of loan. It also described another concept viz., hawalah being the transfer of right. It was explained that hawalah is the transfer of that right which has been created as a result debt, the transfer of the right of the principal debtor to the new debtor. It has been found that even the criticism made by the West for holding hawalah for the promotion of criticism is incorrect.

In the way, the criticism is made depicts that different transactions related to transfer of loans and those involving instruments also become subject to criticism. Most of the transactions discussed in Chapter 2 have been criticised as they were hit by this rule. It was also discussed in order to clear the basic doctrine of Islamic commercial law, i.e., loan and debt should not be dealt with one yard-stick.

It has been examined the application of the doctrine of hawalah in different transactions. The result extracted from the chapter is that most of the hawalah based transactions are used for commercial purposes which are against the purpose of hawalah. It was found that the distinct principles, i.e., debt, loan and right have been mixed up while using the doctrine of hawalah. It was discussed in the chapter that in most of transactions debts have been created without occurring some commercial activity and credit sale against which some debt must have taken place. It has been found that even the criticism made by the West for holding hawalah for the promotion of criticism is incorrect. The way in which the criticism is made is incorrect. In the way, the criticism is made depicts that different transactions related to transfer of loans and those involving instruments also become subject to criticism.

Hawalah was found in the form of *suftaja* and negotiable instruments subject to the condition that some trade activity and credit sale should be involved in different transactions. It was further argued that transactions like bank remittances, *hundi* and money transfer are not based upon hawalah principles. They are, rather, transactions of *sarf* and only they can only be confined to *sarf* rules of Islamic law.

Hawalah requires the existence of debt which is created through some commercial activity. It is a convenient way through which the traders seek to avoid risk of way while carrying cash money for fulfilling trade transactions. It is for this reason that some

instrument is used as a guarantee for payment. Such instruments can not be used for trade purposes as it will amount to sale of debt which is strictly prohibited by the Holy Prophet (SAW). It was further added that hawalah should not be mixed up with the concept of transfer of loan because in this way loans for trade purposes would be encouraged. In other words, it would amount to violation of the principle of Islamic commercial law, i.e. prohibition of loans for commercial purposes.

Some of the transactions which have been discussed in Chapter 2 involve the sale of debt. The debt is transferred in such a way which amounts to sale of debt. It has been described that hawalah doctrine was used exclusively for the commercial purposes instead for a convenient arrangement among the traders. Some of transactions are based upon loans, i.e. loans are transferred among the traders which use loans for trade purposes on the one hand and transfer such loans without involving instruments on the other. Another factor which is violated in hawalah based transactions is trading under deferred payment. Some of *sarf* transactions have been described which involve delaying payments.

It has also been examined the legal frame work regarding hawalah. It discussed different laws based upon hawalah. For this purpose, different sets of laws, viz., different sets of laws were viz., the Negotiable Instruments Act, 1881, the AAOIFI *Shari'ah* Standard No 7, the *Majallah* and the Money Laundering Ordinance, 1960 were examined along with their respective *Shari'ah* Appraisals. It was discussed that the laws constituted in the form of Negotiable Instruments Act, 1960 are in compatible with hawalah on the doctrine of analogy.

However, the analogy was found inappropriate. In the said Act, the two distinct terms, i.e., loans and debt have been mixed up. Thus a back-door has been opened for using loans for commercial purposes. Some of the sections in the Negotiable Instruments

Act, 1960 contain the element of interest (*Riba*) which have been are subject to be deleted. Some sections have been found to be amended and described with explanations. It was found that the laws regarding hawalah in the said Act are not appropriate in the true sense.

It has also been discussed the laws constituted by *AAOIFI* regarding hawalah. The sections related to the very jurisprudence of hawalah were appreciated up to great extent. However, those related to the application hawalah in modern transactions have been found as they were subject of agency contracts. It has been further described the two contracts, viz., hawalah and agency, though, are permissible by Islamic commercial law; however, they have their own distinct jurisprudences which were mixed up. It was further argued that the rules made by Majallah were worth of appreciation. They contain the worth of implementation in modern transactions.

It can further be concluded from the study that the concept of Islamic banking has been acknowledged by international community, with an increasing willingness to accept its products. It has agreed to transform their economies in order to get a harmonization in economies of the world. However, the very concept of Islamic banking and its products are subject to harsh criticism even by Islamic jurists. One reason among other is that Islamic banks are run by the traditional economists who do not know Islamic commercial principles while the Islamic jurists who are specialists in Islamic commercial law are unaware of the modern economic system.

It can also be inferred from the study that Islamic law does not permit that its main principles regarding commercial and trade activities should be violated. It is for this reason that its each and every doctrine has its distinct jurisprudence which is required to follow strictly. Any kind of leniency may harm the rest of the Islamic commercial law principles. This is what has been witnessed in the current study. Most of the transactions fulfill the

basic principles of *hawalah*. The argument can be exemplified by distinct principles of loan and debt which have been mixed up in most of the transactions based upon the doctrine of hawalah.

Recommendations:

The following measures can be suggested:

- The application of *hawalah* in modern transactions should be used only a convenient way of payment among traders and should be confined to credit sales which should have taken place through some commercial activity.
- Only those laws should be adopted which contain the basic structure of the jurisprudence of hawalah. The laws made by *Majallah* can be adopted for the modern transactions of hawalah. In other words, while constituting new laws related to hawalah, the laws of *Majallah* should be considered and should be taken as grund-norm for the transactions based upon *hawalah*.
- Such transactions should be confined to Agency contracts and a separate *Shari'ah* Standard should be constituted in which these transactions should be incorporated.
- Only those laws should be adopted which contain the basic structure of the jurisprudence of hawalah. The laws made by *Majallah* can be adopted for the modern transactions of *hawalah*. In other words, while constituting new laws related to *hawalah*, the laws of *Majallah* should be considered and should be taken as grund-norm for the transactions based upon *hawalah*.

BIBLIOGRAPHY

A) Primary Sources

I) Books

- Ali, Abdullah Yousaf, *The Meaning of the Holy Qur'an*, Markfield/Leicester, Islamic Foundation, 2002.

II) Laws and Acts

1. The Negotiable Instruments Act, 1881.
2. Shariah Standards, 2003 constituted by The Audit and Accounting Organizations for Islamic Institutions.
3. *Al-Majallah al-Ahkam al-'Adaliyyah,*(Codified Civil Law of Ottoman Caliphate, Turkey).
4. Anti Money Laundering Bill, 2010.
5. The West Pakistan Money Laundering Ordinance, 1960.
6. A.M. Choudhry, P.L.D Publishers.
7. 9/11 Commission Final Report, 2002.

B) Secondary Sources

I) Books:

1. Kasani, Ibni Masaood, *Bida'i' al-Sana'i' fi Tartib al-Shara'i'*, Karachi, Education Press, 1979.

2. Mansoori, Muhammad Tahir, *Islamic Law of Contracts and Business Transactions,* Islamabad, *Shari'ah* Academy International Islamic University, 2nd Edition. 2004.

3. Nyazee, Ahsan Imran, *Outlines of Islamic Jurisprudence,* Islamabad, Advanced Legal Studies Institute, 3rd Ed. 2005.

4. Ayub Muhammad, *Understanding Islamic Finance,* John Wiley & Sons Ltd, 2007.

5. Zuhaili Wahbatul, *al-Fiqh ul-Islami wa Adilatuhu,* Damascus, Darul Fiqr al-Muasir, 1984.

6. Tehmaz, *al-Fiqh ul-Hanafi fi Saubil Jadeed,* .....

7. Dasooki, Muhammad ibn Ahmad, *Hashia ul-Dasooki ala al-Sharhul Kabir*, Cairo: Isa al-Babi al-Halabi, 1350 H.

8. Shawkani, *Nayl al Aowtar Shah Munaqa al-Akhbar*, Matba'ah Mustafa al-Halabi, Cairo, 1982.

9. Nabil Salih, *Unlawful Gain and Legitimate Profit in Islamic Law,* Graham & Trotman, 1992.

10. Marginani Burhanuddin, *al-Hidayah Shah Bidayah al-Mubtadi,* Maktabah Imadadiyyah, Multan, Pakistan.

11. Abu 'Abd al-Rahman ibn Shu'ayb Nasai, *Kitabl al-tajarah,* Sunan, Istanbul: Dar al-Da'wah.....

12. Mufti Taqi Uthmani, *An Introduction to Islamic Finance,* Idaratul maarif, Karachi, 1998.

13. Poonawala, I, K, H, "Book of Business Transactions and Rules Concerning Them", " in: the Pillars of Islam Da A Im al-Islam of Al-Qadi al Nu'Man, Vol II, 2004.

14. Ruffin & Gregory, Glenview, Illinois, *Principles of Economics,*: Scot, Foresman and Company, 1983.

15. Atiq al-Zafar, *Riba aur Bank ka Sud translation of Yusuf awis,*Fawaid al-Bunuk hiya al-Riba al-Muharam.

16. Wills, Primack, Vass & Holmes, Redding, *Explorations in Macroeconomics*, California: CAT Publishing Company, 1989.

17. Imran Ahsan Nyaee, *The Concept of Riba and Islamic Banking,* Islamabad, First Edition, Publishing House 332 Sawan Road, G-10-1, Islamabad.

18. Nor Mohamed Yakob, *Money Market in Islamic Banking: The Problems of Thin Trading,* Paper presented in the conference on SPTF and Islamic Banking Products, December 1995.

19. Ibrahim Muhammad, *al-Muqarania baina al-Shariah wa Qanoon ul-Wadai ala Al-Hawalah,* LLM thesis, International Islamic University, Islamabad, 1989.

20. Al-Manshawi, Abdul Hameed, *al-Taleeq ala al-Qanoon al-Tijari al-Jadeed,* Mansha al-Maarif bil-Sikandria, 2005.

21. Abbasi, Ahmad, Manzoor, *Kitabul Fiqh alal Mazahib al-Arbaa* Lahore, Ulema Academy department of Awqaaf, Punjab.

22. Abd al-Latif Amir, *al-Duyun wa Tawthiquha fi al-Fiqh al-Islami*, Cairo. (n.d).

II) Articles/Journals

1. Thompson A. Edwina A., *'Misplaced Blame: Islam, Terrorism and the Origins of Hawala'* in A. von Bogdandy and R. Wolfrum (Ed.), *Max Planck Year Book of United Nations Law*, Vol. 11, 2007, pp 279-305.

2. Schramm. M and Taube M, *Evolution and institutional foundation of the hawala financial system,* International Review of Financial Analysis, Volume, 12, Issue, 4, 2003, pp. 405-420.
3. Sharma Divya, *Historical Traces of Hundi, Sociocultural Understanding, and Criminal Abuses of Hawala,* International Criminal Justice Review—A quarterly journal issued by the Department of Criminal Justice, Georgia State University, Georgia.
4. Glushchenko Galina, *Hawala—A Vestige of the Past in the Service of Globalization*, an Article published in a Russian Politics and Law journal, vol. 43, no. 5, September–October 2005, pp. 28–44.
5. Vaknin Sam, *Hawala, or the Bank that Never Was" Global Politician Magazine*- an article published in the Online International Political News Journal, Storobin & Associates Corporate Offices, 14 Wall Street, 20 Floor New York, N.Y. 10005.
6. Lieber A.E., *Eastern Business Practices and Medieval European Commerce*", an article published in the Economic History Review 21(2) (August) (1968).
7. Rahman Abd Hj Zaharuddin Ust, *Rulings On Debt Trading In Shariah.* Article was published by Business Times, NST, Malaysia on 21st June 2006.
8. *"Order Of The Supreme Court's Appellate Bench In Riba Case"* published in the Review of Islamic Economics, No. 9, 2000, pp.155-194.

III) Internet Sources

1. Action Aid, *Inclusive Circles Lost in Exclusive Cycles*, 2002, www.imf.org/external/np/prspgn/review/2002/comm/v2.pdf

2. A presentation given by Harjit Sandhu on the topic: *Terrorism-Criminal Nexus, Non banking conduits, Vienna, March 2004,* available on: http://www.osce.org/documents/sg/2004/03/2514_en.pdf.
3. *Evolution and institutional foundation of the hawala financial system,*2003. http://www.elsevier.com/wps/find/journaldescription.cws_home/620166/bibliographic
4. *Sahih Bukhari*, http://www.ummah.net/Al_adaab/hadith/bukhari/had37.html.
5. *Historical Traces of Hundi, Sociocultural Understanding, and Criminal Abuses of Hawala,* http://icj.sagepub.com/cgi/content/abstract/16/2/99.
6. *Hawala, or the Bank that Never Was" Global Politician Magazine.* http://www.globalpolitician.com/2882-crime.
7. Debt Transaction. http://www.islamicbanker.com/glossory.html.
8. Ottoman Empire.http://en.wikipedia.org/wiki/Ottoman_Empire#cite_note-3
9. *Rulings On Debt Trading In Shariah.* www.zaharuddin.com. http://www.kantakji.com/fiqh/Files/Finance/169.txt 27/07/09.
10. 16th convention, held at Mekka on 5-10th January 2002. http://in.answers.yahoo.com/question/index?qid=20081118224650AAdnm8X.29/07/09
11. The Time Value of Money Concept in Islamic Finance: *http://i-epistemology.net/economics-a-business/899-the-time-value-of-money-concept-in-islamic-finance.html*
12. Merriam-Webster online dictionary: http://mw4.m-w.com/dictionary/remittance.

13. Marie,Hawala remittance system and moneyLaundering:*http://www.google.com.pk/search?hl=en&q=remittance&start=20&sa=N* http://www.fatf-gafi.org/dataoecd/16/8/35003256.pdf).

14. Delivering Migrant Remittances: the logistical challenge http://www.casas.org.uk/papers/hawala.html

15. *Critical Analysis of the Current Islamic Banking System*: http://www.accountancy.com.pk/articles.asp?id=178

16. Bills of Exchange, Interest Bans and Impersonal Exchange in Islam and Christianity:http://www.google.com.pk/search?hl=en&source=hp&q=Bills+of+Exchange%2C+Interest+Bans+and+Impersonal+Exchange+in+Islam+and+Christianity*&btnG=Google+Search&meta=&aq=f&aqi=&aql=&oq=&gs_rfai=

17. A discussion on current account: http://www.islamic-finance.com/item150_f.htm.

18. Permissibility of bank guarantees, for more details:http://www.islamonline.net/servlet/Satellite?pagename=IslamOnline-English-Ask_Scholar/FatwaE/FatwaE&cid=1119503545328#ixzz0uXR60Psr

19. The Negotiable Instruments Act, 1881: http://photographerinme.blogspot.com/2009/03/law-negotiable-instruments-act-1881.html

20. A.M.Choudhry, P.L.D Publishers: http://photographerinme.blogspot.com/2009/03/law-negotiable-instruments-act-1881.htm.