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EXPLORING ALTERNATIVE TO *BAY' AL-DAYN* CONTRACT IN ISLAMIC BANKS

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Abstract

Global use of bay' al-dayn in the Gulf Cooperation Council and Middle East is limited due to concerns about Shariah compliance, specifically its permissibility. Acceptance and rejection of scholars on bay' al-dayn have created confusion, hindering Malaysian banking products in international markets. Despite 15 years of discussions, Malaysia's Islamic finance industry has not made substantial changes. Bay' al-Dayn offers a debt-securitization option in conventional trade financing adhering to Shariah principles. This research intends to compare the opinions of Muslim scholars and Islamic bank practitioners on the ruling of bay' al-dayn in Islamic banks. The second objective is to examine the application of bay' al-dayn to Islamic banking products. The third objective is to investigate alternatives to bay' al-dayn practiced by Islamic banks. This research uses a qualitative approach, collecting data from Quranic texts, Hadith, related journal articles, and heritage books. Interviews with practitioners from Islamic banks provide practical insights. This study concludes that Shariah compliance, rather than operational issues, is the primary reason for Islamic banks' reluctance to embrace bay' al-dayn, driven in part by the desire to access international markets. As alternatives, bay' al-dayn bi al-sila' and tawarruq are considered suitable replacements. To enhance understanding and innovation in the Islamic banking industry, this research recommends expanding the sample size to study banks rejecting bay' al-dayn and exploring the potential use of bay' al-dayn bi al-sila' in non-banking institutions. These steps could help address the challenges posed by bay' al-dayn and its alternatives while meeting the diverse needs of Islamic finance.

Keywords: *Bay' al-Dayn, Islamic, Banks, Application, Alternative.*

INTRODUCTION

The history and development of Islamic finance can be traced back to the time of Prophet Muhammad. It has similarities to modern banking transactions. Islamic banking promotes an ethical banking system, is recognized worldwide, and is witnessing growth (Hailu & Gambia, 2021; ISRA, 2016). In Malaysia, it began with the establishment of the Pilgrims Management and Fund Board (Lembaga Tabung Haji) in 1969 and Bank Islam Malaysia Berhad as the first full-fledged Islamic bank was established after the enactment of the Islamic Banking Act 1983 (Mohd Thas Thaker et al., 2020). The adoption of *bay' al-dayn* contract, a financial instrument, varies between countries due to differences in Islamic scholars' views. Bank Negara Malaysia (BNM) provides Shariah standards policy documents for Islamic financial institutions (IFIs) but has not issued a specific policy for *bay' al-dayn* due to controversy.

Currently, seven (7) out of 16 Islamic banks and one (1) out of six (6) Development Financial Institutions (DFI) in Malaysia use *bay' al-dayn* in their products, primarily in trade finance (Bank Negara Malaysia, 2023). Thus, the Islamic banks that operate *bay' al-dayn* are Affin Islamic Bank Berhad, Alliance Islamic Bank Berhad, Bank Islam Malaysia Berhad, Bank Muamalat Malaysia Berhad, CIMB Islamic Bank Berhad, OCBC Al-Amin Bank Berhad, and Public Islamic Bank Berhad. Then, Bank Pertanian Malaysia Berhad (Agrobank) is the only Development Financial Institution that operates *bay' al-dayn*. All the information was taken from the banks' websites in 2023.

Although Malaysia is a leader in Islamic finance, criticism surrounds the *bay' al-dayn* products offered in the market, particularly by Middle Eastern Countries scholars (Ismail & Hassan, 2021). This situation arises from concerns about the contract's legitimacy, causing confusion for the public and customers (Radzali et al., 2019). Despite these issues, some Malaysian banks still use *bay' al-dayn*, the criticisms resulted in a lack of capital supply from Middle Eastern investors to the Malaysian Islamic Bond Market. As a result, Malaysian banking and capital market products which are using *bay' al-dayn* were unable to penetrate the international market.

BNM and Securities Commission (SC) have issued resolutions regarding *bay' al-dayn*, namely Shariah Resolutions in Islamic Finance in 2010 (Bank Negara Malaysia, 2010) and Resolutions of the Securities Commission Shariah Advisory Council (Securities Commission Malaysia, 2007), and amendments have yet to be made to this contract, despite more than 15 years of discussion. Islamic banks in Malaysia depend on their Shariah Committees approval on each contract that is used in the banks including *bay' al-dayn*.

Moreover, *riba* (usury) is prohibited by Shariah, and this issue exists in the debt-securitization process implemented by conventional trade financing facilities, requiring the use of a Shariah-compliant contract to make this facility valid (Che Seman, 2002). *Bay' al-dayn* is one of the appropriate Islamic contracts that may be employed in that particular instrument to accord with Shariah rules. This is because the nature of the contract itself obtain debt-securitization to conform with Shariah.

Prior studies made by Radzali et al. (2019) discussed *bay' al-dayn* but lacked in depth in terms of the discussion on the rulings from the viewpoint of the Muslim scholars. Radzali et al. (2019) and Rahim et al. (2013) also introduced *bay' al-dayn* in Islamic banking without delving into its practical aspects, this research examines its application, contributing to better comprehension. Additionally, Khan et al. (2021) discussed acceptance and rejection but lacked detail discussion on the issues of *bay' al-dayn*. Our research offers insights and alternative contracts to address these issues, benefiting Islamic Financial Institutions (IFIs).

This research aims to bridge these gaps by delving into the acceptance and rejection of *bay' al-dayn* from heritage and contemporary sources, its practical application, and potential alternatives. Failure to address these issues can lead to market confusion, reduced transparency, and hindered growth in the Islamic finance sector. Thus, this research intends to fill that gap by exploring classical Muslim scholars' perspectives, providing a more comprehensive understanding on the ruling of *bay' al-dayn* in Islamic banks and compare them to the opinions of Islamic bank practitioners. Examining the application of *bay' al-dayn* in Islamic banking products is the second objective while investigating the potential alternatives to *bay' al-dayn* practiced by Islamic banks is the third objective.

LITERATURE REVIEW

Literal Meaning

The term *'bay''* is derived from *'baa''* (sell), and it signifies the exchange of a commodity, making both contracting parties as sellers. *Bay' al-dayn*, meaning 'Sale of Debt', involves selling a payment right, whether to the debtor or a third party, with immediate or deferred payment (*al-nasiah*) (Amin, 2007). In Islam, *'al-bay'* denotes the contract of sale, governing both sales and purchases. It involves the exchange of desirable items with mutual consent and a specific process (Najeeb, 2014).

'Al-dayn', an Arabic word derived from *'dana'* (debt), encompasses various meanings: loan, selling on credit, absence, death, penalty, or reward. It can also symbolize humiliation and indicate as *'loan'* or *'qard'*, representing something absent or a temporary loan (Ibn Manzur, 2013).

Technical Meaning

The word *al-bay'* (sale) was defined technically with several definitions. According to Hanafi scholars, the word *"al-bay"* (sell) in Arabic means exchange of property for property with mutual consent (al-Zayla'i, 2000). According to Hanafi scholars, the technical meaning of *al-bay'* is the practice of exchanging commodities owned by one person for another with mutual consent, such as the practice of *ijab wa qabul* (offer & acceptance) (al-Tamalawi, 2007).

Meanwhile the Maliki school offers two different interpretations of the meaning of *al-bay'.* In the broadest meaning, *al-bay'* is a net worth deal with no rewards or pleasure. In the most particular meaning, it is a contract of trade for neither advantages nor God's pleasure with equal exchange. One of its replacements being neither money nor silver, and a definite thing other than the *'ain* (object) in it (Ahmad, 2022). Meanwhile, Shafi'is defined *al-bay'* as a financial exchange contract that benefits the property of an object or a benefit for a person endorsement (Ahmad, 2008). According to Hanbali's school, *al-bay'* is an exchange of money, even if it is in the possession or a benefit that is absolutely permissible other than usury and a loan.

Ibn Manzur (2013) defines debt as "All that is not in presence is a debt". Meanwhile *Majalla al-Ahkam al-Adliyyah* in article 158 defines it as "Something that has been determined to be owed". According to al-Zuhayli (2003)*, Al-dayn* in the technical meaning of the jurists has two meanings which are general and specific:

1. *Al-dayn* in the general sense is every fixed right in the life. Whether it is really financial or non-financial, whether it is from the rights of God or the rights of people. Based on this meaning, *al-dayn* was defined as the necessity of a right in the obligation or what was in it *dhimmah* (obligation) or what follows in the *dhimmah.*
2. As for *al-dayn* in the specific sense, the jurists have two (2) opinions about it:
   - The majority of Maliki, Shafi'i, Hanbali, and some Hanafi scholars argue that *'al-dayn'* refers to money fixed in one's life obligation, encompassing various financial obligations, including sales, damages, dowries, and rents. It is considered a debt, even if not in exchange for another debt, but it also includes obligations like zakat.
   - The majority of Hanafi scholars hold the view that *'al-dayn'* specifically pertains to money fixed in one's life obligation, such as the price of a sale, a loan, rent, dowry, or compensation for damaged property. In this context, *'al-dayn'* is akin to zakat, representing an obligation to provide money without it being a substitute for something else (al-Sarakhsi, 1993).

Bay' Al-Dayn

Bay' al-dayn, an Arabic term meaning 'sale of debt', is a transaction where high-quality debt is sold, typically with a low default risk and created through a Shariah-compliant business transaction (Amin, 2007).

The process of *bay' al-dayn* differs from typical sales contracts. It involves selling a debt, either to the lender or a third party, to release the debtor from their obligation (al-Qaradaghi, 2001). The seller often offers a discount to make the sale attractive. *'Dayn'* refers to an owed object, whether monetary or in the form of commodities like food or metal. *Bay' al-dayn* involves the sale of a payment right to the debtor or a third party, with either immediate or deferred payment (al-Zuhayli, 2003). The concept is mentioned in Al-Baqarah, verse 282.

Al-Jassas (2014) points out that the verse includes all types of debt contracts that must be postponed and emphasizes proper recording of such transactions. The term *'al-dayn'* has two meanings based on hadiths. The general meaning encompasses both the rights of God and human rights. The specific meaning relates to property secured on a liability (Al-Qardawi, 2011).

Both Qur'anic and hadith references stress the importance of recording accounts receivable transactions to prevent future disputes. Jurists consider both the general and specific meanings of *'al-dayn'* concerning obligations, contracts, debts, and kinship.

METHODOLOGY

This research employs a qualitative research approach, specifically using inductive inquiry to analyze the identified problem statement. The primary data sources for this study involve library research, including *Turath* (origin) publications and indexed journal articles, as well as semi-structured interviews with informants from Affin Islamic Bank Berhad (Affin Islamic) and Maybank Islamic Berhad (Maybank Islamic), held the position as Head of Shariah Department and Head of Transaction Department. Both informants expressed the need to remain anonymous and to have their names hidden. As a consequence, they will be identified as Informants 1 and 2. Additionally, the study relies on a range of literature sources, such as prominent books, indexed journal articles, and banking websites related to *bay' al-dayn*. Given the limited availability of literature on this subject, the use of semi-structured interviews was essential to gather insights into the practical aspects of *bay' al-dayn* within the Malaysian trade finance industry.

This research draws upon well-established primary sources of Islamic law, including the Qur'an, Sunnah, *Ijma'* (consensus of legal opinion), and *Qiyas* (analogy). These sources are integral to understanding the concept of *bay' al-dayn*. Various Quranic verses and hadiths are cited as core evidence to support the research's objectives, with *Ijma'* considered to explore differing viewpoints among Muslim scholars. All four (4) of these sources are utilized to interpret and comprehend the concept of *bay' al-dayn*. To overcome the scarcity of literature on the subject, semi-structured interviews were employed to complement and reinforce the findings, ensuring the robustness of the study's conclusions.

RESULTS AND DISCUSSION

Opinions Of Muslim Scholars And Islamic Banks' Practitioners Regarding The Ruling Of *Bay' Al-Dayn* In Islamic Banks

The perspectives on the *bay' al-dayn* or Sale of Debt fall into two (2) main categories: Sale of Debt to The Debtor and Sale of Debt to The Third Party. These viewpoints originate from two (2) distinct groups of scholars, namely Classical Juristic Scholars and Contemporary Scholars. Furthermore, each of these opinions is thoroughly justified, and the endorsement of Islamic Banks' practitioners lends further credence to them. A comprehensive explanation of these themes follows.

Historical juristic scholars engaged in a comprehensive discourse on *bay' al-dayn*, reflecting their commitment to reaching equitable decisions that consider all parties involved and aim to harmonize diverse viewpoints. In fact, each scholar offered their unique perspective, supported by justifications and reasoning. This study reveals that the permissibility of *bay' al-dayn* can be divided into two (2) parts: one (1) pertains to situations where the debt is sold to the debtor themselves, and the other pertains to situations where the debt is sold to a third party or another debtor.

Table 1: Permissibility of Sale of Debt to The Debtor Themselves by Classical Juristic Scholar

Classical Juristic Scholar	**Permissibility**
Hanafi, Maliki, Shafi'i dan Hanbali	✓
Zahiri	✗
Hanbali	✓ (With conditions)

Source: (Humud, 2012)

Table 2: Permissibility of Sale of Debt to The Other Debtor/Third Party by Classical Juristic Scholar

Classical Juristic Scholar	Permissibility
Maliki, Shafi'i, some Hanbali	✓ (With conditions)
Hanafi, some Shafi'i, Hanbali, Zahiri	×
Some Shafi'i	✓ (With the exception of Salam debts)
Maliki	✓ (With conditions)

Source: (Humud, 2012)

Table 3: Permissibility of *bay' al-dayn* by Contemporary Muslim Scholar

Contemporary Juristic Scholar	Permissibility
Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI)	×
Majma' Fiqh Islami	×
Shariah Advisory Council of BNM and SC	✓

Source: (AAOIFI, 2015; Bank Negara Malaysia, 2010; Islamic Fiqh Academy & Islamic Development Bank Jeddah, 2000; Suruhanjaya Sekuriti, 2020)

According to the informant, the Shariah concerns related to the *bay' al-dayn* contract are explained. The informant also provides insights from AAOIFI, the global standard-setter for Islamic financial institutions, and BNM's perspective on this contract. There is a significant focus on Shariah issues surrounding *bay' al-dayn*. Some Muslim scholars permit the contract, while others reject it based on their own reasons.

In Malaysia, the regulatory authority holds considerable influence over Shariah compliance matters and allows the practice of *bay' al-dayn*. Consequently, many Malaysian banks continue to use *bay' al-dayn*. The endorsement from the regulatory authority is highly influential in the Malaysian banking industry. However, it is important to note that certain banks are exploring alternatives in alignment with AAOIFI and BNM standards, showing diversity in approaches within Islamic finance. AAOIFI sets global standards adopted by many countries, but Malaysia's regulatory bodies like BNM also have a substantial role in issuing specific guidelines and permissions. Therefore, the permissibility and use of *bay' al-dayn* can vary depending on the regulatory framework and the decisions of the highest Shariah authority in a particular jurisdiction.

In light of this, this research does not advocate the use of *bay' al-dayn* in Islamic financial services but recognizes the need for specific measures and actions. Malaysian Islamic banks should actively explore alternative contracts to replace *bay' al-dayn*, considering options that align with Shariah requirements in expanding the demands their trade finance offerings on an international scale. This will contribute to the advancement of Islamic finance and the overall development of the banking industry.

The Application Of *Bay' Al-Dayn* In Islamic Banking Products

Affin Islamic and Maybank Islamic offer various trade finance products, including Islamic Accepted Bills-i (AB-i) - Sales, Islamic Export Credit Financing i (ECR-i) - Post Shipment, Islamic Domestic and Foreign Bills of Exchange Purchased-i/Authority to Purchased (D/FBEP-i/AP) Sales/Export, and Islamic Onshore Foreign Currency Account-i (OFCF-i) – Exports.

The AB-i - Sales and OFCF-i products utilize the *bay' al-dayn* concept for financing solutions. The AB-i Sales product facilitates the purchase of AB-i from customers, using *bay' al-dayn* as the underlying mechanism, providing efficient financing options (Bank Negara Malaysia, 2003). Similarly, the OFCF-i product serves customers seeking foreign currency financing for onshore activities, leveraging bay' al-dayn principles to maintain Islamic compliance (Radzali et al., 2019).

The Domestic and Foreign Bills of Exchange Purchase (D/FBEP-i/AP) product allows exporters dealing with Letter of Credit (LC) or collection to benefit from the bank's debt purchasing capabilities (Radzali et al., 2019). This product aligns with *bay' al-dayn* principles and offers practical solutions for exporters' cash flow needs. Additionally, Maybank Islamic Berhad plans to transition the ECR-i product to *bay' al-dayn bi al-sila'* to enhance its appeal and align it with Shariah principles, aiming to overcome market restrictions and customer preferences (Maybank Berhad, 2023).

The Alternative For *Bay' Al-Dayn* As Practiced By Several Islamic Banks

In the pursuit of a solution for a challenging contract, the bank has been guided by a fundamental principle in Islamic jurisprudence called *"al-khuruj minal khilaf awla wa afdhal"*. This principle emphasizes the preference for harmony and consensus among scholars rather than engaging in disputes or disagreements.

Bay' al-Dayn bi al-Sila'

Both Affin Islamic and Maybank Islamic have proposed substitutes for the discontinued *bay' al-dayn*, including the introduction of *bay' al-dayn bi al-sila'*. This innovative concept involves the purchase of debt while considering the involvement of tangible commodities. By combining the principles of *bay' al-dayn* with tangible assets, *bay' al-dayn bi al-sila'* addresses past concerns and shortcomings, aiming to enhance transparency, reliability, and compliance within the trade finance products of Affin Islamic and Maybank Islamic. In this approach, debt is sold to a new creditor, with the original debtor receiving payment in the form of commodities such as crude palm oil, plastic resin, and rubber, effectively eliminating interest-related concerns as stated in figure 1 below.

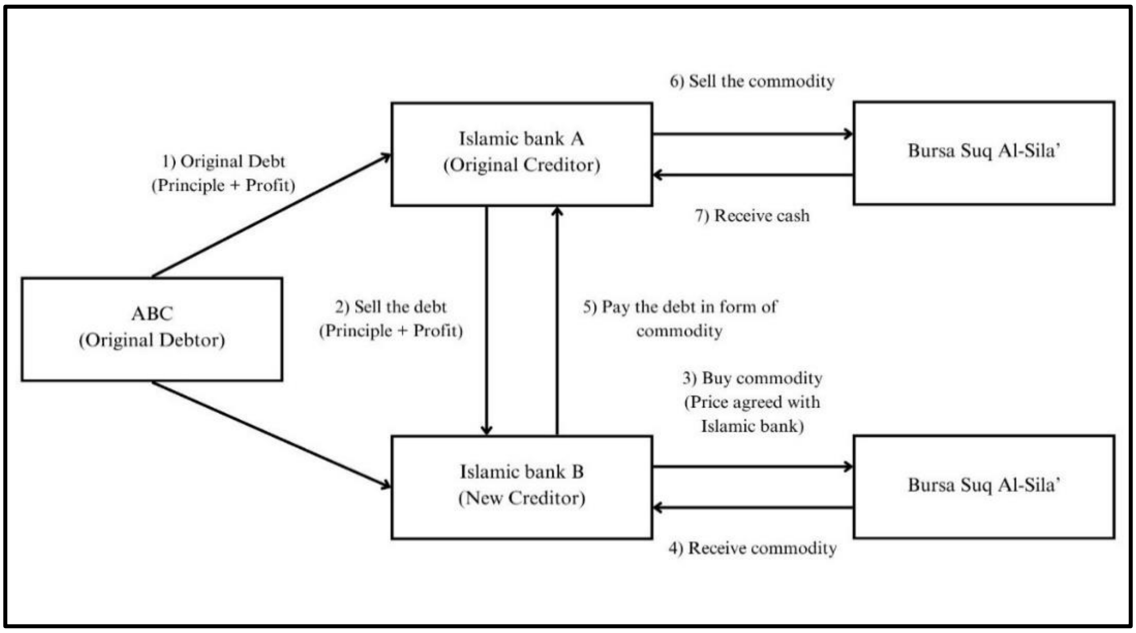

Figure 1: *Bay' Al-Dayn bi Al-Sila'* (illustrated by informant 2)

Figure 1 shows how Islamic banks use *bay' al-dayn bi al-sila'*. Here is how it works:

1. There is a debt between ABC and Islamic Bank A, say RM100k. The bank wants cash before the due date.
2. So, Islamic Bank A sells the debt to Islamic Bank B for RM90k, with RM10k profit.
3. Islamic Bank B buys commodities worth RM90k from Bursa *Suq al-Sila'* to pay Islamic Bank A.
4. Islamic Bank B gets the debt in the form of commodities without a set monetary value.
5. Islamic Bank A sells the commodities on Bursa *Suq Al-Sila'* to get cash.
6. Now, Islamic Bank B owns the debt, and the responsibility for it shifts from Islamic Bank A to Islamic Bank B. This method avoids direct cash payments and allows flexible pricing based on commodity values.

Tawarruq

Tawarruq, also known as commodity *murabaha*, emerges as a widely used and highly effective contract in Islamic finance, particularly in trade and personal financing. *Tawarruq* offers a mechanism to access cash or liquidity without involving interest, a practice strictly prohibited in Islamic finance. This arrangement involves a sequence of transactions where one party buys a commodity on credit and then sells it to a third party for cash at a reduced price as stated in figure 2. The third party subsequently sells the commodity in the market to obtain immediate cash. The bank serves as an intermediary, facilitating these purchase and sale transactions. The client repays the bank at a deferred payment, typically exceeding the cash received, which reflects the bank's profit. This structure enables access to funds without the need for interest-based transactions.

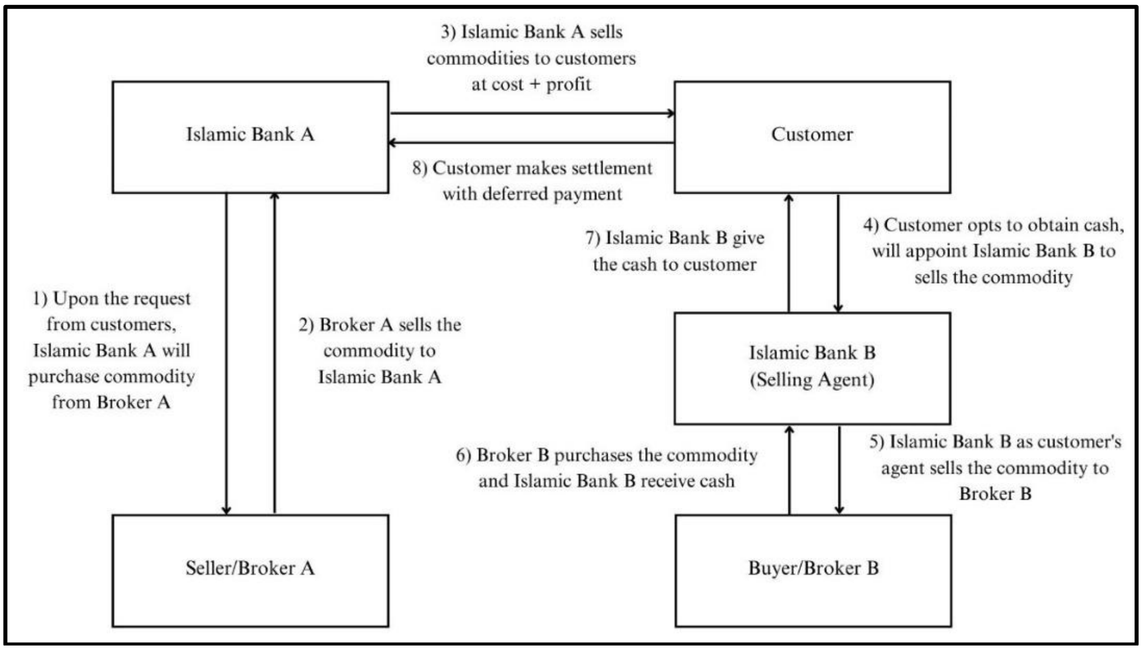

Figure 2: *Tawarruq*

Figure 2 shows how Islamic banks use *tawarruq*. Here is how it works:

1. Customer initiates financing with Islamic Bank A, which then buys a commodity from Broker A on credit.
2. Broker A transfers the commodity to Islamic Bank A.
3. Islamic Bank A sells the commodity to the customer at a deferred price, enabling the customer to own it without immediate payment.
4. The customer appoints Islamic Bank B to sell the commodity to Broker B for instant cash at a discount.
5. Islamic Bank B sells the commodity to Broker B for cash.
6. Broker B buys the commodity from Islamic Bank B and pays in cash.
7. Islamic Bank B provides cash to the customer.
8. Customer repays Islamic Bank A over an agreed period, often in installments, with the bank calculating its profit based on the deferred price and payments.

This research findings suggest that *bay' al-dayn bi al-sila'* and *tawarruq* are effective solutions for Islamic banking institutions like Affin Islamic Bank Berhad and Maybank Islamic Berhad. These innovative approaches align with Islamic finance principles while providing practical alternatives for financial transactions.

CONCLUSION

This research successfully addressed its initial questions, delving into the Shariah issues of *bay' al-dayn* from both a theoretical and practical perspective within Islamic banking products like those used by Affin Islamic Bank Berhad and Maybank Islamic Berhad. It aimed to clarify various aspects of *bay' al-dayn* and explore alternative contracts, such as *bay' al-dayn bi al-sila'* and *tawarruq*, while examining why these banks choose to reject *bay' al-dayn*. This research highlights the primary focus of *bay' al-dayn* in trade finance and its crucial role in supporting commercial transactions within Islamic finance. It emphasizes the importance of aligning Shariah compliance with practical and regulatory considerations at both domestic and international levels. In conclusion, this research provides valuable insights for policymakers, industry practitioners, and scholars, encouraging innovation within Shariah-compliant frameworks. For future research, it is recommended to expand the sample size of banks that avoid *bay' al-dayn*, compare the practices of banks using and avoiding it, explore *bay' al-dayn bi al-sila'* in non-banking institutions, and delve into alternative contracts like *tawarruq*. Additionally, examining the perspectives of Middle Eastern Countries practitioners on Shariah issues arising from *bay' al-dayn bi al-sila'* can offer valuable insights, further enriching our understanding of these topics within Islamic banking.

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