

## APPLICATION OF 'URF IN ISLAMIC AND CONVENTIONAL BANK

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### ABSTRACT

*'Urf or Customary law is one of the most important supporting sources in Islamic law. This can be seen through many legal rulings (ahkam) in Islamic law, which was based on 'urf in which most of these ahkam will change according to the change of circumstances, place and time. As for basis of 'urf or custom, it is the product of the nature of the people and their culture, it grows in strength and popularity by means of imitation that transfers and implants it in the lives of people. Moreover, Contemporary financial system poses great problem and even great challenges to Muslims. Muslims are not permitted by Islamic Law to indulge in ribā. Since contemporary financial system is based on interest, Muslims have great problems in participating in it. Therefore, this paper stands to explain the application of 'urf in Islamic and conventional Bank. The concept and principle of 'urf in Islamic law was critically analysed such as application of 'urf in Islamic law, differences between 'urf and consensus of jurists, also between 'urf and adah, in addition, classification of 'urf, conditions of valid 'urf and so on. Furthermore, the application of 'urf in deposit products under Islamic and Conventional bank were well examined, types of conventional deposit products as well as Islamic deposit products. In fact the product shows that a little different was in-between them which can be easily avoid.*

**Keywords: 'Urf, 'Adah, Islamic & Conventional Deposit Products**

### INTRODUCTION

This article compares the application of 'urf (custom) under Islamic law of banking with the practice of conventional banking. The study is necessary due to the criticisms, especially from the Muslim world, against the practices of Islamic banking system, which is structured after the template of the conventional banking system. The example of such criticisms is as follows:

"Collection of deposits, Islamic banks uses the concept of *mudarabah* to collect deposits whereas conventional banks use interest rates. If one understands the concept of *mudarabah*, one knows that an Islamic bank cannot quote a deposit rate upfront; the return on the deposits will only be known on maturity. In a low-liquidity situation, conventional banks merely hike interest rates, but Islamic banks are helpless to compete.<sup>1</sup>

The comparison is limited to account deposits in both systems of banking. The application of 'urf in Islamic Finance can be traced back as early as from the time of the Prophet (s.a.w). This could be observed through the recognition of certain pre-Islamic practice of transaction by the Prophet, In the *jahiliyyah* period, there were various types of commercial contract practiced by the people and some of these contracts have been approved and practiced in Islam whereas some other have been forbidden. For instance, the contracts that were practice at that time are the contract of sale.<sup>2</sup>

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<sup>1</sup>Saeed, Abdullah, *Islamic Banking and Interest: A Study of Prohibition of Interest and its Contemporary International* (New York: Leiden Brill, 2<sup>nd</sup> Edn., 1999), at 102.

<sup>2</sup>MohamadAkramLaldin, *The Theory and Application of 'urf in Islamic law*, (PhD, unpublished thesis, Edinburgh: University of Edinburgh, 1995), at 113.

There were several types of sale contract, which among others are:

- (1) Sale of goods for goods as an exchange of goods or barter (*muqayadah*). Sale of goods for money, a form of sale commonly being used (*bay'*).
- (2) Sale in which the price was paid in advance, the article to be delivered at a future date, this sale being called (*Salam*).
- (3) Sale with option to revoke (*Khiyar*).
- (4) Sale at less than cost price (*Wadi'ah*).

The contract of *mudarabah* was also known among the people in that period. This contract means that a person who has money will give it to another person to trade and both of them will share the profit according to the agreement between them. The *Quraysh* sent caravans to *Syria* and *Yemen* and on this trip, those who had money would give it to the traders to do business in order to share the profit.<sup>3</sup> Islam has approved this kind of practice. *al-Qard* was another type of contract practiced during that period. This contract means that a person would borrow something including the borrowing of money from another person and upon giving or paying it back the borrower would have to pay usury (*Ribā*) on the goods or money that he borrow.

Islam recognised the contract of *qard* as mentioned in a *hadith* of the Prophet in which he said, "If a Muslim loans to another Muslim, the reward from it is twice that of *sadaqah*".<sup>4</sup> However, Islam has forbidden the practice of usury as mentioned in the *Qur'an* which says "But God hath permitted trade and forbidden usury".<sup>5</sup> This means that Islam preserved the original idea of *qard* with the banning of interest (*Ribā*). This show that Islam has been considered some practice of *jahiliyyah* and not totally abandoned the practice of that period, also taken into consideration some practice of conventional bank as '*urf*' (custom) among the customers, which does not contradict any *Shari'ah* principle. Moreover, as function of *Shari'ah* is to reevaluate or ratify the existing practice when it does not violate Islamic law. Similarly, '*urf*' has been played a good role in Islamic and conventional bank.

The operations of both banks in deposit products are based on '*urf*', which are current, saving and investment account, because they are well known to depositor and depositor. The current account in Islamic and conventional bank operates in the same way, which is accepting deposits from customers. This is also known as the 'demand deposit' as the deposited amount is payable to customer on demand without any notice. As banks use current account at their own risk, the depositors of this types of account are not entitled to any share in the profit earned by the bank. However, operation in savings and investment account is totally different, because in offering Islamic financial services, institutions are bound by a common thread in Islamic finance, where all transactions must compliance with *Shari'ah*.

#### APPLICATION OF 'URF IN ISLAMIC LAW

Lexically, '*urf*' means '*custom*'. It is the noun of the verb of the Arabic word '*arafa*', which means to know as a conventional term.<sup>6</sup> '*Urf*' literally means 'that which is known 'as opposed to "what is unknown". It refers to customs and common practices of a given society whether good or bad. The two words, '*urf*' and '*ma'rif*' are synonymous and are mentioned in the *Qur'an*.<sup>7</sup>

Various definitions of '*urf*' have been given by the Muslim Jurists.<sup>8</sup>

Khallaf defined '*urf*' as, "What is established and practiced by people from their saying and doing, or not doing."<sup>9</sup> The other definition is propounded by Badran who defines '*urf*' as, what is established and common in a group of

<sup>3</sup>Zaydan 'Abdul al-Kareem, *Al-Madkhal Lidirasah al-Shari'ah al-Islamiyah*, (Baghdad: Dar al-Wafi, 1992), at 34.

<sup>4</sup> Al-Shawkani Muhammad Bin 'Ali, *Nayl al-AwtarSharhMuntaqa al-Akhbar Min AhadithSayid al-Akhyar*, (Cairo: Dar al-hadith, 1993), vol. 5, at 347.

<sup>5</sup> Qur'an 2: 275.

<sup>6</sup> Mohammad AkramLaldin, *Introduction to Shari'ah and Islamic Jurisprudence*, (Kuala Lumpur: CERT, 2006), at 117.

<sup>7</sup> Ibn Manzur, Muhammad Bin Karam, *Lisan al-'Arab*, (Beirut: Dar as-Sadir, 1955), vol. 9, at 236-243. See also, Al-Zubaydi Muhammad Bin Mohammad Bin 'Abdu Al-Rozak, (M.H., ED) *Taj al-'Arus min fawdhir al-Qamus*, al-Kuwait: Wizarat al-'Ilam, 1987), vol. 16, at 135.

<sup>8</sup>id., 6.

<sup>9</sup>Khallaf, 'Abd al- Wahab, '*IlmUsul al-Fiqh*, (Kuwait: Dar al-Qalam, 1978), at 89.

people (*jumhur*) from their saying and doing, and is consistently repeated until it influences them and is therefore accepted by their reason".<sup>10</sup>

Al-Zarqa has defined *'urf* as "The behavior of a group of people in their sayings or doings", or recurring practices that are acceptable to people of sound nature.<sup>11</sup> *'Urf* refers exclusively to the common practice which has been established as good by the testimony of reason and has become acceptable to people's disposition (*ma istaqqarratal-nufus alayhi bi-shahadatal-uqulwatalaqqathualtaba'iu'bi al-qabul*).<sup>12</sup>

The above definitions indicate that in order for *'urf* to constitute a valid basis for legal decision it must be the consistent practice of a group of people.

#### **DIFFERENCE BETWEEN 'URF AND 'ADAH**

Word *'adah* is derived from the Arabic root of (*al-'Aodah*) which means "to return" or "to repeat". It refers to a habit or a continuous practice, (*daydan*).<sup>13</sup> *'Urf* and *'adah* are largely synonymous, and the majority of *'ulama* have used them as such. Some others distinguished between them,<sup>14</sup> holding that *'adah* means repetition or recurrent practice, and can be used with regard to both individuals and groups. We refer, for example, to the habits of individuals as their personal *'adah*. However, *'urf* is not used in this capacity: we do not refer to the personal habits of individuals as their *'urf*. It is the collective practice of a large number of people that is normally denoted by *'urf*. The habits of a few or even a substantial minority within a group do not constitute *'urf*.<sup>15</sup> It is the collective practice of a large number of people that is normally denoted by the word *'urf*.<sup>16</sup> Finally, it can be said that there is no clear distinction between the two terms.

#### **DIFFERENCE BETWEEN 'URF AND IJMA' (Consensus of Jurists)**

It would be useful in this connection to distinguish *'urf* from *ijma'*, for they have much in common with one another, which is why they are sometimes confused. Nevertheless, despite their similarities, there are substantial differences between *'urf* and *ijma'*, which may be summarised as follows:

- 1) *'urf* materialises by the agreement of all or the dominant majority of the people and its existence are not affected by the exception or disagreement of a few individuals. *Ijma'* on the other hand requires, for its conclusion, the consensus of all the *mujtahidin* of the period or the generation in which it materialises. Disagreement or dissension has no place in *ijma'*, and any level of disagreement among the *mujtahidin* invalidates *ijma'*.<sup>17</sup>
- 2) Custom does not depend on the agreement of the *mujtahidin*, but must be accepted by the majority of the people, including the *mujtahidin*.<sup>18</sup>
- 3) The rules of *'urf* are changeable and a custom may in course of time give way to another custom or may simply disappear with a change of circumstances. However, this is not the case with *ijma'*. Once an *ijma'* is concluded, it precludes fresh *ijtihad* on the same issue and it is not open to abrogation or amendments.<sup>19</sup>
- 4) Lastly, *'urf* requires an element of continuity in that it can only materialise if it exists over a period. *Ijma'* can, on the other hand, come into existence whenever the *mujtahidin* reach a unanimous agreement, which, in principle, requires no continuity for its conclusion.<sup>20</sup>

<sup>10</sup>Badran, *Usul al-Fiqh al-Islami*, (Alexandri: MuasasaShabab al-Jami'ah, 1984), at 224.

<sup>11</sup>Al-Zarqa, *al-Madkhal al-Fiqhi al-'Amm*, (Damascus: Matabi'AlifBa', 1967), vol.1, at 131.

<sup>12</sup>Al-Siyidi al-Jurjani 'Ali Bin Mahammad, *Kitab al-Ta'rifat*, (Cairo: Dar al-Kutub al-'Ilmiyah, 1978), at 152.

<sup>13</sup>Ibn Manzur, *Lisan al-'Arab*, (Beirut: Dar Ihya' al-Turath al-'Arabi, 1999), vol. 3, at 316.

<sup>14</sup>Ibn 'Abidin Muhammad Amin Bin 'Umar "Nashr al-'Arf fi bina' Ba'di al-Ahkam'ala al-'urf in *Majmu'ahrasa'il ibn 'Abidin*, (Riyad: Maktabah Aramayni, 1980), at 112

<sup>15</sup>Zuhaili, Wahabah, *al-'urf wa al-'Adah*, (1997), at 9-10.

<sup>16</sup>Abu Sinnah, Hamad Fahami, *al-'urf wa al-'Adah fi rayi al-Fuqahi* (2<sup>nd</sup> Edn., 1992), at 34, See also, al-Zarqa, *al-Madkhal al-Fiqhi al-'Amm*, vol. 2, at 872.

<sup>17</sup>Matlub, 'Abdul al-Majeed Mahamud, *Usul al-Fiqh al-Islami*, (Cairo: al-Muktara, 2005), at 196

<sup>18</sup>Ibid.

<sup>19</sup>Id., 15, at 12.

<sup>20</sup>Badran, *Usul al-Fiqh*, at 225. See also, Isma'il 'Ali Ahmad, *al-Adillah al-Mukhtalaffihi Atharuhu fi al-Fiqh al-Islami*, (Cairo: Dar al-Muslim, note dated), at 291.

## CLASSIFICATION OF 'URF

Islamic jurists have developed a classification of the different types of 'urf and have divided them into various types. The classifications are:

### 1. The Verbal Custom ('Urf al-Qawli) and Practical Custom ('Urf al-'Amali).

The verbal 'urf consists of the general agreement of the people on the usage and meaning of words for purposes other than their literal meanings. Because of such agreement, the customary meaning tends to become dominant and the original or literal meaning is reduced to an exception. For example, word *salah*. The literal meaning of this word is *al-Du'a*<sup>21</sup> which means supplication or request, which has, however, been used in the Qur'an to describe the obligatory ritual prayers of the Muslims. This second usage eventually became dominant on as far as the literal meaning of this word is reduced to obscurity.

As for the practical 'urf, it consists of commonly recurrent practices of the people in daily life and in civil transactions. Recurrent practices in normal daily life means the private practices in life, which have nothing to do with other people. Such as eating, sleeping, cultivating and other such matters. The recurrent practices in civil transactions refer to the practices that are meant to avoid causes for legal disputes. This would normally involve two contracting parties. i.e. sales, rents, marriages and other similar contracts. For example of practical 'urf which occurs in normal daily life in the practice of people in certain places of taking vacation on this days, e.g the New Year day. Therefore, taking vacations on this day is considered as a 'urf for a certain group of people and can be used by such a group every year.

### 2. The General Custom('Urf al-'amm) and Particular Custom('Urf al-Khass)

'Urf, whether verbal or in practice is divided into two types; general ('Urf al-'Amm) and particular ('Urf al-Khass). The general 'urf is the common custom that is prevalent everywhere among all people in a matter regardless of the passage of time. An example of this is the contract of *istisnaa*<sup>22</sup> in many matters such as clothing, furniture etc. This type of contract is a necessity and is commonly practiced everywhere. Particular custom ('Urf al-Khass) is 'urf, which is prevalent in a particular locality, professional of trade. This type of 'urf is accepted by the people in a particular place and not in all places. The example for this type of 'urf is such as the practices among the traders in wholesale trading which allow the payment of goods to be deferred to certain period of time, which is not practiced in retail transactions.<sup>23</sup> According to the preferred view of the Hanafi School, special 'urf does not qualify the general provisions of the *nass*, although some *hanafi* jurists have held otherwise. Consequently, this type of 'urf is entirely ignored when it is found to be in conflict with the *nass*.<sup>24</sup>

### 3. The Valid Custom('Urf al-Sahih) and Invalid Custom ('Urf al-Fasid)

Finally, custom is once again divided into valid ('Urf al-Sahih) and invalid custom ('Urf al-Fasid). The valid custom is the 'urf that is practiced by the people, which does not contravene the *Shari'ah* and deny the interest of people and at the same time does not bring corruption.<sup>25</sup> Many of the example mentioned above come within the scope of this type of 'urf. On the other hand, the invalid custom is the custom that is practiced by the people but there is evidence to show that is against the principles of *Shari'ah* or it denies the interest of people or it brings corruption. An example of this type of 'urf is the practice of usury in transactions (paying interest to the customer). Although it is common among many people, it clearly contradicts the clear text of the *Qur'an* and *Sunnah*. Therefore, such transactions are invalid and must be avoided.<sup>26</sup>

<sup>21</sup>Al-Razi, Mahammad Bin AbiBakri, *Mukhtarr al-Sihah*, (Cairo: Dar al-Hadith, 1<sup>st</sup>Edn, 2000), at 368.

<sup>22</sup>"Istisna' means the order for the manufacture of goods at an agreed price. According to a Hadith, "The Prophet prohibited sale of non-existing objects but he permitted salam. The general prohibition in this Hadith would equally apply to istisna' as in this case to the object of sale in non-existing at the time of contract. But since istisna' was commonly practiced among people of all ages, the jurists have validated it on the grounds of general 'urf."

<sup>23</sup>Id., 23, at 119/20.

<sup>24</sup>Kamali Mohammad Hashim, *Principle of Islamic Jurisprudence* (2<sup>nd</sup>edn., 2000), at 290.

<sup>25</sup>Id., 27, at 253.

<sup>26</sup>Mohammad AkramLaldin, *Intriduct to Shari'ah & Islamic Jurisprudence*, (2006),at 120. See also, Khallaf, 'Abdul al-Wahab, *'IlmUsul al-Fiqh*, (12<sup>th</sup>Edn., 1978),at 86.

## CONDITIONS OF VALID 'URF

Muslim scholars have laid down the conditions that must be fulfilled in a customary practice in order to consider it as valid 'urf. Besides being reasonable and acceptable to the people with wise reason and sound behaviour, 'urf in order to be authoritative, must fulfill the following requirements:

- 1) It must be common and recurrent phenomenon. This means that the 'urf must be practiced by the people commonly and frequently in their daily life. The practice of a few individuals or of a limited number of people within a large community would neither be authoritative.<sup>27</sup>
- 2) 'Urf must be in practice at the time of transaction. In contracts and commercial transactions, effect is given only to customs, which are prevalent at the time the transaction is concluded, and not to customs of subsequent origin.<sup>28</sup>
- 3) Custom must not violate the *nass*, that is, the definitive principle of the law. The opposition of custom to *nass* may be either absolute or partial. If it is the former, there is no doubt that custom must be set aside.<sup>29</sup>
- 4) Custom must not contravene the clear stipulation of an agreement. A custom can only be applied if there is no contractual agreement made in a particular transaction. This is because a custom is only an equivalent of an implied condition. The general rule is that contractual agreements prevail over custom, and recourse to custom is only valid in the absence of an agreement. Since contractual agreements are stronger than custom.<sup>30</sup>

## THE BASIS (HUJJIYAH) OF 'URF

The majority of the scholars (*jumhur*) recognized 'urf as a supportive source of the *Shari'ah*<sup>31</sup> and they have quoted several proofs in order to support their view. Among these proofs are:

The verse from al-Qur'an usually quoted in support of 'urf is:

"Keep to forgiveness, enjoin 'urf and turn away from the ignorant".<sup>32</sup>

Many *mufasssirin* suggested that the meaning of 'urf in this verse is synonymous to *ma'ruf* which means anything that is good. Mustafa al-Zarqa', in discussing the proof of 'urf, maintains that the word 'urf in this verse can be taken as a proof of 'urf through its literal meaning which is "the good deed which is acceptable", albeit the meaning of the word 'urf here is different from its meaning as a technical term in *usul al-fiqh*. He further argued that it could be a proof of 'urf (as a technical term) in the sense that the customary practice of people, whether in their doings or their transactions, is normally the practice that is good to them and acceptable by reason.<sup>33</sup>

## 2. The Sunnah

Among the familiar proofs that are quoted by the scholars as an indirect evidence in support of 'urf is the following saying of the prominent Companion, 'Abd Allah b. Mas'ud, that "what the Muslims deem to be good is good in the sight of Allah".<sup>34</sup>

## 3. The Consensus of Jurists (Ijma')

In addition to the above evidences, earlier and more contemporary scholars of Islamic law have agreed that 'urf is an important source in Islamic law. They have not objected to the role of 'urf in solving the problems that arise in Islamic law.<sup>35</sup> This is obvious in the past and present literature of fiqh in which 'urf has been utilised by the jurists to solve many problems of fiqh.<sup>36</sup>

<sup>27</sup> Mahmood Shamam, al-'Urf bina al-Fiqh wa al-Tatbiq, *MajallatMajm' al-Fiqh al-Islami*, (Kuwait: 1988), vol. 4, at 3381.

<sup>28</sup> Al-Jamal Mohammad Mahamood Mohammad, *Tatbiqat al-'Urf*, (Alexandria: Dar al-Fike al-Jamii'. 2008), at 47.

<sup>29</sup> AbuZahrah *Usul al-Fiqh*, (1997), at 127.

<sup>30</sup> Al-Shqar 'Umar Sulaiman, Al-'urf bina al-Fiqh wa al-Qanon. *MajallatMajm' al-Fiqh al-Islami*, (Kuwait: 1988), vol. 4, at 3239.

<sup>31</sup> Badran, *Usul*, at 226, See also, Isma'il, Adillah, at 396.

<sup>32</sup> Ibn Kathar Imam Ad-Din Isma'il bin 'Umar, al-Qurash, *TafsirbnKathir*, (Riyadh: D'Er as-Salam, 2000), vol.4, at 240

<sup>33</sup> Al-Zarqa, *Al-Madkhal*, vol. 1 at 133.

<sup>34</sup> This Hadith was related by Ahmad b. Hanbal in his *Musnad* and is considered as *mawqaf* because the chains (sanad) stop at 'Abd Allah b. Mas'ud.

<sup>35</sup> Badran, *Usul*, at 226, Kamali, principles, at 372, Zaydan, al-Wajid, at 254.

<sup>36</sup> Mohamad, AkramLaldin, *Itroduction to Shari'ah & Islamic Jurisprudence* (2006), at 124.

### LEGAL MAXIMS (*al-Qawa'id al-Fiqhiyyah*) UNDER 'URF

The legal maxims of *fiqh* (*qawa'idkulliyya al-Fiqhiyya*) are as a distinctive general of *fiqh* literature side by side. There are some important legal maxims that are derived from the statement of Ibn Mas'ud that "what the Muslims deem to be good is good in the sight of Allah", Legal maxims that is recorded by the Shafi'i jurist (al-Suyuti), in his well-known work,<sup>37</sup> 'What is proven by 'urf is like that what is proven by *Shari'ah* proof.' This legal maxim is also recorded by the Hanafi jurist (al-Sarakhsi), and was subsequently adopted in the Ottoman *Majallah*, which provides that custom, whether general or specific, is enforceable and constitutes a basis of judicial decisions.<sup>38</sup> Therefore, there are many legal maxims in *fiqh* formulated by the jurists that have described the role of 'urf that can affect the decision on certain matters. However, the maxim, which read as (*al-'Adah Muhakkamah*)<sup>39</sup>, is considered by al-Suyuti, Ibn Nujaym and al-Zarqa as the main maxim and all the other maxims related to 'urf are regarded as branches of this main maxim. These branches indicate the different types of 'urf and the conditions of a valid 'urf. These can be seen at footnote.<sup>40</sup>

### APPLICATION OF 'URF IN DEPOSIT PRODUCTS UNDER ISLAMIC AND CONVENTIONAL BANK

The fundamental difference between Islamic banks and the existing commercial banks is the avoidance of *ribā* in Islamic banking. Islamic banks are also universal or multipurpose banks and not purely commercial banks - a crossbreed between commercial banks and investment banks, investment trusts and investment-management institutions. Since the Islamic bank would share in the risks of the consignment, venture, business or indemnity, it would need to be more careful in the evaluation of applications.

The activities of the bank will be based on the commercial transactions allowed in Islam, including *mudarabah*<sup>41</sup>, *Ijarah*<sup>42</sup>, *Bay' bi-Thaman 'Ajal*<sup>43</sup> and *Murabaha*.<sup>44</sup> During the 1970s, efforts were made in various Muslim countries to establish Islamic banks. The objectives of these Islamic banks in general have been to promote, foster and develop the application of Islamic principles, law and tradition to the transaction of financial, banking and related business affairs.<sup>45</sup>

### CONVENTIONAL DEPOSIT PRODUCTS

Conventional banks play an essential role in an economy as an intermediary between those who have surplus money to deposit (that is, lending to the bank) and those who have a need for money (borrowing from the bank). By accepting deposit from customers and lending the money out in terms of a loan, the bank is able to not only earn a profit but also enable commerce to take place in the process. Without the bank as intermediary, surplus

<sup>37</sup> al-Suyuti, Jalalu al-Din, *al-Ashbahwa al-Nazair* (Riyad: MaktabahNazarMustofa al-Baz, 2<sup>nd</sup> edn., 1997), vol. 1, at 148.

<sup>38</sup> Document; 'Urf and Istishab, Retrieved from <[http://www.witness.pioneer.org/vil/Books/SH Usul/urf](http://www.witness.pioneer.org/vil/Books/SH%20Usul/urf)>. December 16, 2011.

<sup>39</sup> Kamali, Mohammad Hashim, *Qawa'id al-Fiqh: The Legal Maxims of Islamic Law, The Association of Muslim Lawyers*, (UK: 2008), at 3.

<sup>40</sup> (*al-Ma'rufu'urfankal-mashrutushartan*), (*Inamah- tu'tabar al-'adah idhataradat aw aglabat*), (*Al-'Ibarat Lil- galib al-shai' la lil-nadir*), (*al-Haqiqahatrukbidilalah al-a'dah*), (*Isti'mal al-anashujahyjb al-'Malubeha*), (*Isti'mal al-Anashujahyjb al-'Amalubeha*), (*al-Ta'yin bi-al-'urf ka-ta'ayin Bi al nass*), (*La yunkartagyir al-hakambitagyir al-'Uaman*), (*al-Ma'rufbayna al-Tujarkal-mashrutbaynaum*), (*al-kitabkal-Khita'b*), (*al-Ishar'at al-Ma'hudahlil-'akhrasKal-Bayan Bilisan*).

<sup>41</sup> Profit-Sharing. A contract of profit sharing where one party contributes his entrepreneurial efforts while the other provides capital.

<sup>42</sup> Leasing. Refers to an arrangement under which the lessor lease an equipment, a building or other facilities to a client at an agreed rental against a fixed charge, as agreed by both parties. For example, a contract under which a bank purchases and leases out equipment required by its client for a rental fee.

<sup>43</sup> Deferred payment sale. A sale of goods contract on a deferred payment basis at a price, which includes a profit margin agreed by both parties. The client may be allowed to settle payment by installment within a pre-agreed period.

<sup>44</sup> Cost-plus or sale with determined mark-up. Commodity exchanged for is delivered immediately and sale price, comprising cost-plus profit margin, is paid in lump sum at a later date. In other words, it refers to the sale of goods at a price, which includes a profit margin as agreed by both parties. Such sales contract is valid on the condition that the price, other costs and profit margin of the seller are stated at the time of the agreement of sale.

<sup>45</sup> 'Ali Adnan Ibrahim, *The Rise of Customary Businesses in International Financial Markets: An Introduction to Islamic Finance and the Challenges Of International Integration*, (2008), *AM. U. International law. Revival*, at 665. See also, Ahmad Ibrahim, *Legal Framework of Islamic Banking*, Volume: 1, Issue: 1. (1997), *Journal Undang- Undang: IKIM Law Journal*, at 1.

funds could remain idle while customers who need funds to carry out business will find it difficult to do so. The economy would sputter along as a result.

### **Deposit Accounts**

When you open a deposit account with a bank, your money is securely kept by the bank and you can subsequently withdraw that money on demand. Banks may charge a fee for this service as well as pay you some interest on your deposited funds. There are three main types of deposit accounts- cheque checking accounts, saving accounts and fixed deposit-although there are many variations of these.<sup>46</sup> The types of deposit accounts under Conventional Deposit Accounts are as follows:

### **Current Accounts or Checking Accounts**

Current accounts or Checking accounts allow you to write cheques on the money you have in your account. These accounts usually earn no interest or pay the least, compared with savings accounts and fixed deposits. The purpose of a checking account is to securely and quickly provide frequent access to funds on demand, through a variety of different channels for transactions. Checking accounts are not meant for earning interest or for savings, but for the convenience of business and personal users. Hence, they usually do not bear interest.<sup>47</sup>

### **Savings Accounts**

Savings accounts pay interest but cannot withdraw such as by writing a cheque. These accounts let customers set aside a portion of their liquid assets while earning a monetary return. Obtaining funds held in a savings account may not be as convenient as a checking account. For example, one may need to visit an ATM or bank, instead of just writing a cheque. Some savings accounts may even limit the withdrawals, payments and transfer that you can perform every day. True saving accounts do not offer cheque-writing privileges, although some institutions may call their higher-interest, checking accounts "savings accounts."<sup>48</sup>

### **Fixed/Investment Deposits**

A fixed deposit usually pays interest but cannot be withdrawn for a certain term or period. When the term is over, it can be withdrawn or it can be rolled over (that is held for another term). The longer the term, the better will be the yield on your money.<sup>49</sup>

## **ISLAMIC DEPOSIT ACCOUNTS**

Based on legal maxims under the concept of *'urf* which are a matter recognised as customary amongst merchants is regarded as if agreed upon between them, (*al-Ma'rufbayna al-Tujarkal-mashrutbaynaum*),<sup>50</sup> a matter established by custom is like a matter established by a legal text, (*al-Ma'rufu 'urfankal-mashrutushartan*).<sup>51</sup> Islamic Deposit Accounts are like Conventional banks, Islamic banks rely on depositor's funds as well as their own capital as major source of funds. Therefore, Deposits are mainly in the form of current deposits (demand accounts), savings and time deposits.<sup>52</sup>

### **Current Accounts**

For a conventional bank, a current deposit facility is a deposit facility in which the owner is entitled to receive his or her funds on current and to write cheques on the account, which transfers legal ownership of funds to others. This facility is widely known as current account and is designed for those who need money for transaction purposes. The purpose of using this facility is for convenient or to make payments for daily commitments. Interest is seldom paid on this account. In fact, commercial banks in some countries will impose a moderate service fee on this account, besides charging the unavoidable cost such as the cost of the cheque book and stamp duty.

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<sup>46</sup> ABDULLAH Daud Vicary & CHEE Keon, *Islamic Finance why it makes sense*, (Singapore: Marshall Cavendish Business, 2010), at 118.

<sup>47</sup> *Ibid.*, at 119.

<sup>48</sup> *Ibid.*

<sup>49</sup> *Ibid.*, at 120.

<sup>50</sup> Majallah Al-Ahkam: Article 44.

<sup>51</sup> *Ibid.*, Article 43.

<sup>52</sup> Lee Mei Pheng & Detta Ivan Jeron, *Islamic banking & Finance Law*, (Selangor: Pearson Longman, 2007), at 59.

There are, however, current deposit facilities which provide returns to account holders. In the US for example, commercial banks are allowed to provide the NOW Account (Negotiable Order of Withdrawal) facility. NOW accounts are just current deposits that pay interest. The banks, however, have the option to request seven days' notice period to withdrawal of funds from these accounts. Similarly, in Malaysia, some commercial banks provide current account facilities that pay interest. There are, however, certain conditions to be fulfilled before account holders are entitled to receive interest.<sup>53</sup>

Since this account can be devoid of the interest element, Islamic banks are permitted by *Shari'ah* to offer similar facilities. Generally there two *Shari'ah* principles, that is, *qard hassan* and *wadi'ah* which are used by Islamic banks in providing this facility. Islamic banks in some countries clearly indicate that they accept current deposit, which is based on the principle of *qard hassan*. The Law Usury- Free Banking of 1983 in Iran, for instance, specifies that current bank accounts in Iran be operated on *qardhassan* basis. Similarly Dubai Islamic Bank of the United Arab Emirates and the Kuwait Finance House of Kuwait use the principle of *qardhassan* to govern their current deposit facilities. Among Islamic banks, which apply the principle of *wadi'ah*, are banks in Bangladesh, Jordan and Malaysia. In Malaysia, however, instead of *wadi'ah*, the principle is called *wadi'ah yad damanah* or 'guaranteed custody'.<sup>54</sup>

In Jordan, the current deposit facility is known as the 'trust accounts' facility.<sup>55</sup> For example, states:  
Trust accounts are cash deposits received by the bank where the bank is authorized to use the deposits at its own risk and responsibility in respect of profit or loss, and which are not subject to any conditions for withdrawal and depositing.<sup>56</sup>

Trust accounts, which are available at the Jordan Islamic Bank, are further divided into two types of accounts called 'current' and 'demand'. Current account services offered by the Jordan Islamic Bank are basically the same as those offered by the other Islamic and conventional banks. In the case of demand deposits, balances are represented by pass-books. Deposit and withdrawal are made upon presentation of these pass-books. In short, the Jordanian demand deposit is a current account without chequing facilities. Islamic banks in some countries do not indicate the types of *Shari'ah* principles that govern their demand deposit facilities. However, monetary authorities of some countries do issue rules and regulations pertaining to current accounts to be followed by Islamic banks.<sup>57</sup>

#### The Obligation of Banks and account Holder in Current Account

The elements usually apply in the contract between Islamic banks and current account holders:

1. Money given to the bank will be considered as a loan if the principle of *qard hassan* is applied, but the money is given to the bank for safe custody when the *wadi'ah* principle is used.
2. If the deposit is made under the principle of *wadi'ah*, the bank seeks permission from customers to use these deposit at the bank's own risk as long as the funds remain with the bank. Permission is not needed under the principle of *qard hassan*. No reward will be given to the customers.
3. The account holders may withdraw a part or the whole of their deposits at any time they so desire, and the bank guarantees to honour such requests.
4. Both parties will abide by the rules and regulations related to the operational aspects of demand deposit accounts.<sup>58</sup>

There is little difference between conventional banks and Islamic banks as far as the operation of current accounts is concerned. However, the common features of these accounts, as operated by Islamic banks, are listed below:<sup>59</sup>

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<sup>53</sup> Ibid.

<sup>54</sup> Ibid., at 60.

<sup>55</sup> The Jordan Islamic Bank for Finance and Investment Law No 13 of 1978.

<sup>56</sup> Id., 55.

<sup>57</sup> Ibid.

<sup>58</sup> Ibid., at 62.

<sup>59</sup> Ahmad Ausaf, Contemporary Practices of Islamic Financing Techniques, (Jeddah: Islamic Research and Training Institute, Islamic Development Bank, Saudi Arabia, 1993), at 4.

1. This facility is available to all parties who have the capacity to contract. In the case of an individual, for example, only a person who has reached maturity age as stipulated by Islamic jurisprudence is allowed to maintain an account with the bank. According to Islamic jurisprudence, only a person who is '*aqil*' and *ba'ligh*<sup>60</sup> has the capacity to contract. Although the maturity age according to the majority Islamic jurists is 12 years old, banks usually conform to the age established by common law and usually, no individual below 18 years old is permitted to open a current account.
2. For business entities, Current accounts govern what is commonly known as call deposits or demand deposits. These accounts can be opened either by individuals, companies, clubs, societies and associations, certificates of registration and documents such as memorandum and articles of association, and the minutes of meetings relating to the opening of an account must also be present to the bank. In domestic currency or in foreign currency, if the bank is allowed to operate in the foreign exchange market and the holding of current balances in foreign currency is legal under the law of the land.
3. The bank uses its own discretion to determine the minimum balance required to open account.
4. The bank will supply the account holders with a cheque book. Withdrawal from the account may be made on demand by issuing cheques or other written instruction given by the account holders. The cheques issued by customer will be honoured by the banks subject to the conditions that they are in order and funds are available in the technical reasons such as difference in signature, post-date or out-of-date and invalid amendments.
5. A service charge may be imposed by the bank for servicing and maintaining the account.
6. A penalty charge may be imposed for any cheque returned due to insufficient balance in the account.
7. The termination of the relationship between the bank and the account holders can be effected either upon the customer's request or at the discretion of the bank. Due notice of such intention must, however, be given by the intended party. The account will also be suspended in the case of death or bankruptcy of individual customers and winding up of a company or other legal instruction such as orders from the court.<sup>61</sup>
8. The bank guarantees the full return of these deposits on demand and the depositor is not paid any share of the profit or a return in any other form.
9. Depositors authorize the bank to utilize funds at the bank's own risk. Hence, if there is any profit resulting from the employment of these funds, it accrues to the bank and if there is any loss, it is also borne by the bank.
10. Usually, account holders have a right to draw checks on their own accounts.<sup>62</sup>

Therefore, Based on legal maxim under the '*urf*' that a matter recognised by customary amongst merchants is regarded as if agreed upon between them (*al-Ma'rufbayna al-Tujarkal-mashrutbaynaum*).<sup>63</sup> There is a little difference between the operational procedures of demand deposits facilities of conventional and Islamic banks. Current account customers do not participate in the share of the profit from investment of their funds. Although no reward is given to current account holders by most Islamic banks, Islamic banks in Iran are allowed to reward their customers. As stated in the Law for Usury-Free Banking of 1983 of Iran.<sup>64</sup> In Malaysia, Bank Islam, at its own discretion, provides rewards to accounts maintained by the Federal or state Governments and Statutory Authorities provided they maintain a daily balance of not less than Malaysian Ringgit (RM) 25,000.00.<sup>65</sup>

### **Saving Accounts**

The second category of deposits is the savings accounts. To conventional banks, this account is to facilitate those who wish to save money and at the same time earn an income. The three *Shari'ah* principles used by Islamic banks for savings accounts are *qard hasan*, *wadi'ah yad damanah* and *mudarabah*. The depositors in this category are those who hold money primarily because of precautionary motive, while instantaneously induced

<sup>60</sup> (*Aqil and ba'ligh* is defined as a person who is of sound mind and has attained the age of 12 years).

<sup>61</sup> *Id.*, 58, at 62-63.

<sup>62</sup> Ahmad Ausaf, *Contemporary Practices of Islamic Financing Techniques*, (1993), at 4-5.

<sup>63</sup> *Majallah Al-Ahkam*: Article 44.

<sup>64</sup> *Id.*, 61, at 63.

<sup>65</sup> *Ibid.*

by an investment motive.<sup>66</sup> Although all Islamic banks are operating savings accounts except Islamic banks in Turkey,<sup>67</sup> there are some differences in the operation of these accounts. A typical example is that of the Bank Islam Malaysia, which defines savings accounts in the following way:

The Bank accepts deposits from its customers looking for safe custody of their funds and a degree of convenience in their use together with the possibility of some profits in the form of Saving Accounts on the principle of *al-wadi'ah yad damanah*. The bank requests permission to use these funds so long as these funds remain with the bank. The depositors can withdraw the balance at any time they so desire and the Bank guarantees the refund of all such balances. All the profits generated by the Bank from the use of such funds belong to the portion of the Bank. However, in contrast with the current account, the Bank may at its absolute discretion reward the customers by returning a portion of the profits generated from the use of their funds from time to time.<sup>68</sup>

It must be pointed out that any return on capital is Islamically justified only if the capital is employed in such a way that it is exposed to a business risk. If savings depositors are guaranteed that their amounts will be refunded in full, when they want them, as is the case with traditional banks, then, they are not participating in a business risk. Under these circumstances, it has to be made clear that savings depositors are not Islamically entitled to any return. If an Islamic bank, refunds some portion of the profits generated from the use of saving deposits to the depositors, it is absolutely at the discretion of the bank concerned and it must be treated as a gift.<sup>69</sup> Some Muslim scholars argue the lawfulness of the practice of rewarding savings accounts customers that operation via principle other than *mudarabah*. The procedures relating to savings accounts adopted by Bank Islam Malaysia has been questioned and it was argued that rewards to saving account holders of done on a regular basis is a form of *ribā*.<sup>70</sup>

In fact, this can be argue that this is does not violate any *Shari'ah* principle as narrated from *hadith* of Prophet Muhammad (*s.a.w*) that He has encouraged borrowers to pay more than the principle loan, also the practice will not become an '*urf* or norm forbidden by *Shari'ah*. The addition, however, are not contractually stated in the loan agreement and it must not be conditioned in the contract. Narrated by Jabir bin 'Abdullah: "I went to the Prophet (*s.a.w*) while he was in the mosque. After the Prophet (*s.a.w*) told me to pray two *Rak'at* he repaid me the debt he owned me and gave me an extra amount.<sup>71</sup> On another occasion, the Prophet (*s.a.w*) says, "The best amongst you is he who repays his debts in the most handsome manner"<sup>72</sup> The extra payment was not made contractually binding, but release according to the paying capacity of the borrowing party, and most important, his willingness to give more.<sup>73</sup> Moreover, give *hibah* and gift is highly recommended and appreciated as suggested in this verse:

"but if they choose of their own accord to make over to you a part of it, then you may enjoy it with pleasure and good cheer."<sup>74</sup>

Besides that, there is no impediment in *Shari'ah* to apply the concept of *hibah* in contract since *hibah* is a benevolent act and is at the discretion of the giver of *hibah*. A similar position was taken by the *Shari'ah* Supervisory Board of the Faisal Islamic Bank of Sudan. This Board had issued a *fatwa* which suggests that it is permissible to give prizes for savings accounts without prior knowledge of its holders so long as the prizes are varied and made on a non-regular basis.<sup>75</sup>

<sup>66</sup> Lee Mei Pheng & Detta Ivan Jeron, *Islamic banking & Finance Law*, (2007), at 64

<sup>67</sup> Ibid.

<sup>68</sup> Bank Islam Malaysia Berhad, *Organization and Operations*, Mimeograph, (not dated), at 11-12

<sup>69</sup> Ahmad Ausaf, *Contemporary Practices of Islamic Financing Techniques*, (1993), at 6

<sup>70</sup> Id., 64, at 65

<sup>71</sup> Al-Bukhari *Sahih al-Bukhari*, (Cairo: al-Matba'ah as-Salafiyyah, 1982), vol. 2, at 173, Hadith No. 2934.

<sup>72</sup> Ibid., at 146, Hadith No. 2305.

<sup>73</sup> Rosly, SaifulAzhar, *Critical Issues on Islamic Banking and Financial Markets Islamic Economics, Bankings, Takaful and Financial Planning*, (Kuala Lumpur: DinamasPinggirZaaba, 2005), at 161.

<sup>74</sup> Qur'an, 4: 4.

<sup>75</sup> Id., 70.

### Investment Accounts

The third category of deposit facility is for those who keep money for investment motives. Customers who have idle funds usually want better returns.<sup>76</sup> Investment deposits are Islamic banks' counterparts of term deposits or time deposits in the conventional system. They are also called (PLS) Accounts or Participatory Accounts. However, they can be distinguished from traditional fixed term deposits in the following manner:

- i) Fixed term deposits in the conventional system operate on the basis of interest, while investment accounts in Islamic banks operate on the basis of profit sharing which is a straightforward (*mudarabah*). *Mudarabah* is where the provider of the funds, 'the saver' entrusts their money to an expert the investor, 'the bank' so that they can make a profit from it. Instead of promising depositors a predetermined fixed rate of return on their investment, the bank tells them only the ratio in which it will share the profits with them. How much profit each depositor earns depends on the final outcome of the bank's own investment.
- ii) While fixed term deposits are usually distinguished from each other based on their maturities; investment deposits can be distinguished based on maturity as well as based on purposes, as it is possible to give special instructions to the bank to invest a particular deposit in a specified project or trade.<sup>77</sup>

All these terms and practice are permissible to apply the concept and the principle may not be the same, based on the following Fiqh maxim consideration is based on the prevailing practice and not on the isolated cases, (*Al-'Ibarat Lil- galib al-shai' la lil-nadir*).<sup>78</sup> Also Public usage is conclusive evidence and action must be taken in accordance there with (*Ist'mal al-anashujahyajib Al-'malubeha*).<sup>79</sup> Moreover, whatever is close to something it would take the same ruling (*Ma Qaruba al-shae' U'tiyahukmuh*).<sup>80</sup>

### CONCLUSION

'*Urf* (Custom) is recognised as source of law in almost all legal systems, including *Shari'ah*. The changing needs of a society are often reflected in its customs, which are in many ways the bus of society's adjustment to new conditions. Custom is also a pointer at once of the people's needs, and their acceptance to change. It is inherently active and open-ended, and always remains susceptible to further refinement. The role that custom has played in the development has great deal of what is known in the name of *ijma'* (consensus of Jurists), *maslahah* (public good) and fatwa (juristic opinion) often originates in the customs and living experience of the community. Moreover, the application of '*urf* in Islamic Finance can be trace back as early as from the time of the Prophet (s.a.w).<sup>81</sup> Furthermore, the operation of both banks in deposit products are based on '*urf*, which are current, saving and investment account, because they are well known to depositee and depositor, while all the forms of bank deposits in conventional banking are governed with interest, which is prohibited in Islamic bank. The taste of some of the practice products assimilated the differences between conventional and Islamic bank, Islamic bank forbids *ribā*, unjustness and earning a return without taking risk, but encourages profit and risk sharing at the end, while the difference in actual cash flow could be the same, the underlying structures are quite distinct. There is some competition for funds, especially in a two system where both conventional and Islamic banking are available. In this case, it is sometimes difficult to identify difference between both products unless one carefully examines their underlying structures.

<sup>76</sup>Ibid., at 67.

<sup>77</sup> Millar Roderick, *Islamic Finance A guide for international business and investment* Anwar Habiba, Edn.,) (London:GMB, 2008), at 33.

<sup>78</sup>Ahmad al-Zarqa, *Sharh al-Qawa'id al-Fiqhiyyah*,(Kuwait, Dar al-Qalam, 1989), at, 235.

<sup>79</sup>*Majallah Al-Ahkam*: Article 37.

<sup>80</sup>AL-Ahmad Al-Nadwi, *Jamharah al-Qawa'id al-Fiqhiyyah fi al-Mu'amalat al-Maliyyah*, 2000), v.1, at. 468.

<sup>81</sup>MohamadAkramLaldin, *The Theory and Application of 'urf in Islamic law*, (PhD, unpublished thesis, Edinburgh: University of Edinburgh, 1995), at 113.