

## **ECONOMICS OF AR-RAHNU (ISLAMIC PAWNBROKING): ISSUES AND CASES IN BRUNEI DARUSSALAM**

(Ekonomi Ar-Rahnu (Pajak Gadai Islam): Isu dan Kes di Brunei Darussalam)

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### **ABSTRACT**

The aims of this paper are to discuss issues on Ar-Rahnu in relation to Islamic jurisprudence and as a financial product in Brunei Darussalam. There are critical issues of *Rahn* in Islamic jurisprudence. The first issue is the debtor fails to repay his debt at maturity (default) and the second issue is benefiting from pledged property. Furthermore, Ar-Rahnu products in Brunei have strong characteristics as a financial product for SME (small and middle enterprises). Ar-Rahnu products in Brunei also can help entrepreneurs to purchase textile machines, necessary equipment and other crucial materials for their paddy planting and processing business. There are two feature of Ar-Rahnu products, first feature is the discussion on property. In the case of default, the creditor pays over the surplus to a borrower after the creditor has auctioned the borrower's collateral. This proves that there is a difference between Ar-Rahnu products and conventional pawnbroking with regard to the concept of property. Therefore, it is important to make further research on this subject to enhance Islamic financing. The second feature of Ar-Rahnu products is it is a financial product for SME, but it can also be used for lower-income groups, especially for assisting with living expenses. This shows the diversity of Ar-Rahnu products. Therefore, researches of Ar-Rahnu products have more importance in the future in terms of Islamic jurisprudence and financial products.

**Keywords:** Economics; Ar-Rahnu; Islamic pawnbroking; Brunei

## ABSTRAK

Tujuan kertas kerja ini adalah untuk membincangkan isu-isu Ar-Rahnu yang berkaitan dengan perundangan Islam dan sebagai produk kewangan di Negara Brunei Darussalam. Antara isu-isu kritikal Ar-Rahnu dalam perundangan Islam adalah penghutang gagal untuk membayar balik hutangnya pada tarikh matang (lalai) dan mendapat penghutang mendapat faedah daripada harta dicagarkan. Sementara itu, produk Ar-Rahnu di Brunei mempunyai ciri-ciri yang kuat sebagai produk kewangan bagi PKS (perusahaan kecil dan sederhana). Produk Ar-Rahnu di Brunei juga boleh membantu usahawan untuk membeli mesin tekstil, peralatan yang diperlukan dan bahan-bahan penting yang lain untuk menanam padi dan menjalankan perniagaan pemprosesan. Ciri-ciri produk Ar-Rahnu adalah yang pertama, perbincangan mengenai harta. Dalam kes lalai, pemiutang membayar lebih lebih kepada peminjam selepas pemiutang telah dilelong cagaran peminjam. Ini membuktikan bahawa terdapat perbezaan antara produk Ar-Rahnu dan pajak gadai konvensional dengan mengambil kira konsep harta. Oleh itu, adalah penting untuk membuat kajian lanjut mengenai perkara ini bagi meningkatkan pembiayaan Islam. Kedua, produk Ar-Rahnu adalah satu produk kewangan untuk PKS, tetapi ia juga boleh digunakan untuk golongan berpendapatan rendah, terutamanya bagi membantu perbelanjaan sara hidup. Ini menunjukkan kepelbagaian produk Ar-Rahnu. Oleh itu, kajian produk Ar-Rahnu adalah lebih penting pada masa akan datang dari segi produk kewangan perundangan Islam.

**Kata kunci:** Ekonomi; Ar-Rahnu; pajak gadai Islam; Brunei

## INTRODUCTION

The research of *Rahn* (Islamic pawnbroking) services belongs to a frontier field in Islamic economics and finances. al-Du'ailaj (1986) was the pioneer of this field, and his academic research is regarded as a comprehensive work that concluded the principles, the rulings, the pillars and the issues related to *Rahn* (Sharif et al. 2013).

The pioneer nation for providing this financial product is Malaysia, which began providing Ar-Rahnu products through the establishment of Muassasah Gadaian Islam Terengganu, MGIT (Terengganu's Islamic Pawnshop Corporation) in Malaysia by Majlis Agama Islam dan Adat Melayu Terengganu, MAIDAM (Terengganu Religious and Malay Custom Council) in 1992. Since then, these services have been expanded not only in Malaysia but also in Brunei Darussalam. However, there are no surveys in the field of Ar-Rahnu products in Brunei Darussalam.

This paper firstly aims to introduce issues on *Rahn* in relation to Islamic jurisprudence, or as a financial product. Secondly, it study the issues and cases in Brunei Darussalam.

## 1. Issues in Islamic jurisprudence

### i. *Rahn* in Quran, Hadith, and Islamic jurisprudence

The Arabic word رهن (*Rahn*) means pawning, pledging in the Quranic verses. For instance, derivatives of the word are used in (al Baqarah 2: 283), (al-Tur 52: 21) and (al-Muddaththir 74: 38). In addition, *Rahn* is mentioned in Hadith. The Prophet Muhammad (PBUH) says:

A riding animal is used in return for its expenses if it is pledged and milk is drunk in return for its expenses, if (the animal) is pledged. He who rides the animal or drinks the milk has to pay the expenses.

A pledge does not become the property of the mortgagee; it remains the property of its owner who mortgaged it he is entitled to its benefits and he is liable for its expenses.

It can be understood that a pledge does not become binding except with receipt of the object. It cannot be conducted other than by a person who is free, accountable, adult and discerning and under no interdict for insanity or bankruptcy (Kharofa 1997).

In Islamic jurisprudence, there are differences among scholars in defining *Rahn*. According to Hanafi jurists, *Rahn* is to retain (*habs*) a valuable property to protect a right, which can be claimed from the property. The term ‘valuable property’ means that all non-traded items such as humans, or valueless items such as liquor and pigs, are rejected from the ‘valuable property’ classification. The Malikis define *Rahn* as granting something, which is allowed to be sold as a collateral for a right (*haq*) or for any uncertainty that is stipulated in contract. The Shafi jurists define *Rahn* as the giving of an object (*‘ain*) as security for a loan, whereby the loan is claimable from the security if the loan is not repaid. The Hanbali jurists define *Rahn* as a kind of property (*mal*), which is granted as a security for a loan, which is claimable from the *mal* upon the debtor’s failure to repay. In this case, the word *mal* has a general meaning, which comprises tangibles, i.e. an object or an intangible asset such as usufruct (Naim 2013).

### ii. The pillars of *Rahn* in Islamic jurisprudence

There are disagreements among scholars when discussing and determining the pillars of the *Rahn* contract. The majority of Hanafis believe that there is only one pillar in the contract of *Rahn*, that is the verbal offer (*ijab*). The verbal

acceptance (*qabul*) by the pledge is just a condition but is not compulsory, because *Rahn* is a charitable contract (Naim 2013).

However, the majority of jurists from Maliki, Shafie and Hanbali schools concurred that there are four main pillars of *Rahn*. These include the two contracted parties, the *sigba* (verbal offer and acceptance), the pledged item and the protected thing such as the debt (Naim 2013).

The first pillar is the two contracted parties, the pledger (*rabin*) and the pledgee (*murtabin*). The agreement on this pillar is mainly focused on the eligibility of the person to make the transaction, i.e. the person who makes a contract is sane and reached maturity age (Naim 2013).

The second pillar is offer and acceptance. There are discussions among Islamic jurists about *sigba* i.e. verbal offer and verbal acceptance. There was no consensus among them with regard to the minor issues of *sigba*. The majority of Hanafi jurists held the view that the offer (*ijab*) is the single pillar for a contract of *Rahn*. The verbal acceptance (*qabul*) is permissible but not necessarily a compulsory. However, the majority of Islamic jurists from differing schools of thought stipulated the requirement of existence of both elements of *sigba* i.e. offer and acceptance (Naim 2013).

The third pillar is the protected debt and right in a pawn contract. The majority of jurists unanimously agreed that pawning is permissible to create a debt. However, they have contradicting views regarding in pawning an object. Thus, the Shafi jurists and a group from the Hanbalis and the Zahiris held the view that pawning is prohibited for an object because Allah SWT permits pawning for debt only. The Maliki jurists and the majority of the Hanbalis professed the absolute permissibility of pawning an object. However, the jurists of Hanafi stated that the permissibility of pawning for an object is specific to the object which is categorized as '*ainmithli* (i.e. a similar object exists in the market and it is replaced) (Naim 2013).

The fourth pillar is the thing giving as pawn. There were conclusive agreements among the majority of jurists on the permissibility of taking any objects which were permitted to be sold as pawn for debt, on the grounds that the purpose of the pawn is to protect the debt by claiming the debt from the price of the pawn, in cases when the failure of payment occurred. However, the Hanafis states that the purpose of a pawn is to hold up. Therefore, it is permitted to pawn whatever thing which is allowed to be sold, but with some exceptions such as the item belongs to partnership (*musha'*) (Naim 2013).

iii. Main issues of *Rahn* in Islamic jurisprudence

There are critical issues of *Rahn* in Islamic jurisprudence. The first issue is that the debtor fails to repay his debt at maturity (default). Under normal circumstances, the pledged property would be sold by the debtor or his agent, since the debtor is the owner. Nevertheless, the creditor's permission is necessary. This is related to the creditor's claim to the financial value of the pledged property. On the other hand, if the creditor does not give permission to the debtor to sell the pledged property, the debtor can institute a suit in a court of law. The judge should direct the creditor to allow the debtor to sell the pledged property. A default on debt repayment at maturity of the underlying debt may occur if the debtor dies. In this case, if the debtor does not have other property with which to pay his debt, and if the debtor dies with his property pledged in lieu of his debt, then his plenipotentiary or heir becomes entitled to selling the property with the creditor's permission (Hussin & Hussin 2011; Naim 2013).

The second issue is benefiting from pledged property. Jurists have different views related to the debtor benefiting from the pledged property. The Shafi'i jurists ruled that the debtor is authorized to utilize the pledged property, as long as its utilization does not harm the creditor. In contrast, the Hanafi, Hanbali and Maliki jurists ruled that the debtor is not permitted to benefit from the pledged property during the pledging period. The Hanafi jurists allow benefiting from the pledged property (by the debtor) with the permission of the creditor. The Hanbali jurists agreed with the Hanafi jurists that the debtor is only allowed to use the pledged property with the creditor's permission. Furthermore, the Maliki rulings in this regard were stricter than the Hanafi and Hanbali rulings (Naim 2013). It must be understood that the contract of *Rahn* does not mean that the creditor possesses or can utilize (benefit) the pledged property, since the right of ownership is on the debtor as the owner. Therefore, according to majority view the creditor cannot use the pledged property in any way (Naim 2013).

Kharofa states that the mortgagee is not entitled to take any benefit from the collateral, and the mortgagor is not entitled to draw any benefit from the pledged object except with the permission of the mortgagee (Kharofa 1997).

2. Ar-Rahnu products as financial product and the cases in Brunei

i. Concepts and scheme

Ar-Rahnu products as a financial product is based on four Shari'a concepts, which are referred to as Qard Hassan, Wadia Yad Damana, *Rahn*, and Ujra. The first is a loan without interest, and is called a 'benevolent loan'. The

second refers to guaranteeing a loan with valuable goods. Banks that supply this type of *Rahn* charge a safekeeping fee (Ujra). This concept differs from conventional pawnbroking in its approach to profits. This safekeeping fee for *Rahn* should be lower than the interest charged by conventional banks. In addition, this fee is based on the value of the collateral and not on the amount of the loan, as would be the case in conventional pawn broking. *Rahn* means collateral, which customers pawn to banks. In an Islamic pawnshop, only gold is accepted as collateral.

*Rahn* is based on these concepts and provided to customers through the following procedure. At first, a creditor lends money to a borrower with no interest (Qard Hassan). Next, the borrower pawns his collateral (*Rahn*) and the creditor charges safe keeping fees (Ujra). Third, the creditor keeps the borrowers collateral until the repayment (Wadia Yad Damana). Finally, the creditor returns the borrower’s collateral after the borrower has settled the debt. The following diagram shows this procedure.

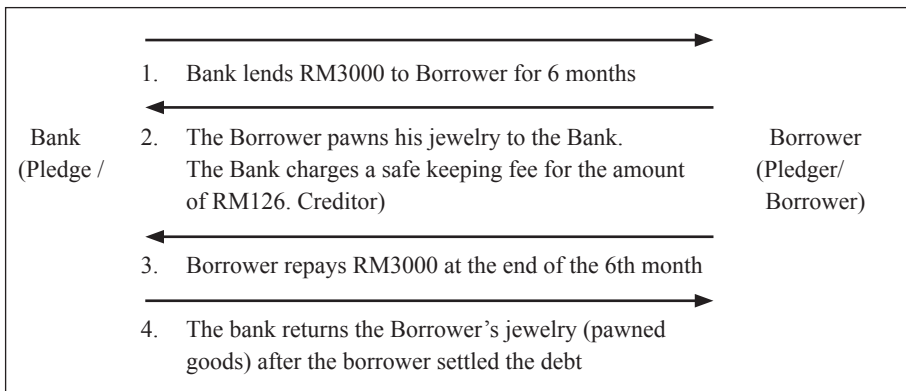


FIGURE 1 Ar-Rahnu products Scheme

Source: (Ramali & Aminuddin 2011)

ii. Objectives of Ar-Rahnu products scheme

Ar-Rahnu products is a quick and easy access to short-term financing for lower income groups, so it has two main objectives (Aziz 2012; Ismail & Maamor 2013). The first is to provide capital for a small business. There are a lot of small traders facing the problem of securing capital, either to start or expand their businesses. Therefore, the Ar-Rahnu products scheme can contribute to their business since one of the main obstacles that small traders face when trying to get micro credit from a financial institution is the issue of collateral. In addition, the bank usually asks for a detailed list of information

about the business and requires a guarantor. However, these requirements are difficult for small entrepreneurs to fulfill. For Ar-Rahnu products, only basic information and the items to be pawn are required, so they can easily get micro credit through this scheme.

The second objective is financing living expenses for consumer needs. Ar-Rahnu products offers the best option as it conforms to Islamic principles and meets the customer's need with its reasonable lending rates. Thus the Ar-Rahnu products institution is able to reduce and help combat the illegal activities of 'Ah Longs' (loan sharks).

### iii. Ar-Rahnu products in Brunei Darussalam

#### a. Regulation

There are two regulations on pawnbroking, which are pawnbrokers Order 2002, and State Mufti's Fatwa in Brunei (The State Mufti's Office 1997). The State Mufti's Office. (2000). Regarding pawnbrokers Order 2002, the long title of this order is 'An Order to regulate the business of pawnbrokers in accordance with *Hukum Syara* means the laws of any sects which the court considers valid' (Section 1(3)). According to the order, a 'pawnbroker' is defined as any person who, holding a valid license, carries out the business of receiving articles from pawners as security and grants them loans under the provisions of this Order and 'pawner' as a person who delivers an article to a pawnbroker as security for getting a loan thereon (Section 2(1)). When it comes to failure to repay the loan, if the proceeds of the sale or auction are greater than the amount so due, the pawnbroker shall hand over the surplus to the pawner (Section 27(2)).

The State Mufti's Fatwa Office (1997) defined pawn as a thing of fixed value thing excluding the property of a waqaf (trust) for repayment in the case of default. In addition, according to the fatwa, the thing pawned must not be harmful to the creditor. The duties in the pawn business are the verbal offer (*ijab*) and the verbal acceptance (*qabul*) (The State Mufti's Office 1997). That is why the fatwa belongs to the view of the majority of Islamic jurists except the Hanafis. The State Mufti's Fatwa Office (2000) states that the interest a pawnshop charges is *riba* (usury), so a loan given out by a pawnshop is prohibited in Islam.

#### b. Economic activity of Ar-Rahnu products

The Bank Islam Brunei Darussalam (BIBD) provides the Ar-Rahnu products service. There are two types: al-Jauhar for gold items and precious stones, and Az-Zahab for gold items only. In addition, safekeeping fees are BND 1.10 per

BND 100.00 of the collateral in case of al-Jauhar, and BND 0.95 per BND 100.00 of the collateral in case of Az-Zahab. Administrative fees are BND 20.00 for al-Jauhar and BND 15.00 for Az-Zahab.

TABLE 1 Bank Islam Brunei Darussalam Ar-Rahnu products

	al-Jauhar	az-Zahab
Accepted Collaterals	Gold items and precious stones	Gold items only
Financing Limit	95% of collateral's prevailing market rate, up to BND 45,000.00	80% of collateral's prevailing market rate, up to BND 40,000.00
Minimum Daily Transaction Limit	BND 300.00	BND 100.00
Maximum Daily Transaction Limit	BND 9,000.00	BND 8,000.00

Resource: <http://www.bibd.com.bn/consumer/financing/personal-financing/micro-financing/>

Ar-Rahnu products in Brunei have strong characteristics as a financial product for SME (small and middle enterprises). For example, Ar-Rahnu products can help an entrepreneur to purchase a textile machine or BIBD Ar-Rahnu products can help peasants to purchase necessary equipment and other crucial materials for their paddy planting and processing business (Bank Islam Brunei Darussalam Press Release 2013).

Adverting claiming its achievements has been increasing recent years. For example, the explanation on how Islamic pawnbroking and can provide a safe alternative to borrowing money from loan sharks was presented to members of the Brunei Darussalam Girl Guides Association (PPPBD) on June 15, 2012 (Anna Abu Bakar 2012). In addition on July 26th, 2012, some 55 employees and teachers at the Youth Development Centre (YDC) attended a briefing on the Ar-Rahnu Micro-Financing Scheme, which allegedly could help entrepreneurs of small-medium enterprises (SMEs) to expand their businesses (Sally Piri 2012).

## CONCLUSION

We have discussed the *Rahn* contract in terms of Islamic jurisprudence, and shown how Ar-Rahnu products have become popular with people in Malaysia and Brunei in recent years. In this conclusion, the following two features are pointed out.



The first feature is the discussion on property. In the case of default, the creditor pays over the surplus to a borrower after the creditor has auctioned the borrower's collateral. This proves that there is a difference between Ar-Rahnu products and conventional pawnbroking with regard to the concept of property. Therefore it is important to make further research on this subject to enhance Islamic financing.

The second feature of Ar-Rahnu products is that it is a financial product for SME, but it can also be used for lower-income groups, especially for assisting with living expenses in Malaysia. This shows the diversity of Ar-Rahnu products.

Therefore researches of *Rahn* and Ar-Rahnu products have more importance in the future in terms of Islamic jurisprudence and financial products. Furthermore, future research on the issues needs to be approached both from the aspect of Islamic jurisprudence, and as a financial product.

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