



BANK NEGARA MALAYSIA
CENTRAL BANK OF MALAYSIA

Bai`Inah
(Shariah Requirements and Optional Practices)

Exposure Draft

Issuance date: 6 December 2013

BNM/RH/CP 028-2	Islamic Banking and Takaful Department	<i>Bai` Inah</i> (Shariah Requirements and Optional Practices) Exposure Draft
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As part of the objective to strengthen the Shariah-compliance culture among Islamic financial institutions (IFIs), Bank Negara Malaysia (the Bank) is embarking on an initiative to develop a Shariah-based regulatory framework. The purpose of the framework is to ensure that the IFI comply with Shariah. In this regard, the Bank is issuing a series of policy documents on Shariah contracts to enhance the end-to-end compliance with Shariah.

This Exposure Draft (ED) outlines the Shariah requirements and optional practices relating to *bai` `inah* to facilitate IFIs in developing Islamic financial services and products including the features of *bai` `inah* and its arrangement with other Shariah contracts or concepts.

The Bank invites written comments from your institution on this ED, including suggestions for particular issues, areas to be further clarified/ elaborated and any alternative proposal that the Bank should consider. To facilitate the Bank's assessment, please support each comment with clear rationale, accompanying evidence or illustrations, as appropriate.

Written comments in the form of a softcopy are preferable and may be submitted to **shariahstandard@bnm.gov.my** by 10 January 2014. Hardcopy of the written feedback may also be submitted to:

Pengarah
Jabatan Perbankan Islam dan Takaful
Bank Negara Malaysia
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50480 Kuala Lumpur
Malaysia

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PART A OVERVIEW

1. Objective

- 1.1 This policy document outlines the Shariah requirements and optional practices relating to *bai` `inah* to be observed by the Islamic financial institution in developing Islamic financial services and products.
- 1.2 This policy document also covers arrangement of *bai` `inah* with other Shariah contracts or concepts.
- 1.3 This policy document aims to facilitate the understanding of the Shariah requirements relating to *bai` `inah* that the IFIs must adhere in order to ensure its validity.

2. Applicability

- 2.1 This policy document is applicable to all IFIs as defined in paragraph 5.2.

3. Legal provisions

- 3.1 The requirements in this policy document are specified pursuant to section 29(1) of the Islamic Financial Services Act 2013 (IFSA).

4. Effective date

- 4.1 This policy document comes into effect on XX XX XXXX.

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5. Interpretation

5.1 The terms and expressions used in this policy document shall have the same meanings assigned to them in the Financial Services Act 2013 (FSA), IFSA and DFIA unless otherwise defined in this policy document.

5.2 For the purpose of this policy document:

“**S**” denotes a standard, requirement or specification that must be complied with. Failure to comply may result in one or more enforcement actions;

“**G**” denotes guidance which may consist of such information, advice or recommendation intended to promote common understanding and sound industry practices which are encouraged to be adopted.

“**Islamic financial institutions**” or “**IFI**” means –

- (a) licensed Islamic banks and licensed takaful operators under the IFSA;
- (b) licensed banks and licensed investment banks under the FSA which are approved under section 15(1)(a) FSA to carry on Islamic banking business; and
- (c) prescribed institutions under the DFIA which are approved under section 129(1) DFIA to carry on Islamic banking business or Islamic financial business.

6. Related legal and policy document

6.1 This policy document must be read together with the following legal and policy documents:

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- (a) any Shariah Advisory Council (SAC) rulings published by the Bank¹; and
- (b) Shariah Governance Framework for Islamic Financial Institutions.

¹ Including Shariah resolutions in Islamic Finance, standards, circulars or any directive pertaining to Shariah matter issued by the Bank.

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PART B DEFINITION AND NATURE OF *BAI` `INAH*

7. Definition

- S** 7.1 *Bai` `inah* refers to an arrangement that involves sale of an asset to the purchaser on a deferred basis and subsequent purchase of the asset at a cash price lower than the deferred sale price or vice versa, and which complies with the specific requirements of *bai` `inah*.

8. Nature

- S** 8.1 Each sale contract in a *bai` `inah* arrangement is binding in nature. Thus, neither of the sale contracts shall be terminated unilaterally by any of the contracting parties.
- S** 8.2 The inherent nature of each sale contract in a *bai` `inah* arrangement is the transfer of ownership of the asset from the seller to the purchaser in two separate and independent sale contracts.
- G** 8.3 The *bai` `inah* arrangement may occur in the following forms:
- (a) the owner sells the asset to the purchaser at a deferred price and subsequently the initial owner buys the asset on a cash basis at a lower price than the deferred sale price; or
 - (b) the owner sells the asset to the purchaser on a cash basis and subsequently the initial owner buys the asset at a deferred price which is higher than the cash sale price.

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PART C COMPONENTS OF *BAI` `INAH*

9. Contracting parties

- S** 9.1 Contracting parties in a *bai` `inah* arrangement are a seller and a purchaser in two separate and independent sale and purchase contracts.
- S** 9.2 The contracting parties shall have the legal capacity² to enter into the *bai` `inah* arrangement.
- G** 9.3 The contracting parties in a *bai` `inah* arrangement may be a natural person or a legal person.
- G** 9.4 A party to the *bai` `inah* arrangement may execute the sale contract through a third party agent.
- S** 9.5 Each sale contract in the *bai` `inah* arrangement shall be entered into through an offer and acceptance between the contracting parties.
- G** 9.6 The offer and acceptance may be expressed by appropriate documentation or by any other methods accepted by customary business practice (*`urf tijari*) which do not contravene the Shariah principles.
- S** 9.7 Any term or condition mutually agreed upon which does not contravene the Shariah shall be binding on the contracting parties.

² The legal capacity of a person is defined as capacity to assume rights and responsibilities; and capacity to give legal effect to his action. Among the important conditions are that the person must possess sound mind and the capacity to distinguish between what is harmful or beneficial to one's interests. Legal capacity of a legal entity is defined as eligibility of an entity to acquire rights and assume responsibilities.

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10. Asset

- S** 10.1 Asset to be traded in a *bai` `inah* arrangement shall meet the following conditions:
- (a) the asset is recognised by the Shariah, valuable, identifiable and deliverable; and
 - (b) the asset is already in existence and owned by the seller.
- G** 10.2 The *bai` `inah* asset may be a tangible or an intangible asset.
- S** 10.3 The following assets shall not be traded under *bai` `inah* arrangement:
- (a) asset to be constructed or asset under construction; and
 - (b) asset which is debt in nature.
- S** 10.4 Trading of *ribawi* asset under a *bai` `inah* arrangement shall meet the following conditions:
- (a) any of sale contract in the *bai` `inah* arrangement shall not be effected on *ribawi* asset within the same type and category; and
 - (b) any of the sale contract in the *bai` `inah* arrangement shall not be effected on *ribawi* asset within the same category but of different type on deferred basis.
- S** 10.5 The ownership in the *bai` `inah* asset must be effectively transferred from the seller to the purchaser.
- S** 10.6 The transfer of ownership is effected upon entering into a valid sale and purchase contract even though there is no legal registration of the ownership, provided that the sale and purchase is supported by evidence of transaction.

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- S** 10.7 The transfer of ownership shall take effect by the seller disposing of the right of ownership (*takhliyah*) resulting in the purchaser having access to the asset (*tamkin*) and assuming its risk through any mechanism permitted by the Shariah and generally accepted by business practices (*'urf tijari*).
- S** 10.8 Possession of the asset shall be either in the form of physical possession (*qabd haqiqi*) or constructive possession (*qabd hukmi*).
- S** 10.9 The rights and liabilities of the purchaser as the owner of the asset are established upon his possession of the asset.
- S** 10.10 The seller shall bear the liability for loss or damage of the asset before disposing of the right of ownership (*takhliyah*) that results in the purchaser having access to the *bai` `inah* asset (*tamkin*).
- G** 10.11 Multiple *bai` `inah* arrangements shall not be entered into simultaneously on the same asset.
- S** 10.12 Any defect in the asset which is discovered and consented to by the purchaser at the time of entering into each sale contract in the *bai` `inah* agreement shall disqualify the purchaser from entitlement to the defect option (*khiyar al-`ayb*) with respect to the defect.
- S** 10.13 Any defect in the asset which occurred upon or before the entering into of each sale contract in the *bai` `inah* arrangement but is discovered by the purchaser after entering into each sale contract, as the case may be, shall entitle the purchaser to the defect option (*khiyar al-`ayb*).
- G** 10.14 Pursuant to paragraph 10.13, the purchaser has the right to terminate the contract. Alternatively the purchaser may choose to continue with the contract as it is or with any mutually agreed variation of the terms of the contract.

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- G** 10.15 The contracting parties may mutually agree to specify the period for the exercise of the defect option at the time of entering into the contract.
- G** 10.16 The contracting parties may mutually agree to stipulate a condition to waive liability for any defect on the asset before entering into the contract.

11. Price

- S** 11.1 The price and the currency used shall be determined and mutually agreed at the time of execution of each of the two independent sale contracts.
- S** 11.2 In the event that the price for any sale contract of the *bai` `inah* arrangement is on a *murabahah* basis, all requirements of price under a *murabahah* sale shall be complied with.
- G** 11.3 The price of each sale contract in *bai` `inah* arrangement may be paid on the spot, progressively or by deferred payment in the form of installments or bullet payments at any time agreed by the contracting parties.
- G** 11.4 The purchaser and the seller may agree to make payment of the instalments or full settlement in a currency different from the currency specified in the contract at the agreed prevailing exchange rate on the payment or settlement date respectively.
- G** 11.5 The contracting parties may agree to extend or reschedule the payment period of the remaining debt without any increase in amount to the remaining debt.

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- S** 11.6 Notwithstanding paragraph 11.5, the contracting parties may agree to settle the outstanding debt obligation by entering into a new contract that may results in a new debt obligation.

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12. Requirements of the *bai` `inah* arrangement

- S** 12.1 Each sale contract in a *bai` `inah* arrangement shall satisfy all necessary conditions of a valid sale and purchase contract under Shariah.
- S** 12.2 *Bai` `inah* arrangement shall be executed by entering two separate and independent sale contracts.
- S** 12.3 The sale contracts in *bai` `inah* arrangement shall be entered into in such a way that the purchaser in the first sale contract has the right to take delivery of the asset.
- S** 12.4 Each sale contract in *bai` `inah* arrangement shall be entered into through an offer and acceptance between the contracting parties.
- S** 12.5 The execution or signing of the two sale contracts must be performed at different intervals.
- S** 12.6 Written documentation of both sale contracts must be prepared and represented by two separate sets of documents.
- S** 12.7 All documentary or verbal evidence used in *bai` `inah* arrangement shall not:
- (a) stipulate in any part of the documentary or verbal evidence, any terms and conditions requiring the contracting parties to repurchase or resell the *bai` `inah* asset; and/or
 - (b) describe in any manner that the whole *bai` `inah* arrangement and the sequence of executing *bai` `inah* arrangement creates an obligation for any of the contracting parties to repurchase or resell the *bai` `inah* asset.

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- S** 12.8 The offer and acceptance must be executed in the following manner, whereby the seller sells the *bai` `inah* asset to the purchaser by entering into the first sale and purchase contract, and subsequently, the contracting parties may mutually agree to enter into another sale and purchase contract.
- S** 12.9 Pursuant to paragraph 12.8, both contracting parties in the *bai` `inah* arrangement are required to fully observe the following requirements:
- (a) the execution and/or signing of both sale and purchase contracts must be initiated by the respective seller in the respective contract and followed by the respective purchaser;
 - (b) neither contracting party to the *bai` `inah* arrangement shall pre-sign both sale and purchase contracts; and
 - (c) neither contracting party in the *bai` `inah* arrangement must provide either a written or verbal promise to repurchase or resell the asset.
- S** 12.10 Any amount paid to the seller before entering into the sale contract in the *bai` `inah* arrangement shall not be treated as part of the selling price including profit.

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PART D ARRANGEMENT OF *BAI` `INAH* WITH OTHER CONTRACT OR CONCEPT

13. Arrangement of *bai` `inah* with assurances

- G** 13.1 For the purpose of assurances, *bai` `inah* may be arranged with other contract such as *kafalah*, *takaful* cover, or *rahn*.

a) Assurance through *kafalah*

- G** 13.2 A guarantee may be arranged to guarantee the payment of the outstanding debt amount of the sale contract in a *bai` `inah* arrangement in the case of default by the purchaser.
- S** 13.3 Execution of each guarantee contract in any sale and purchase contract in the *bai` `inah* arrangement shall be independent of the other.
- G** 13.4 Notwithstanding paragraph 13.3, the guarantee may be arranged before entering into the *bai` `inah* arrangement to secure debt which is yet to be established by the contracting parties.
- G** 13.5 A third-party guarantee through *kafalah* may be arranged together with *bai` `inah* arrangement whereby the arrangement is to guarantee the following:
- (a) payment of the price of the *bai` `inah* asset within the agreed time;
 - (b) delivery of the agreed *bai` `inah* asset by the seller within the stipulated time; and/or
 - (c) acceptance of the agreed *bai` `inah* asset by the purchaser.

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b) Assurance through *takaful* cover

- G** 13.6 The seller may require the purchaser to subscribe to a *takaful* cover to guarantee payment of the price of the *bai` `inah* asset in the event of loss of legal capacity by the purchaser.

c) Assurance through *rahn*

- G** 13.7 Collateral (*marhun*) in the sale and purchase contract of the *bai` `inah* arrangement (if any) shall be a Shariah-compliant asset.
- S** 13.8 Notwithstanding paragraph 13.7, interest bearing debt based asset such as Conventional Fixed Deposit Certificate, may be used as collateral provided the collateral is valued up to the principal amount.
- S** 13.9 The collateral shall be utilised to recover payment of the outstanding debt amount.
- G** 13.10 The contracting parties may agree to include the claim on actual costs incurred for the recovery of the outstanding debt payment from the collateral.
- G** 13.11 For the purpose of extension or variation of the outstanding debt, the seller may demand additional securities from the purchaser.

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14. Incorporation of *ibra'* (rebate) in *bai` `inah*

- G** 14.1 The seller may consider waiving part of the outstanding or remaining unpaid price of the sale and purchase contract in the *bai` `inah* arrangement in the form of a discount to the purchaser upon pre-payment and/or early settlement.
- S** 14.2 A rebate clause shall be incorporated in the sale and purchase contract provided that it is a requirement imposed by the authority.
- G** 14.3 In the event that the sale contract in the *bai` `inah* arrangement involves payment of the deferred price in instalment, the seller may provide periodic rebate based on certain benchmark agreed by the contracting parties.

15. Arrangement of *bai` `inah* with *ta`widh* and/or *gharamah*

- G** 15.1 The contracting parties may agree to include a clause in the sale contract on late payment charges as determined by the relevant authorities.
- S** 15.2 Pursuant to paragraph 15.1, the late payment charges shall consist of:
- (a) *ta`widh* (compensation) for actual loss borne by the seller, which may be recognized as income to the seller; and/or
 - (b) *gharamah* (penalty) , which shall not be recognized as income. Instead, it shall be channelled to charitable bodies.

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PART E DISSOLUTION (*FSAKH*) AND COMPLETION (*INTIHA*) OF *BAI` `INAH*

16. Dissolution in *bai` `inah*

- G** 16.1 A *bai` `inah* arrangement is dissolved upon dissolution of any sale and purchase contract entered into under the *bai` `inah* arrangement.
- S** 16.2 The sale and purchase contract in a *bai` `inah* arrangement is dissolved under the following circumstances:
- (a) the purchaser exercises the defect option (*khiyar al-`ayb*) to terminate the sale and purchase contract;
 - (b) any of the contracting parties exercises the mutually agreed options to terminate the sale and purchase contract within the agreed time period;
 - (c) the contracting parties exercise the option to terminate the sale and purchase contract due to breach of terms; or
 - (d) both contracting parties mutually agree to terminate the sale and purchase contract.
- S** 16.3 Upon dissolution of any of the sale and purchase contracts in the *bai` `inah* arrangement, the asset shall be returned to the respective seller and the price shall be returned to the respective purchaser.
- S** 16.4 Pursuant to paragraph 16.3, the dissolution of contract shall be effective provided that the asset can be returned to the seller

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17. Completion of *bai` `inah*

- S** 17.1 The *bai` `inah* arrangement ends upon fulfilment of the contracting parties' obligations, which include the following:
- (a) full settlement of the remaining or outstanding deferred selling price due to the following situations:
 - i. settlement by the purchaser prior to or on the maturity date;
 - ii. claim by the seller due to breach of specified terms (*mukhalafah al-shurut*) of the contract by the purchaser; or
 - iii. settlement after the demise or dissolution of the purchaser.
 - (b) transfer of the obligation to pay the remaining or outstanding deferred selling price to a third party (*hiwalah*);
 - (c) waiving the right by the seller to receive the remaining or outstanding deferred selling price through a rebate (*ibra`*); or
 - (d) set-off (*muqassah*) of debt obligations between the contracting parties.
- S** 17.2 Upon completion of the *bai` `inah* arrangement, the contracting parties are free from any contractual obligations.

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APPENDICES

18. Appendix 1 Legitimacy of *bai` `inah*

18.1 The legitimacy of the *bai` `inah* arrangement is derived from the Quran and founded on the Sunnah of Prophet Muhammad (peace be upon him).

The Quran

18.2 The following Quran verse implies the general permissibility of *bai` `inah*.

i. وَأَحَلَّ اللَّهُ الْبَيْعَ وَحَرَّمَ الرِّبَا

“...whereas Allah SWT has permitted trading and forbidden usury...”
(*Surah al-Baqarah*, verse 275)

18.3 Two sales contracts executed separately and independently, with no interrelation with one another are the important elements in the *bai` `inah* arrangement and, therefore, it is a valid contract in the Shariah.

ii. يَا أَيُّهَا الَّذِينَ آمَنُوا إِذَا تَدَايَنْتُمْ بِدَيْنٍ إِلَىٰ أَجَلٍ مُّسَمًّى فَاكْتُبُوهُ

“O believers! When you contract a debt from one another for a fixed period, put it (its amount and period of payment) in writing...”
(*Surah al-Baqarah* verse 282)

The Sunnah of the Prophet Muhammad (peace be upon him)

18.4 There is no direct juristic authority from the *Sunnah* of the Prophet (peace be upon him) on the legitimacy of the *bai` `inah* arrangement. It is deemed permissible based on the general permissibility of sales in Islamic law.

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18.5 The following *hadiths* imply the general permissibility of *bai` `inah* arrangement.

i. عن رفاعة بن رافع -رضي الله عنه- أن النبي -صلى الله عليه وسلم- سئل: أي الكسب أطيب؟ قال: عمل الرجل بيده, وكل بيع مبرور.

The Prophet Muhammad (peace be upon him) was reported to have said: "The best earning is what man earns with his own hands and from a permissible trade" (*Narrated by Hakim, Al-Mustadrak, Hadith no. 2160*)

ii. عن أبي هريرة رضي الله عنه أن رسول الله صلى الله عليه وسلم استعمل رجلا على خيبر فجاءه بتمر جنيب فقال رسول الله صلى الله عليه وسلم: أكل تمر خيبر هكذا؟ قال: لا والله يا رسول الله إنا لناخذ الصاع من هذا بالصاعين والصاعين بالثلاثة، فقال رسول الله صلى الله عليه وسلم: لا تفعل، بع الجمع بالدراهم ثم ابتع بالدراهم جنيبا.

The Prophet (peace be upon him) appointed a person as governor of Khaybar, who [later] presented him with an excellent type of dates. The Prophet asked, "Are all the dates of Khaybar like this?" He replied, "[No, but] we barter one sa` of this (excellent type) for two sa` of ours, or two sa` of it for three of ours." Allah's apostle said, "Do not do that (as it is a kind of usury), but sell the mixed dates (of inferior quality) for money, and then buy the excellent dates with that money (*Sahih Bukhari, Hadith no. 2201*)."

19. Appendix 2 Glossary

Terms	Definition
<i>Bai` `inah</i>	An arrangement that involves sale of an asset to the purchaser on a deferred basis and subsequent purchase of the asset at a cash price lower than the deferred sale price or vice versa, and which complies with the specific requirements of <i>bai` `inah</i> .
<i>Gharamah</i>	Penalty.
<i>Hiwalah</i>	Assignment of debt from the liability of the original debtor to the liability of a third person so that the original debtor becomes free of liability.
<i>Ibra'</i>	Rebate.
<i>Khiyar al-`ayb</i>	Option arising from a defect; the option of dissolving the contract on discovery of a defect in the goods purchased.
<i>Marhun</i>	Collateral.
<i>Mukhalafah al-shurut</i>	Breach of terms and conditions.
<i>Muqassah</i>	Offsetting.
<i>Qabd haqiqi</i>	Physical possession. It refers to a state where a person has actual possession and the rights to control an asset.
<i>Qabd hukmi</i>	Constructive possession. It refers to a state where a person does not have actual possession but has the legal rights to control an asset.
<i>Rahn</i>	Pledge/Charge
<i>Ribawi asset</i>	Assets which are subject to specific rules in sales to avoid the implication of <i>riba</i> . These assets consist of

	<p>six (6) types and are classified into two (2) categories:</p> <p>(a) Medium of exchange (currency) represented by gold and silver and any items used as currency; and</p> <p>(b) Staple food represented by wheat, barley, dates, and salts.</p> <p>If an exchange involves the same type of asset such as gold for gold or wheat for wheat, then it must be of equal counter-value and on spot basis. If the exchange involves assets of different type but within the same category such as the exchange of gold for paper currency, then it has to be done on spot basis.</p>
<i>Takaful</i>	An arrangement based on mutual assistance under which <i>takaful</i> participants agree to contribute to a common fund providing for mutual financial benefits payable to the <i>takaful</i> participants or their beneficiaries on the occurrence of pre-agreed events.
<i>Takhliyah</i>	Relinquishing or abandoning the rights of ownership.
<i>Tamkin</i>	Enabling the person who has the ownership of an asset transferred to him to make full use and assume liability of the asset.
<i>Ta`widh</i>	Compensation.
<i>`Urf tijari</i>	Common business practice which is acceptable by the community and does not contradict the Shariah rulings.