

## An Appraisal of Hire Purchase under Shirkah al-Milk (HPSM) in Islamic Banking and Finance: A Conceptual Study

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*[Abstract: Islamic banks, since the inception of the Islamic financial system (IFS), have been offering – in several jurisdictions– various Shariah-compliant financial products by adapting and reshaping classical products. One such example is Hire Purchase under Shirkah al-Milk (HPSM), which is a modified variant of conventional hire purchase. In its conventional form, hire purchase serves as two contracts: ijarah (leasing) and sale. However, HPSM combines three distinct contracts: shirkah (partnership), ijarah (leasing), and sale. The ownership of the subject matter in the HPSM contract is transferred from the lessor to the lessee through a gift (hibah) contract, token amount, gradual sale, or a specific amount. To implement this investment mode, banks provide equipment or goods on a rental basis, with the condition that ownership will be transferred to the lessee at the end of the contract. This synthesis of contracts is allowed as a financing and asset acquisition means in accordance with Islamic principles. To represent the execution of HPSM within the Islamic financial system (IFI), this article adopts a descriptive approach as part of the qualitative research method. The study draws upon secondary data from various sources, including library resources, product manuals, and online databases. By leveraging these sources, the article aims to provide an appraisal of HPSM in the context of the IFI.]*

**Keywords:** HPSM, Hire Purchase, Shariah, Musharakah, Ijarah, Sale.

### Introduction

HPSM, which stands for musharakah, ijarah, and sale, is a sequential combination of three types of contracts commonly used in both Islamic and conventional commercial activities. These contracts have a long history predating the time of the Prophet Muhammad (SAW) and originally served as simple transactions rather than modes of financing. For instance, ijarah was primarily used for exchanging the usufruct based on an agreed-upon period and specific consideration. However, with the recent reforms in many Islamic financial institutions, experts in the field have recognized that musharakah, ijarah, and sale are well-established modes of investment worldwide. They realised that by properly following certain conditions, a combination of these contract modes can be made compatible with Shariah principles. Consequently, these contracts have been adopted as modes of financing in various Islamic financial institutions across the globe. This chapter will delve into the definition, legality, classifications, and permissibility of these contracts from a Shariah perspective, as well as explore some related issues. This article will be outlined into two sections, in the first section, the discussion of the definition of HPSM, its legality, history and development and the stages of HPSM will take place and the consecutive section will confer the contracts of HPSM, their definition and legality and Shariah requirements of implementation.

### Comprehension of HPSM

Hire Purchase under Shirkah al-Milk (HPSM) represents a hybrid contract that merges three distinct contracts: shirkah (partnership), ijarah (hire), and sale. In practice, HPSM involves a contractual agreement facilitated by the bank, wherein equipment, machinery, buildings, vehicles, or other durable assets are leased to customers at a rental price typically higher than the prevailing market rate. Crucially, the bank commits to transferring ownership of the leased assets to the lessees upon the completion of the lease period, usually for a nominal price.<sup>1</sup>

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### Historical Background of Hire Purchase Contract

The term HPSM is recognised as “leasing ending with ownership” which is in Arabic called “*ijarah muntahiyah bi al-tamlik*”. The practice of hire-purchase, known as lease purchase or lease ending with ownership in English, can be traced back to the 19th century in England. In Arabic, this concept is referred to as “*ijarah muntahiyah bi al-tamlik*”.<sup>2</sup> The hire-purchase contract was originally introduced by a British musical instruments seller to facilitate the sale of his goods to customers. This innovative approach gained popularity quickly and led to a surge in demand for hire purchase contracts worldwide. Notably, major companies like “SINGER,” renowned for their production of home appliances and electronics, also embraced the hire-purchase model in their business run.<sup>3</sup> In 1952, the hire-purchase contract gained further recognition and popularity in the United States when it was introduced under a new name, “leasing,” by the United States Leasing Corporation. This development paved the way for the expansion of the concept to other parts of Europe, primarily through the efforts of the Mercantile Credit Company. Notably, the first leasing company in France, named “Locafance,” was established in 1962. Subsequently, the idea of hire purchase spread rapidly to various regions across the globe.<sup>4</sup>

The concept of hire-purchase contracts was relatively unfamiliar to classical Muslim scholars, as there was no prominent written evidence specifically addressing it. Instead, scholars traditionally discussed hire and purchase as separate topics, categorizing them under different headings such as “The Book of Sale” (*Kitab al-Bay*) and “The Book of Letting” (*al-Ijarah*) in their Islamic jurisprudence (*fiqh*) books. Interestingly, these two topics were often presented sequentially, reflecting their close relationship and their significance in commercial activities. While classifying various types of contracts in Islamic commercial activities, “the basic contract in many cases and situations are contracts of exchange and contracts of utilization of usufruct. The former is a contract of sale or bay’ which implies the transfer of ownership of a property from one party to another; while the latter is a leasing contract (*ijarah*) which affects the transfer of usufruct of a property from one to another. According to Bakar, both contracts of sale and

hire constitute the main commercial activities because all residual contracts are mostly dependent on these two contracts”.<sup>5</sup>

Islamic finance institutions introduced hire purchase in the 1980s, and since then, it has emerged as a significant component of Islamic banking products. Hire purchase is recognised by various names in different jurisdictions, such as *al-ijarah al-muntahiyah bi al-tamlik*, *al-ijarah bi al-shart al-tamlik*<sup>6</sup>, *al-ijarah ma’a al-iqtina’*<sup>7</sup>, *al-ijar al-muntaha bi al-tamlik*<sup>8</sup>, *al-ijar alladhi yantahi bi al-tamlik*<sup>9</sup>, *al-ta’jir al-muntaha bi al-tamlik*<sup>10</sup>, *al-ta’jir al-muntaha bi al-tamalluk*, *al-ta’jir ma’a al-mawai’dah bi al-tamalluk*<sup>11</sup>, *al-ijar al-satir li al-bay’*<sup>12</sup> *al-ijar al-muqtaran bi al-wa’d*<sup>13</sup>, hire purchase under *Shirkah al-milk*.

### Shariah Background of HPSM

The concept of *ijarah muntahiyah bi al tamlik* or HPSM is similar to a regular *ijarah* contract, except for the lessor’s commitment to transfer ownership to the lessee after the *ijarah* term.<sup>14</sup> Wahabah al-Zuhayli<sup>15</sup> cites that in the Islamic hire-purchase contract, the *ijarah* (leasing) and sale contracts, which form its foundation, are typically executed separately in different time sessions. This separation is essential, as combining the two contracts within a single transaction would render the entire operation invalid. Therefore, the *ijarah* and sale contracts operate autonomously and sequentially, rather than simultaneously. This adherence to separate time sessions contributes to the Shariah compliance of the Hire Purchase under the *Shirkah al-Milk* (HPSM) product.

According to Shariah rulings, there is a general principle that everything is initially considered acceptable (*mubah*) for use, consumption, or transactions unless there is a clear prohibition against it from a Shariah perspective. In the case of HPSM, since the contracts involved occur in separate time sessions rather than simultaneously, there is no obvious restriction from a Shariah perspective. Even a combination of *ijarah* and sale contracts within a single agreement is permissible in the Maliki school of thought. An example that illustrates this is when a buyer purchases a cloth with a specific price, but with the condition that the seller (tailor) will also make or sew it for the buyer. In this scenario, the buyer effectively hires the tailor to create the dress and subsequently

purchases it.<sup>16</sup> Thus, Hire Purchase under Shirkah al-Milk (HPSM) can be deemed as a Shariah-compliant product.

Moreover, no valid reason has been found to prohibit the use of hire purchase contracts in transactions. This is due to the broad principle that allows engagement in contractual dealings that are not explicitly forbidden by Shariah. The application criteria of hire purchase contracts strictly adhere to the prohibition of *riba* (interest) and *gharar* (uncertainty), ensuring compliance with the fundamental principles of all combined contracts. Therefore, the Islamic hire-purchase contract is considered permissible as it does not involve any element of *gharar*. Consequently, both the contract itself (*aqd*) and the subject matter are deemed permissible for transactions.

The legitimacy of the Islamic hire-purchase contract was resolved through a fatwa issued by the International Islamic Fiqh Academy during its meeting in Jeddah on 10-16 Rabi al-Awwal 1406 / 28 December 1985. The Academy approved the permissibility of combining *ijarah* (leasing) and sale contracts when the subject matter remains the same. Hence, if hire purchase was not considered permissible, such a fatwa would not have been approved by the academy. Moreover, the International Association of Muslim Scholars approved a fatwa during its meeting held in Kuwait on 7-11 March 1988, stating that the Islamic hire-purchase contract can be validated by combining two different contracts: *ijarah* (leasing) and gift (*hibah*). However, certain conditions must be fulfilled for the contract to be considered valid. Firstly, the duration of the leasing period must be clearly specified and agreed upon by both parties, and the rules of the *ijarah* contract must be adhered to throughout that period. Secondly, each instalment amount must be predetermined and fixed. Finally, the ownership of the asset would effectively be transferred to the lessee through the implementation of the gift (*hibah*) contract. This fatwa also ensures the compliance of the hire-purchase contract with Shariah principles.<sup>17</sup>

### Application Phases of HPSM Contract

The HPSM contract comprises three distinct phases. The initial phase involves the purchase of the property or asset under joint

ownership, also known as *shirkah al-milk*. *Shirkah al-milk* refers to a contractual arrangement where two or more individuals contribute equity, jointly acquire an asset, share the benefits according to the agreed terms, and bear the losses proportionate to their respective equity holdings.<sup>18</sup>

The second stage of HPSM is changing the *shirkah al-milk* contract into *ijarah*. This means in the HPSM the financing *ijarah* is a hybrid form of *ijarah* conceptualised by the modern Islamic banking and finance industry with a combination of *ijarah* and sale contracts. The duration of this *ijarah* takes an extensive time frame, where the instalments of rental of the asset would be higher than the current market price so that the paid rent can recover the price of the leased asset within the estimated period. Under this payment structure, the lessor is obligated to transfer the ownership of the leased asset to the lessee upon the completion of the lease period, provided that all instalments have been paid according to the agreement. In financial *ijarah*, it is crucial to explicitly specify the method by which the ownership or legal title of the leased asset will be transferred after the tenure concludes. Various methods may be employed to effectuate the transfer of ownership or legal title to the lessee, and these should be clearly outlined in the agreement.<sup>19</sup>

The final phase of the HPSM contract involves the transfer of legal title through *ijarah muntahiyah bi al-tamlik*. In the HPSM arrangement, the lessor makes a prior commitment to the lessee that they will sell the property upon the completion of the *ijarah* period. This serves as a method of transferring ownership from the lessor to the lessee in accordance with the terms of the contract.<sup>20</sup>

### Literature review

#### Comprehension of a Musharakah or Shirkah Contract

A Musharakah contract is initiated when two or more parties enter into a contract. In the context of Islamic modes of financing, the term “*musharakah*” specifically refers to a joint partnership where the parties collectively own equity or property. The distribution of shares among the parties is determined based on their negotiation or mutual agreement. It is important to note that the term “*musharakah*” carries a more specific connotation within this context, compared to the broader term “*shirkah*”.<sup>21</sup> According to

Sami, musharakah is characterised as a contractual arrangement between an Islamic bank and one or multiple partners or clients, with the provision for termination within a specified agreed period or upon the fulfilment of specific conditions. In this joint venture contract, one partner can contribute a higher percentage of the total capital, while the other partner entrusted with the management of the musharakah has the flexibility to employ any means that are conducive to generating profits.<sup>22</sup> The AAOIFI Shari'ah standard defines musharakah as an agreement in which two or more parties come together, combining their assets, labour, or liabilities to generate profits<sup>23</sup> whereas the Central Bank of Malaysia delineates musharakah as a contractual agreement between two or more parties to jointly invest in a specific business venture. Each party contributes capital, which can be in the form of cash or other assets. The profits generated from this partnership business are distributed among the parties based on their agreed-upon ratio. Similarly, any losses incurred are also shared by the parties proportionate to their respective contributions.<sup>24</sup>

### Shariah Backgournd of Musharakah or Shirkah Contract

The concept of musharakah is traced in the Qur'an, i.e. 38:24 and 4:12, in Sunnah, i.e. Mishkat al-Masabih, hadith no. 2933 and Sunan Abi Dawud, hadith no.3383. The address to Sai'ib ibn abi Sai'ib as a partner by the Prophet (pbuh) on the day Makkah conquer is an example in this regard.<sup>25</sup> The indication of the permissibility of musharakah among the companions is also evident, instances are, "the profit is based on what has been conditioned and the loss is based on the amount of the capital (contributed by partners)"<sup>26</sup> and "the loss is based on the amount of the capital, and the profit is based on what has been stipulated".<sup>27</sup> Shariah scholars<sup>28</sup> generally consider the musharakah contract permissible since there is no explicit prohibition against it in Islamic law. Musharakah on the other hand, is permissible by reasoning (qiyas) because of its common practice as one of the fundamental transactions in all societies since the arrival of Islam. However, some scholars hold a different opinion arguing that the musharakah is an interest-based contract, as the initial intention of

the contract is to provide a loan to the clients to generate additional funds from the same loan amount.<sup>29</sup>

### Classification of Musharakah Or Shirkah

Shirkah contract is divided into two types mainly:

1. **Shirkah al-milk:** Refers to joint ownership of a property or asset by two or more parties. This type of contract can take two different forms. In some cases, it is a deliberate choice made by the contracting parties. For example, if two or more individuals decide to jointly purchase a property, they enter into a shirkah al-milk agreement regarding that property. The relationship among the parties is established based on their intention and mutual agreement. On the other hand, shirkah al-milk can also arise as a consequence of certain events or incidents, rather than being a deliberate choice. For instance, when a person passes away, their heirs automatically inherit their property, leading to joint ownership among the heirs. In this case, joint ownership occurs as a natural outcome of the death of the person, not as a result of the heirs' intention.<sup>30</sup>
2. **Shirkah al-aqd:** Refers to a business partnership that is formed through a mutual agreement. It can be described as a joint commercial enterprise where two or more parties come together to engage in a business venture. Shirkah al-aqd can be further classified into three different types<sup>31</sup>, which are:

**Shirakh al-amwal** is a form of business partnership where each party invests capital into a commercial enterprise. **Shirkah ala a'mal**, also known as shirkah al-taqabbul, shirkah al-sanai', or shirkah al-abdan, is a type of partnership that occurs when all partners jointly agree to hire the services of a third party. This third party provides services to customers on behalf of the partnership, and the fees charged to the customers are then distributed between the two parties (the partnership and the hired third party) according to their agreed-upon ratio. **Shirkah al-wajuh** is a contract in which all parties jointly own commodities without any initial investment, with the intention to sell them immediately at a higher spot price than the purchase price. The resulting profit earned from the sale is distributed among the

parties in proportion to their agreed-upon or mutually understood terms.<sup>32</sup>

### Contemporary Types of Musharakah Contract

Musharakah can also be classified as mentioned by Sami into three distinct classifications<sup>33</sup>, they are:

- a) **Commercial musharakah** is a specific type of contract with a singular objective, such as the purchase and sale of machinery and commodities. In this arrangement, both the bank and the partner contribute capital, but the partner takes on the primary responsibility for managing, marketing and handling the accounts related to the venture. Meanwhile, the bank's role is focused on providing banking services, monitoring the progress of the enterprise, and other related activities.
- b) **Decreasing participation in musharakah** is a particular musharakah contract, the bank facilitates a gradual ownership transfer of the venture or asset to the partner. The partner involved in this contract typically aims to obtain legal ownership of the asset as quickly as possible. However, there is a condition that the bank will receive a portion of the profit from its financed portion as agreed upon in the contract<sup>34</sup>, this is also known as Musharakah Mutanaqisah Partnership (MMP).
- c) **Permanent participation musharakah** is a contract wherein the bank becomes a shareholder by investing a portion of the capital in a specific venture. Both the bank and the partner actively participate in the management and supervision of the venture, sharing profits and losses accordingly. The term "Permanent" does not imply an endless duration but signifies that the participation will continue until the completion of the venture or the expiration of the agreed-upon duration of the participation.<sup>35</sup>

AAOIFI has incorporated contemporary classifications of musharakah contracts, which Uthmani introduce as "modern corporations" as follows:

- a) **Musharakah based on a stock company**: in which the capital is divided into equal units known as commercial shares. In this arrangement, each shareholder or partner assumes limited

liability that is restricted to their respective capital contribution.<sup>36</sup>

- b) **Musharakah based on joint liability company**: The joint liability company is a type of partnership where individual partners are required to publicly declare their association as a registered company with a distinctive trademark. In this form of partnership, all partners assume personal responsibility for the company's obligations and liabilities. If the company's current assets are insufficient to meet its obligations, each partner is personally liable for fulfilling those obligations.<sup>37</sup>
- c) **Musharakah based on financing partnership**: Where operating partners are differently treated in terms of determination of the ownership of partners. And in this partnership, the ownership is calculated based on disproportionate lots of shares, not on the proportional basis of shares which are equal in number. The financing partner is considered a sleeping partner. Therefore, all managing partners are responsible for any obligation and liability of the company from their personal assets based on the joint liability. However, the liability of the sleeping partner will be limited according to his share lots whose liability does not extend to his personal wealth.<sup>38</sup>
- d) **Musharakah based on company limited by share**: is a form of personal partnership in which participation is determined by an equal number of shares. In this type of partnership, both the managing and sleeping partners share the same obligations and liabilities as in a financing partnership.<sup>39</sup>

### Comprehension of Ijarah

Literally, it means the sale of usufruct or "possessing of a usufruct for a consideration".<sup>40</sup> School of Hanafis define the ijarah as a contract for the use of the usufruct for a counter value or price<sup>41</sup>, Malikis and Hanbalis define it as the transfer of the use of usufruct of a permissible object for known counter value<sup>42</sup>, and the Shafi'is define it as a contract for the use of a permissible, determined, and known usufruct, capable of being spent, for a known counter value or price.<sup>43</sup> Shariah Standard of AAOIFI defines ijarah as "leasing

of property pursuant to a contract under which a specified permissible benefit in the form of a usufruct is obtained for a specified period in return for a specified permissible consideration”.<sup>44</sup>

Ijarah can be classified into two distinct subject matters. The first pertains to the employment of a person’s services, where the person is hired and paid wages as compensation for their services. In this scenario, the employer is referred to as *musta’jir*, the employee as *ajir*, and the payment of wages as *ujrah*.<sup>45</sup> Second “to transfer the usufruct of a particular property to another person in exchange for a rent claimed from him”. The subject matter, in this case, is the usufructs of assets and properties, not human beings.

In the context of Islamic commerce, *ijarah* represents a contractual agreement between a property owner and an individual seeking to lease the property. The involved parties enter into a lease contract, also known as a hire contract, outlining the terms and conditions of the arrangement.<sup>46</sup> On the other hand, in the context of Islamic banking, *ijarah* is a lease contract that involves a bank or financial institution leasing equipment or a building to its clients for a fixed charge. Upon the termination of the lease period, the bank typically offers the property for rent again to ensure it remains in use and is not left idle for an extended duration. The ownership title of the property remains with the bank, which means it assumes the risks associated with ownership, including economic downturns and other related risks.<sup>47</sup>

### Shariah Background of Ijarah Contract

Ijarah contract is principally permitted originating from the Qur’an, i.e. 28:26, 65:06 and 18:77, the Sunnah, i.e. Ibn Majah, hadith no. 2443 and Mishkat al-Masabih: 2982 and consensus (*ijma’*) of the legal community and reasoning (*qiyas*).

The permissibility of *ijarah* transactions is widely accepted across various schools of thought within the Muslim Ummah. There has been a consensus among scholars from the time of the companions of Prophet Muhammad (pbuh) up to the present day regarding the validity and acceptability of *ijarah* transactions except Adul Rahman Ibn al-Assam who opined that it is prohibited due to *gharar* as it is a contract on usufruct not yet found. However, the

unanimous agreement among scholars demonstrates the longstanding recognition of *ijarah* as a permissible and legitimate contract within Islamic finance. The acceptability of *ijarah* is supported by rational reasoning (*qiyas*), as it provides a convenient means for individuals to access and utilise assets that they may not own.<sup>48</sup> Not everyone has the ability or means to own tangible assets outright, and *ijarah* allows for the acquisition of the right to use such assets without the requirement of ownership.

### Classification of Ijarah

Ijarah exhibits various variations in terms of its nature and applications. These variations can be broadly categorized into two classifications. Primarily, *ijarah* is classified based on the subject matter<sup>49</sup> and another is based on the contractual relationship between the institution and customer.<sup>50</sup> Ijarah based on the subject matter consists, firstly, **ijarah ‘ain**, which refers to the leasing of the usufruct (beneficial) of a specified good or asset based on fixed and upfront rental payment at the initiation of the lease contract, or deferred and paid periodically payment over the lease term. The assets or goods involved in *ijarah ain* can encompass tangible like properties, transportation, and factories as well as non-material entities like facilities. Importantly, in *ijarah ain*, the transfer of ownership of the leased asset to the lessee does not occur. Another category of the *ijarah* based on the subject matter is *ijarah ‘amal*, which is to employ the services of a person on wages to him with consideration for hired services or skills. There are two types of workers in this *ijarah* contract; a), an employee works only in the interest of employers and has no right or choice to serve other people or employers during the contract period and b) is independent contractor or service provider who serves for the general public as a freelancer. Ijarah ‘amal refers to the employment of a person’s services in exchange for wages or compensation for their hired skills. This type of *ijarah* contract involves two categories of workers: **a) employees**: these individuals work exclusively for their employers and do not have the right or freedom to serve other individuals or employers during the duration of the contract. Their services are dedicated solely to their employer’s interests. **b) Independent contractors or service**

**providers:** these individuals are considered freelancers or independent contractors who offer their services to the general public. They are not bound by exclusivity and have the freedom to provide their services to multiple clients or employers. However, the last category of ijarah based on the subject matter is ijarah mawsufah fi al-dhimmah is a lease contract in which the lessor commits to thoroughly providing the specified usufruct. This type of ijarah contract draws upon the qualities of a salam contract, ensuring clarity and eliminating potential conflicts regarding the usufruct. It applies to both the benefits derived from an object, such as leasing a specific car, as well as services provided by individuals, such as tailoring or teaching.<sup>51</sup> The application of this ijarah is being considered as a supporting contract in Musharakah Mutanaqilah Partnership (MMP) based financing for houses that are still under construction.

On the other hand, ijarah based on contractual relationships comprise, firstly, operating ijarah, originated from the ijarah 'ain, in which both the lessor and lessee mutually agree upon a specific duration for leasing where the lessor receives rent from the lessee, and the lessee enjoys the benefit and use of the asset based on either short or long-term, with the renewal option of renewal for an extended period upon the expiry of the first contract. This operating ijarah does not involve the transfer of ownership to the lessee, nor is there any prior promise to transfer ownership. Financing ijarah, the second category of ijarah based on contractual relationships is the financial ijarah, which is a contemporary form of ijarah developed by the Islamic banking and finance industry. It combines elements of both ijarah and sale contracts. This type of ijarah typically involves a longer duration, and the rental instalments for the leased asset are set higher than the current market price. This approach allows the lessee to recover the cost of the leased asset through the paid rent over the estimated period. The payment structure entails an obligation for the lessor to transfer ownership of the leased asset to the lessee at the end of the lease period, once all the agreed-upon instalments have been paid. This aspect distinguishes financial ijarah from traditional ijarah, as ownership is eventually transferred to the lessee upon completion

of the payment terms.<sup>52</sup> Hire Purchase under Shirkah al-Milk is considered one of the types of financing ijarah.

### Comprehension of Sale Contract

The term “sale” originates from the Arabic word “bay’”, which encompasses the concept of both buying and selling. Sale can be understood as the act of exchanging one commodity for another, engaging in barter trading, exchanging a commodity for money (ordinary sale), or exchanging money for money (sarf) on mutual consent. In the Hanafi school, a sale is defined as the act of trading an owned commodity for another in a specified manner, while to the Shafi'i scholars, a sale is characterised as the exchange of an owned commodity for another, resulting in the transfer of ownership and the new owner taking possession of the exchanged item.<sup>53</sup> Sale is also referred to as a contract of exchange between two properties on the basis of ownership of the price and commodity.<sup>54</sup> Ibn Rushd, explains the nature of a sale as the exchange of two properties, hence, ascertains that the exchange can occur between two tangible properties, or it can involve the exchange of tangible property for a corresponding obligation or the exchange of an obligation for another obligation. In each of these three forms of exchange, the transaction can be either immediate or deferred.<sup>55</sup>

### Shariah Background of a Sale Contract

The legitimacy of the sale contract, when it is implemented according to its Shariah principle considered legal and permitted by Shariah. The legitimacy of the sale is evident by the Qur'an i.e. 2:275, 4:29 and 2:282, by the Sunna, i.e. Ibn Majah, hadith no. 2139, 2185 and 2187, Tirmidhi, hadith no.1209 and Abu Dawud, hadith no. 3503. Muslim jurists unanimously agree on the permissibility of sale transactions, provided that all conditions are met and the parties involved adhere to the terms of the sale contract<sup>56</sup> as a sale transaction enables individuals to fulfil their own needs and requirements through cooperation with others who are also seeking to fulfil their own needs. Consequently, there is no prohibition on sale transactions in this regard.<sup>57</sup> Hence, al-Shafi'i asserted that the general rule for all sales is permissible as long as

they are ended with the consent of both parties, except what has been forbidden by the Qur'an and the Sunnah.<sup>58</sup>

### Discussion

It is crucial to adhere to the Shariah requirements in the HPSM contract like in any other Shariah-compliant contract. When Shariah requirements are properly met, the contracting parties can engage with each other with satisfaction and confidence. However, it is important to note that a contract may be considered invalid if its necessary elements (rukn) are missing. These necessary elements are essential for the existence of the contract. Additionally, there are specific conditions for the contracting parties in HPSM. Failure to include these conditions in the contract may have negative consequences for its validity and effectiveness in the future. As discussed earlier, the HPSM consists of three sequential contracts, each with its own specific elements and conditions. However, it is noteworthy that the elements and conditions remain largely consistent across these three contracts since they involve the same parties throughout different stages of the transaction. In essence, the elements and conditions revolve around the same set of contracting parties throughout the various stages of the HPSM contract.

As the shirkah is the initial contract in HPSM, it is required to attain the elements and conditions of the shirkah contract first. Shirkah refers to something owned jointly through a partnership. Hence, the partnership is one of the fundamental elements of the shirkah contract. The partners, as the foundation of a shirkah contract must be fitted with necessary qualities which are considered as the conditions of the contract such as the sound mind, maturity (rushd) and puberty (bulugh) of age to enter the contract in order to acquire the capacity. However, it is important to note that the contract can be valid if it is entered into by a legal representative or guardian (wali) on behalf of a child. Additionally, it is crucial that both parties willingly and voluntarily agree to enter into the contract, hence, none of them is allowed to enter the partnership upon a force. Likewise, both parties must not be declared bankrupt which hinders the contract's validity.

The second component of a shirkah is the contract itself whose primary purpose is to eliminate uncertainties by outlining the investment and profits distribution percentage among the parties involved using definitive, clear, decisive, and absolute language in accordance with their agreed terms or mutual understanding.<sup>59</sup> Moreover, the capital must be ready to invest and contributed by all parties which either can be a monetary asset such as cash or a non-monetary asset which includes tangible and intangible properties.<sup>60</sup>

The third element of the shirkah contract is the asset whose necessary condition is, to be in existence at the time of contract execution and deliverable immediately, which must be specified by address. And the asset must produce Sharia-compliant substance and owned by the owner and known to all partners. Another element of the shirkah contract is the benefit of the asset where necessary conditions are; the asset must contain the full value of the money in its quality and appearance. The purpose of use should be in favour of Shariah<sup>61</sup> so, it cannot be used for the Shariah prohibited purposes such as a shop where the shopkeeper sells pork, or for a factory where they produce alcohol.

On the other hand, ijarah as to be the second contract of the HPSM contract, is also required to be applied in accordance with its essential elements and conditions. The ijarah contract consists of several crucial elements, each of which incorporates specific conditions that adhere to Shariah principles. The initial element of the ijarah contract involves the contracting parties, namely the lessor and lessee. It is essential that both the lessor and lessee satisfy the same conditions required for partners in shirkah contracts since they assume the roles of lessor and lessee within the ijarah contract. However, both the lessor and lessee have some unique responsibilities in a lease contract. For example in the case of a lessor, he is obliged to deliver the leased asset to the lessee at the agreed-upon time, yet the possession of the leased property and its legal title will remain under the ownership of the lessor. However, it is important to note that items that cannot be used without being consumed are not eligible for leasing. Therefore, objects such as money, perishable food items, fuel, and ammunition cannot be leased, as their use necessitates



consumption. If such items are mistakenly leased, the transaction would be considered a loan, subject to the rules pertaining to loans. Any rental charges imposed on such an invalid lease would be regarded as interest charged on the loan.

During the rental period, the owner is held responsible for maintaining the property in its usual condition, ensuring that it generates the intended benefit for which the lessee is paying rent. On the other hand, the owner assumes all liabilities associated with ownership, including government taxes, management fees, and insurance. Throughout the lease period, the leased asset remains the responsibility and risk of the lessor. This means that any harm or loss resulting from factors beyond the control of the lessee will be borne by the lessor. However, the lessor is not permitted to unilaterally increase the rent, and any agreement attempting to do so is considered invalid.

In terms of the lessee's responsibility in the contract, he is responsible for maintaining the property in its usual condition and ensuring it is not used in a harmful or unlawful manner. The lessee is obligated to cover the customary maintenance costs associated with the property's use, as well as utility bills such as electricity and water expenses. If the lessee rents a car, for example, he is responsible for fuel and engine oil expenses. Essentially, any liabilities arising from the use of the property are to be borne by the lessee too. The lessee is granted exclusive permission to use the property for the designated purpose as stated in the agreement. For example, if the property is rented solely for personal use as specified in the agreement, the lessee is not allowed to convert it into a shop or any other purpose not mentioned in the agreement. In such cases, the lessee is obligated to seek prior permission from the lessor. The lessee bears the responsibility to compensate the lessor for any harm or damage caused to the leased asset due to misuse or negligence on the part of the lessee.

The other element of an ijarah contract is the asset itself, and it must meet the same conditions that are mandatory for assets involved in shirkah contracts since it is the very same asset utilised in the ijarah contract as well. The subsequent element of the ijarah contract is the benefit or use derived from the leased asset. In order to align with Shariah principles, the benefit in the ijarah contract

must adhere to Shariah-compliant standards. This means that the benefit cannot involve any harmful use or usufruct that is prohibited by Shariah, such as engaging in the sale of pork within the leased premises or leasing a factory that produces alcohol or wine. Usufruct (*manfa'ah*) can only be assumable when the underlying asset exists. For instance, in the case of renting a house, the house must physically exist for the rental arrangement. If the house does not exist, the leasing contract to that specific house becomes irrelevant. However, in such cases, the ijarah contract can be transformed into a forward ijarah, where the customer and the Islamic financial institution jointly share rights over the asset under construction through a *musharakah mutanaqisah* contract. The Islamic financial institution then leases its portion of the asset to the customer under the contract of forward ijarah (*ijarah mawsufah fi al-dhimmah*), as the asset is still being constructed. During the construction period, the customer pays advanced rent. Once the asset is completed, the customer continues to pay the full rent to enjoy the usufruct of the asset.

The rent can be the further element in an ijarah contract which must be specified in the contract whether will be fixed or subject to variation throughout the entire duration of the ijarah contract. This clarification is important because the rental rate can either remain constant or be tied to a mutually agreed variable for a specified period. The currency name must be specified when stating an amount, such as Ringgit Malaysia (MYR) or US Dollars (USD) and must be in absolute amount. Merely stating a number, like five hundred (500), without mentioning the currency is not sufficient to finalise the contract. Accordingly, the agreement must clearly state the intervals of payment, whether they are on a daily, weekly, or monthly basis. Additionally, the methods of payment, such as cash, banking cheques, or banking transfers, should be explicitly mentioned. In the absence of specified methods, local customs relating to payment will be considered.

In addition, the contract itself is another element in the ijarah contract, which entails conditions that prevent the mechanism from any uncertainty. For example, in an ijarah contract, the offer and acceptance must be absolute and in definite and decisive language. Therefore, it must not be conditional. And it must be in the present

or past tense and neither in future tense nor imperative. The acceptance must agree with the offer, and both must be made at one and the same meeting.

Finally, the sale contract is the last stage of the HPSM contract. In the process of the sale contract, both seller and buyer must adhere to the same conditions as the lessor and lessee do in an ijarah contract, as well as the partners in the shirkah contract. The reason for this requirement is that the buyer and seller in a sales contract, the lessor and lessee in an ijarah contract, and the partners in a shirkah contract all represent the same individual or entity in the whole process. The only variation lies in their roles within the respective contracts, which shift sequentially according to the contractual intervals.

Another essential element of a sales contract is the asset or item being sold, which shares the same necessary conditions as the contracts of shirkah and ijarah. Additionally, the price of the sold item is a crucial aspect of the sales contract, and its determination and currency at the time of contract formation are essential conditions. The final element of a sales contract is the formal agreement itself, which encompasses conditions similar to those found in the ijarah and shirkah contracts that have been mentioned previously.

### Conclusion and Recommendation

The HPSM is a Shariah-compliant contract as hire and purchase separately are permissible transactions in the classical practices, whereas HPSM being a hybrid contract consisting of shirkah, ijarah and sale should also be allowed as it complies with all the Shariah requirements, essential elements and necessary conditions which have been incorporated in the study. Forming a new contract like HPSM is to be preferred based on the development of verses and hadiths if the contract does not contradict the Shari'ah requirements. However, the current IBF industry requires frequently innovative products that fit people's modern needs in line with Shari'ah. If forming a new contract gets prohibited, the people's lives will be in hardships and difficulties, which Islam wants to remove. On the other hand, the IBF is to keep its growth competing with its conventional counterparts; in this hindrance, if

innovation or forming a new contract is restricted, the long-cherished hope for the people who seek to transact according to Shari'ah concerning their holy faith would open the door for non-Shari'ah transactions.

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