MONEY IN ISLAM: A SOCIAL CONTRACT PERSPECTIVE

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Abstract

Money being the blood of economy and main determinant of many human transactions is an important topic to be discussed. Throughout the history there have been many who tried to explain nature and desired form of money in their writings. This topic has not skipped writings of Islamic religious scholars and economists as well. Current work attempts to review some of recent literature about essence of money from Islamic prospective. The review works which express different views from both Religious and Economic perspectives by six selective authors with diverse backgrounds. In the review, we mainly focus at the role of money as a social contract (between State and its citizens) and at some sharia compliance issues faced by commodity (gold and silver) and paper (fiat) currencies. Some of our important findings show that the commodity currency had problem of breach from State's side in some occasions, while paper currency is considered as an invalid contract by majority of the authors. The work concludes with summary of the authors' opinions and points out their relative strengths and weaknesses from Sharia and Economic prospective, which is extended with some recommendations for further research.

Keywords*:* *Islamic Money, Barter System, Commodity Currency, Fiat Money*

A. INTRODUCTION

Money is exciting topic of discussion both for religious and nonreligious people alike. If religious people are concerned about true concept of money because of its impact on their religious and worldly affairs, others are also concerned about its impact on their financial and social wellbeing. Among all religions, Islam as a religion brought by Prophet Muhammad (SAW[1]), can be argues to be the most pragmatic in terms of keeping worldly and spiritual matters in balance. In fact concept of religion (*deen*) in Islam is not limited to spiritual matters only but covers all of the matters in human life. Hence, we can notice that unlike in other religions many of worldly affairs are well defined in Islam.

Money being blood of economy and main determinant of many human transactions is a very important topic to be discussed. Throughout the centuries, it has taken many forms starting with various commodities and shifting to precious metals till it came to current form of paper or electronic currency.

[1]This is abbreviation of the phrase pronounced by Muslims upon hearing name of their Prophet mentioned, that reads in Arabic as '*sallallāhu ʿalayhiwa-sallam'* which is translated as "prayer and peace of Allah be upon him".

Many Muslims consider it important to truly define correct concept, role and form of money acceptable in *Sharia*. Especially after re-emergence of Islamic Economics and Finance in 1970s, concept of money in Islam became quite debatable topic. Not only its Islamic definition but also its economic considerations are important factor in those discussions. While some scholars of Islamic Economics took position of 'necessity of returning to true Islamic money in form of gold Dinar and silver Dirham, others insist that such return is neither practical from Economic prospective nor desirable from *Maslahah* (social wellbeing) prospective. Thus, this work attempts to revisit this debate and summarize arguments and comment on strength and weaknesses of each side.

This work will try to look at money as 'the subject matter of a social contract' between involved parties (the State and its citizens), which serves as medium of exchange in economic transactions. As a subject matter, it must meet all of its requirements from *sharia* prospective. On the other hand, from the social contract prospective it needs to meet all of the Islamic contractual law requirements as well. While keeping those concepts in mind this work will review some selected literature by authors with various backgrounds and viewpoints. Namely, it will analyse works of Umar Ibrahim Vadillo (2006) and Imrān N. Hosein (2007), religious scholar from Andalusia (modern day Spain) and Trinidad and Tobago respectively who have strong economic intuitions along with their deep knowledge of religious sources. Two papers of Ahamed Kameel Mydin Meera and Moussa Larbani (2006a, 2006b) will be viewed as well. Those Malaysian scholars of Islamic Economics are among the main proponents of gold Dinar. Finally, views of two opponents of gold Dinar (or proponents of paper money), i.e. Zubair Hasan (2008) and Murat Cizakca (2011) who seem to bring economic, historic and political facts and arguments out to the surface are also considered to keep balance in this review. Now, getting acquainted with main objective and list of works to be considered we can proceed with general definition of money in Islam.

B. GENERAL CONCEPT OF MONEY IN ISLAM

Meera & Larbani (2006) seem to give most broad and widely accepted definitions of the money as "anything that is accepted as payment for goods and services or debt". However, they also mention that in people's view it should be in form of notes and coins which is not necessarily true. As was pointed out by authors themselves, in history of humanity people used different commodities such as rocks, leather, salt, shells and other things as money which were later replaced with precious metals such as silver and gold. Three *main functions* of money from general economic literature that is mentioned by them are:

i. *Medium of exchange*: That is to function as a go in between thing for economic actors in purchase of goods and services. This function, they say, is important for improving economic efficiency and thus standard of living.

ii. *Unit of account*: This means that money is used as benchmark for measuring value of other goods and services. Therefore, there is no need to quote prices between each pair of goods and services, as it is required under barter trade.

iii. *Store of value:* Which means it keeps value over time to store some savings for future consumption. Good store of value should not depreciate much in value over time, which is not the case for perishable goods such as good with limited shelf-live. Authors also conclude that current paper money is not good store of value since its value reduces over time because of inflation.

Nevertheless when it comes to concept of money from Islamic prospective Hosein (2007) give more precise definition. This definition is based on his interpretation of the famous hadith about six ribawi items[2] which goes as follows:

AbiSa'id al-Khudri reported Allah's Messenger (SAW) as saying: "Gold for gold, silver for silver, wheat for wheat, barley for barley, dates for dates, and salt for salt. (When a transaction is) like for like, payment being made on the spot, then if anyone gives more or asks for more, he has dealt in riba, the receiver and the giver being equally guilty." (Sahih Muslim).

Hosein's interpretation comes up with three general characteristics of 'money' in Islam:

1. Money in Islam is limited to either precious metal such as gold or silver, or commodities such as wheat, barley, dates or salt, which have shelf-life and could be used as money in case of shortage in precious metals. In fact he argues this was the case in times of Prophet (SAW), where dates were used as money from time to time in markets of Medina. Additionally, other things which could be used as money are any agricultural or other type of commodities which is common in a particular locality and meet requirement of having some shelf-life and being generally accepted, such as rice in South-East Asia or Sugar in many Latin American countries. Another restriction that author derives from the hadith is that those metals or commodities should be used in equal amounts and on the spot when traded between same specie (i.e. gold for gold or date for date). This is however not necessarily the case for other non-money commodities such as cattle or clothing[3].
2. Commodities used as money (precious metal, foodstuff or others with shelf-life) should be traded for their intrinsic value, not for their nominal value such as contemporary paper currency. Thus author argues that value should be 'inside' the money not 'outside' being nominated by some regulatory authority.
3. Lastly, Hosein argues that money must be located in commodities that are created by Allah (SWT[4]) and their values are assigned by Himself. That property, in author's opinion, is related to Allah's (SWT) quality of al-Razzak (i.e. the provider of sustenance and the creator of all wealth).

If we generalize Hosein's interpretations, it would mean that money in Islam ('*Sunnah*money' as he calls it) must store value within itself, which would make it "immune to arbitrary external manipulation and devaluation". Therefore, he believes paper money could not serve purpose of money in Islam because it does not meet neither of three characteristics listed above and it is subject to manipulation. But, Hasan (2008) and Cizakca (2011) do not agree with him and in the section devoted to paper money we will bring details of their argument.

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[2] Those items are taken from several authentic narrations of Prophet (SAW) and include six commodities, namely gold, silver, wheat, barley, dates and salt.

[3]This also tells us that the hadith does not prohibit barter trade as some wrongly believe. See Cizakca (2011) for more details.

[4]SWT stands for Arabic phrase "*Subḥānahūwa-taʿālā"* which means "May He be praised and exalted", which is uttered by Muslims after name of Allah is pronounced.

However, if we look from *FiqhMuamalat* (Islamic rulings on transactions) perspective, Hosein's definition seems to be fair to both parties in any economic transaction. If one side is giving up something which is of true value (such as a car), it is only fair to get as a price something that has true intrinsic value (such as certain weight of gold). On the other hand, if seller of a car is paid by something that has nominal value only (such as a pack of banknotes) and that value is subject to change by some authority (such as central bank) it may be considered as unfair exchange.

C. BARTER IN ISLAM AND SCHOLARS OPINION ABOUT IT

As is expressed in most of economic history texts, barter was the general form of exchange before introduction of money to the scene, even though some of our authors may not agree with this concept. Among those who support this idea are again Meera and Larbani (2006b), who believe that barter trade is inferior to one with money because it poses some problems during exchange. Some of those problems are double coincidence of wants, unidentified medium of exchange and limited diversification of production. They believe that in barter economy efficiency is lower because of scattered medium of exchange function of money and, therefore, the standards of living would be lower than what would be in case of monetary exchange. Thus they reason introduction of money does not only solve the issues of barter trade, but then "promotes specialization, encourages trade and improves the overall well-being of people" as well.

In this article, economic historian Cizakca (2011) came into conclusion that Prophet (SAW) with Allah's (SWT) divine guidance was planning to make Makah as the global trade hub. Therefore, there was a need for promoting monetary trade by moving away from barter. Thus, Cizakca believes Prophet (SAW) prohibited barter through some of his al hadith while declaring it as a form of *riba* (i.e. *riba al-fadl*). And for that reason Prophet (SAW) allowed used of non-Muslim coins of Byzantine and Persia. This concept seems to be taken from interpretation of scholars such as Chapra (1985) and others who support this view.

Vadillo (2006) is very critical of above view of Riba al-fadl offered by Chapra (1985), thus that of Cizakca (2011). He believes Islamic economist misunderstood the concept and it opened door to various wrong interpretations about Riba. However, we will not go into detailed discussion of Riba by Vadillo, but only refer to concept related to the topic of barter. As he points out the prohibition of increase in exchange of six *Ribawi* items, by many *ahadith* of the Prophet (SAW), is not related to stopping barter trade or limited to trade of those items.

Vadillo (2006) argues that in fact that prohibition was on an increase in amount during trade of same species. Prophet (SAW) tried to prevent any unfair raise in quantity that could also be because of delay in payment, therefore such exchanges must be "hand to hand" (i.e. spot transaction) as well. Thus such restriction was put on commodities which played role of money as it was mentioned by Hosein (2007) earlier. But there were no such restrictions of trade in non-money commodities. All of those arguments imply that ahadith narrated from Prophet (SAW) related to 'Riba al-fadl' should not be understood as either prohibition or discouragement of barter.

D. GOLD AND SILVER MONEY FROM EARLY PERIODS OF ISLAM

The gold Dinar and silver Dirham served as money during the early and the rest of the Muslim history. As was rightly mentioned by Cizakca (2011) Muslims did not invent those coins but rather adopted them from Rome and Persia. Prophet (SAW) did not discourage use of such money and they were widely used during his lifetime as well. However, Hosein (2007) bring evidence from both Qur'an and Sunnah to support Dinar and Dirham to be legitimate currencies in Islam[5]. He also brings evidence from Qur'an and Sunnah to show that high status of gold and silver will also be maintained on the Judgement Day and the hereafter as well. For instance he quotes following verse from Surah al-Fatir:

"Gardens of Eternity will they enter: therein will they be adorned with bracelets of gold and pearls; and their garments there will be of silk." (al-Fatir 35:33).

Thus he concludes that above evidence show that"gold and silver were created by Allah Most High with great value bestowed on them, and that such value would survive this mundane world to be retained in the next world as well". Therefore, he concludes that it also means that Allah (SWT) created gold and silver to be used as money among other permissible commodities.

Meera and Larbani (2006b) list following five characteristics given in Economics literature that must be present in a commodity for it to function as money effectively:

1. *Standardisable/Homogeneity*: Its value should be easily ascertainable.
2. *Acceptability*: This requires the money to be something intrinsic value. Such value should be widely recognized by public and commodity should be rare in nature[6].
3. *Divisibility*: This is required to the exchange of a range of values, both high and low.
4. *Mobility*: Money should be easy to carry around and thus should not be burdensome.
5. *Durability/Stability*: It must not deteriorate, perish, deplete or erode easily over passage of time.

When authors compared six *Ribawi* commodities (i.e. commodities there were used as money during Prophet's (SAW) time) their analysis revealed following results presented in the table below:

Table1:Commodities with money characteristics

Characteristic Commodity	***Homogeneity / standardisable***	***Acceptability***	***Divisibility***	***Mobility***	***Durability / stability***	***Rareness***
Date	Good	Good	Good	Good	Good[a]	Fair
Wheat	Good	Good	Good	Good	Good[a]	Fair
Barley	Good	Good	Good	Good	Good[a]	Fair
Salt	Excellent	Good	Excellent	Good	Good[a]	Fair
Gold	Excellent	Excellent	Excellent	Good	Excellent	Excellent
Silver	Excellent	Very good	Excellent	Good	Excellent	Good

[5] Among many evidences, the verse 75 from surah of Al-'Imran (3: 75) and the verse 20 from surah Yusuf (12:20) seem to be more apparent.

[6] Authors note that: "Since fiat money has no intrinsic value of its own, it is made 'acceptable' by means of law, and hence the term 'legal tender'."

Notes: [a]*these items are perishable through bacterial activity, fungal, pest, water, fire etc. and are also destroyed in the process of consumption*
Source:Meera and Larbani (2006b), Seigniorage of fiat money and the Maqasid al-Sharia.

Analysing this table authors conclude that among those six commodities gold and silver dominate the other in terms of all characteristics. Therefore they say gold and silver are "also capable of playing the role of international money".
Meera and Larbani (2006b) mention that claim for gold and silver to be *Shari'ahmoney* is not their own view or new thing, but it has been stated my many scholars throughout history of Islam. Some examples such scholars include al-Ghazzali, ibnTaymiyyah, QudamaibnJaafar, ibnKhaldun and al-Maqrizi. They specifically highlight statement by al-Asfahani that only gold and silver could be used as money. Another example that they bring is of al-Maqrizi, who believed that "the change of money from gold and silver to copper *fulus*during the reign of Muhammad al-Kamilibn al-'Adil (615 – 35 H/1218 – 38 AD) in Eqypt and Syria, were among the reasons for the sufferings that population of Egypt has faced at that time, which included inflation and scarcity of necessities of life".

However, Hasan (2008) believes the system of bimetallism (i.e. use of gold and silver interchangeably) could bring disastrous results as was observed in history. He states that the ratio of prices for gold and silver did not remain the same in the market despite fixed exchange rate between the coins announced by the mint. Thus, the more valuable metal would be replaced by relatively cheaper one in monetary exchanges, and hence leaving only one metal in the circulation.
Our comment on this would be that such practices may have been witnessed in West or during time of Muslim sultans where *Shari'ah* rule regarding money exchange (i.e. bay al 'sarf) was not strictly followed. However, there are clear ahadith which prohibit fixing of price of gold to silver regarding any future exchanges. Prophet (SAW) did not discourage use of one metal instead of the other for payment of debt or other monetary obligations, but required spot market rate to be followed for date of final transaction. That means no fixed ratio for gold and silver exchange for future date could be ascertained neither by the mint nor by any other authority in Islam.

Hasan (2008) further argues that price of the gold or silver coins will depend on supply and demand for those metals in the global market. And inflow and outflow of those metals to particular country will have negative effect on price stability. Therefore, inflow would cause inflation while outflow would cause deflation. Cizakca (2011) thus comments such influence of change in quantity of precious metals on economy resulted to formation of Mercantilism throughout the Europe, who fiercely tried to ensure that gold inflow was always more than its outflow.

Cizakca (2011) adds two more reasons for inflationary tendency of gold and/or silver based money. First, he states findings that discovery of new silver mines resulted to increase in supply thus causing inflation throughout Europe. The second reason for this inflation was debasement (reduction in gold/silver content) of those coins. As he explains this was done by governments by "striking more coins from a given amount of pure gold". He presents some evidence to prove that such events were not only witnessed in Christian world of Europe, but also there were such cases in certain periods of Ottoman Empire.

Above and previous reasons that are given by Cizakca (2011) and Hasan (2008) would result into working of so called *Gresham's Law*. According to this law, *'bad money drives good money out'*, which means after being aware of debased or devalued coins people withdraw those with higher gold content or value out of circulation and only cheap/low content coins will be left in the circulation. As a result the general price level will increase causing inflation in the economy.

Observing comments of both Hasan (2008) and Cizakca (2011) about gold and silver money, we can see a general flaw in their arguments. Almost all of the issues they raise are problems with the issuer or controller of those coins not the coins themselves. We may consider coinage of gold and silver by particular government or authority and peoples acceptance of those coins in their intrinsic value as some sort of social contract. In such a contract, one side (i.e. a Muslim government) is offering to coin and circulate gold and silver money in its true value and other side (i.e. citizens of such state) accepting such an offer. However, as soon as citizens notice breach of contract from government's side by trying to sell debased coins above their true price (at price of not debased coins) they will take action. This puts into motion *Gresham's Law* and public starts withdrawing unaffected coins because of breach of contract from side of the government. Such action is not allowed according to *Shari'ah* law and any such attempt by a Sultan or anyone in the authority should be equivalent to deception (that would result to breach of contract). Thus any party guilty of such public crime should be punished respectively.

E. INVENTION OF PAPER MONEY AND DEBATES RELATED TO IT

Vadillo (2006) explains how paper money went through three stages; the fact which is known through economic history literature as well. The first stage started by banks issuing a promissory note to the depositor of gold and silver currency which were convertible at any time upon depositors demand[7]. In the second stage governments or central banks took over privilege of issuing those promissory notes from banks on themselves. Afterwards gold or silver backing of those notes decreased and eventually was revoked. The third and final stage, where there is no backing of notes by any specie and legal value of the currency is determined by state's mandate had officially started with abolishment of Bretton Woods agreement in 1971.

By identifying and explaining those stages, what Vadillo is trying to get across is that current paper moneys represent a mutilated form of original contract that bank depositors had with the bank in the first stage. He claims and it is obvious that the promissory note of the first stage represented debt. This debt was in return for certain weight or units of identified specie payable to the depositor upon presenting of the certificate to the issuing bank. However, when it came to the current stage currency notes issued under 'legal tender' mandate do not promise anything in return. This means that governments or central banks

[7] In theory those notes were supposed to be 100% backed by species, but in reality they were rarely so. Start of fractional reserve banking practice was the main reason. See Section 6 on fractional reserve banking for more details.

took those obligations of the bank on their shoulders, but later totally abandoned obligation part of the contract.

Vadillo (2006) questions whether promissory note of the first stage could be used as money. According to him it cannot, simply because it represents debt and debt could not be interchanged without prior agreement of the debtor. Here he provides fatwa by Imam Malik (R.A.) as saying:"One should not buy a debt owned by a man whether present or absent, without the confirmation of the one who owes the debt, nor should one buy a debt owed by a dead person even if one knows what the deceased man has left. That is because to buy it is an uncertain transaction and one does not know whether the transaction will be completed or not." Imam Malik continues as: "There is another fault in that as well. He is buying something which is not guaranteed for him, and so if the deal is not completed, what he has paid becomes worthless. This is an uncertain transaction and it is not good." Thus here Imam Malik is talking about *gharar* (great uncertainly) involved in such transaction and bad consequence resulting from it. We can see some real life example of such defaults in bank runs of late 19th and early 20th century in Europe and the U.S., as well as huge defaults during Great Depression of 1929-32.

There are also some restrictions pointed out by Vadillo (2006) for use of paper notes backed by either gold or silver. Firstly, if we are to follow rules of bay al-sarf (monetary exchange) in *Sharia*, it is not allowed to use the gold or silver for exchange unless it is physically present. Therefore, the paper notes that represents obligation of gold or silver could not be used to purchase any physical gold or silver. Additionally, as he pointed out paper money (promissory note) could not be used for purchase of other paper moneys because of prohibition of *Debt-for-Debt* transaction. Finally, he generalized this case for any foodstuff that could be used as payment (i.e. any of *ribawi*items) and then to any form of 'common money'. Thus he concludes that paper money (i.e. promissory note) can't be used in an exchange, but could only be considered as a private contract.

However, Hasan (2008) and Cizakca (2011) may not agree with this argument simply because they consider present form of money as not promissory note but rather a 'legal tender'. It stands on its own and does not represent any specific commodity or specie. Hasan (2008) argues from economic prospective by highlighting undesirability of wasting precious metals to be used as money, he concludes if 'worthless chits of paper' could do the job why should we insist on used of gold or silver. He bring analogy of "insisting that cinema tickets must be printed on chocolates; for, if one does not see the movie one may eat his".

Cizakca (2011) believes there is nothing Unislamic about paper money and bring fatwas form some Muslim scholars to his support. He writes: "*Some of the most respected classical Muslim scholars, particularly Muhammad ibn al-Hasan al-Shaybani, Ibn al-Qayyim and IbnTaymiyyah did not limit currency to gold and silver coinage only. Ahmad ibnHanbal ruled that there was no harm in adopting as currency anything that is generally accepted by the people. Thus, these scholars, among themselves, opened the way for Muslims of future centuries to utilise paper money. Leading contemporary scholars like Yusuf al-Qaradawi and Muhammad TaqiUsmani are also of the same opinion*" (Cizakca (2011), pp. 52-53).

Something interesting that we observe in those literatures is that sometimes both supporters and opponents of gold and silver money bring quotes from same Muslim scholars as evidence for their argumentation. For instances, if Meera and Larbani (2006b) give example of Ibn Taimiyyah among those who support use of gold and silver for money. On the other hand, Cizakca (2011) also give example of Ibn Taimiyyah among scholar who did not limit currency to those metals only as we could see above. Probably, there is some misinterpretation of historical scholars' statements either by one of the groups or both of them. Hosein's (2007) comment regarding use of paper for currency could put some light into such disagreement.

Hosein (2007) write that some scholars argue that the mankind is free to use anything such 'as grain of sand or shell found on the seashore' as money[8]. For those arguments his response is as follows: "*Our response is that grains of sand or shells found on the seashore cannot qualify in Islam as money according to the Hadith since they are neither precious metals nor commodities that are consumed regularly as food*" (Hosein (2007), pp. 15). Additional reasons for his rejection of the paper money are the non-existence of intrinsic value in it and it being human innovation rather than being true creation of Allah (SWT).

Meera and Larbani (2006b) list some disadvantages that paper money has compare to money based on precious metals. They argue creation of fiat (non-backed paper) money could result to inflation, market bubbles and amplification of business cycles, increase in unemployment, requirement of continuous growth for sustainability, increase in inequality, seigniorage, bank failures and financial crisis. Additionally, they believe that existence of many national fiat currencies would open doors for currency speculation, manipulation and arbitrage. Authors say having fiat currency could make developing nations susceptible to destabilization by international speculators and manipulation by developed nations due to ease of transferring electronic money, and monopoly of international trade by currencies of developed nations.

F. WHAT IS DESIRABLE FORM OF MONEY IN ISLAM

Having observes arguments for and against gold or silver as well as paper money one may wonder, so what is desirable form of money in Islam. Here we will turn to arguments by each side once again. Cizakca (2011) argues that because paper money did not exist during Prophet's (SAW) lifetime, he could not have used it. However, he questions if there was such choice given to him, what would he do? Cizakca then continues speculating since Prophet (SAW) had strictly followed Qur`an, and because there is no requirement to use some particular currency but the strong prohibition of the interest in Qur'an; Prophet's (SAW) choice would be obvious. Cizakca believes that Prophet (SAW) would prefer paper money to gold or silver coins simply because while paper money fulfils requirement of "zero percent rate of interest", coinage does not.

Reading Cizakca's (2011) article one is certain to get confused by what author means by "*zero percent rate of interest*". While talking about near zero percent interest of paper money he quotes very

[8] This is similar to Hasan's (2007) and Cizakca's (2011) arguments for support of paper money.

low interest rates observed in Japan and some European countries recently. However, when claiming existence of high interest rates under gold and silver coinage he quotes some evidence of price appreciation from history of gold and silver usage mainly because of debasement and seigniorage. So, what exactly does author mean by interest rate? Is it the interest charge on loan or the inflation or both of those? It seems as if he is using double standard, quoting low rates of interest on loans for certain paper currencies (while keeping silent about general level of inflation on paper money) and quoting inflation for gold and silver coins which was observed during some periods of their usage.

Meera and Larbani (2006a) are more specific about Riba that could result from modern paper money and banking system. They mention three features of the current system that can result to Riba. If we stick to general definitions of Riba as an unjustified increment in borrowing or lending money, thinks will appear clearer to us. *First form* is in the devaluation of fiat money of any forms (including demand deposits and electronic money). *Second one* in the form of interest paid over the amount of money borrowed[9]. *The last one* is in form of any increase resulting from modern tool of fractional reserve banking. These three characteristics of paper money and resulting banking system, authors claim, are "fundamental to the process of money creation by the banking sector" and thus may amount to Riba.

Hosein (2007) bring some evidence from the Qur'an and Sunnah to support of argument similar to one above. More specifically he quotes verse 85 of surah Hud as below, where Prophet Shuaib (peace be upon him), who is known in Biblical literature as Jethro, tells to his nation following words:

"And O my people! Give just measure and weight, and do not deprive people of what is rightfully theirs by diminishing the value of their things and do not commit evil in the land with intent to corrupt and destroy." (Hud, 11:85)

Hosein (2007) write Prophet (SAW) has declared as Riba any transactions based on deception, and that yields a profit or gain to which one is not justly entitled. In a hadith narrated from Anasibn Malik, Messenger of Allah (SAW) said: *"Deceiving a mustarsal (someone who is unaware of market prices) is Riba." (SunanBaihaqi)*.

Thus, the author argues that "The modern monetary system based on non-redeemable paper currencies that constantly lose value constitute precisely such deception that yields profit or gain to which the founders of the monetary system are not justly entitled". Therefore, Hosein is convinced that such action would be recognised as Riba.

Hasan (2008) is nevertheless content with such a system; because he believes what is important is ultimate exchange which is between goods and/or services while money is something as a go-in-between. He thinks the necessary condition for something to serve as money is just general acceptability. The modern 'promise to pay' which is serving as money he argues is a wonderful development. Therefore, it is "worth more than all the money of Nobel Foundation if it were the product of conscious research" he writes.

Vadillo (2006) on the other hand argues supporters of fiat money (such as Cizakca and Hasan) are wrong in their perceptions. He argues while "*Gold Dinar and the Silver Dirham become a currency out of*

[9]One may think there must be no controversy over this type of Riba, but still there are some Muslim scholar debating issue of banking interest being classified as Riba. For more details see Farooq (2009).

free choice, not as the result of decree. Paper money is imposed on people". If one looks at money as form of social contract perspective, Vadillo identifies few problems of *Sharia* compliance when it comes to concept of fiat currency. *Firstly*, he points out that in such contract offer has fraudulent nature. It is because State is obliging people to accept something above its value; true value of paper money, he says, is zero. *Second* objection to such contract is about the obligation of the offer. Public is obliged to accept it whether they like it or not, which is the nature of 'legal tender' law. *Finally*, the application of State laws that prohibit any other means of payment is enforcing the State monopoly on the currency, by inserting illegal stipulation on the first contract. Thus from *Sharia* prospective fiat money would be unacceptable as social contract, while gold and silver money would be acceptable because on non-existence of such flaws.

To the question of what is acceptable for money in Islam, Vadillo (2006) brings a quote from Imam Malik in which he states "*any merchandise commonly accepted as a medium of exchange.*" Vadillo interprets it to imply two things:

Primarily, money should be in form of any merchandise[10]. This could be in form of paper as well. However, such paper should be accepted for its actual value, not for what is written on it. Thus he emphasises that money must be something tangible (*'ayn*). Therefore, it cannot be a liability of any kind (*dayn*). Additionally, money in Islam must be commonly accepted. Therefore acceptance could not be imposed on people. Which means nobody has right to enforce acceptability of any money on people, include that of gold Dinar or silver Dirham, author concludes.

G. FRACTIONAL RESERVE BANKING, ELECTRONIC AND INTERNATIONAL CURRENCIES

With the first stage of introducing paper money through promissory notes given by banks in return for deposits of gold and silver was born notion of fractional reserve banking. Bankers advanced those deposits as new loan while also encouraging the lenders to keep gold and silver coins as deposits while using new promissory notes as money. As the majority of our authors believe, such trickery by early bankers was start of systemized deception of modern fractional reserve banking system (Hosein, 2007; Meera & Larbani, 2006a, 2006b; Vadillo, 2006).

Meera and Larbani (2006a) argue that using such fractional reserve system the banking sector is responsible for the most of money creation. Such newly created money takes the form of accounting entries or just electronic records. This carries with it new purchasing power, which results to the seigniorage of fiat money created out of '*thin air*'. They caution since all this new money is primarily introduced into the economy as loans; seigniorage is further extended by requiring interest payment. Islamic banks are not exception; because they also operate in such a system as authors note. Thus, they also create money in this form, but using '*Shari'ah compliant*' products and principles.

Meera and Larbani (2006a) continue arguing that money and debt are balance sheet counterparts simply because multiple credit creation channel of money creation. The resulting debt they argue would

[10]Hosein (2007) may disagree with this statement, mainly because he limits money to precious metals and foodstuff only. His conclusion is based on above mentioned hadith regarding six *Ribawi*items.

eventually end up in the economy in as private and public sector debt. According to them bank money (loans) comprise the majority of money supply while paper money account for much smaller in most countries. Per their calculations for sixty-two countries, they found hard currency and coins to represent only around 34% of the broad money (M2), while remaining 66% was largely created by banks in form of loans.

On the other hand, Meera and Larbani' s (2006a) calculations show that the average growth rate of M1 (narrow money) and M2 (broad money) were shocking 36.92 % and 41.40% per annum respectively. Which means GDP has to growth at least in similar rates to cancel out inflationary pressure of such system and it is well known fact that such growth is impossible under any circumstances. Therefore, the system of fractional reserve banking and electronic money further magnifies issue of seigniorage (i.e. unjustified increase in money supply) that exists under fiat currency system.

However, Hasan (2008) argues that growth of financial transactions has no boundaries and more than a trillion USDsare circulated in the world stock markets every 24 hours in from of speculative trading. Similarly, he estimates amount of foreign exchange spot transaction being as large as seventy times of world's real output. Thus, he is confident that supply of money if tied to gold would not be able to meet such a huge demands. Therefore, he concludes return to gold is impossible. Even though it is hard to deny authenticity of facts presented by Hasan (2008), one may question desirability of such speculations from Islamic perspectives. If reintroduction of gold and silver money is going reduce such speculative activities in any extend one may conclude such action becomes even more desirable. Such conclusion can be based on the agreement by majority of *Sharia* scholars on prohibition of speculative financial transactions due to present of *Gharar* (excessive uncertainty) and *Maysir* (gambling) elements in them.

Furthermore, Meera and Larbani (2006a) point out that status of international reserve currency which is given to some selected developed countries' currencies (such as U.S. dollar, British pound or Euro) puts others in disadvantage. Especially, most of developing nations lose tremendously due to seigniorage of those 'international reserve currencies'. Since those reserve currencies can be used freely outside they domain it becomes relatively easy to print and disperse large amounts of additional money outside the respective country without placing much inflationary pressure domestically. As a result resources of the developing nations are getting stolen trough this 'the magic of international seigniorage'. Therefore, even though such fiat currency system may be beneficial for some developed countries with international reserve currency privilege, it is an obvious disadvantageous for those developing countries which are deprived of such privilege.

H. SUMMARY OF AUTHORS OPINIONS AND RECOMMENDATIONS

In his book Vadillo (2006) concludes that paper money (be in its current form or in any form of its historical existence) is an invalid contract (*'aqadbatil*) in Islamic Law. Therefore, according to him the *Sharia money* is limited to Gold Dinar and the Silver Dirham, and to any merchandise generally accepted to be a medium of exchange. But, his recommendation for future action which is also hinted on title of his book could be considered objectionable. Even though there is no issue with his recommendation of opening gold account or promoting used of gold and silver coins, there may be some objections about his later recommendation. In it he recommend not to abandon or reject interest earned from conventional accounts, but to receive it and used it for enhancement of the monetary system based on *Sharia*. This is brings question of could '*haram*' means be used to achieve '*halal*' objectives. Answer is most probably 'no'. Analogy to it could be '*one cannot use stolen money to build a mosque*' and it is clear that there is no reward for such deed.

Hasan (2008) sticks to his opinion and concludes with following four points: *Firstly*, he states that it is neither desirable nor practicable to return to gold standard in international level. Amendments to the IMF articles in 1978 that forbade its members to express the value of their currencies in terms of gold makes such practice impossible for IMF member countries. *Secondly*, because gold standard could not work neither as hedge against inflation nor as a good investment alternative, there is no need to have such as standard for one country. *Thirdly*, gold Dinar is not money which is required by *Sharia*. Fatwa of the International Fiqh Academy not opposing the use of fiat money is evidence to it. *Finally*, according to theory of monetary economics the main goal should be to keep the supply of money under control. Thus, money being of something valuable as gold is not necessary for that purpose.

Hosein's (2007) conclusion is, as expected, much contrary to one above. He believes that if Muslims want to follow the Qur'an and the Sunnah, they should return to the gold Dinar and silver Dirham and ask forgiveness for past betrayal of accepting paper money. Thus, he recommends two stage process in going back to true '*Sunnah* money'. *In the first stage*, he recommends Muslims to mint gold Dinar and silver Dirham and start using them for payment of *Zakat*[11], *Mahar* (dowry in marriage), Hajj expenses and others as soon as possible. He also believes, introduction of Dinar and Dirham will help to restore money's 'store of value' function. It is particularly so since both gold and silver store value better than any fait currency that exists. Even though poor will not be effected much because of their limited saving, but importance of this stage in terms of awareness and public education should not be forgotten.

For the second stage, he recommends people in the countryside to refuse acceptance and use of paper currency or electronic money of any sort. For instance rice farmers may ask for payment in gold or silver for their crops. If customer does not agree they may refuse to sell and use rice as money instead. He admits that use of rice as money will be limited to micro transactions, but at least this would be first step in the right direction. Later on, this practice may spread to urban areas and eventually save Muslim countries from evil of paper and electronic money.

Cizakca (2011) however concludes that idea of internationally accepted *Islamic paper money* should not be '*imposed from above*' by academicians or governments but rather result from Muslims' demand. Therefore, he believes it can result only from increased trade among the Muslim countries. Thus he says Muslims should priorities expanding trade with their own existing currencies rather than trying to introduce common currency for all Muslim nations. Against this point, one may argue since there is not a single Muslim country with internationally accepted currency how would it be possible to conduct such trade with 'their existing currencies'? For instance, if a Malaysian company wants to import some carpets from Turkey, could they find any Turkish factory willing to accept Malaysian Ringgit (MYR) for

[11] In his book Vadillo (2006) also mentioned that Zakat should be paid in gold or silver, and not allowed to be paid in paper money because it is similar to *dayn* (debt). Zakat cannot be paid in *dayn*.

payment? Conversely, even if the Malaysian company wants to pay in Turkish Lira (TRL), direct exchange of large sums would be nearly impossible. Therefore, the Malaysian company would either have to exchange MYR to US dollars and then to TRL to pay or just pay in US dollars. Anyway, such expansion of trade would benefit the U.S. economy (from seigniorage) rather than benefiting either of Malaysian or Turkish economies.

Finally, Meera and Larbani (2006b) argued that introduction of the gold Dinar is compatible with the *Maqasid al-Sharia*, because it fulfils protection of wealth and a necessity (*daruriyyah*) component of the *Maqasid*. But in contrary, they argue fiat money actually hinders the attainment of the *Maqasid al-Sharia*[12]. They argue that the gold Dinar, which is compatible with a 100 percent reserve requirement has characteristics (that does not exist in fiat money) of an Islamic money system and it is necessary for the realization of a true Islamic economics and financial system.

Additionally, Meera and Larbani (2006b) observe that since the Islamic economic system is an exchange economy where goods and services are exchanged value for value. They argue that the commodity money solves the problems associated with barter, because they have the characteristics of money, as well. Finally, from their analysis they conclude that gold and silver are best of these commodities to be used as money.

I. CONCLUSION AND RECOMMENDATIONS

From the review of some limited literature related to issue of Money in Islam and considering concept of money as social contract that must be *Sharia* compliant we could generalize some conclusions. If we consider money to be social contract between people and the State it must fulfil minimum some general requirements of *Sharia*. While most of the commodity moneys fulfilled such requirement, there is serious double about paper (fiat) money fulfilling those requirements.

In this work we highlighted at least four arguments in favour such criticism. *Firstly*, one of the requirements of subject matter to be something of real value. As some of the authors argued 'true value' of fiat money is zero or close to zero. Or if we consider paper money as promissory note, most scholars do not allow exchange transaction to be considered in debt(s). *Secondly*, contract in Islam should be free of any duress. Law of 'legal tender' violates this condition because it forces mandatory acceptance of national currency in all exchanges within the territory of that country. *Thirdly*, it is considered breach of contract if the state is continually devaluing its currency through different mechanisms of money creation. *Finally*, stipulation of law of 'legal tender' regarding non-permissibility of using other payment mechanisms is not compliant with *Sharia* principles either.

From above observation and authors arguments we see definite shortcomings of paper money both from *Sharia* and Economic perspectives. Even Hasan (2008) and Cizakca (2011) admit some of those problems with paper money. Despite clear advantage of gold and silver coins over contemporary paper monies, its proponents seemed to be confused about best mechanism that could bring that money into

[12] Which is opposite of what Hasan (2008) has been arguing.

practical use. Thus, the issue of practical implementation seems to be apparent research gap the needs further research and investigation by *Sharia* scholars and Islamic economist alike.

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