



# The Role of Agent in Islamic Financing A Critique

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**Abstract:** This study explores the role of agent in the Islamic modes of financing in order to identify ambiguities/issues related with the role of agent in Murabaha, Salam, Istisna and Tijara. The research further discovers the view of the *Shari'ah* experts with respect to such ambiguities so that they can either be verified as *Shari'ah* issues or non-*Shari'ah* issues. The role of agent was examined using content analysis of the model documents used by Islamic banks followed by soliciting the views of the *Shari'ah* specialists through interviews. No *Shari'ah* issue was found in hiring the customer as agent by the bank in any Islamic modes or binding the agent to act as an “undisclosed agent”. Conversely, the supplier’s risk, was declared to be the obligation of the bank and transferring this risk to the agent was observed as a real issue from *Shari'ah* point of view in the practice of Murabaha. Similarly, the principal is not allowed to charge any penalty to the agent if he is working without negligence and in good faith. Shifting charges like transportation, storage, etc., to the agent is not correct. However, no *Shari'ah* issue was found in binding the agent to provide collateral/security, etc., to the bank. Nevertheless, no consensus was observed on binding the agent to provide corporate guarantee. This research appears to be a preliminary but important attempt of its nature examining the critical role of agent in Islamic modes of financing adding value to the body of knowledge in Islamic banking.

**Keywords:** Agent, *Shari'ah*, issue, *murabaha*, *istisna*, *tijara*, supplier.

**JEL Classification:** G21

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## Introduction

Agency arrangement is used in almost all modes of financing including *Murabaha*, *Salam*, *Istisna*, *Ijarah*, and Diminishing *Musharakah*, etc. (Ayub, 2007, p.348). Therefore, the role of agent acquires paramount significance in the current usage of Islamic modes of financing. In case of *Murabaha*, the customer requests an Islamic bank for provision of certain goods. However, the bank usually appoints the same customer (i.e. buyer) as agent to purchase the same goods on behalf of the bank for him/herself. Similarly, in *Salam*, *Istisna* and *Tijara* or *Karobar*<sup>1</sup> finance the customer sells goods to the bank and the bank, in return, appoints the same customer (i.e. seller) to sell the same goods on behalf of the bank. However, the over utilization of the role of agent in the implementation of *Murabaha* (Shah & Niazi, 2019b), *Salam*, *Istisna* and *Tijara* creates many doubts in the *Shari'ah* compatibility of these Islamic modes of financing. Researchers have been investigating the Islamic banking and finance since long. Nevertheless, the role of agent in the Islamic modes of financing is yet to be explored. Therefore, this research is planned to explore the role of agent and the associated issues in the practices of Islamic modes of financing.

This study initially examines the role of agent in the Islamic modes of financing based on the model agreements used by Islamic banks in Pakistan for the purpose of identifying certain issues related with the role of agent in implementing *Murabaha*, *Salam*, *Istisna* and *Tijara*. After identifying ambiguities/doubts/issues, if any, associated with the role of agent in the existing usage of Islamic financing, the researcher approaches various *Shari'ah* scholars for obtaining correct/true *Shari'ah* opinion regarding such ambiguities/doubts/issues.

It is important to note that despite plenty of research in Islamic banking and finance, rare attention has been paid to the practical role of agent in the Islamic modes of financing. The previous research (Sarker, 1999; Ayub, 2007; Shamsuddin & Ismail, 2013) has explored the application of agency in Islamic financial contracts and described the principal-agent relationship in such contracts applied in Islamic banking and finance, accordingly. However, apparently the existing literature seems silent with respect to examining the role practically assigned to the agent

1 *Tijara* and/or *karobar* finance (finished goods financing) is a financing mode used by Islamic banks in Pakistan. It is just like *Istisna*, with the difference that this type of financing facility is provided for already manufactured/finished goods while in *Istisna* the goods are manufactured after the agreement as per given specification. In *Tijara* or *karobar* finance, the bank purchases finished goods from the customer on cash payment and subsequently employs the customer as its agent to sell the same goods in the market for the bank.

in the prevailing usage of Islamic financing. The current research is therefore an essentially required effort to pave the way for understanding the practical usage of the critical role of agent in Islamic modes of financing. This study directly seeks the views of *Shari'ah* scholars and explore an up to date knowledge regarding the role of agent in the current usage of Islamic modes of financing.

## Literature Review

The role of agent remains significant in almost all Islamic modes of financing. At times, it is the Islamic bank that acquires the role of agent to the customer. However, in most of the cases, it is the customer, who is assigned the role of agent by an Islamic bank to undertake certain transactions on its behalf. Agent is appointed owing to the inability and/or unwillingness of the principal to undertake the respective activity personally. "It may be easier to appoint an agent to exercise certain functions" (Hart, Childs & Ross, 2011). The AAOIFI issued *Shari'ah* standard No. 23 in order to elucidate the "*Shari'ah* rulings that govern the activities of Islamic financial institutions in appointing agents or becoming agents of others" (AAOIFI, 2017, p. 609). This standard expounds the obligations of the principal as well as agent in light of the *Shari'ah* principles. The said *Shari'ah* standard defines agency as "the act of one party delegating the other to act on its behalf in what can be a subject matter of the delegation and it is, thus, permissible". Regarding the commitments of the principal (5/1/1), the said *Shari'ah* standard states that "in contract of procurement agency, the price and other expenses should be borne by the principal. Besides the price of purchased commodity, the principal should reimburse to the agent expenses such as those of transportation, storage, taxation, maintenance and insurance" (AAOIFI, 2017, p.616). Regarding the commitments of the agent (5/2), the standard states that the "agent is considered as a trustee in holding the asset in question, and therefore, he is not bound to indemnify the principal for that asset in case of damage. He shall be held responsible for indemnity only when the damage results from his own misconduct, negligence or breach of contract, breach of terms or stipulations of the contract" (AAOIFI, 2017, p.616).

The application of agency can be found in the life of the great Prophet (pbuh), who assigned the task of buying a "goat/sheep" to a companion (Ayub, 2007, P.347; Shamsuddin & Ismail, 2013; Ellias, Haron & Mohammed, 2014). Similarly, at the time of leaving Makkah during the night, the holy Prophet delivered the valuables and goods kept by the people of Makkah with him as *amanah* to Hazrat Ali in order to be handed over to the respective owners.

Based on these theoretical concepts Islamic modes of financing are implemented maximally with the use of agent. Agency arrangement is applied by Islamic banks in almost all financing activities (Ayub, 2007, p. 348). It is however worth mentioning that the role of agent has not yet been properly explored and examined. Nonetheless, the role of agent has been referred to in part and parcels of discussion on *Murabaha* (Gundogdu, 2014; Tabet, 2015; Shah & Niazi, 2019b), and *Salam* or *Istisna*, etc. Tabet (2015) elaborated that the risk used to be diverted to the customer, being appointed as agent, especially if the goods were acquired directly in the name of the agent (customer). In case of *Murabaha*, the role of agent starts since the customer requests to the bank for acquisition of the requisite goods. The bank appoints the same customer as agent to buy and take over custody of the desired goods for the bank. Shah and Niazi (2019b) examined the appointment of customer as agent by the bank in *Murabaha* and discovered that hiring customer as agent was not prohibited by *Shari'ah*. However, the ownership related risks belong to the bank, at least theoretically. Nevertheless, practically banks shift “all risks including the ownership risk to the agent” in *Murabaha* (Shah & Niazi, 2019b).

Kaleem and Abdul Wajid (2009) examined *Salam* as mode of agricultural financing and suggested that banks can hire “middlemen as agents” in order to make the screening of borrowers (farmers) easier and monitoring of loans effective resulting in higher recovery in case of weak crops productions. However, Ehsan and Shahzad (2015) criticised the appointment of middlemen as agents due to the involvement of higher costs that could reduce farmers’ share of profit. Ehsan and Shahzad (2015) suggested the appointment of an agent at maturity of the contract to receive the delivery of goods from the farmer (seller) or the appointment of farmer (seller) as agent to “buy/deliver” crops on bank’s behalf. However, such arrangement/contract must be independent of the original *Salam* agreement. Thus, the crops come in constructive possession of the bank that can be sold in the market. Nevertheless, Shah and Niazi (2019a) suggested that the customer might not be necessarily appointed as agent. Alternatively, the bank should hire independent individuals/institutes to receive the goods/crops from the seller/supplier and offer them to “actual buyers in the market”.

The role of agent has acquired a critical significance in the implementation of Islamic modes of financing. However, the existing literature paid little attention to this important dimension of Islamic banking covering the practical role of agent in the Islamic modes of financing. As mentioned earlier, theoretically the application of agency concept in Islamic banking and finance has been expounded enough. Therefore, this research appears to be an initial but imperative attempt of its nature that critically examine the role of agent in *Murabaha*, *Salam*, *Istisna* and *Tijara*.

## Methodology

The current research is predominantly qualitative in nature primarily exploring, describing and analyzing the role of agent and the associated issues in the current use of Islamic financing techniques in Pakistan. This is an exploratory research discovering the role of agent and associated issues in the existing usage of Islamic modes of financing and examining their *Shari'ah* compatibility in the light of discourse offered by *Shari'ah* scholars.

It is 'interpretivist' in the sense that it is concerned with how the role of agent in Islamic modes of financing is "interpreted, understood, or experienced" (Mason, 2002, p.3). Interpretivists take an "insider view" of the social reality (Blaikie, 2000, p. 115). This study applied the same process through arranging interviews with the *Shari'ah* scholars for obtaining their views/opinions regarding the role of agent and associated issues in the contemporary practices of *Murabaha*, *Istisna* and *Tijara* or *Karobar* finance.

First, the role of agent in Islamic modes of financing was explored using content analysis of the model agreements including agency agreements devised for *Murabaha*, *Salam*, *Istisna* and *Tijara* by State Bank and two Islamic banks working in Pakistan. During this process, different ambiguities/doubts associated with the role of agent in Islamic modes of financing were identified and described making the study descriptive in nature. In fact, the respective clauses/sections of the model agreements were appraised in order to formulate the key findings/issues (Saunders et al., 2009, p. 117). These key findings (ambiguities/doubts) were converted into open-ended questions for seeking the views of *Shari'ah* scholars regarding these ambiguities/doubts in the second step of the study. Hence, the research design applied in this research can be called a "mixed research design" (Eid, 2012).

The study applied an inductive approach attached to the interpretivist philosophy of research (Saunders et al., 2009, p. 124). Owing to the blended spirit of "exploratory and descriptive" research design in this study (Robson, 2002, p. 59; Eid, 2012; Neuman, 2014, p. 38), the "data collection, organization and analysis" were conducted predominantly on the basis of "inductive" approach. This approach is more appropriate to generate data, analyze it and observe the emerging "theoretical themes" proposed by the data in a relatively new area of research in which the available literature is not sufficient to develop a proper theoretical framework (Saunders et al., 2009, p. 123, 127).

## Population and Sample Selection

This research was undertaken in two steps, therefore an independent population was defined during the two respective steps. In the first steps, the role of agent in the 4 Islamic modes of financing and the associated issues were assessed using data available in the model/sample documents. Hence, the set of model documents used for Islamic financing constituted the population in the initial phase of this research (Bryman, 2012, P. 11; Shah & Niazi, 2019a; Shah & Niazi, 2019b). After exploring the role of agent in the Islamic modes of financing and identifying the associated doubts/misgivings, a questionnaire containing open-ended questions was designed for seeking the views of *Shari'ah* scholars having had understanding of Islamic finance. Therefore, the *Shari'ah* scholars having had understanding of Islamic finance became the population for the final phase of the current research.

Like two population, this research required an independent sample in each of the two steps of the study. Therefore, in the first step, the model agreements for *Murabaha*, *Salam* and *Istisna*, *Tijara* and *Karobar* finance were sought on the basis of purposive sampling, from State bank of Pakistan (SBP) and two Islamic banks to be referred to as IB-I and IB-II. Ahmed (2006) adopted “purposive random sampling” using “file study and questionnaire survey” in his study on “*Mudaraba* and *Musharaka*”. Similarly, another previous research also relied on data of only two Islamic banks (Samad, Gardner & Cook, 2005).

After examining the documents of *Murabaha*, *Salam*, *Istisna*, *Tijara* and *Karobar* finance, 12 doubts/misgivings associated with the role of agent were identified on the basis of content analysis. These doubts were converted into a list of 12 open ended questions in order to be discussed with a diverse group of *Shari'ah* scholars for soliciting their opinion. It was intended to investigate that whether the doubts/misgivings associated with the role of agent in the usage of Islamic financing techniques were critical from *Shari'ah* perspective or not.

Hence, the researcher approached various relevant scholars, however, many of them did not respond to the request of the researcher for meeting. So, data could be collected from only 30 individuals that included banks' *Shari'ah* advisors, *Shari'ah* board members, *mufti* associated with Darul uloom/madrassas, and academician/researchers having specialization in Islamic banking and finance. Previous research also used such a limited sample. For instance, Ahmed (2006) used questionnaire for collecting primary data from only 23 “policy makers, executives and customers of Islamic banks”. Zamil (2014, p.207) interviewed 31 people working in Islamic banks. The regional/position wise distribution of the sample is shown in table 1, given below.

**Table 1***Regional and Institutional Distribution of the Sample of Shari'ah Scholars*

Region Position	Islamabad, Rawalpindi	Lahore	Faisalabad	Peshawar, Swat Mardan, Akora	Total
<i>Shari'ah</i> Board members	2	3	1	4	10
<i>Shari'ah</i> Auditor	1	0	0	1	2
<i>Mufti</i>	6	0	0	4	10
Academic Researchers	6	0	0	2	8
<b>Total</b>	<b>15</b>	<b>3</b>	<b>1</b>	<b>11</b>	<b>30</b>

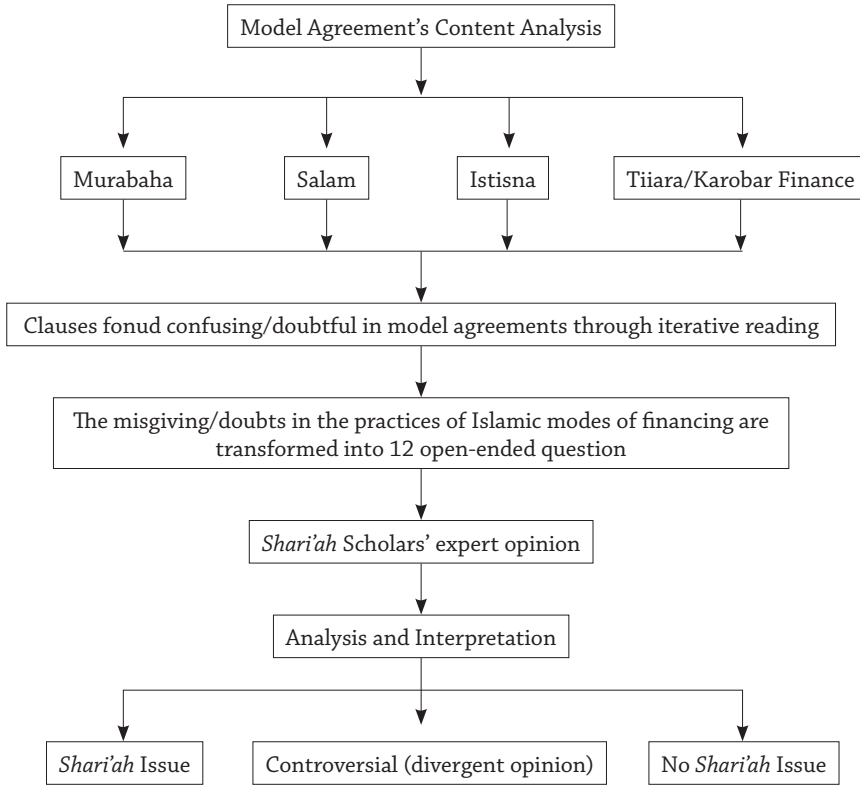
## Data Gathering and Analysis

Model documents obtained from the SBP website and the two Islamic banks (IB-I, IB-II) were examined based on content analysis so that the role of agent and the associated issues in the current usage of Islamic financing could be explored. Resultantly, various clauses/sections were identified being confusing/ doubtful from *Shari'ah* point of view. Such confusing and doubtful clauses were required to be discussed with *Shari'ah* scholars for obtaining an explicit opinion with respect to their being *Shari'ah* complaint or otherwise. Consequently, a total of 30 *Shari'ah* scholars, nominated on the basis of judgmental sampling, were interviewed. Previous research (Zamil, 2014; Ullah, 2012, p.5) also collected data through interviews. The interviews were properly transcribed and subsequently analysed. Thus, the final stage of this study is built on primary data composed via interviewing 30 *Shari'ah* scholars and researchers about the doubts/misgiving identified in the current usage of Islamic financing techniques.

After analyzing the interview data, the doubts/misgivings associated with the role of agent in the Islamic modes of financing were either found as “no *Shari'ah* issue” or established as “*Shari'ah* issue” or acknowledged “controversial” if an obviously divergent opinion of *Shari'ah* experts was noticed.

Figure 1 diagrammatically shows the steps applied during this study.

**Figure 1**  
*Process of Content Analysis*



### Analysis of Model Agreements

In *Murabaha*, the bank engages the customer as agent to purchase and receive the desired goods on bank's behalf as agent. Later on, the agent purchases the same goods from the bank on credit through an exchange of offer and acceptance between the bank and agent (now as customer) (Shah & Niazi, 2019b). The agent collects the "pay order/cross cheque, in the name of supplier" from the principal (bank) to buy the requisite goods (SBP, 2004, MMFA, Clause, 2.01). However, if the supplier fails "to supply the said goods within the period specified in the Purchase Requisition", the agent undertakes to "refund the full amount and all cost and consequences in terms of the Agency Agreement" (SBP, 2004, MMFA, *Murabaha Document # 4, Receipt*). Further, the agent receives "the goods directly from the supplier in terms of purchase requisition duly endorsed by the bank and provides a declaration to the bank confirming the acquisition of the goods along with relevant details" (SBP, 2004, MMFA, *Agency Agreement*).



Concisely, the Murabaha procedure comprises three steps including (a) buying the goods by the bank itself or via an agent, (b) the customer's proposal to buy "the goods from the bank", and (c) the bank's consent to sell the same "goods to the customer". However, these three steps are technically blended in a single document (i.e., Declaration) containing three parts for the three steps respectively (SBP, 2004, Murabaha Document # 5). However, it implies that the concerned documents (Declaration) must be completed at three different times with respect to the three different steps in order to keep the role of agent and customer separate from each other. Nevertheless, it is observed that virtually all the documents can be filled and signed simultaneously as a formality only "to meet the *Shari'ah* requirements" theoretically and forestall concerns of *Shari'ah* audit (Shah & Niazi, 2019b). Though, it is stated that the bank can appoint the customer or someone else as an agent to purchase the goods on behalf of the bank and sell the same to the customer but keeping all the transactions independent and separately documented from each other (SBP, 2004).

Further, in case of *Istisna* and *Tijara* or *Karobar* finance, the customer (seller/manufacturer/trader) is selected as agent by the bank (principal). The agent is assigned the job of selling "the sale goods in accordance with the terms and conditions" of the agency contract to the proposed buyer (theoretically) on behalf of the bank at a price defined in "the notice" and deliver the amount to the bank on the "maturity date" (IB-I, *Istisna* Agency Agreement, Clause, 2.01 & 3.01; IB-II, Master Agency Agreement for *Istisna*, Clause, 2 & 3). Further, the customer is constrained to work as an "undisclosed agent" and not to disclose, without the written consent of the bank, that he/she is acting as an agent of the bank (IB-I, Finished Goods Agency Agreement, Clause, 2.01 & 2.02).

In case of failure to "pay the minimum sale price by the relevant maturity date", the agent would pay a fine "calculated @ 24% per annum for the entire period of failure, calculated on the total amount of the obligations remaining un-discharged or any other amount acceptable to the bank", though such amount is paid straight to a charity fund, established by the bank (IB-II, Master Agency Agreement for *Istisna*, Clause, 16; IB-II, Master Agency Agreement- *Karobar* Financing Transaction, Clause, 24; IB-I, Finished Goods Corporate Guarantee, 16).

The agent is also responsible to complete all matters relating to the sale of goods including legal and procedural formalities (IB-I, Finished Goods Agency Agreement, Clause, 4.01), paying charges related to "stamp, documents, registration, duties or taxes", etc., and "indemnify the bank against any liability arising" due to "any delay or omission" by the agent to pay such duties or taxes (IB-I, Finished Goods Agency

Agreement, Clause, 4.02). The agent is also bound to bear all costs incidental to the sale of the “sale goods” including but not limited to transportation, storage etc. (IB-I, Istisna Agency Agreement, Clause, 4.03). Further, the agent is constrained to provide collateral/security, deliver such other documents and deeds, as may be required by the bank (IB-I, Finished Goods Agency Agreement, Clause, 7.0; IB-II, Master Agency Agreement, Clause, 22), and “execute a demand promissory note in favour of the bank/principal” (IB-II, Master Agency Agreement, Clause, 22).

It is observed that the customer is working as agent but is constrained to pay penalty for delay in payment (by the buyer) to the bank. In such situation it is possible that the “sale goods” may not eventually be sold to an actual (third party) buyer by the given “maturity date” due to any practical reasons. Nevertheless, the agent is bound to pay the “sale price” to the bank (principal) on the given “maturity date”. It implies that the agent needs to pay the amount from his/her own sources i.e. purchasing the goods from the bank on the stated “sale price”.

Likewise, the agent is deemed to have selected the buyer “whether in relation to a buyer who has submitted a Purchase Order or who has opened a Letter of Credit or otherwise,” and is fully liable “for the collection of the sale price” (IB-I, Istisna Agency Agreement, Clause, 3.03; IB-I, Finished Goods Agency Agreement, Clause, 3.03). Further, the agent must “indemnify the principal against any and all losses, expenses, costs, damages, proceedings, actions, claims suffered by the bank (principal) arising as a result of the agency transactions” (IB-II, Master Agency Agreement for Istisna, Clause, 14).

Moreover, the agent is required to undertake “all necessary and appropriate due diligences as are required to ascertain the creditworthiness of the buyer” and obtain “properly secured contracts and other collaterals from the buyer” in order to ensure the payment of the sale price on or before the due date (IB-I, Istisna Agency Agreement, Clause, 3.06; IB-I, Finished Goods Agency Agreement, Clause, 3.06; IB-II, Master Agency Agreement, Clause, 6). Nevertheless, “the agent (and not the principal)” is responsible “for any loss or damage suffered by the agent during the agent’s performance of its services under this agreement” (IB-I, Istisna Agency Agreement, Clause, 3.07; IB-I, Finished Goods Agency Agreement, Clause, 3.07).

On the other hand, it is clearly expressed that on behalf of the principal, “the agent has no right or authority, expressed or implied to: (a) make any guarantee, warranty or representation in respect of any of the sale goods; or (b) incur any obligation or enter into any contract of sale other than in accordance with the expressed terms of this agreement or as set out in the notice issued by the principal” (IB-I, Istisna Agency Agreement, Clause, 2.03; IB-I, Finished Goods Agency Agreement, Clause, 2.03).

The agent is also constrained to “irrevocably and unconditionally, guarantee the punctual payment of the sale price”. However, if the agent or any buyer “fail to pay any amounts due on account of the sale price”, the agent is bound to immediately and “unconditionally pay all the sale price for sale goods due to the bank under and pursuant to the agency agreement” (IB-I, Finished Goods Corporate Guarantee, Clause, 1). In case of default by the customer/agent and/or any buyer, the bank has the right to enforce this guarantee against the customer/agent (IB-I, Finished Goods Corporate Guarantee, Clause, 4).

Moreover, all payments under the guarantee must be complete, without any right of set-off or counterclaim and deductions/withholdings on the due date to the bank (IB-I, Finished Goods Corporate Guarantee, Clause, 6). If the customer (agent) is “required to make any deduction or withholding in respect of any taxes, duties or other charges or withholdings from any due payment,” the agent undertakes to increase “the sum due in respect of such payment to the extent necessary to ensure that the bank receives a net sum” full and complete without being reduced by “such deduction or withholding” (IB-I, Finished Goods Corporate Guarantee, Clause, 7). It implies that the taxes are also transferred to the agent by the bank.

After thoroughly reading and analyzing the contents of the model agreements including the agency agreements used by the Islamic banks in connection with *Murabaha*, *Istisna*, finished goods facilities and the submission of guarantee by the agent, the following misgivings/issues are identified for further analysis in order to clarify them from *Shari'ah* point of view.

- (i) Is appointing the customer as agent for buying the required goods for the bank and then purchasing the “same goods from the bank as buyer”, on credit, permitted by the *Shari'ah* principles (Shah & Niazi, 2019b)?
- (ii) Is compelling the agent for the refund of “the full amount and all cost and consequences” to the bank (principal), allowed by *Shari'ah* even if the supplier (third party) does not provide the goods in the agreed/scheduled period of time?
- (iii) Who is responsible to accept/tolerate the “risk of supplier failure in sale transaction”, according to the *Shari'ah* principles?
- (iv) Is buying goods from the customer by the bank and then employing the same customer as agent for selling the same goods for the bank (buyer) allowed by *Shari'ah* principles?
- (v) Do the *Shari'ah* principles allow binding the agent to perform as an “undisclosed agent” for the bank (principal)?

- (vi) Is it allowed to constraint the agent to sell the goods at a 'stated price' before a specific date (maturity date), pay the amount to the bank by the specific "maturity date", and impose penalty on the agent for not paying the "minimum sale price" to the bank by the "relevant maturity date", even if the goods are not sold?
- (vii) Is it allowed to declare the agent fully liable "for the collection/recovery of sale price and its payment" to the bank within a defined period of time and pay penalty from his/her own sources to the bank (principal), if the payment is delayed by the ultimate buyer?
- (viii) Is it allowed to constraint the agent to bear charges related to "stamp, documents, registration, duties or taxes" and all costs incidental to the sale of the "sale goods" including transportation, storage, etc.?
- (ix) Is it allowed to constraint the agent to provide collateral/security or such other documents and deeds and demand promissory note to the bank (principal)?
- (x) Is it allowed to declare the "agent (and not the principal in any circumstances) liable for any loss or damage suffered by the agent during the agent's performance of his/her services?
- (xi) Is it allowed to constraint the agent to "indemnify the principal against any and all losses, expenses, costs, damages, proceedings, actions, claims suffered by the principal due to the agency transactions"?
- (xii) Is it allowed to constraint the agent for guaranteeing (submitting a corporate guarantee) the credit worthiness and all deals/default of the buyer to the bank?

## Analysis and Discussion

The **question 1** has been well covered and explained by Shah and Niazi (2019b). They found almost all the *Shari'ah* scholars unanimously accepted appointing the customer as agent, in Murabaha, though it was considered the least desired option. One of the *Shari'ah* scholars explained the three options available to an Islamic bank in the following words.

*There are three possibilities. Number 1, the bank should have its own trading stores but practically the bank is not a trading store, and it is impracticable. Number 2, the bank should appoint an independent person other than the customer as agent. Number 3 is to appoint the customer as agent. The third option has some practical benefits/convenience to the bank and is therefore popularly used and it is acceptable from Shari'ah point of view.*

Another *Shari'ah* scholar stated as follows.

*Appointing the customer as agent is permissible but it is not ideal/preferable mode and there must be genuine reasons for making the customer as agent.*

Thus, it is owing to explicit rationales that Islamic banks favour appointing the customer as agent (Shah & Niazi, 2019b). A *Shari'ah* scholar said:

*The banks don't have expertise in purchasing the requisite goods so the customer being part of that business usually has expertise and is appointed as agent.*

It can be inferred that there is no *Shari'ah* issue in appointing the customer as agent by the bank. Nevertheless, it is the minimum desired alternative, at least hypothetically. Nonetheless, practically Islamic banks desire appointing the customer as agent in nearly all Murabaha transactions.

With respect to the agent's responsibility (i.e. **question 2**) to "refund the full amount and all cost and consequences" in case of "failure of the supplier to supply the said goods within the specified period" (SBP, MMFA, Murabaha Document#4, Receipt), variability in experts' response was found. The "bankers and *Shari'ah* advisors/board members" argued that such an agent would be the ultimate user of such goods being purchased, so he/she may postpone the purchase/delivery of goods for possible utilization of the funds for some different purposes, if he/she (agent) is not declared liable "in such manner" (Shah & Niazi, 2019b). They argued that the agent might intentionally delay the delivery of goods in connivance with the supplier for using the money for other purposes. If the agent was allowed exemption from the supplier's risk, then the probability of collusion between the supplier and the agent would rise and the bank would be exposed to higher risk of supplier's failure. One of the *Shari'ah* scholars argued in the following words.

*The agent can be declared responsible because the agent actually purchases the goods for himself and it is possible that in connivance with the supplier, the agent may be involved in any fraudulent activities. So, in order to ascertain discipline, agent is made responsible.*

Nevertheless, majority of the scholars argued that the agent should only be declared liable in case of negligence, misconduct, or irregularity on his/her part. As a general rule of business, the agent is not responsible to repay the funds to the bank if already paid to the supplier and the supplier failed to provide the goods in the agreed time. A *Shari'ah* scholar explained this argument in the following words.

*The agent is bound to work in good faith and without negligence and therefore need to take all possible steps so that the supplier delivers the goods in time. However, he is not responsible to refund “the full amount and all cost and consequences” to the principal, if the supplier still fails to supply the goods in the required time.*

In response to **question 3** regarding the supplier’s (third party) risk, almost all the respondents expressed that supplier’s risk belonged to the bank and the bank should endure such risk if the supplier failed to offer the desired goods in time. It was stated that:

*The supplier risk is the responsibility of the principal (the actual purchaser) i.e. bank.*

On the other hand, some scholar justified shifting of supplier’s risk to the agent with respect to Murabaha as the agent was presumed to be the eventual purchaser/consumer of the said goods. So, exempting agent from such risk may enhance the possibility of collusion between the supplier and the agent resulting in an increased supplier’s failure risk for the bank. A *Shari’ah* scholar responded in the following words.

*It belongs to the bank, but if the agent is found guilty of negligence then this loss can be shifted. The reasons are required to be investigated for this purpose. Generally, the supplier risk is the bank’s responsibility, not the agent.*

It is observed that the third party (supplier’s) risk is the responsibility of the bank and transferring this risk to the agent, for any reasons is a real *Shari’ah* issue in the uses of Murabaha. The agent can only be declared liable if he/she is discovered committing negligence, misconduct, or any other such irregularity.

With respect to **question 4**, almost all the scholars accepted that there was no issue in buying the goods from a customer and appointing the same person as agent for selling the same goods for the bank (principal buyer). However, the two deals must be independent of each other. The second deal (appointing the seller as agent) must be concluded after the first transaction between the bank and the seller (customer) had been completely settled. A *Shari’ah* scholar responded in the following words.

*Yes, possible, but the two deals should be independent. If the first deal is independently completed, bank pays and takes possession, then it is permissible.*

Thus, appointing the same person as agent for selling the same goods on behalf of the bank (principal buyer) does not create any *Shari’ah* issue.

**Question 5** enquired about the *Shari'ah* position with respect to the condition of binding the agent to act as an “undisclosed agent” for the bank (principal). Majority of the scholars mentioned that there was no compulsion from *Shari'ah* point of view for an agent to disclose his/her identity to every customer that he/she was working for a specific person (principal). However, some of the scholars were of the opinion that imposing such a condition on the agent might lead to social or even *fiqh* problems. They observed that there were still many Muslims in the country who did not like to have any dealings with the banks including Islamic banks. Thus, if such people indulged in any deal with the agent of a bank without knowing his/her status and later on became aware of the fact, then they might ask the agent for concealing the fact of his/her position. So, such circumstances could lead to an undesired situation and could create a social issue. A *Shari'ah* scholar stated that:

*It is not correct. There is gharar. Such condition can lead to disputes or other problems of fiqh.*

Hence, there is no *Shari'ah* issue in binding the agent to act as an “undisclosed agent” for the bank (principal). However, such condition may lead to social or even *fiqh* problems and can create undesired situations.

**Question 6** actually comprised a comprehensive theme conveying an important issue. The respondents were unanimous in declaring that there was no issue in binding the agent to sell the goods of the bank according to the instructions/guidelines of the bank/principal including the desired price. It was also agreed that the principal (bank) could define a precise time period for a specific job (selling of goods) by the agent. In such case the agent must work honestly, efficiently, without any negligence and in good faith. However, if despite of the best efforts by the agent, the goods could not be sold, such goods would remain the property of the principal (bank) and no penalty would be imposed on the agent. The goods might not be sold due to many other factors beyond the control of the agent. One of the responding scholars explained this point of view in the following words.

*It is not allowed. The agent is bound to work in good faith and without negligence and therefore need to take all possible steps to sell the goods in time. However, if they are not sold despite all efforts, the agent should not be bound to pay the “stated price” of the goods to the bank/principal. Otherwise, the agent would pay from his own sources and it is equivalent to lending money on the basis of interest. Therefore, no penalty should be imposed on the agent. It is not allowed.*

It is observed that there is no issue in binding the agent to sell the goods of the bank at the desired price by the given maturity date. However, imposing penalty on

the agent in case he fails to deposit the sale price to the bank by the given maturity date if the goods are not sold, creates a serious *Shari'ah* issue. The agent is only bound to work honestly, efficiently, without negligence and in good faith.

In response to **question 7**, regarding the responsibility of the agent “for the collection/recovery of sale price and its payment” to the bank, the respondents contended that the agent would make full efforts for the recovery of the sale price and subsequent payment to the bank/principal. It was the primary responsibility of the agent to sell goods on behalf of the bank, collect the sale price from the buyer on the spot or on the maturity date in case of credit sale and paying the amount to the principal. Nevertheless, the principal was not allowed to charge any penalty to the agent if he was working without any negligence, dishonesty or misconduct and in good faith. However, if the agent was found guilty of any negligence or misconduct, then he would be liable to compensate the bank for actual losses, if any. One responding scholar explained it in the following words.

*Yes the agent may be made responsible for the recovery but no penalty is allowed. He/she will make all possible and sincere efforts to recover the amount from the buyer. However, there is no penalty on agent in Shari'ah if he/she is working in good faith and without negligence. Conversely, if the agent is found guilty of any negligence, dishonesty or misconduct, then he/she must compensate the bank for the respective losses, but the actual losses, which should not include any opportunity costs.*

It is observed that imposing penalty on the agent if he fails to recover the sale price from the ultimate buyer (if sold to a third party) is also not correct if the agent is working without negligence, dishonesty or misconduct and in good faith. Thus, imposing such a condition creates a *Shari'ah* issue in the practices of Islamic modes of financing. The agent is only responsible to put in all possible efforts helping the bank to recover the sale price from the buyer.

In response to **question 8**, regarding the charges related to “stamp, documents, registration, duties or taxes” and all costs incidental to the sale of the “sale goods” including transportation, storage, etc., the respondents almost unanimously declared the principal (bank) responsible for all such expenses. It was disclosed that if the agent paid such expenses, then the principal would need to reimburse such amount to the agent. The payment of these expenses was also linked with the benefits by one scholar who expressed that such expenses should be paid by the beneficiary if it was the bank or the agent. The respective scholar stated that:



*Such charges should be borne by the beneficiary; whosoever is getting the benefit should pay such expenses. Sometime the agency is in the benefit of the bank and sometimes it may be in the benefit of the agent so such expenses should be paid by the actual beneficiary.*

Thus, shifting such charges that are incidental to the sale of the “sale goods” including transportation, storage, etc., to the agent is not correct according to the *Shari’ah* principles. Such practice apparently makes the whole arrangement conditional leading to the emergence of a *Shari’ah* issue.

In response to **question 9**, regarding binding the agent to provide collateral/security, etc., to the bank (principal) two different views appeared. One type of respondents was of the opinion that agent was *amen* and the principal/bank should not ask him/her for security. The agent was appointed on the basis of trust and if the bank did not trust a person, then he/she should not be appointed as agent. On the other hand, according to the other group of respondents the bank could ask the agent for collateral/security due to two reasons. One, the *Shari’ah* did not prohibit such practice, and second was the level of prevailing ethical standards in the society. As the bank used to assume a funded exposure and in order to secure its interest against the agent’s risk of possible dishonesty/fraud, the bank could ask for security. However, such security should be kept as *amanah* and only in case of agent’s failure to perform his job without negligence the bank should utilize such security to compensate the actual loss but not any opportunity cost (cost of funds). A relevant excerpt from one of the interviews is mentioned below.

*As there is risk that the agent may escape, otherwise there is no such compulsion on agent. However, in this case the bank can ask for security in order to mitigate the risk. Shari’ah does not prohibit such practice. However, bank should deal such security as amanah and should not use it for any personal benefits.*

As far as the collateral/security is concerned, there is no *Shari’ah* issue in binding the agent to provide collateral/security, etc., to the bank (principal).

Question 10, and 11 inquired about agent’s responsibility to bear “any loss or damage suffered by the agent” and “indemnify the principal against any and all losses, expenses, costs, damages, proceedings, actions, claims suffered by the principal due to the agency transactions”, respectively.

In response to **question 10**, it was explained that if the agent suffered any personal losses during his duty, he would bear it. However, if any losses occurred to the principal property/goods without any negligence on the part of the agent then such losses would be borne by the principal not the agent. A *Shari’ah* scholar explained this situation in the following words.

*If any personal loss occurs to the agent, the agent will bear it but if any business loss occurs, it belongs to the principal. But the agent must work in good faith and without negligence.*

Similarly in response to **question 11**, the respondents unanimously explained that if any losses occurred to the principal's property/goods without any negligence on the part of the agent then such losses would be borne by the principal, not the agent. The following argument was shared by a *Shari'ah* scholar in this regard.

*If it is due to the negligence of the agent, then it is ok. But if it is not due to the negligence of the agent then the principal should bear it. If the agent identifies and keeps the bank's goods separately and takes due care of them, then it is the responsibility of the bank to bear losses, if there is any.*

Making the agent responsible, as a general rule, to bear "any loss or damage suffered by the agent" and "indemnify the principal against any and all losses, expenses, costs, damages, proceedings, actions, claims suffered by the principal due to the agency transactions", respectively, is not correct. Such conditions create *Shari'ah* issues in the contemporary practices of Islamic modes of financing. It should be subject to negligence on the part of the agent.

**Question 12** enquired the *Shari'ah* position regarding binding the customer (as agent) for guaranteeing the credit worthiness and all deals/default of the buyer to the bank. The respondents agreed that the agent was assumed to sell only to such people who were known to him (the agent) as credit worthy and reliable for paying the sale price by the due (maturity) date. As far as the formal corporate/personal guarantee by the agent was concerned, there was a difference of opinion. One group of scholars explained that the agent could not work as guarantor at the same time because the agent was working on behalf of the principal possessing the same status as that of the principal. A *Shari'ah* scholar stated that:

*It is not correct. These two are separate matter. Agent cannot be guarantor of the buyer to the principal at the same time.*

However, the other group of scholars justified that it was the responsibility of the agent to guarantee the credit worthiness of the buyer and the recovery of the sale price from him on or before the maturity date. They explained that bank should not be suffered for such deal which it would be totally unaware of. A *Shari'ah* scholar explained that:

*In my opinion, it is correct. Agent can be guarantor of the buyer to the principal. If the agent is making the deal between the principal and the buyer so the bank does not know the buyer but the agent knows him. So, the agent can be made responsible.*

Another minority view was also observed that if the agent willingly/voluntarily agrees to guarantee the credit worthiness and recovery of the sale price, then there was no *Shari'ah* issue.

A division of opinion is observed on binding the agent to provide corporate guarantee for guaranteeing the credit worthiness and all deals/default of the buyer to the bank. The bank purchases goods from a customer and then appoints him to sell the same goods to other customers (third parties) and ask the agent to guarantee the recovery of sale price. It means that in case of non-payment by the ultimate buyer, the agent will pay from his/her own sources. It is not correct. Nevertheless, it was unanimously agreed that if any losses suffered by the principal due to any negligence on the part of the agent, then such losses must be borne by the agent and principal should be compensated accordingly.

## Conclusion and Recommendations

The role of agent has acquired critical importance in the contemporary practices of Islamic modes of financing particularly in *Muarabaha*, *Salam*, *Istisna*, and *Tijara/Karobar* finance. The agent is primarily responsible to perform his/her duties according to the instructions/guidelines given by the principal. However, such instructions should follow the *Shari'ah* guidelines for establishing the roles of principal and agent. Appointing the customer as agent is probably the actual convenience available to the Islamic banks in the application of *Muarabaha*, which make shifting almost all types of risks to him/her much easier. Though, appointing the customer as agent is permissible in *Shari'ah*, however, such practice may create doubts in *Shari'ah* acceptability of *Murabaha* transactions. For instance, all the *Murabaha* related documents may be signed simultaneously by the bank and the customer only to pretend a *Murabaha* transaction. Similarly, the principal (bank) is liable to afford the third party (supplier) risk. Nevertheless, actually the Islamic banks transfers all these risks to the agent. Therefore, it is suggested that the bank as principal should accept such risk if the supplier does not offer the required goods within the stipulated time.

In case of *Tijara/Karobar* finance, binding the agent to act as an “undisclosed agent” is an undesired and unnecessary compulsion imposed on the agent that may lead to social or even *fiqh* problems. Therefore, the agent should be left

independent in deciding to disclose or not to disclose as per requirements of the situation in order to avoid creating any undesired situation that may result in any social/ethical problems.

There are built in flaws in imposing penalty on the agent for not selling the goods and/or not paying the “minimum sale price” to the bank by the “relevant maturity date” or if he fails to recover the sale price from the ultimate buyer (if sold to a third party). The goods may not be sold by the given deadline due to many uncontrollable factors including market conditions, competition, price or quality, etc. In such situation, the agent may be constrained to pay the stated price from his/her own sources in fact buying back the same goods at a higher price which were initially sold by him/her to the bank at a lower price. It is also possible that the agent does not want to sell the goods for the bank and only sold it for obtaining funds and intends to pay back the desired/stated price to the bank on the given maturity date. In either case no real sale occurs but only exchange of money takes place between the customer (agent) and the bank with a profit margin (interest) added to the amount to be returned to the bank. It is simply a sale buy back that is prohibited in *Shari'ah*. Therefore, the principal should not charge any penalty to the agent if he is working without negligence, dishonesty or misconduct and in good faith. However, if the agent is found guilty of any negligence or misconduct, etc., then he is liable to compensate the bank for any actual losses.

Expenses/charges related to “stamp, documents, registration, duties or taxes” and all costs incidental to the sale of the “sale goods” including transportation, storage, etc., are required to be borne by the principal (bank). Conversely, the bank assumes a funded exposure in respect of the agent and need to secure its interest against the agent’s risk of possible dishonesty/fraud, therefore, the bank can ask for security.

If the agent suffers any personal losses during the performance of his/her duties/services, then the agent should bear it but if any losses occurred to the principal’s property/goods without any negligence on the part of the agent then such losses need to be borne by the principal not the agent. However, the agent may be required to indemnify the principal/bank against “any and all losses, expenses, costs, damages, proceedings, actions, claims suffered by the principal” due to the negligence or misconduct of the agent. Nevertheless, the indemnity should not be applicable without considering the actual reasons. Similarly, binding an agent to provide corporate guarantee to the principal/bank on behalf of the buyer does not seem logically justified.

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