

where the transactions would be settled through book-keeping entries at a central computer. If one takes a closer look at the mechanics of the induction of legal tender (rupee notes in Pakistan or dollar bills in the United States) into an economy, the scope of 'printing of money' to finance government purchases becomes discernible. However, this prospect is to be seen in the light of monetary management of the economy from an Islamic point of view. The details of this subject (in the Shari'ah perspective) are still a challenge for Islamic economists.

An important message of this essay is that there is a need for an entirely new orientation by the fiscal establishment. The question of financing of the Government's budget will prove to be the biggest hurdle in the way of the elimination of riba. Some obstacles in this regard can be removed with the following fiscal reforms.

1. Separation of zakah (welfare) budget—both its making and management—from the rest of the government budget.
2. Distinction between economic and non-economic uses of funds. The latter mostly relate to the administrative role of the Government; their quantum will determine the urgency for reforming the tax system. The nature of economic application of funds will determine the sources which may be tapped to generate necessary funds.
3. Separation of combat-related defence budget (expenditures on armaments, border defence and their likes) from the rest of the defence budget (expenditures on maintenance of cantonments in main cities, garrison schools and colleges for wards of defence forces, military hospitals, etc.). The latter category covers such benefits as are not offered to other Pakistanis in recognition of their role in building the country. From a Shari'ah point of view, their expenses ought to be charged to the beneficiaries rather than the public at large through the national exchequer. The present

taxation or interest-free loans. The latter may also take the form of temporary transfer of resources (loans) from one head of government expenditure to another during a given fiscal year. Pure "loans" from independent sources should not be expected. The case for "compulsory" borrowing from the well-to-do and financial institutions rests on a proper definition of public interest within the Shari'ah framework. The possibility of the Government buying salaried services on credit—either directly from the workers (employees) or some other agencies—is akin to conceding its State role; this ought to be resisted.

In all cases where the acquisition of some goods or services is involved, a wide array of trading and participatory financing arrangements can be conceived. For example, tanks can be purchased under *ba'ey mo'ajjal* (sale on deferred payment terms) with the financing agency who can directly pay to the manufacturer. Big dams and power projects can be made under a combination of trading and participatory financing arrangements. In projects of a strategic importance, the principle of *Shirakah alMutanaqisah*—participatory financing with the stake of the financier (s) decreasing over time—may be followed.

The idea of perpetual modarabah bonds, along the lines of the NIT (National Investment Trust) units, may also be developed for financing existing and future economic-oriented activities by the Government. In order to initiate such a scheme, however, there ought to be a clear specification of the goals of the fund and the principle of distribution of profits and the sharing of the losses. If the funds are properly managed, losses would be a mere theoretical possibility: highly unlikely in practice.

One of the means to finance government purchases may be printing of money! This idea is not as abominable as it has been made to be. Note that no one disputes the needs for a legal tender.—Perhaps an exception may be a futuristic society

we ignore the existing commitments and obligations of the Government in order to arrive at clear and proper answers. In this short essay, we also avoid the question of international transactions at the government level and the Shari'ah status of the state's membership of international financial organizations, such as the International Monetary Fund and the World Bank.

At present, the Government of Pakistan performs the following functions:

- A. General administration, including law and order
- B. Defence
- C. Social welfare programmes
- D. Development programmes
- E. Debt servicing

As expected, practically the first four government functions involve purchases of scores of goods and services and financing arrangements in order to meet the consequent payment obligations. Persistent budgetary deficits of the past have also made debt servicing a regular feature of the Government budget.

The case of debt servicing is the simplest. Sooner or latter—regardless of whether the elimination of riba is an issue or not—the nation has to concede that public debt is essentially deferred taxation, and fork out money for this purpose. The elimination of riba will have one immediate implication: an end to the option of raising new interest-base loans in order to retire the old ones. However, the Government may explore the prospects of replacing some of the existing interest-based loan contracts with financially equivalent but Islamically admissible contracts; this would amount to replacement of Shari'ah-proscribed and, hence, invalid contracts with proper ones.

In all other cases, whether A, B, C or D, when the Government acquires services under wage contracts, it is obliged to pay in cash. This, in turn, requires generation of revenue ahead of the expenditure commitments either through

dominant mode. In this case, the overriding consideration for the financier is to recover his funds with a return. Though checks and balances may be built into a loan transaction through suitable guarantees, the lender is least concerned about what transpires with the funds at the borrower's end. Technically speaking, the lender is not a party to the use of funds while those are with the borrower. Thus, the creditor's provision of funds and their practical application on the borrower's side become two independent operations. An Islamic economy is free from such a dichotomy. Therefore, the elimination of *riba* will lead to all financing being tied to either the sharing of the ownership control (equity financing — *modarabah* or *musharakah*) or the end-use of funds (such as credit sales). Pure "loans" without any end use are unlikely to be a regular source of financing. The fiscal implications of the elimination of *riba* have to be seen in this background—for all cases where tax revenues are not available to finance a given public expenditure.

Government is an institution which represents its electorate with diverse and often mutually exclusive interests. Though it is a 'legal' person, it can change hands. The government transactions differ from the private in several respects. These include, among other things, complex and time-consuming legal formalities, because the personal positions of those representing the government are not at stake. Moreover, the government transactions represent the needs of one quarter—defence or political establishment—but the responsibility of another—the treasury, not to mention future generations. The decision-makers usually operate in a short run while the obligations have a long-term character. Thus there is asymmetry in perceptions about the relative importance of needs and financial constraints. These factors imply that *any solutions for the problem of **riba** are bound to be complex, and are likely to face resistance for all sorts of reasons.* Notwithstanding these apprehensions, the problem of *riba* has to be faced head on in order to obey the express Orders of Allah 'Azza wa Jall. It is in this spirit that

FISCAL IMPLICATIONS OF THE ELIMINATION OF RIBA

(Sayyid Tahir¹)

The Islamic world view is that this life is a test. For this purpose, Allah *Tabarak wa Ta'aala* has prescribed certain modes of transactions besides, of course, certain acts of personal worship such as Salah and Saum. The case of riba is to be seen in this perspective.

The issue of riba arises whenever a transaction between two parties involves a direct exchange of items of the same general kind—with or without a time lag in the give and take back process. If such a transaction is not on a one-to-one and equal basis, it becomes a ribawi transaction, and the discrepancy riba. It is strictly forbidden by Allah *Sub`hanahu wa Ta'aala*. This prohibition applies irrespective of whether the parties to a transaction are two individuals, two institutions (including the state) or one individual and one institution.

Notwithstanding the prohibition of riba, the Shari`ah permits numerous ways for pursuing legitimate ends. The prohibition of riba indeed restricts the number of options available in an Islamic economy as compared with a capitalistic economy. However, in practice, this is a blessing in disguise. It serves the all too important purpose of restraining unbridled, undisciplined, irresponsible and socially harmful behaviour by the members of the economy—be they individuals, businesses, financial institutions or the state.

Traditionally, in a capitalistic framework financing takes two forms: Equity or loans—the latter with the promise of a return. Unlike a loan, equity financing involves sharing of the ownership control by the financier. Loan financing is by far the

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