

## Reciprocal Loans\*

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ABSTRACT. The matter of reciprocal loans , whereby a loan is tied to an equivalent ( reciprocal ) loan in terms of amount and period , raises many questions particularly from the shariah point of view . This necessitates looking into the existing contracts , whether by individuals or corporations, pertaining mainly to whether they come under “ a loan that entails a benefit “ or “ tied-in loans “ . Legitimizing reciprocal loans based on promise rather than being part of contract , may not constitutes a shariah accepted solution , according to some scholars .

The issue of reciprocal loans or more generally loans that are contingent upon counter loans, is the subject of intensive debate as far as their legal admissibility from an Islamic viewpoint is concerned and consequently as far as the legal permissibility of the proposed forms for their application, whether they be private, institutional, or more specifically inter-bank loans. The proposed forms resting essentially on the exchange of loans or the conditioning of a loan upon a counter loan. In view of the theoretical significance of the issue on the one hand, and the existence of such proposals and applications on the other hand, this paper aims at a discussion of the subject that seeks to foster an exchange of views with the aim of arriving at findings that can be relied upon and adhered to. lend you, provided you lend me.

### I. Core of the Issue

The issue under discussion can be formulated in the following question:

Can a lender require the borrower to give him a loan as a condition for the former's loan? More generally, can the lender stipulate the obtainment of a loan for him or someone else, from the borrower or someone else, in exchange for the loan he made to the borrower? Since it is known that a required increment (*ziyada*) on a loan is

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deemed proscribed usury (*Riba*), in fact it is the very '*Riba*' of the pre-Islamic era forbidden by the Quran and the Prophetic Tradition (*Hadith*) as well as by the unanimous resolution of the jurisprudence consensus (*Ijma'*), is the making of a loan contingent upon the acquirement of a counter loan a kind of requisite increment? Is a loan against another a kind of contingent benefit which makes the first loan fall under the category of "a loan that brings a benefit [to the lender]" (*qard jarra naf'*), and is it so prohibited? Can making a loan contingent upon a reciprocal loan be classified as binding a contract upon another contract?

Approaching the issue from a different perspective, can a loan that is contingent on a reciprocal loan be permitted because the lender did not gain an appraisable or a benefit but just obtained another loan—the benefit of the loan not being appraisable, since Islam has proscribed the acquirement of any increment in exchange for the loan? Can a loan that is contingent upon a counter loan be admissible on the grounds that no one amass any wealth or assured returns by dealing in reciprocal loans?

## **II. Significance of the Issue**

As has been stated above, the importance of the issue of reciprocal loans derives from the existence of several applications actually available and proposals submitted that are essentially based on the offer of loans in return for counter loans. Yet, if such operations are permissible they would undoubtedly create new prospects for financial and banking institutions to provide and obtain financing as well as to cooperate and deal with other financial and banking institutions.

## **III. Reciprocal Loan Application**

### ***III.1 Bank Deposits Contingent upon Lending***

A bank deposit, in a jurisprudential modulation, is nothing but a loan made by the depositor to the bank, because the bank acts as the guarantor of the deposit and is at the same time authorized to make use of it. If the depositor then requires the bank to grant him a loan in exchange for the deposit, whatever form that loan may take, he is in effect conditioning a loan on a counter loan. According to some respondents working in the banking business, this method is employed by some people both at the private and institutional levels to avoid usurious transactions. So, instead of requiring a cash return, a client would demand of his bank, in return for the deposit, a direct loan or permission to overdraw his account (allow the account to run into debit) up to a set limit and for a set term, and so on. This method may also be used in transactions between banks, as a bank may open a (deposit) account at another (correspondent) bank in order to assign to it various forms of transfers on condition that the correspondent bank allow the account to be overdrawn for an amount equivalent to the deposit for the same term or perhaps for a smaller amount and a longer term or for a greater amount and a shorter term according to the well-known numeric system.

### **III. 2. Lending against Deposits<sup>(1)</sup>**

This is the opposite case of the above, where in one proposed form a bank offers a loan to a loan applicant in exchange for a deposit by the applicant of part of the loan at the bank upon receiving the loan for a term that is commensurate with the ratio of the deposit to the amount of the loan according to the numeric system. For instance, if the bank grants a loan to an individual of SAR 100,000 for a term of three months, it stipulates that the borrower deposits a part of the loan at the time he receives it for a longer term, let us say 10% of the loan (i.e., SAR 10,000) for 30 months ( $100,000 \times 3 = 10,000 \times 30 = 300,000$ ). Thus after three months, the borrower pays the full SAR 100,000 and after 30 months, he obtains SAR 10,000. Therefore, he has given the bank a loan from the same loan he obtained from it in exchange for obtaining that loan.

### **III. 3 Loans from Central Banks in Return for Bank Loans to the Public<sup>(2)</sup>**

In this case, the Central Bank undertakes to offer loans to banks which grant interest-free loans (*qard hasan*) to the public. In this eventuality, it has been proposed that the loans offered by the Central Bank be commensurate in size with the size of the loans offered by banks, for example by initiating the size to the range of 20 to 25% of the loans made by banks to individuals.

### **III. 4. Mutual Loan Societies<sup>(3)</sup>**

These are mostly informal societies, wherein a group of employees or individuals may agree that each of them contribute a part of his income for the members of the society to benefit from the pooled amount according to varying arrangements. In reciprocal loans, two cases of mutual loan societies (*jam'iyat al-muwaddafeen*) are pertinent:

**Case One:** Here a group of individuals may agree to pay a periodic installment, mostly on a monthly basis, by each of them, and then each individual (in order) would borrow the proceeds of the pooled installments. The agreement may stipulate for the society to continue operating for another cycle in reverse order.

**Case Two:** Here a group of individuals may agree to pay a periodic installment by each of them, so that the pooled amounts are allotted to lending whoever society member needs a loan in accordance with agreed rules regarding priority for borrowing, borrowing limits, and payment methods.

The first case involves loans that are contingent upon counter loans, if the society's membership comprises three or more individuals. Supposing the membership is three and the society's installment is SAR 1,000, the first person receives SAR 3,000 including his installment of SAR 1,000 and SAR 2,000 as loans from the second and third persons. The second person receives in the second month SAR 3,000 including his installment of SAR 1,000, SAR 1,000 from the first person as payment of the loan that he granted the first person in the first month, and SAR 1,000 as a loan from the third person. The third person will receive SAR 3,000, including his installment of

SAR 1,000, SAR 1,000 from the first person as payment of the loan that he granted him in the first month, and SAR 1,000 from the second person as payment of the loan that he granted him in the second month. Thus, the first person is an outright borrower; the last one is an outright lender, while the other person (or persons) are lenders to those preceding them and borrowers to those following them in the chain. As a person gets nearer to the first person in the queue his borrowing increases while his lending decreases, but as a person gets nearer the last one in the queue, his lending increases while his borrowing decreases<sup>(4)</sup>. Thus, each person lends to those preceding him provided those following him lend to him. If it is stipulated that the society continue to operate for a second cycle in reverse order, an additional condition is enforced, which is that the one who lends those preceding him in the society in the first cycle requires them to lend him in the second cycle. Hence, the first case of mutual loan societies involves a loan against a loan from someone other than the borrower, but also from the borrower if a second cycle is required in reverse order.

In the second case, it is obvious that there are loans that are contingent upon counter loans as each person has a joint stake in the society's proceeds allocated to lending and each person allows the other to borrow from his share (the person's share) in return for the other person allowing him (the first one) to borrow from his (the second person's) share, but also in return for the other persons allowing him to borrow from their shares.

### ***III.5 A Loan in One Currency against a Loan in a Different Currency<sup>(5)</sup>***

This form has been proposed as a way to provide foreign currencies to banks without them having to sell their foreign exchange holdings at an inopportune time, which may engender a loss for the banks. The idea rests on inter-bank loans in different currencies with each bank lending the other in the currency of which it has a surplus. For example, if a Saudi bank had a surplus of pounds sterling and needed American dollars whereas a Kuwaiti bank had a surplus of American dollars and needed pounds sterling, instead of each of them having to sell its foreign exchange holdings in order to obtain the currency it needed, they may agree to make an exchange of loans in the currency available to each. Such loans are undeniably reciprocal ones: you lend me pounds sterling and I lend you American dollars. It is also undeniable that there is a clear stipulation of a loan against a loan.

Those are the major forms and applications of reciprocal loans, although other individual and institutional transactions may exist which resemble them in terms of being based on a loan for a loan wherein obtaining a loan is made contingent upon offering a counter loan.

## ***IV. A Loan for a Loan in Islamic Jurisprudence***

In reviewing the views of Islamic jurists, regarding the question of a loan for a loan, we find most of them in favor of proscription and inadmissibility. For instance, *Mawahib Al-Jalil* states that "there is no divergence of opinion on the inadmissibility

of a person lending to another for the latter to subsequently lend to the former"<sup>(6)</sup>. The *Commentary* asserts: "Regarding his statement 'or for someone else to lend that person', it means for the borrower to grant the lender another loan and not for the borrower to lend to the lender, since that case would 'bring a benefit' (*jarro naf'*) for the lender and hence be inadmissible. So, consider that."<sup>(7)</sup> *Kashshaf Al-Qina'* affirms that "if the borrower stipulates that he should pay back less than what he borrowed, then that is inadmissible, as it would entail a loss of analogy; whereas if someone requires another to sell, lease, or lend him, then that is proscribed, as it would be analogous to 'two sales in one' (*bay'atayn fi bay'a*), which has not been permitted"<sup>(8)</sup>. *Al-Mughni* maintains that "if the loan is made contingent on the borrower renting the lender his house, or selling him something, or lending him in turn, then that would not be permissible because the Prophet (PBUH) prohibited the combination of a sale and a loan and because the borrower bound a contract upon another, thus invalidating the transaction as if he had sold his house to the borrower provided he sold him his house in return"<sup>(9)</sup>.

Similarly, the late Sheikh Abdulaziz bin Baz, ruled that a loan that is made contingent upon a loan from the borrower to the lender is inadmissible. Responding to the following question: "What is your judgment of lending someone on condition that he repays the loan within a specific term and then makes you a loan of the same amount for the same term? Is the Prophetic Tradition 'Any loan that brings a benefit is usury' applicable to such a case, noting that I did not ask for an increment?", Sheikh Abdulaziz replied as follows: "Such a loan is inadmissible as it is contingent upon obtaining a benefit, which is the counter loan. Scholars have unanimously agreed that any loan that is conditional upon a benefit constitutes usury. A number of Companions of the Prophet (PBUH) have also made rulings to that effect. As for the Prophetic Tradition mentioned—'Any loan that brings a benefit is usury'—it is a weak one (*da'eef*). However, our reliance here is on the ruling of the Companions and scholarly unanimity prohibiting the case in question"<sup>(10)</sup>. The inadmissibility of this form of lending is also attributed to Sheikh Saleh Al-Fawzan and Sheikh Abdulaziz bin Abdullah Al Al-Sheikh, in their inference that a mutual loan society is not permissible on the grounds that it involves a loan made contingent upon a counter loan<sup>(11)</sup>.

Sheikh Mohammed bin Saleh bin Otheimeen and Sheikh Abdullah bin Abdurrahman bin Jibreen are also reported to have ruled on the admissibility of a loan for a loan, as it can only imply the requirement of a benefit for the lender on a par with the benefit obtained by the borrower and thus the loan does not involve an increment<sup>(12)</sup>.

On reciprocal loans in the same currency or in differing currencies, a ruling (*Fatwa*) has been issued, within the framework of Ramadan Jurisprudence Discussion Forums held by Dallah Al-Barakah, which states that "if two banks agree for each of them to provide the other with the amount that either of the two may request as a loan in the same or in a differing currency, such an agreement is permitted for the purpose of avoiding transactions at interest which is taken or given on debtor accounts between

the two banks provided no loan is made contingent upon the other"<sup>(13)</sup>. It would appear then that the latter case falls under a non-binding arrangement as it would appear that the above ruling confirms the inadmissibility of reciprocal loans if the counter loan is a condition of the initial loan.

### Endnotes

- (1) *Islamic Thought Council of Pakistan. Eliminating Interest from the Economy (Council Report). ('Ilgha' Al-Fa'ida min Al-'Iqtrisad)*. Translated by Abdul'aleem Al-Sayed Mansi. Jeddah: King Abdulaziz University. 2<sup>nd</sup> Edition, 1404H. p. 31.
- (2) **Mohammed Najatullah Siddiqi**. *The Non-Interest Banking System* (in Arabic). Jeddah: King Abdulaziz University. 1<sup>st</sup> Edition, 1405H. pp. 43, 73.
- (3) **Saad bin Hamdan Al-Lihyani**. *Credit in Islamic Economy* (in Arabic). *Doctorate Thesis*. Makkah: Umm Al-Qura University. 1419H. p. 195 and subsequent pages.
- (4) The loan sum that is obtained by a person in the mutual loan society can be computed according to the following formula:  

$$Q = I (M - O)$$
 whereas the loan sum he lends in the society can be computed according to the following formula:  

$$R = I (O - 1)$$
 Where Q is the loan sum obtained by the society member, R the loan sum he lends, I the society's Installment, M the society's Membership, and O the Member's Order in the society's queue.
- (5) **Sami Hammoud**. *Tatweer Al-A'mal Al-Masrifiya bima Yattafiqu wa Al-Shari'a Al-Islamiya*. Unpublished. 2<sup>nd</sup> Edition. 1402H. pp. 350-351.
- (6) **Mohammed bin Mohammed Al-Hattab**. *Mawahib Al-Jalil li-Sharh Mukhtasar Khalil*. Libya: Maktabat Al-Najah. Undated. 4/391.
- (7) **Suleiman Al-Bajeermi**. *Hashiyat Al-Bajeermi 'ala Manhaj Al-Tullab*. Turkey: Al-Maktabat Al-'Islamiya. Undated. 2/356. See also: **Suleiman Al-Jamal**. *Hashiyat Al-Jamal 'ala Sharh Al-Manhaj*. Egypt: Al-Maktabat Al-Tijariyyat. Undated. 3/262.
- (8) **Mansur bin Yunes Al-Bahuti**. *Kashshaf Al-Qina'*. Beirut: 'Alam Al-Kutub. Undated. 3/317.
- (9) **Abdullah bin Ahmad bin Qudama**. *Al-Mughni*. Riyadh: Maktabat Al-Riyadh Al-Haditha. 1401H. 4/355.
- (10) **Abdulaziz bin Baz**. *Al-Fatawa*. Mu'assasat Al-Da'wa. 2<sup>nd</sup> Edition. 1408H. 1/152.
- (11) **Abdullah bin Abdulaziz Al-Jabreen**. *Jam'iyat Al-Muwaddafeen*. Makkah Al-Mukarramah: Dar 'Alam Al-Fawa'id. 1<sup>st</sup> Edition. 1419H. p. 11.
- (12) *Ibid*. p. 54.
- (13) **Abdulsattar Abu Ghuda, et al.**, "*Fatawa Halaqat Ramadan Al-Fiqhiya Al-Thaniya lil-Qadaya Al-Masrifya Al-Mu'asira*"; Jeddah, 8-9 Ramadan 1413H (1-2 March 1993) in *Kitab Al-Fatawa Al-'Iqtisadiya*. Ed. Research and Development Department, Dallah Al-Barakah. 4<sup>th</sup> Edition. 1414H. p. 164.

## References

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