

The Concept and Challenges of Islamic Pawn Broking (*Ar-Rahnu*)

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Abstract: The introduction of Islamic pawn broking (*Ar-Rahnu*) in Malaysia is seen as a new micro credit instrument. This paper aims to provide a review on *Ar-Rahnu*'s concept and challenges faced by Islamic pawn shops in Malaysia. The study employs library and archive research to achieve the objectives of the paper. Islamic pawn broking consists of four basic concepts namely *Qardhul Hasan*, *Ar-Rahnu*, *Al-Wadi'ah* and *Al-Ujrah*. The Islamic pawn broking have several advantages over conventional pawn broking because it provides a cheaper way to obtain financing and is free from interest. In addition, assets pawned are guaranteed to be kept safely and there is a fair practice in auctioning and bidding. In addition, *Ar-Rahnu* also helps finance educational needs and provides capital to small businesses and entrepreneurs. It implies that this instrument will help the community to increase economic capability of their families. Future research should study effective ways in managing challenges faced by Islamic pawn shops.

Key words: Islamic pawn broking • *Ar-Rahnu* • Micro credit instrument

INTRODUCTION

The first Islamic pawn shop in Malaysia was established by the Terengganu State Government and known as *Muassasah* Gadaian Islam Terengganu (MGIT) in 1992. The establishment of MGIT is to provide immediate financing to assist individual in overcoming cash flow needs through methods which are considered *halal* by the Shariah regulation [1]. Ever since the introduction of Islamic pawn broking, the demand for it increases continuously [2]. *Ar-Rahnu* scheme is now offered by several banks including Bank Rakyat, EON Bank and Bank Pertanian Malaysia.

From the Islamic perspective, the pawning contract is a voluntary charitable contract (*tabarru'*), whereby the pawned object is given without any financial compensation. It is also one of the contracts involving non-fungibles, which are not considered totally binding until the object of contract being delivered [8]. Shariah based pawn broking or known as *Ar-Rahnu* consists of four basic concepts, namely *Qardhul Hasan* (the borrower is only required to pay the amount borrowed. However, as token of appreciation, the

borrower may pay extra to the lender), *Ar-Rahnu* (the borrower is required to place a valuable asset for the loan extended by the lender and it may be utilized as payment if the debt is not repaid within the agreed period), *Al-Wadi'ah* (The borrower is required to produce a valuable asset (usually gold) as collateral to ensure repayment of the loan. The lender is responsible to take the necessary precaution to ensure the security of the asset placed by the borrower; however, the lender is not required to replace the item if it is not due to the lender's negligence) and *Al-Ujrah* (the lender is allowed to charge a reasonable fee for keeping the pawned items safe and in good condition).

The introduction of Islamic pawn broking (*Ar-Rahnu*) in Malaysia is seen as a new micro credit instrument [3] as it provides a financial product for the lower income group and small businesses which usually have limited capital or have been excluded from the mainstream financial system [4]. It also offers investment opportunities besides preventing illegal or unlicensed financing activities [5]. This paper aims to provide a review on the Islamic pawn broking (*Ar-Rahnu*) concept and challenges faced by Islamic pawn shops in Malaysia.

Unique Features and Pillars of Ar-Rahnu: Ar-Rahnu in Arabic means withholding or holding back. It derives from the word in Quranic verse:

“And those who believe and whose families follow them in Faith,- to them shall We join their families: Nor shall We deprive them (of the fruit) of aught of their works: (Yet) is each individual in pledge for his deeds” [al-Thuur: 21]

Ar-Rahnu is also mentioned in the following verse:

If ye are on a journey and cannot find a scribe, a pledge with possession (may serve the purpose). And if one of you deposits a thing on trust with another, Let the trustee (Faithfully) discharge His trust and let him fear his Lord. Conceal not evidence; for whoever conceals it,- His heart is tainted with sin. And Allah Knoweth all that ye do” [al-Baqarah : 283].

Thus, from the above related verse, the word of “*ar-rahnu*” (mortgage or security money) in Islamic jurisprudential terminology means: “possessions offered as security for a debt so that the debt will be taken from them in case the debtor failed to pay back the due money”. The foundations regarding Ar-Rahnu are also mentioned in the Hadith. The Prophet Muhammad p.b.u.h says:

“A riding animal is used in return for its expenses if it is pledged; and milk is drunk in return for its expenses, if (the animal) is pledged. He who rides the animal or drinks the milk has to pay the expenses” and;
“A pledge does not become the property of the mortgagee; it remains the property of its owner who mortgaged it; it is entitled to its benefits and he is liable for its expenses”.

Based on the above mentioned Hadith, it can be understood that the pledge does not become

binding except with reception of the object. It cannot be conducted other than by a person who is free, accountable, adult and discerning under no interdiction for insanity or bankruptcy [6]. Moreover, it has to be by permission of the mortgagor. If the pledge is transportable, then receiving it means vacating it on the part of the mortgagor and taking hold of it free of any hindrance by the mortgagee. In addition, the Islamic scholars also states that any individual may pawn their weapons to *ahl-zimmah* (non-Muslims who pay taxes to the Islamic government) [7].

A pillar is an important element in Islamic contract because it determines the validity of a contract. Hence, the concept of Ar-Rahnu in Malaysia has several pillars [9] as presented in Table 1.

Ar-Rahnu consists of several features. The purpose of Ar-Rahnu is to help the lower income groups to obtain quick and easy access to cash, by taking valuable asset as collateral. Other features of Ar-Rahnu are described in Table 2.

The Superiority of Islamic Pawn Broking (Ar-Rahnu):

The Islamic pawn broking (Ar-Rahnu) offers several advantages as compared to conventional pawn broking. Firstly, the cost involved in borrowing from an Islamic pawn broking is simpler and cheaper way to obtain financing compared to conventional pawn broking. For instance, customers at *Muassasah Gadaian Islam Terengganu* will be charged a reasonable fee for the safekeeping service of the customer’s jewellery ranging from no charge to RM0.75 for every RM100 of gold value per month depending on the amount of loan [1]. The service charges imposed on Ar-Rahnu’s customers are cheaper than the conventional pawn broking, which charges rates of more than 25% per annum, Islamic pawn broking cost less than 20% per cent per annum [15].

Secondly, in Ar-Rahnu agreement, *usury* (interest) is prohibited and *haram*. Ar-Rahnu customer is required to place a valuable asset as collateral for the loan extended by the institution/bank and no interest will be incurred and only minimum fee is charged for the safekeeping of

Table 1: Pillars of Ar-Rahnu

Concept	Description
Borrower (al-Rahin)	A party that borrows money from another party by placing valuable asset as collateral
Lender (al-Murtahin)	A party that lends money to another party and responsible for the safety of the valuable asset pledged by the borrower. From the other aspect, the contract also should have the willingness from both parties (borrower and lender) [10].
Pawn Items (al-Marhun)	Items pawned as collateral.
Loan Amount	The amount of loan needed by the borrower.
Sighah/Agreement	Agreement between the borrower and lender between the loan amounts related issues. In addition, the contract of Ar-Rahnu will be continuously applied albeit the death of both parties (lender and borrower) [11].

Table 2: Features of Ar-Rahnu

Features	Description
Loan Amount	Loan amount up to RM1,000 or collectively up to RM25,000 maximum depending on banks and institutions. There are institutions with higher provision which offer amount of loan up to RM50,000 [12].
Margin of Loan	Customers receive a loan of up to 80% of the value of the item pledged. Unlike the conventional system, customers get lesser loan. Usually, valuation is based on the purity of the gold item.
Tenure of Loan	Usually the financing tenure for Ar-Rahnu scheme is six months. However, borrower may request to extend the payment period. In the event if the borrower failed to redeem his gold or jewelry, the bank will give him notice of auction.
Fees	Customers will be charged a minimum safekeeping fee depending on the value of the pawned item. The fees ranging from free to RM0.75 for every RM100 of gold value depending on institutions.
Pawn Products	Pawn product that is normally accepted is gold. This item maybe utilized if the borrower is not able to make the repayment within the agreed period.
Repayment Method	Repayment can be made either by installment or lump sum amount through cash or cheque.
Settlement	In this situation, if the customer is not able to make the repayment, goods will be sold [13].
Utilization of Pawn Goods	Pawn goods can be utilized with the permission for free. The person will not be charged for any damages made [14]

Note: USD1=RM3.20

the values. Unlike the conventional pawn broking, customers will be charged an interest (up to 2% on loan amount) in addition to the service charge. This interest earned is an income to the conventional pawn broker and it is *haram* in Islam. It has been reported that the conventional pawnbrokers are likely to offer a higher interest rate compared to the rate stated in the Pawnbrokers Act 1972 [4]. Abdul Razak [4] further explains that this often happens to illiterate customers or impoverished people and villagers from rural areas.

Thirdly, jewellery and pawned assets will be kept safely whereby Islamic pawn broking institutions will give guarantee on safety matters and will be responsible on the pawned assets [16]. Thus, client should not be worried on their pawned assets. For example, Ar-Rahnu Scheme under EON Bank insures all the jewelry and pawned assets under the Takaful insurance scheme throughout the financing scheme.

The fourth advantage of Islamic pawn broking in comparison to the conventional broking is on the bidding notice and auctioning process. In Ar-Rahnu, in the event of default and if the institution has to sell the jewellery or pawned items, advance notice on bidding will be given and the jewellery or pawned items are disposed or sold via open tender system which reflects the fairness and non-exploitative system of Islamic finance. Unlike the conventional pawn broking, many customers do not know when their collateral will be auctioned off. The notices about the auction are only publicised in Chinese and English language papers. Usually, these notices will be

overshadowed by other more interesting notices. This is a disadvantage to the conventional pawn shop customers who are usually Malays from the villages or Indians from the estates. Only a handful of them read the English or Chinese papers and some of them are illiterate. This will cause them to lose the opportunity to reclaim their goods [4].

Finally, Ar-Rahnu is less stringent in terms of the repayment period unlike conventional pawn broking. Repayment period is reasonable whereby customers may request to extend the repayment period. For example, Ar-Rahnu customers at AgroBank will be given a duration of six months to make repayment. Then, the repayment period can be extended for another three months and lastly for another two months. If the customer fails to pay after the extension period, the collateral will be auctioned to pay off the loan. If there is any surplus after the loan has been settled, it will be returned to the customer. On the other hand, conventional pawn broking demands additional payment from the customer if the customer is unable to pay back the debt within the period.

Roles of Ar-Rahnu as a New Instrument of Micro Credit:

Micro credit has emerged as an important instrument to relieve poverty in developing countries. For instance, during the Asian economic crisis in 1998, the governments of the Asian countries have paid greater attention for the micro credit sector to help small businesses in rural areas [17]. In Nigeria, the micro-credit facilities serve one million people and the numbers are increasing [18].

The existence of Ar-Rahnu as one of micro-credit instruments which is an interest free source of micro-credit has given clients the option to choose for best service provider for financing. According to Mohd Ali [3], there are five main roles of Ar-Rahnu in socio-economic development. First, Ar-Rahnu is a source of capital to the small business. It provides quick and easy system compared to getting loans from commercial banks or finance companies procedures [2]. Secondly, Ar-Rahnu could be a source of financing educational needs, especially at the beginning of school term or prior to enrolment at tertiary level [3]. Thirdly, people who run agricultural projects and small industries in the villages use this scheme as one of their rolling capital mechanisms [3]. Fourthly, Ar-Rahnu also plays an important role as a means of community service. This scheme fulfills the desperate needs of low income families. This is an alternative from using the illegal scheme such as “Ah Long” [3]. Lastly, Ar-Rahnu acts as an instrument to encourage saving and investment among the community. Activities of buying and selling gold is a form of investment, which double the profit out of gold price differences and proceeds from business using the Ar-Rahnu [3].

Challenges Faced by Islamic Pawn Broking in Malaysia:

The Islamic pawn broking has been introduced in Malaysia for the last 20 years. Since its establishment, it is observed that Islamic pawn shops have faced several challenges in their daily operations. First, although Ar-Rahnu is seen as a source of capital for many activities, customers still prefer to patronize the conventional pawn shop or lend money from illegal source such as ‘Ah Long’. They prefer to borrow from the conventional pawn shop or illegal source since they can provide higher margin to value of collateral and unlimited time to redeem [2]. For example, customers can borrow up to 90 percent of the value of the asset pledged from any conventional pawn shop, whereas customers are only able to borrow up to 65 per cent of the value of collateral.

Secondly, consumers are quite reluctant to choose Islamic pawn broking because it is perceived by the society as products that are meant for poor and needy people. Therefore, Ar-Rahnu scheme providers face the challenge of educating the consumers on the benefits and advantages of Islamic pawn broking in order to increase the acceptance of Islamic pawn broking. Finally, Islamic pawn brokers also have been reportedly received gold that turn out to be fake. If this situation occurs continuously, it will destroy the future of Islamic pawn broking as a source of capital or financing.

CONCLUSION

Ar-Rahnu contract is one of the *muamalat* contracts. It is also a form of contract in Islamic economic system which has the nature of assets securities. It will benefit the community from various aspects since it plays the important role of providing capital, cash incentives, financial resources (loans) for businesses and education purposes. In addition, the existence of Ar-Rahnu institutions will help expand income generation for Muslims community. Future research studying ways of managing challenges faced by the Islamic pawn shops is recommended to ensure the effectiveness of Ar-Rahnu as a new micro credit instrument.

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