

## **USURY (RIBA) AND BANK INTEREST ARE THE SAME - A MISCONCEPTION OR REALITY**

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### **Abstract**

*In recent years we have seen tremendous growth in Islamic Banking & Financial sector globally, but this growth has not translated into numbers in countries like India. It has been observed that most of the population is under the notion that Riba is deemed as Bank Interest and therefore banking and allied services too are prohibited for Muslims around the world. The present study will investigate the relationship between usury and interest. It will also try to throw light on some of the major misconceptions related to Islamic financing. This paper aims to figure out the difference between the two and bridge the gap so that inclusive financial growth can be opted by people in India also.*

**Keywords: Riba, Usury, Bank Interest, Islamic Finance**

### **Introduction**

The concept of Islamic Financing or aptly Ethical Financing in recent years has roots that date back to fourteen hundred years. Before this period lending loans for unproductive purposes and charging hefty interest on the amount was common. This practice led to another social problem of slavery. Slavery became a common problem in these areas. It was only after of Islamic religion that such practices were prohibited. Islam prohibited usury but permitted business financing and profit sharing based on risk sharing. Islam encouraged the business risk appetite of individuals/groups and promoted a sustainable financial business model to the world.

It was due to the lack of Islamic financial literacy among the common people that Islamic financing took such a long time to prosper.

The most common verse of the Holy Quran which prohibits lenders to charge extra or excess amount states:

*GOD has permitted trade, and forbidden usury (riba). Whosoever receives an admonition from his Lord and gives over, he shall have his past gains, and his affair is committed to God; but whosoever reverts — those are the inhabitants of the Fire, therein dwelling forever.*

Islamic scholars must critically analyze why in the Holy Quran trade and usury were compared simultaneously together. According to the verses in the Holy Quran, Trade is permitted while Usuary is prohibited in Islam. Usury is the unethical and immoral practice of lending loans that will unfairly enrich the lender. Before the advent of Islam, people due to their financial needs took loans from money lenders who took their needs as an advantage for their own financial growth. There was an unethical practice of a huge amount of usuary and if they were unable to pay the required amount in time the borrower, he may land up ending a slave to the money lender. This practice of

usury was discouraged in Islam while trade financing was permitted. Trade was permitted as it not only increases employment and promotes productivity and prosperity in the society but also helps in building a strong State while Usury does the opposite.

### **Literature Review**

In India people generally have a habit of saving money for bad times and avoid taking money from lenders on interest. Indians deposit money in saving accounts in banks and are financially rewarded by a certain fixed percentage amount being credited to their accounts by the bank. The problem arises with the Muslim depositors as they neither take loans in the time of crisis nor take bank Interest as a reward for their savings. This problem has arisen as most scholars took the concept of Usury and equated it to Bank Interest.

**Siddique, M. Z. (2022).** had a view that most Islamic scholars and researchers have failed to establish the link between money and riba in the modern world because they followed a wrong methodology while describing the concept of riba.

**Harahap, B., &Risfandy, T. (2022)** have done their research on Islamic finance in Indonesia. They had done primary study on the perception of riba and bank interest and concluded that they had received mix response from the public while all agreed that riba is prohibited in Islam.

**Wibowo, A. T., &Ayunda, V. (2022).** In their research on Riba and it's global effect concluded that there is still a prevalent debate among muslim scholars that one should equate riba with bank interest on not but all the scholars are in consensus that usury is prohibited in Islam.

**Ulama'i, A. H. A. A., Rahmawati, F., & Din, M. U. (2022)** have concluded that riba is prohibited in all major religions of the world.

**Eyerci, C. (2021)** had done research on an alternative approach in Islamic economy. He concluded that since any type of interest is prohibited in Islam and any alternative instruments can be used for finances which includes Partnership Musharakah, Murabaha, Mudaraba, hire purchase, Ijarah Leasing and Iqtina.

**Hasriadi, H. (2021)** concluded in his paper on 'The equation of riba and interest' that the only difference between riba and bank interest is that the former is for consumptive loans, while bank interest is for loans that are productive.

**Khan, W., &Nomani, A. (2021)** were of the view that farmers will be more comfortable in taking loans from a non-interest-based financing system.

**Said, L. R., Bilal, K., Aziz, S., Gul, A., Shabbir, M. S., Zamir, A., &Abro, H. (2021)** in their article titled A comparison of conventional versus Islamic banking customers attitudes and judgment have concluded that the main objective of conventional banks are profit maximization while the main objective of Islamic banks is social justice.

**Ercan, H., Karahanoglu, I., & Walter, G. (2021)** had done research on whether Islamic banking in Turkey interest is free or not. Surprisingly they found that although islamic banks in Turkey were claiming that profit-sharing ratios were different from interest rates paid to the depositors on their deposits in conventional banking, they are highly correlated.

**Ahmed, M. U. (2014)** classified riba as unnatural, unjust, immoral, and evil. He concluded that the Islamic form of financing promotes entrepreneurship and trade while the traditional system only promotes borrowing and lending.

**Abdullah, A. K. (2013).** Concluded that the basic inefficiency of interest-based lending, the various forms of instability it causes, and the large debts it has given rise to, constitute good reasons for phasing out this mode of financing and replacing it with a mode of financing that is more conducive to economic growth: profit and loss sharing

**K.P. Mazoor( 2013)** concluded that the major objective of any financial institution must be social-economic development. He also focused that a strong and effective legal system must be established before the introduction of Islamic banking in India.

**Siddiqi, M. N. (2004).** wrote that trade created exchange value. The traders can take a margin for their selling efforts and take risk of investment.

**M Bellalah and S Ellouz (2004)** suggested that Islamic finance has failed to get the attention of the majority population because it discourages interest on loans on a false pretext of value creation.

**Saeed, A. (1996)** has studied different types of riba and claimed that none of the authentic ahadith attributed to the Prophet in relation to riba mention the terms loan (qard) or debt (dayn) is present.He also argued that the system of riba collection is the exploitation of the economically disadvantaged borrower by the relatively affluent money-lenders and that the contemporary Muslim scholars should permit interest.

### **Objective of the Study**

The objective of the study is to discuss the difference between Riba and Bank Interest and bridge the gap between the less fortunate individuals and the elite class availing banking services.

**Methodology**

The present study is based on secondary data collected from various journals, books, magazines and websites.

**Discussion**

During the regime of Caliph Umar (634-644 CE) the concept of sustainable Islamic economic system was initiated. During those times all forms of riba under the notion of its literal meaning extra were classified as prohibited. This positively led people to invest in business rather than to save but a class of old age population which were risk averse were left with no option but to consume the principal amount of savings. Later on, scholars and reformers like Sir Syed Ahmad Khan argued the difference between usury(riba) and non riba(interest) which was earned out of productive investment. Later on, such an argument paved the pathway of creating an ethical/ Islamic bank. Dubai Islamic Bank became the first commercial Islamic bank. Other Muslim nations later adopted the concept of ethical banking under the supervision of sharia law.

India inspite of having third largest Muslim population of the world have not shown interest in opening an Islamic bank because of lack of demand of it. Still people of India consider bank interest as riba and so it's deemed to be self-prohibited. "Muslims try to avoid riba by avoiding the standard debt-contract, but this is not possible in most situations" Khan, F. (2010, p 14) Even most of the Muslim population was hesitant of using a conventional bank account because of this reason. The Government of India even initiated the JAN DHAN Scheme to incorporate the less fortunate people into the banking mainstream by this. The misconception of equatingriba and bank interest needs to be removed so that majority of Muslim population can avail the financial the benefits of the banking sector and become more financially stable.

The term 'riba' means the extra or excess amount the lender charges apart from the principal amount. There is a lot of difference between Riba and Bank Interest. "there are some Muslims who wish to do the same by arguing that what Islam has prohibited is riba and not interest" Chapra, M. U. (2008 p-2). Some of them are mentioned below

**Table 1: Difference between Riba and Bank Interest**

|                    | <b>Riba</b>               | <b>Bank Interest</b>   |
|--------------------|---------------------------|--|
| <b>Origin</b>      | Loan                      | Deposit  |
| <b>Risk</b>        | There is no risk          | If bank defaults the depositor is at risk  |
| <b>Social Evil</b> | It promotes slavery       | It promotes protection of value of deposit   |
| <b>Amount</b>      | It is time value of money | Fixed percentage of profit sharing on deposit  |
| <b>Type</b>        | One sided Contract        | Contract of Mutual benefit   |
| <b>Charge</b>      | It is charged arbitrarily | The financial regulator regulates it's amount considering the demand and supply and other economic factors |

*Source: Developed by the author*

**Reasons for Prohibition of Riba**

Muslims around the globe do not need any other reason than its prohibition in the Holy book Quran. Many scholars have pointed out many social and cultural reasons other than religious one why we must include riba in our economic system. Some of the reasons are

1. It is not ethical to charge an extra amount than the principle if the lending amount is being used for a non-productive purpose.
2. Interest on non-productive lending will ultimately lead to inflation.
3. Riba leads to negative growth in the economy.
4. It is an unjust practice as it promotes exploitation of the needy.
5. It deepens the gap between the rich and the poor class.

**Table 2: Reasons supporting the Bank Interest not to be included as Riba**

| Prohibition of Riba   | Permission of Bank Interest  |
|---|--|
| The borrower needs money.   | The Depositor has excess money left with himself/herself.                                      |
| The borrower cannot dictate his terms and conditions of repayment                   | The Depositor has the right to withdraw his/her deposited money at his/her convenience.        |
| The borrowed money will create an artificial negative change in the value of money. | The deposited money will be circulated in the economy thereby boosting the economic condition. |
| There is no or negative productivity in the economy                                 | The banks make profit out of it.   |

*Source: Developed by the author*

“Based on some Qur'anic verses from Surah al-Baqarah, the author argues that the rationale of the prohibition of riba is the exploitation of the economically disadvantaged by the relatively affluent money-lenders and that the contemporary Muslim scholars should permit interest in view of the difference of circumstances between our time and earlier times” Saeed, A. (1996 , p.35).

#### **Misconception about financing**

- Profit sharing if fixed in a trade financing amounts to Riba.
- Taking loans on cars or vehicles is prohibited since you must pay a fixed interest on them.
- A housing Loan cannot be taken as you must repay a greater amount than you have borrowed.

#### **Conclusion**

India is not only the youngest country in terms of the average age of its citizens but a highly populous country as well. The banking system in India must be strengthened by strict lending norms. Indian banks must be instructed to promote productive lending thereby encouraging young entrepreneurs and helping in creating new jobs. Productive lending will in turn not promote Muslims to share the reward of their investment, but this step will also reduce the amount of Non-performing assets. There is no doubt that Islamic financing will boost the Indian economy and will strengthen it. Islamic financing is not only ethical but can act as a tool to fasten the growth of our economy.

There is no doubt that usury is unethical, unjust, and against the principles of Islam. Traditional Banks provide loan for both productive and unproductive purposes. If Banks promotes financing new ventures for budding entrepreneurs and charge fee for it then the distribution of profits among the bank depositors will not be unethical or against the principles of Islam. Changing the lending structure can give a boost to any economy and incorporate all sections of the society into the banking system.

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