

A FRAMEWORK OF ISLAMIC ECONOMICS WITH REFERENCE TO ISLAMIC TAXATION AND ALLOWABLE EXPENDITURES

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ABSTRACT

The concept of Islamic Economics underscores the view that Islam, as a religion dictates a total way of life. The system of taxation in Islam, which is a prominent part of its economics is said to be divinely designed to arrest poverty in the Muslim community. Zakaat has often been cited as a good example of this system of taxation. It is generally accepted as an act ordained by God to ensure fair re-distribution of economic resources among the followers of Islam. This paper examines Islamic economics, and in doing so, it evaluates the meaning of Zakaat with a view to throwing more light on its uniqueness as an Islamic form of taxation. It also highlights allowable expenditures for tax purposes that are available to business entities, subject to levy of business Zakaat. It compares such tax deductions with conventional ones operating in non-Islamic settings, specifically in common law jurisdictions. The article concludes

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that despite ambiguity surrounding the Islamic taxation especially on issues of tax base, treatment, procedures, interpretation of law, and several others, Islamic tax policies are meant to foster plans on development in their entirety and to ensure social security with the objective of alleviating poverty in the Muslim community.

Keywords: Islamic economics, Islamic taxation, income tax, Zakaat, allowable expenditures.

RANGKA EKONOMI ISLAM DENGAN RUJUKAN KEPADA PENCUKAIAN ISLAM DAN PERBELANJAAN DIBENARKAN

ABSTRAK

Konsep ekonomi Islam menggariskan pandangan bahawa Islam sebagai sebuah agama merencanakan satu cara hidup. Sistem pencukaaian Islam yang merupakan bahagian penting ekonomi Islam dikatakan direka bentuk oleh Tuhan untuk menghalang kemiskinan dalam masyarakat Muslim. Zakat sering disebut sebagai contoh terbaik sistem pencukaaian ini. Umumnya ia diterima sebagai satu perbuatan yang diperintah oleh Tuhan untuk memastikan pengagihan semula sumber ekonomi yang adil di kalangan pengikut agama Islam. Makalah ini meneliti ekonomi Islam, dan dalam melakukannya, ia menilai makna zakat dengan tujuan untuk melemparkan cahaya ke atas keunikannya sebagai satu bentuk pencukaaian Islam. Ia juga menyerlahkan perbelanjaan dibenarkan untuk tujuan cukai yang boleh didapati pada entiti perniagaan, tertakluk kepada levi zakat perniagaan. Ia membandingkan pemotongan cukai sedemikian dengan sistem konvensional yang beroperasi dalam seting bukan

Islami, khususnya dalam bidang kuasa common law. Makalah ini disimpulkan bahawa walaupun ketaksaan mengelilingi pencukaaian Islam terutamanya isu asas cukai, layanan, prosedur, tafsiran undang-undang dan beberapa yang lain, dasar cukai Islam bermaksud untuk menggalakkan rancangan untuk pembangunan yang menyeluruh dan memastikan keselamatan sosial dengan tujuan mengurangkan kemiskinan dalam masyarakat Muslim.

Kata kunci: ekonomi Islam, pencukaaian Islam, cukai pendapatan, zakat, perbelanjaan dibenarkan

INTRODUCTION

Poverty is the summary measure of the state of well-being of people, thus, it serves as a gauge through which the effectiveness of governance may be determined. In line with the modern world, it has been suggested that embedded in the measurement of poverty are such variables as income, education, employment, and access to basic necessities of life such as housing, clothing, food, water, etc. “Breaking the vicious circle of poverty and inequality vis-a-vis insecurity, low savings – low investment and low and fragile growth traps constitute a central concern of public policy.”¹ In addition to financing the state activities, the main objectives of Islamic tax system may be stated as alleviating poverty, improving income distribution, and creation of a just society.² The appropriate tax

¹ See Chukwuma Charles Soludo, ‘*Breaking the Dynasties of Poverty in Nigeria*,’ published as personal opinion at the Back Page of THISDAY Newspapers, a daily news publication in Nigeria, on Monday, 26th November, 2012. It is also available on the Internet at THISDAY LIVE: <http://www.thisdaylive.com/> accessed on Monday, 26/11/12.

² See Ali Reza Jalili, ‘*A Descriptive Overview of Islamic Taxation*,’ part one of a two-part paper on taxation under Islamic jurisprudence, New England College, Department of Business, Henniker, p.6. It is an unpublished work but the author can be reached via the following email address: ajalili@nec.edu.

policy to move the Muslim society “toward these goals will be a policy which provides stimuli for investment and discourages idle hoarding of cash and wealth.”³

According to United Nations Organisation, (UN), everyone has the right to a standard of living adequate for the health and well-being of himself and of his family, including food, clothing, housing and medical care and necessary social services, and the right to security in the event of unemployment, sickness, disability, widowhood, old age or other lack of livelihood in circumstances beyond his control.⁴ On the basis of this UN’s position on human security which is closely related to social security, one may argue that safety for people from both violent and non-violent threats stresses freedom from fear, but includes freedom from want and this may “comprehensively cover all the menaces that threaten human survival, daily life and dignity.”⁵ Surprisingly, efforts by various international bodies in mobilising resources to ensure social security for all have yielded little or no result. However, many Muslims are of the view that, although the secular world is struggling to create a ‘rule,’ there are revealed directions for social security in Islam. It is from this perspective the Islamic stance on taxation and the issue of allowable expenditure should be viewed.

Human nature, if untamed, is characterised by selfishness and greed. The fear of God is one of the measures, an effective one that enables man to place under control the ugly aspects of his nature which include selfishness and greed. This underlines the essence of religion in which man is constantly urged to let the fear and consciousness of God reflect in everything he does with a view to overcoming his weaknesses. Islam is a holistic religion and prescribes a regulatory framework encompassing all aspects of life: spiritual, social, economic and political.⁶

³ *Ibid.*

⁴ See Article 25, United Nations Universal Declaration of Human Rights (1948).

⁵ See Gary King and C.J.L. Murray, ‘*Rethinking Human Security*,’ *Political Science Quarterly* Vol. 116, (2002) at pp.585-610.

⁶ See Sami Hasan, ‘*Muslim Philanthropy and Social Security: Prospects, Practice, and Pitfalls*,’ a paper presented at the 6th Information Security and Testing Research (ISTR) Biennial Conference held in Bangkok, (9-12 July 2006) at p. 7. The author, a lecturer at University of Technology, Sydney, is reachable via: Samiul.hasan@uts.edu.au.

In the Islamic system of taxation and administration of the society as a whole it is, thus hard to separate religion from governance of people.

On the basis of recognising Islam as a complete way of life, devoted Muslims let faith govern all aspects of their lives. As a religion, it is not only concerned with the spiritual invigoration or uplifting of its followers, it is equally concerned about their material and physical well-being. Islam is described as an institution that focuses on training the individual spiritually and ethically to suppress selfishness and greed and to promote goodness.⁷ Consequently, Islam guides Muslims not only in financial and economic matters, but also in social and political affairs as well as in moral and personal spheres of human life.⁸

In Muslim societies, the choice of a tax or a combination of taxes, level of exemption, rate bands, scope for deductions and definition as well as measurement of tax bases etc ought to be remarkably guided by the dictates of the Shariah (i.e. Islamic Jurisprudence) but familiarity with Shariah principles seems to be only useful conceptually and not operationally. It should be pointed out that comprehending the concept of such principles may provide the general framework for analysing and understanding Islamic taxes and their spirit. Essentially, in term of practical value, Shariah-based prescriptions are yet to manifest in full in many, if not all of the existing Muslim sovereign states.

Islam suggests and promotes a decentralised system of codification and practice within the fundamental framework based on the spirit of submission and prayer to God, equality of human beings, justice and peace. In the absence of a centralised system of regulatory control, many Muslims individually and collectively, over the years have tried to exploit the perceived 'vacuum' for personal, group, or community benefits.⁹ For instance, it is pertinent to note that throughout the history

⁷ See Yahia Abdul Rahman, 'The Economic Dilemma' in 'Interest Free Islamic Banking: Lariba Bank, Foundation for a United & Prosperous Community,' first published in USA 1994 as Lariba Bank, Malaysian edition, Al-Hilal Publishing, (1999), Malaysia, at Chapter Two, p. 7.

⁸ See Sayyid Muhammad Rizvi, 'An Introduction to the Islamic Economic System: The Middle Path,' in 'A Khums (The Islamic Tax)' Third (revised) edition, published by Sayyid Muhammad Rizvi, 7 El Dorado Street, Richmond Hill, Ontario, Canada (1992) at p. 2.

⁹ See Sami Hasan, 'Muslim Philanthropy and Social Security: Prospects, Practice, and Pitfalls,' a paper presented at the 6th Information Security

of Islam various interpretations and differences of opinions have emerged on details and mechanism of taxation. Due to many conceptual vagueness and generalities in Islamic economic doctrine, it is extremely difficult to present a concise, coherent and uniform understanding of the Islamic tax system. Other factors contributing to this phenomenon include: subjective interpretation by different authors, the writers' ideological tendencies, large and frequently conflicting accounts of events, and outright mistakes in translation of sources.¹⁰

Nevertheless, the outline, intent and spirit of the original Islamic tax law are rather clear in the sense that Islamic tax system contains both 'general' as well as 'selective' or 'classified' taxes.¹¹ Specific taxes and tax system are prescribed. Disregarding, degrading or contradicting these prescriptions can turn out to be catastrophic to the developmental policies and policy-making institutions in Muslim societies. Hence the essence of paying attention to Islamic economics as a whole with a view to ensuring not only the operation of a reasonable tax system but also the existence of a fair and just society in line with the Qur'anic injunctions.

ISLAMIC ECONOMICS

One of the first points emphasised by Islamic authors is that Islamic economics is not capitalism minus interest plus Zakaat (compulsory tax payable by Muslims on income that exceed prescribed Nissabs i.e. minimum amount of wealth liable to tax payment) or socialism minus state control plus God; rather it is something unique and different and exclusive to Islam.¹² How unique or how different is essentially the key

and Testing Research {ISTR} Biennial Conference held in Bangkok, (9-12 July 2006) at p. 7.

¹⁰ See Ali Reza Jalili, 'A Descriptive Overview of Islamic Taxation,' part one of a two-part paper on taxation under Islamic jurisprudence, New England College, Department of Business, Henniker, at p. 6. It is an unpublished work but the author can be reached via the following email address: ajalili@nec.edu.

¹¹ *Ibid.*

¹² See Yahia Abdul Rahman, 'Definition of Islamic Economics' in 'Interest Free Islamic Banking: Lariba Bank, Foundation for a United & Prosperous Community,' first published in USA 1994 as Lariba Bank,

issue. A look at the definition of Islamic economics offered by some of the Islamic authors may show the uniqueness that differentiates it from other types of economic activities.

Islamic economics is defined as the knowledge and application of injunctions and rules of the Shariah that prevent injustice in the acquisition and disposal of material resources in order to provide satisfaction to human beings and enable them to perform their obligations to Allah (SWT Subhaanahu Wa Ta'ala meaning, The Glorified and the Exalted) and society.¹³

Similarly, Islamic economics has been defined as aiming at the study of human *falah* (salvation) achieved by organising the resources of earth on the basis of co-operation and participation. The role of the Islamic Jurisprudence, the notion of *adl* (justice) and salvation, co-operation and sharing are central themes to Islamic economic philosophy.¹⁴

Thus, one may argue that the Islamic economic system is not in itself complete; it is a part of the overall system of life. Islam is a compact system of life in which all its aspects (religious, ideological, social, political and ethical) are well synchronized. "Muslims will succeed only if they put the whole system into work, and not just choose and pick from it according to their likes and dislikes."¹⁵ As such, a policy maker in a Muslim society must bear this in mind constantly, especially when devising and implementing socio-economic policies including taxation.

Furthermore, there are a host of Islamic concepts and values that define the extent and nature of economic activity. Similarly, Islamic thoughts encompass several schools and interpretations. Shiite School and four Sunni Schools, namely, Mālikī, Shāfi'ī, Hanafī and Hanbali, are the most popular and predominant schools offering interpretations.

Malaysian edition, Al-Hilal Publishing, (1999), Malaysia, at Chapter Three, p. 20.

¹³ See S.M. Hasanuz Zaman, 'Journal of Research in Islamic Economics,' Vol. 1 (2), (Winter 1984) at pp. 51-53.

¹⁴ See M. Akram Khan, 'Islamic Economic: Annotated Sources in English and Urdu,' Islamic Foundation, Leicester, England (1983) at p. 28.

¹⁵ See Sayyid Muhammad Rizvi, 'An Introduction to the Islamic Economic System: The Middle Path,' in 'A Khums (The Islamic Tax)' Third (revised) edition, published by Sayyid Muhammad Rizvi, 7 El Dorado Street, Richmond Hill, Ontario, Canada (1992) at p. 2.

To understand the Islamic tax system, Islamic views on several relevant economic categories should be noted. Appreciation of these notions will help one to grasp the nature of the Islamic tax system and its place within the overall Islamic doctrines.

Equally important are the concepts of ownership, concentration of wealth, justice and appropriate consumption which are regarded among the essential ideas that underline the overall Islamic economic system. For instance, in the Islamic code of property relations, a property owner's right to property is limited by the good of the community – if the owner fails to understand his limitation, the control over property may be removed from him. God has made all that is in the earth subservient to human kind,¹⁶ but human beings are not allowed freehold title; they are the trustees – not the absolute owners.¹⁷

The entire universe with all the natural resources and powers is made amenable to exploitation by man, though it is owned by Allah alone. Thus, Islamic property right is not absolute because Allah is the ultimate owner of all there is. He is the only real, actual and final owner of everything as pronounced in the Qur'an: "Whatever is in heavens and the earth belongs to Allah."¹⁸

Similarly, another verse states that "to Him alone belongs everything in the heaven and the earth and all that lies in between them, and all that is beneath the soil."¹⁹ This statement or something similar to it is repeated in many other chapters of the Qur'an. Consequently, human beings are only entrusted with the wealth which enables them to hold property and enjoy the attached benefits as long as they understand that they hold such property in trust and must respect the law of the Real Owner – Allah.

The Islamic principle of property suggests that needy people have a right in the wealth of the rich on the ground that everything belongs to God and He has gracefully bestowed some property on some people who ought to be grateful and must help others in need. The provisions of distribution in Islam are made with a view to preventing property from

¹⁶ See Al-Qur'an 22: Verse 65.

¹⁷ See Naqvi S.N. Haider, *'Ethics and Economics: An Islamic Perspective,'* The Islamic Foundation, London, UK, (1981) at p. 87.

¹⁸ See Al-Qur'an 2: Verse 284.

¹⁹ See Al-Qur'an 20: Verse 6.

being “made a circuit between the wealthy among you.”²⁰ Islam aims to elevate all its followers to the level of ‘*ghina*’ (i.e. being free from want), which is in line with the concept of social security of the UN.

As another author remarks: “the key to economic philosophy of Islam lies in man’s relationship with God, His universe and His people, (i.e. other human beings,) and the nature and purpose of man’s life on earth. Man-God relationship is defined by *Tawhid* (Oneness of God). The essence of *Tawhid* is the total commitment to the will of Allah, involving both submission and mission to pattern human life in accordance with His will. The will of Allah constitutes the source of value and becomes the end of human endeavour. Life on earth is a test, and its purpose should be successful in the test by obeying the commandments of Allah. Life on earth being a test and all the provisions available to man is accountable to Allah and his success in the life hereafter depends on his performance in this life on earth.”²¹

Consequently, the distribution of wealth and the outcome of economic activities including policies and taxes must be ‘just’ and in line with the Shariah principles as provided in the Qur’an. Opposition to fraud, greed, deception and other vices that cause concentration of wealth in few hands including hoarding of idle wealth is traceable to this train of thought.

To explore these issues in detail is a subject matter beyond the scope of this paper; rather the aim here is to briefly capture and present the essence and spirit of Islamic taxation, its philosophy, objectives and institutions with a view to eliciting Islamic perspectives on taxation and allowable expenditures. On this basis, the relevant question to raise now is whether Islamic taxation is the same as any other system of taxation and if this question is answered in the positive, further probes are required to authenticate the genuineness of such response; if, on the other hand, the question is answered in the negative, then to what extent is tax in Islam different from others and is there any similarity between them?

²⁰ See Al-Qur’an 59: Verse 7.

²¹ See Muhammad Nejatullah Siddiqui, ‘*Muslim Economic Thinking*,’ Islamic Foundation, Leicester, England (1981) at p. 23.

DIFFERENTIATING ISLAMIC TAXES FROM TAXES IN COMMON LAW COUNTRIES

The concept of taxation as being practised in common law jurisdictions has no bearing on Islamic system of revenue. Fundamentally, taxation in Islam places emphasis on wealth rather than income. It follows, then, that the Islamic taxation system hardly taxes income the way it taxes wealth. “This means that the average person will be left with more disposable income and will be liable for tax on whatever wealth is left at the end of the year. This will have a significant effect on the economy.”²²

Islamic Jurisprudence recognises individuals as the taxpaying units. As such, households, corporations and other entities are not taxed. Instead, all income and taxable items pass through these institutions to individual owners and are taxed at that level.²³ As a result of the fundamental difference between Islamic taxation and that of neoclassical economies, among which common law jurisdictions happen to belong, searching for Islamic position may turn out to be a vain voyage.

To avoid such a fruitless journey, the concept of Zakaat which occupies a pre-eminent position in Islam and has some features of taxation would be examined as an approach to understanding Islamic stance on the issues of tax relevant to the discussion. In addition, comparison between Zakaat as prescribed in Islam and man-made taxes as decreed by secular taxation system would bring to light the similarities and differences between the two in terms of their nature, foundations, philosophies, characteristics, ratios and proceeds which may enable one to appreciate the strength or weakness inherent in the two systems of taxation.

In Islamic Jurisprudence, there are two levels by which Islam aims to create and preserve the economic equilibrium in the Muslim states and these are: individual and communal (collective). According to

²² See Islamic Economics, ‘*Tax Money in Islam Perspective*’ available at the following website: <http://islam-economy.blogspot.com/2010/04/tax-money-in-islam-perspective.html> accessed on Thursday, 09/08/2012.

²³ See Ali Reza Jalili, ‘*A Descriptive Overview of Islamic Taxation*,’ part one of a two-part paper on taxation under Islamic jurisprudence, New England College, Department of Business, Henniker, p. 9. It is an unpublished work but the author can be reached via the following email address: ajalili@nec.edu.

a work relevant to the discussion, individual level involves charity as a voluntary good deed and at the collective level Islam imposes obligatory taxes on Muslims.²⁴

Under the second category falls Khums, (which literally means ‘one-fifth or 20%’) and Zakaat (which is the third pillar of Islam and one of its essential rites). Both are important tools of Islamic economic system from the perspective of taxation. While Sunni school treats some taxable items under Zakaat, Shiites treat the same items under Khums. For instance, gold, silver, including cash and paper money above prescribed Nissabs (minimum amount of property liable to tax payment) which are subject to Zakaat in Sunni Muslim community attract Khums in Shiite Jurisprudence. However, most of the Islamic taxes mentioned in the Quran come under Zakaat; hence the attention given to Zakaat each time the issue of Islamic taxation is raised.

While the majority of jurists believe that the Zakaat payer may not receive any direct material benefit from the payment of Zakaat, some are of the opinion that even an indirect benefit from Zakaat by the Zakaat payer is not permitted;²⁵ this, among other factors, distinguish Zakaat as a form of Islamic tax from the other kind of taxes in operation in the common law jurisdictions where taxpayers are taxed for the provision of public infrastructures and other benefits provided by the government to the community at large including the taxpayers.

Evaluating the meaning of Zakaat may throw more light on its uniqueness as an Islamic form of taxation.

²⁴ As an author observed, “under ‘individual level,’ we talked about charity which is a voluntary good deed. Under ‘collective level,’ we talked about the taxes which Islam has made obligatory upon Muslims.” See Sayyid Muhammad Rizvi, ‘*An Introduction to the Islamic Economic System: The Middle Path*,’ in his book, entitled, ‘A Khums (The Islamic Tax)’ Third (revised) edition, published by Sayyid Muhammad Rizvi, 7 El Dorado Street, Richmond Hill, Ontario, Canada (1992) p. 2.

²⁵ See Zamman S.M. Hasan-Uz, ‘*The Economic Functions of the Early Islamic State*,’ International Islamic Publishers, Karachi, Pakistan (1981) at p.169.

THE MEANING OF ZAKAAT

The term – ‘Zakaat’ – is an Arabic word and it comes from the root letter za, kaf, ya, which has several meanings. For instance, in the Qur’an Zakaat has been used to mean all of the following: to be clean;²⁶ to be the obligatory charity;²⁷ to be pure and innocent;²⁸ to be better in purity;²⁹ to praise oneself and to justify.³⁰ It has also been described as regular charity³¹ or legal alms.³²

However, from the perspective of this paper, Zakaat refers to a generic compulsory tax and literally means to purify or to grow. To purify in the sense that it purifies the heart from the detested trait of stinginess and also purifies the wealth by donating a portion of that wealth; there is a general belief that it also causes the wealth to grow through Allah’s blessings. While regular charity is strongly recommended and abundantly rewarded by Allah, (SWT), Zakaat is a debt which adult and able bodied Muslims owe Allah (SWT) which must be paid as a part of their belief in His commandments. It is on this basis that Zakaat is said to be payable by all Muslims who are free, in possession of the taxable item, and with ability to utilize the properties and make decision about them.³³

Some Muslim Schools of thought, such as the Shiites and the Hanafis are of the view that minors and insane individuals should be

²⁶ See Al-Qur’an 24: Verse 21 and Al-Qur’an 23: Verse 4.

²⁷ See Al-Qur’an 2: Verse 43.

²⁸ See Al-Qur’an 19: Verse 19 and Al-Qur’an 18: Verse 74.

²⁹ See Al-Qur’an 18: Verse 81 and Al-Qur’an 19: Verse 13.

³⁰ See Al-Qur’an 53: Verse 32.

³¹ See Ali A. Yusuf, ‘*The Holy Qur’an: Text, Translation and Commentary*,’ Dar Al Arabia, Beirut, (1938), note 5353.

³² See M.H. Kamali, ‘*Freedom, Equality and Justice in Islam*,’ Ilmiah Publishers Sdn Bhd, Petaling Jaya, Malaysia, (1999).

³³ See Khoie Aboulquasem, ‘*Towzih-ul-massael*,’ Elmiyeh Publisher, Qum, Iran (1982), at p. 316; see also Montazeri Housain Ali, ‘*Resaleh Towzh-ul-massael*, Qum, Iran (1986) at p. 20, this particular book can also be found on the following website: <http://www.montazeri.com/html/books/resaleh> accessed on Tuesday, 14/08/2012; in addition, see also Khomeini Rouhollah, ‘*Resaleh Towzh-ul-massael*, Qum, Iran (1980) at p. 15, Khomeini’s book is also available at: <http://al-shia.com/html/far/books/feqh/resah> accessed on Tuesday, 14/08/2012.

exempted from Zakaat while other Schools like the Mālikī and the Shāfi'ī believe that in these cases it is the duty of the guardian to pay Zakaat on Zakaatable items belonging to those vulnerable people.³⁴ Importantly, for payment of Zakaat to be valid, the Zakaat payer must have the intention of paying Zakaat, pay it for prescribed categories, and unconditionally transfer the ownership to the recipient.

As an act ordained by Allah (SWT), one of the pillars of the Islamic faith, a fundamental obligation, a cornerstone, and the religion's financial, economic and social system, Zakaat is an extremely important aspect of Islamic code of conduct. Hence the remark of Sheikh Yusuf al Qardawi that in the hierarchy of Islamic faith and religious duties, Zakaat is next to the acclamation of Allah's unity and prophecy of Muhammad (peace be upon him) and the five daily prayers.³⁵

The implication of this is that it is the third pillar of Islam and it is sometimes translated as alms or poor-due but as stated earlier it actually means purification, growth (i.e. increase), goodness and blessing. This meaning is rooted in viewing Zakaat as a part of the wealth and property that adult and able bodied Muslims must pay annually in order to help the poor and the needy in their community. In Islamic concept of social relations, individuals are subject to two constraints. First, the individual must sacrifice part of his income for charity to acquire virtue. Second, he must internalize community preference as a responsible member of

³⁴ See Shad Abdur Rahman, *'Zakaat and Ushr'*, Kazi Publications, Lahore, Pakistan (1986) at p. 57; see also Shaikh Abdul Quader, *'Zakaat and Taxation'*, in *Outlines of Islamic Economics*, Proceedings of the first Symposium on the Economics of Islam in North America, Association of Muslim Social Scientists, Indianapolis, Indiana, USA (1977) at p. 8; see also Khoie Aboulquasem, *'Towzih-ul-massael'*, Elmiyeh Publisher, Qum, Iran (1982), at pp. 316-317; see also Mannan M.A., *'Islamic Economics: Theory and Practice'*, Sha Muhammad Ashraf Publishers, Lahore, Pakistan (1991) at p. 287.

³⁵ See Mohamad Ali Elgari, *'Foreword'* in the book *'Fiqh al Zakah: (Volume 1) A Comparative Study of Zakah, Regulations and Philosophies in the Light of Qur'an and Sunnah'* written in Arabic Language by Yusuf al Qaradawi, Translated by Dr Monzer Khaf, Scientific Publishing Centre, King Abdulaziz University, Jeddah, Saudi Arabia (1969) at pp. i.

his society, and avoid conspicuous consumption such as luxury and extravagance through self restraint checked by individual intelligence.³⁶

Similarly, producers and traders, as ‘individuals in community’ are required to produce community approved goods and avoid profiteering and other unfair trade practices.³⁷ Zakaat as a charity in Islam is meant to be a source of social security.³⁸ It has been the outstanding social pillar of Islam, enabling individuals’ efforts to be steered towards a common goal,³⁹ which underscores its definition as a determined portion taken from the wealthy and allocated to those deserving it.

Therefore, one of the main purposes of Zakaat is to keep those who are wealthy clean, monetarily, with implication of not committing sin in the sense that it is immoral or sinful not to pay Zakaat as and when due. Thus it is a form of sadaqah (charity) which is obligatory on Muslims by Qur’anic injunctions.

ISLAMIC SOURCES OF LAW

The primary source of law in Islam is the Noble Qur’an which for the first thirteen years of revelation (encompassing around 18/30 parts known as the Mecca passage), established the moral and ethical foundation of the Muslim community.⁴⁰ The Mecca passage highlights the fundamentals

³⁶ This suggestion is from Imam Al-Gazali (1058-1111AD), especially in the *Nasithat al-Muluk* (Council of Kings – a book on political theory and governance); see Sami Hasan, ‘Muslim Philanthropy and Social Security: Prospects, Practice, and Pitfalls,’ a paper presented at the 6th Information Security and Testing Research (ISTR) Biennial Conference held in Bangkok, (9-12 July 2006) at p. 2 where the author makes reference to the book in relation to the subject matter.

³⁷ See Ozay Mehmet, ‘Al Ghazzali on Social Justice: Guidelines for a New World Order from an Early Medieval Scholar,’ International Journal of Social Economics Vol. 24, (1997), at pp. 1203-1218.

³⁸ See T.E. Gambling and R.A.A. Karim, ‘Islam and Social Accounting,’ Journal of Business Finance and Accounting, Vol. 13 [1] (1986), at pp. 39-50.

³⁹ See Jonathan Benthall, ‘Financial Worship: the Qur’anic Injunction to Almsgiving,’ Journal of the Royal Anthropological Institute, Vol. 5, 1 (1999), at p. 27.

⁴⁰ See An-Naim Abdullahi, ‘Islamic Family Law in Changing World: A Global Resource Book,’ Zed Books, London and New York, (2002).

that God is the only Creator, the prophet was sent as a ‘Warner,’ everybody has to account on the Day of Judgement, summoning human beings to acknowledge God’s power and goodness and He ought to be worshipped, and to act uprightly in practising generosity and avoiding niggardliness.⁴¹ Since this peaceful and voluntary Mecca message of fundamental social and economic egalitarianism was violently rejected in Mecca and Arabia in general, the Mecca message was deemed not suitable for that stage of human development. Thus, the Prophet’s migration to Medina signifies a tactical move to seek a more receptive environment, and also a shift in the content of the message itself.⁴²

This did not prevent the Mecca passage from being part of the primary source of Muslim laws; it remains so as much as the latter part of the Qur’an (the Medina passage) which advises Muslims on how to deal with the aggressors, proclaims commands for social and economic activities, provides guidance for establishing human relationships, and became codified in Shariah as the model of an Islamic state.

The guidance in the Qur’an in most cases is very broad. For instance, the Qur’an advises Muslims to ‘fulfil obligations,’⁴³ without defining them. The Prophet, Caliphs and the exegetes have elaborated on these obligations which in essence analyse the fundamental issues in Islam. These are interconnected divine obligations guiding the individual, social and public life of Muslims, mutual obligations of commercial and social contracts, treaty-based obligation as citizens of states, and tacit obligations for living in a civil society.⁴⁴ The guidance in the Qur’an is open to varied interpretations but when they are based on the fundamentals of peace and justice misinterpretations are avoided.

Hadiths of Prophet Muhammad (SAW) are therefore meant to interpret the Qur’an and clarify areas that seem unclear. During his life time the Prophet used to give guidance (about property relations, tax collection and use, minority rights, etc.) based on divine revelations, independent reasoning (*aql*) or analogical deductions (*qiyas*) and consultation or discussion with close companions including his wives.

⁴¹ See M. Watt, ‘*Islam and the Integration of Society*,’ Roulledge and Kegan Paul, London, (1961), at p. 44.

⁴² *Ibid*, An-Naim Abdullahi,

⁴³ See Al-Qur’an 5: Verse 1.

⁴⁴ See Ali A. Yusuf, ‘*The Holy Qur’an: Text, Translation and Commentary*,’ Dar Al Arabia, Beirut, (1938), note 682.

Islamic Jurisprudence is essentially built on both the Qur'an and the Hadiths along with many subsequent schools of thought and interpretations that emerged purely to throw more light on both the Qur'an and the Hadiths.

As noted earlier, most of the Islamic taxes mentioned in the Qur'an come under the category of Zakaat. The order to give Zakaat is reinforced several times and many places in the Qur'an.⁴⁵

⁴⁵ The following verses from different chapters demonstrate the order to pay Zakaat as instructed by Allah ; they are some of the commands Allah (SWT) made in the Quran in relation to Zakaat which constitute the divine provisions on the subject:- "Establish regular prayer and pay Zakaat..." Quran 2; Verse 110: "Lo! Those who believe and do deeds of righteousness and establish regular prayer and pay Zakaat, their reward is with their Lord and no fear shall come upon them, neither shall they grieve." Quran 2; Verse 277: "Muslims are those who, if we establish them in the land (in authority) establish regular prayer and give Zakaat, enjoin the right and forbid the wrong: with Allah rests the end of affairs." Quran 22; Verse 41: "So establish worship, pay Zakaat, and hold fast to Allah..." Quran 22; Verse 78: "And they are ordered naught else than to serve Allah, keeping religion pure for Him, as men by nature upright, and to establish worship and to pay Zakaat. That is true religion." Quran 98; Verse 5: "Ta Sin! These are the verses of the Quran and the Book that makes (things) clear, A guidance and good news for the believers, Who keep up prayer and pay the poor-rate (Zakaat), and of the Hereafter, they are sure." Quran 27: Verses 1-3: "And keep up prayer and pay the poor-due (Zakaat) and obey the Messenger, so that mercy may be shown to you." Quran 24: Verse 56: "...keep up prayer and pay the poor-due and offer to Allah a goodly gift, and whatever of good you send on beforehand for yourselves, you will find it with Allah; that is best and greatest in reward; and ask forgiveness of Allah; surely Allah is Forgiving, Merciful." Quran 73: Verse 20: "Take alms out of their property, you would cleanse them and purify them thereby, and pray for them; surely your prayer is a relief to them; and Allah is Hearing, Knowing." Quran 9: Verse 103: "Verily, those who give Sadaqat (i.e. Zakaat and alms, etc.), men and women, and lend to Allah a goodly loan, it shall be increased manifold (to their credit), and theirs shall be an honourable good reward (i.e. Paradise)." Quran 57: Verse 18: "The believers must (eventually) win through, those who humble themselves in their prayers; who avoid vain talk; who are active in deeds of charity." Quran 23: Verses 1-4: "Surely they

SOME OF THE HADITHS OF PROPHET MUHAMMAD (S.A.W) ON ZAKAAT

- Narrated Ibn ‘Umar: *Allah’s Apostle said: Islam is based on (the following) five (principles): To testify that none has the right to be worshipped but Allah and Muhammad is Allah’s Apostle; to offer the (compulsory congregational) prayers dutifully and perfectly; to pay Zakaat (i.e. alms); to perform Hajj; (i.e. Pilgrimage to Mecca), and to observe fast during the month of Ramadan.*⁴⁶
- Further, At-Tabarani relates, on the authority of ‘Ali that the Prophet (SAW) said: *“Allah has enjoined upon rich Muslims a due to be taken from their properties corresponding to the needs of the poor among them. The poor will never suffer from starvation or lack of clothes unless the rich neglect their due. If they do, Allah will surely hold them accountable and punish them severely.”*⁴⁷
- Moreover, Abu Huraira narrated that *Allah’s Apostle said, “Whoever is made wealthy by Allah and does not pay the Zakaat of his wealth, then on the Day of Resurrection his wealth will be made like a bald-headed poisonous male snake with two black spots over the eyes. The snake will encircle his neck and bite his cheeks and say, ‘I am your wealth, I am your treasure.’”*⁴⁸
- Similarly, the Prophet (SAW) was reported to have said: *“For every owner of a hoarded wealth on which he does not pay Zakaat, this wealth will be heated in the fire of Hell and made into sheets with which his flanks and forehead will be branded*

who believe and do good deeds and keep up prayer and pay the poor-rate (Zakat) they shall have their reward from their Lord, and they shall have no fear, nor shall they grieve.” Quran 2: Verse 277.

⁴⁶ See Imam Al-Bukhari Collection of Hadiths, Vol.1, Book 2, No. 7.

⁴⁷ This hadith was related by At-Tabarani in Al-’Aswat and as-Saghir.

⁴⁸ See Imam Al-Bukhari Collection of Hadiths, Vol. 2, Book 24, No. 486.

until Allah passes judgment among His servants on a day that measures fifty thousand years (of our reckoning), then his path will be shown, either to Heaven or to Hell.”⁴⁹

- Abu Dawud reported from Samurah ibn Jundub that: “The Prophet (SAW) used to order us to pay sadaqah (Zakaat) on what we have prepared for trade”⁵⁰

It is also recorded that the companions of the Prophet (SAW) were said to have unanimously agreed, during Abu-Bakr’s term of Caliph to fight those who refused to pay Zakaat; and they did in fact fight those who withheld Zakaat.

CLASSIFICATION OF ISLAMIC TAXES

Some of the taxable items are mentioned in the Qur’an or by Prophet Muhammad himself, while others have been added in later years. The subsequent Caliphs altered the tax base several times. Some items became subject to tax (such as herbs, honey, horses, amber, minerals, lentils, spice, etc.), while others were exempted from it (such as apricot, pomegranates, apples and similar fruits, oil, mica, etc.). Several items were switched back and forth between taxable and non-taxable categories or their rates were changed.⁵¹

However taxes that are prescribed by Islam under Zakaat may be classified among others as Ushr (Zakaat of land); Zakaat on livestock; General Zakaat; Zakaat-ul-Fitr (after Ramadan fast Zakaat); Khums (one-fifth or 20% on spoils of war); Kharaaj (different form of land tax); Jizya (‘Poll Tax’) and Kaffaraat (expiation money).

Zakaat, as a specific amount, was said to have been ordained in Medina during the month of Shawwal of the second year of Hijrah (i.e.

⁴⁹ This Hadith was reported by Imams Bukhari, Muslim and Ahmad.

⁵⁰ See Abu Dawud, Collection, translated by Ahmad Hasan, ‘*Sunan Abu Dawud*,’ Vol. II, Lahore, Sh. Muhammad Ashraf, (1984).

⁵¹ See Zamman S.M. Hasan-Uz, ‘*The Economic Functions of the Early Islamic State*,’ International Islamic Publishers, Karachi, Pakistan (1981) at pp. 155-158.

the year the prophet migrated from Mecca to Medina which was 622 AD). Some authors are of the view that the first Islamic tax was Khums, which, according to such writers, was imposed after the Battle of Badr in the second year of Hijrah; Zakaat-ul-Fitr was also said to have been made mandatory in the same year while Kharaaj was reported to have been imposed in the seventh year of Hijrah and Zakaat, which was voluntary at first, was declared mandatory in the eighth year of Hijrah and Jizya was established in the seventh or eighth year of Hijrah.⁵²

The Islamic taxes are mainly levied against and calculated based on actual taxable items. In other words, these taxes are in-kind taxes but payment may be either in-kind or in equivalent value, for instance, Ushr is a flat percentage tax on some agricultural products. Views on taxability of various crops are not uniform but the rates for Ushr are specified in the Hadiths of Prophet Muhammad (SAW) as 5% of the agricultural produce on artificially irrigated lands and 10% on produce of the lands benefitting from rain or natural spring only.⁵³ Ushr is due as soon as the taxable crop is usable or meets certain conditions which makes passage of a year irrelevant in term of requirement for this tax.

Moreover, Ushr is obligatory, irrespective of the land arrangement, on the cultivator or whoever owns the crops at the time they become taxable. Based on the opinion of many jurists, from this point on, even personal consumption from these crops is subject to taxation; sale of the crops or death of the owner would not eliminate the tax and if the taxes are not paid on time, any loss or destruction is liability of the

⁵² For details on this issue, see Ijtihadi Abolqasim, *'The Fiscal and Tax Situation of the Muslims,'* Soroush Publication, Tehran, Iran (1985), at p. 187; similarly, see Sadr Kazim, *'Fiscal Policies in Early Islam,'* in *Essays on Iqtisad: The Islamic Approach to Economic Problems,'* Al-Hasani, Baqir, Miakhor and Abbas, Editors, Nur Corporation, Silver Spring, MD, USA (1989) at pp. 123 & 143; see also Zamman S.M. Hasan-Uz, *'The Economic Functions of the Early Islamic State,'* International Islamic Publishers, Karachi, Pakistan (1981) at p. 44.

⁵³ See Shad Abdur Rahman, *'Zakaat and Ushr,'* Kazi Publications, Lahore, Pakistan (1986) at p. 215; see also Khomeini Rouhollah, *'Resaleh Towzhi-ul-massael,'* Qum, Iran (1980) at p.18, Khomeini's book is also available at: <http://al-shia.com/html/far/books/feqh/resah> accessed on Tuesday, 14/08/2012.

taxpayer.⁵⁴ Ushr may be paid in kind or in cash and some scholars are of the view that Ushr is a one-time tax, therefore, after the payment of initial tax, holding onto the products does not trigger additional taxes.⁵⁵

Meanwhile, when it comes to Zakaat on livestock, some jurists consider animals to be subject to Zakaat only if they meet additional conditions such as being idle during the year, or fed from the public pasture that is not cultivated by anyone, or pastured more than six months.⁵⁶ Each category of animals has its own pre-determined Nisaab and Zakaat is applicable based on the number of holdings beyond Nisaab in each category while the rate structure is expressed in quantity and type of animals. Zakaat on livestock applies to cattle, camel, and sheep older than one year. The implication of this is that this type of Zakaat is extendable to similar animals such as goats, rams water-buffalos and alike. Horses and riding animals were originally exempted but during the reign of the second Caliph, Umar, the exemption was limited to animals used for personal riding and the rate of 5% was established for horses utilized in trade.

Holdings of fish or poultry also fall under the exemption but if they are sold, Zakaat would be applicable to the proceeds from sale. Similarly, wild games are tax-exempt unless they constitute the owner's

⁵⁴ See Montazeri Housain Ali, '*Resaleh Towzh-ul-massael*,' Qum, Iran (1986) at pp. 25-26, this particular book can also be found on the following website: <http://www.montazeri.com/html/books/resaleh> accessed on Tuesday, 14/08/2012; see also Shad Abdur Rahman, '*Zakaat and Ushr*,' Kazi Publications, Lahore, Pakistan (1986) at p.75; see also Khomeini Rouhollah, '*Resaleh Towzh-ul-massael*,' Qum, Iran (1980) at pp. 14-18, Khomeini's book is also available at: <http://al-shia.com/html/far/booksfegh/resah> accessed on Tuesday, 14/08/2012.

⁵⁵ *Ibid.*, (Khomeini Rouholla) at p. 18; see also Montazeri Housain Ali, '*Resaleh Towzh-ul-massael*,' Qum, Iran (1986) at p. 25.

⁵⁶ *Ibid.*, (Khomeini Rouholla) at p. 22; (Montazeri Housain) at p. 20; Shad Abdur Rahman, '*Zakaat and Ushr*,' Kazi Publications, Lahore, Pakistan (1986) at pp.70-7; Rahman Fazlur, '*Economics Doctrines of Islam*,' Four Volumes, Islamic Publication Ltd, Lahore, Pakistan, (1986), at p. 218; Sadr Kazim, '*Fiscal Policies in Early Islam*, in *Essays on Iqtisad: The Islamic Approach to Economic Problems*,' Al-Hasani, Baqir, and Mirakhor, Abbas, Editors, Nur Corporation, Silver Spring, MD, USA (1989) at p. 142.

trade. Generally, in a situation where animals are kept for business purposes such as trade, procreation and breeding, or dairy, they would be taxable, but when the holdings of animals are for personal uses such as meat consumption, riding, assisting in agricultural activities, or transportation, they are not taxed unless these activities are the owner's trade. Some scholars argue that if the animals are kept in the taxpayer's business as 'merchandise,' they would be treated as such. Accordingly, these animals are subject to general Zakaat and not Zakaat of animals.⁵⁷ The former is in addition to items taxed under the latter and Ushr. Opinions vary on specifics but it seems there is an agreement in which gold, silver, and 'other assets' above prescribed Nisaabs are subject to tax under the general Zakaat. This tax is due whenever the taxable item remains in the taxpayer's possession for one year.

Gold and silver as two distinct categories of taxable items are fairly straightforward in the sense that they are taxed at the rate of 2.5% when they are above Nisaab while the third category is somehow problematic due to the absence of unanimous agreement on what constitutes the appropriate tax base under the 'other assets' category. Items such as wealth, income, idle wealth, hoarded wealth, merchandise, articles of trade, all types of wealth including capital of various types lack a well-defined and universally acceptable tax base in addition to the list of taxable items that is still elusive. Debates on the taxable items and

⁵⁷ For details analysis of this issue, see the following references:- S.A. Siddiqui, *Public Finance in Islam*, Sha Muhammad Ashraf Publishers, Lahore, Pakistan, (1962) at p. 50; Kahf Monzer, *The Calculation of Zakah for Muslims in North America*, the Muslims Students' Association of U.S. and Canada, (1980) at pp. 1-2; Shaik Abdul Aziz, *Concept of Zakah: 'A Survey of Qur'anic Texts and Their Explanations in Shariah and Comtemporary Economics*,' in *Some Aspects of the Economics of Zakaat*, M. Raquibuz, Ed., Ass. of Muslim Social Scientists, Plainfield, Indiana, (1980), at p. 22; Zamman S.M. Hasan-Uz, *The Economic Functions of the Early Islamic State*,' International Islamic Publishers, Karachi, Pakistan (1981) at pp. 45-46; Shad Abdur Rahman, *'Zakaat and Ushr*,' Kazi Publications, Lahore, Pakistan (1986) at p. 218; Ahmad Mahmud Shaikh, *'Economics of Islam: A Comparative Study*,' Shah Muhammad Ashraf Publishers, Lahore, Pakistan, (1995) at p. 78; S.M. Yusuf, *'Economic Justice in Islam*,' Shah Muhammad Ashraf Publishers, Lahore, Pakistan, (1996) at p. 68.

treatment of other concepts such as valuation of Nisaab, amount of Nisaab, Zakaat on capital and inventory, handling of depreciation including the deduction of necessary business expenses, as well as effects of inflation etc are still ongoing without a universally acceptable resolution. Siddiqi provides a partial list of topics and authors who were engaged in this debate in his book.⁵⁸

Khums which literally means one-fifth, in its original form was applied at the rate of 20% to spoils of war. Origin of this tax is in the Qur'an and it states as follows: "and know that whatever ye take as spoils of war, lo! A fifth thereof is for Allah, and for the messenger and for true kinsman and orphans and the needy and the wayfarer..."⁵⁹

Later, the tradition extended this tax to treasure-troves, mines, and all materials extracted from sea or earth. The Sunni Jurisprudence maintains that Khums is only applicable to the excavated articles from land, sea, mines, buried treasures, and spoils of war at the rate of 20%.⁶⁰ The Shiite school of thought agrees with this assessment but it also extends Khums to larger categories of un-invested wealth and income.

Meanwhile, Zakaat-ul-Fitr is due once a year at the end of fasting month of Ramadan. All sane and free adult Muslims, who are not poor by the Islamic standard, must pay this tax. Additionally, each person must pay this tax on behalf of those dependents that are not qualified to pay the tax themselves. Even if the dependents do not live with the

⁵⁸ See Muhammed Nejatullah Siddiqi, *Muslim Economics Thinking: A Survey of Contemporary Literature*, The Islamic Foundation, London, UK (1981), at p. 22.

⁵⁹ See Al-Qur'an 8: Verse 41.

⁶⁰ See Abu Ubayd & Qasim bin Sallam, *Kitabul Amwal* (Book of Possession), Edited by Muhammad Khalil Harras, Al-Azhar University, Cairo, (1968) at pp. 467-553; Shaik Abdul Aziz, *Concept of Zakah: 'A Survey of Qur'anic Texts and Their Explanations in Shariah and Contemporary Economics*, in *Some Aspects of the Economics of Zakaat*, M. Raquibuz, Ed., Ass. of Muslim Social Scientists, Plainfield, Indiana, (1980), at p. 26; Ahmad Mahmud Shaikh, *Economics of Islam: A Comparative Study*, Shah Muhammad Ashraf Publishers, Lahore, Pakistan, (1995) at p. 76; Qardawi Yusuf Al, *Economic Security in Islam*, translated by Muhammed Iqbal Siddiqi, Islamic Book Services, New Delhi, India (1997), at p. 68 & p. 87.

taxpayer or they are not Muslims, this tax must still be paid by the person on whom these individuals depend.⁶¹

The amount of this tax is either in kind, about 3 kilograms (6.6 lbs.) of the main local staple such as wheat, rice, beans, barley etc or its monetary value. There is no specific mention of this tax in the Qur'an, though some scholars often indicate the following as a reference to it: "and render to kindred their due rights, as (also) to those in want..."⁶² However, it has been expressly prescribed by Prophet Muhammad (SAW) Kharaaj is a different form of land tax which has some precedent, albeit not clearly defined and established, from the Prophet's time. The term itself originated from the Persian word 'Kharaag.' The structure and operation of this tax is essentially patterned after the Persian land tax. It was formalized and extended along with some other taxes during the reign of Umar, the second Caliph. From the review of the literature on this subject, it appears that non-agricultural lands are exempt from Kharaaj; thus, it is levied on all agricultural lands and orchards conquered via war by Muslims or surrendered to Muslim due to war threat. These lands are known as Kharaaj Land and are owned by the Islamic state. The state may allow the previous owners or new individuals to cultivate these lands in return for payment of Kharaaj. In this sense, the payment is a form of rent which is obligatory on all cultivators regardless of their religion.⁶³

Jizya or 'poll tax' is a tax levied on non Muslims living under Islamic Jurisdiction. The reference to this tax in the Qur'an is said to be: "Fight those who believe not in God and the Last Day and (who) do not forbid what God and His Messenger have forbidden – such men as

⁶¹ *Ibid*, (Khomeini Rouholla) at p. 18; see also Khoie Aboulquasem, 'Towzih-ul-massael,' Elmiyeh Publisher, Qum, Iran (1982), at pp. 300-307; see also Montazeri Housain Ali, 'Resaleh Towzh-ul-massael, Qum, Iran (1986) at pp. 3-11; Sadr Kazim, 'Fiscal Policies in Early Islam,' in *Essays on Iqtisad: The Islamic Approach to Economic Problems*, Al-Hasani, Baqir, Miakhor and Abbas, Editors, Nur Corporation, Silver Spring, MD, USA (1989) at p. 142.

⁶² Al-Qur'an 17: Verse 26.

⁶³ Details of this subject may be found in the following references: Abu Yusuf al Qadi, Yaqub bin Ibrahim, 'Kitab-al-Kharaaj' (Book of Kharaaj), Dar-al-Marifa, Beirut, Lebanon (1979); Ijtihadi Abolqasim, 'The Fiscal and Tax Situation of the Muslims,' Soroush Publication, Tehran Iran (1985).

practice not the religion of truth, being of those who have given the book – until they pay tribute out of hand and have been humble.”⁶⁴ Women, children not yet at puberty, slaves, poor, unemployed, blind, sick, insane, beggars, priests and the monks of monasteries are exempt from Jizya.⁶⁵ Rates or amounts of Jizya are not mentioned in the Qur’an or specified by the Prophet (SAW). Traditionally different amounts have been suggested. For instance, the amount is reported to be one Dinaar (equivalent of 3 oz of gold) per head annually. It is argued that one Dinaar Jizya is equal to the minimum amount payable by a Muslim, since the minimum taxable income for Muslims is 40 Dinaars on which 2.5% or one Dinaar is collected as tax.⁶⁶ Other reports put the amount of Jizya at forty-eight Dirham per year for the rich, twenty-four Dirham for the middle class, and twelve for the lower income taxpayers.⁶⁷ As a writer observes, there is no threshold for determining ‘rich,’ ‘middleclass,’ and ‘low income,’ thus, that determination, along with variation in the rates are bestowed upon the tax authorities.⁶⁸

Kaffaaraat, or expiation money are fines and penalties for some of the wrong doings and transgressions committed by Muslims; on this basis, they are not taxes in the real sense of taxation but then they constitute a noticeable part of the Islamic state’s revenue, hence the sense in acknowledging them. Examples of finable offences include breaking a fast without a proper cause, breaking one’s oath, transgressions

⁶⁴ See Qur’an 9: Verse 29.

⁶⁵ See Abu Ubayd & Qasim bin Sallam, *‘Kitabul Amwal (Book of Possession),* Edited by Muhammad Khalil Harras, Al-Azhar University, Cairo, (1968) at pp. 38-52; see also Zamman S.M. Hasan-Uz, *‘The Economic Functions of the Early Islamic State,’* International Islamic Publishers, Karachi, Pakistan (1981) at p. 169; Qardawi Yusuf Al, *‘Economic Security in Islam,’* translated by Muhammed Iqbal Siddiqi, Islamic Book Services, New Delhi, India (1997), at p. 68 & p. 97.

⁶⁶ *Ibid,* Zamman S.M. Hasan-Uz, p. 169; Sadr Kazim, at p. 145.

⁶⁷ See Nicolas P. Aghnides, *‘Mohammedan Theories of Finance,’* Premier Book House, Lahore, Pakistan, (1961).

⁶⁸ See Ali Reza Jalili, *‘A Descriptive Overview of Islamic Taxation,’* part one of a two-part paper on taxation under Islamic jurisprudence, New England College, Department of Business, Henniker, p. 24. It is an unpublished work but the author can be reached via the following email address: ajalili@nec.edu.

during the month of Hajj etc. It is stated in the Qur'an that: "Allah will not take you to task for that which is unintentional in your oath, but He will take you to task for the oaths which ye sworn in earnest. The expiation thereof is feeding of ten of the needy with the average of that wherewith ye feed your own folk or clothing of them or emancipation of slaves..."⁶⁹ The amount of Kaffaraat varies in each case and it depends on the specific of each situation. These penalties may also be paid in cash or in kind.⁷⁰

ALLOWABLE EXPENDITURES IN ISLAMIC TAXATION

In early Islamic period, collection of tax and its management were rather easy and straightforward, but following the expansion of Islam which brought about the annexation of new provinces, a more complex and regulated system of assessment, collection and accounting became a necessity.

Although, the issue regarding the deductibility of business and personal expenses are not settled, the general agreement seems to be that all pertinent business expenses incurred in generating profit, including depreciation, transportation and commission are deductible as they are in the western system of taxation. Islam therefore has this common feature with secular taxation; but unlike the latter, where generally only the deduction of wholly, exclusively and necessarily business expenses incurred are allowed, in Islamic taxation, additional 'reasonable' personal expenses of the taxpayer and his dependents may be deducted from income for tax purposes. It is worthy of note that to be deductible, the personal expenses must be necessary, customary, not excessive and correspond to one's social standing.⁷¹

⁶⁹ See Qur'an 5: Verse 89.

⁷⁰ *Ibid*, Ali Reza Jalili, at p. 25.

⁷¹ For details on this issue, see Khomeini Rouhollah, '*Resaleh Towzh-ul-massael*, Qum, Iran (1980) at pp. 3-8; see also Khoie Aboulqasem, '*Towzih-ul-massael*,' Elmiyeh Publisher, Qum, Iran (1982), at pp. 300-307; see also Montazeri Housain Ali, '*Resaleh Towzh-ul-massael*, Qum, Iran (1986) at pp. 3-11.

One of the imperatives set by the levy of Zakaat is that in the calculation of assessable income, incurred expenses are to be deducted in line with rules under Zakaat laws;⁷² however, it is not the opinion of every jurist that allows the deduction of business and production expenses. Similarly, there are jurists who do not consider the deduction of any personal expense.⁷³

Other jurists permit only deduction of explicit expenses, accordingly, some deductions such as compensation for own labour, capital expenditures, depreciation on own equipment and non-compensated inputs are not allowed.⁷⁴ For instance, in relation to Ushr, most jurists consider gross produce to be subject to Ushr tax and disallow deduction of any expenses, even the seeds used in cultivation.⁷⁵

In relation to Zakaat of livestock, no allowances for the taxpayers' personal expenditures or deduction of business expenses are permitted.⁷⁶

⁷² See Sayed Afzal Peerzade, 'Towards Self-Enforcing Islamic Tax System: An Alternative to Current Approaches,' J. KAU: Islamic Econ. Vol. 18, No. 1, Karnataka State Women University, Bijapur, India, (2005 A.D/1426 A.H.) at pp. 3-12.

⁷³ See Shad Abdur Rahman, 'Zakaat and Ushr,' Kazi Publications, Lahore, Pakistan (1986) at p. 75; see also Sadr Kazim, 'Fiscal Policies in Early Islam,' in *Essays on Iqtisad: The Islamic Approach to Economic Problems*, Al-Hasani, Baqir, Miakhor and Abbas, Editors, Nur Corporation, Silver Spring, MD, USA (1989) at p. 134.

⁷⁴ See Khomeini Rouhollah, 'Resaleh Towzh-ul-massael, Qum, Iran (1980) at pp. 17-20.

⁷⁵ See Montazeri Housain Ali, 'Resaleh Towzh-ul-massael, Qum, Iran (1986) at p. 26; see also Khoie Aboulquasem, 'Towzih-ul-massael,' Elmiyeh Publisher, Qum, Iran (1982), at p. 320; see also Muhammad Nejatullah Siddiqui, 'Muslim Economic Thinking,' Islamic Foundation, Leicester, England (1981) at p. 25.

⁷⁶ Details of Nisaabs and structure on the Zakaat of livestock can be found, inter alia, in Khomeini Rouhollah, 'Resaleh Towzh-ul-massael, Qum, Iran (1980) at pp. 22-24; Shaik Abdul Aziz, *Concept of Zakah: 'A Survey of Qur'anic Texts and Their Explanations in Shariah and Contemporary Economics*, in 'Some Aspects of the Economics of Zakaat,' M. Raquibuz, Ed., Ass. of Muslim Social Scientists, Plainfield, Indiana, (1980), at pp. 20-23; Khoie Aboulquasem, 'Towzih-ul-massael,' Elmiyeh Publisher, Qum, Iran (1982), at pp. 324-329; Montazeri Housain Ali, 'Resaleh Towzh-ul-massael, Qum, Iran (1986) at pp. 21-26; Rahman

On the other hand, Khums of 'business profit,' like Zakaat of 'other assets' is calculated after deduction of taxpayer's debt. According to most Shiite jurists, however, the qualified debt seems to be only debts occurred for satisfying personal 'essential needs' and excludes 'commercial loans.' This is contrary to what is obtainable in the common law jurisdiction where deduction of personal expenses is strictly prohibited while expenses necessarily incurred in producing the assessable income are deductible. It should be noted that in Islam, loans that a taxpayer takes to "increase and expand his wealth and assets" or to "buy something that he does not need" are not allowable expenditures for deduction.⁷⁷

Similarly, carryover of loss or profit to a different year and offsetting one year's loss against another year's profit as permitted in the common law jurisdiction are not allowable in Islamic system of taxation.⁷⁸ Credit sales are subject to tax on the year of sale if they are due for collection and are collectable on demand; otherwise they would be counted as income of the year in which they are collected. Mandatory savings, retirement accounts, and life insurance payments, as well as other payments that will yield a benefit in the future are subject to Khums in the year they are distributed as income. Voluntary contributions of this type appear to be considered income of the year they are earned.

Fazlur, '*Economics Doctrines of Islam*,' Four Volumes, Islamic Publication Ltd, Lahore, Pakistan, (1986), at pp. 220-222; Sadr Kazim, '*Fiscal Policies in Early Islam*,' in *Essays on Iqtisad: The Islamic Approach to Economic Problems*,' Al-Hasani, Baqir, Miakhor and Abbas, Editors, Nur Corporation, Silver Spring, MD, USA (1989) at pp. 137-142; M.A. Mannan, '*Islamic Economics: Theory and Practice*,' Sha Muhammed Ashraf Publishers, Lahore, Pakistan, (1991) at pp. 286-287; Ahmad Mahmud Shaikh, '*Economics of Islam: A Comparative Study*,' Shah Muhammad Ashraf Publishers, Lahore, Pakistan, (1995) at p. 78.

⁷⁷ See Sayyid Muhammad Rizvi, '*An Introduction to the Islamic Economic System: The Middle Path*,' in '*A Khums (The Islamic Tax)*' Third (revised) edition, published by Sayyid Muhammad Rizvi, 7 El Dorado Street, Richmond Hill, Ontario, Canada (1992) at p. 5.

⁷⁸ See Khomeini Rouhollah, '*Resaleh Towzh-ul-massael*,' Qum, Iran (1980) at p. 7; see also Khoie Aboulquasem, '*Towzih-ul-massael*,' Elmiyeh Publisher, Qum, Iran (1982), at p. 305; see also Montazeri Housain Ali, '*Resaleh Towzh-ul-massael*,' Qum, Iran (1986) at p. 10.

Purchase of durable item for personal use is allowable expenditure while gifts or purchase of items that are not part of one's annual expenses are not deductible for the taxpayers Khums.⁷⁹ No Nisaab is mentioned and no expense deduction is allowed for Kharaaj purpose.

The coverage, rate, or amount for Kharaaj is not uniform or pre-prescribed. It varies from land to land and place to place in accordance with many criterions. For instance, Kharaaj has been collected sometimes as a fixed amount and sometimes as a percentage of the harvest. It has also been collected based on factors such as acreage, the crop or type of agricultural produce, fertility of land, methods of irrigation, the location and proximity of the land to the market and roads, 'tax-bearing ability' of the land, and several other factors. Some authors assert that the maximum rate has been set at fifty percent,⁸⁰ while others claim that Kharaaj has been set at a level that makes the tax equal to the rent on that land.⁸¹ Deduction of expenses however has no room in Kharaaj for tax purposes.

Essentially, when the issue of liabilities which may be deducted arises, liabilities for Zakaat purposes may be divided into two categories: first, liabilities incurred in acquiring assets which are exempt from Zakaat; for example mortgage on immovable property or instalments due under credit sale agreements in respect of plant and machinery, fitting and fixtures. The amounts of such liabilities are, in the light of modern business conditions, not deductible because if such liabilities were to be deducted, then many businessmen may pay little or no Zakaat.

Second, liabilities incurred in acquiring assets which are subject to Zakaat; for example, trade credits (suppliers of business merchandise inventory), should be deducted from the total value of the assets subject to Zakaat in order to arrive at the net amount on which Zakaat is payable as it is done in the common law jurisdictions. In this regard, the manner

⁷⁹ *Ibid*, Khomeini 1980, at pp. 3-8; Khoie 1982, pp. 300-307; Montazeri 1986, pp. 3-11; Rizvi 1992, pp. 3-8.

⁸⁰ See M.A. Mannan, '*Islamic Economics: Theory and Practice*,' Sha Muhammed Ashraf Publishers, Lahore, Pakistan, (1991) at p. 277.

⁸¹ *Ibid*, Ijehadi Aboqasim, at p. 235; see also Sadr Kazim, '*Fiscal Policies in Early Islam*,' in *Essays on Iqtisad: The Islamic Approach to Economic Problems*, Al-Hasani, Baqir, Miakhor and Abbas, Editors, Nur Corporation, Silver Spring, MD, USA (1989) at pp. 129-132.

in which such liabilities are secured, e.g. by registering a bond over immovable property, may be ignored.

CONCLUSION

Under the Islamic tax system, the tax base, treatment, institutions, procedures and several other factors are vague and unspecified. This ambiguity and lack of specificity make the law of taxation in Islam to be flexible and adaptable to some modifications. The law, to some extent, lends itself to fresh reinterpretation in such a way to adapt to concrete conditions of each era and comply with the specific needs of each period. Malaysia, for instance, has done impressive work in improving the understanding of the purpose, use and outcome of Zakaat.

For Malaysian Muslims, Zakaat payment is calculated by reference to their wealth and income; it is payable annually. Section 6A(3), Malaysian Income Tax Act, 1967, allows the payment of Zakaat by a resident Muslim individual (i.e. natural person) as a tax rebate to be set off against the income tax payable by him. The deduction is allowed provided it is accompanied by original receipts as evidence of Zakaat payment issued by an appropriate religious authority.⁸² Where the income tax payable is insufficient for the tax rebate, the excess cannot be carried forward.⁸³ In the case of companies a Labuan offshore company is granted a rebate for any zakaat paid subject to the maximum of tax charged (i.e. 3% of net profits, or RM20,000 upon election). Tax rebate granted to onshore companies (i.e. non- Labuan companies), cooperatives

⁸² See Malaysian Income Tax Act, section 6A(3) where the statutory provision states as follows: "A rebate shall be granted for a year of assessment for any Zakaat, Fitrah or any other Islamic religious dues payment of which is obligatory and which are paid in the basis year for that year of assessment to, and evidenced by receipts issued by, an appropriate religious authority established under any written law."

⁸³ See section 6A(4) of the Income Tax Act which provides: "Where the total amount of rebate under subsections (2) and (3) exceeds the income tax charged (before any such rebate) for any year of assessment, the excess shall not be paid to the individual or available as a credit to set off his tax liability for that year of assessment or any subsequent year."

and trusts for the payment of zakaat is limited to 2.5% of their aggregate income in the relevant year.

Moreover, based on the main guidance in the Qur'an, the Bait-al-Mal Division of the Islamic Council of Malaysia, empowered with Zakaat distribution, has made a modern re-evaluation of the 'eight groups' of Zakaat recipients with a view to suiting the purpose of the present world and current needs of the concerned people; thereby ensuring an efficient Zakaat system of administration. For example, one of the 'eight groups' suggested in the Qur'an is "those in bondage or to free slaves."⁸⁴ In order to meet the modern needs, Malaysia has included three items under this group: to free Muslims from ignorance; to free a Muslim community from a very oppressive condition; and to free those trapped in prostitution.

In the same vein Malaysia uses Zakaat to service hospitals, provide medical and cash aids to the destitute and poor, fund patient treatment, reforms in the administration of Zakaat, Islamic education institutions, especially the '*pondoks*' (i.e. traditional boarding schools) which are established in Malaysia and operated by Zakaat or Waqf funds.⁸⁵

Similarly in Yemen public hot baths, water facilities, wells for irrigation and household water provision arranged through Zakaat funds have been supporting hundreds of citizens for decades.⁸⁶ It is pertinent to note that these very characteristics of flexibility and adaptability to

⁸⁴ See Al-Qur'an 9; Verse 60 where it was specified that there are eight categories of people eligible to receive Zakaat which can be translated as: "Alms are for the poor, the needy, the employees who administer the funds, those whose hearts have been recently reconciled to the truth, those in bondage, those in debt, in the cause of Allah, and the wayfarer, (thus it is) ordained by Allah, and Allah is most knowledgeable, most wise." (Surah At-Tawbah i.e. Chapter 9; Verse 60).

⁸⁵ See M.A. Bakr, '*Islam, Civil Society, and Ethnic Relations in Malaysia*,' in N. Mitsuo, S. Siddique, and O.F. Bajunid, eds., '*Islam and Civil Society in Southeast Asia*,' Institute of Southeast Asian Studies, Singapore, (2001).

⁸⁶ See Sheila Carapico, '*Civil Society in Yemen: The Political Economy of Activism in Modern Arabia*,' Cambridge University Press, Cambridge, UK, (1998).

some modifications which the Islamic law of taxation seems to be enjoying have also given birth to debates, disputes and controversies.

Furthermore, in Islamic taxation, the nature of the property as well as the conditions comes to play. Various categories of wealth and real properties are treated and taxed differently and in some cases even items within the same class of property treated differently. Some of these different treatments may be observed in taxation of real properties and personal properties, tangible and intangible assets, farm and residential lands and so forth.

It must be admitted that a number of Muslim countries, wherein it is possible to create Islamic societies and establish Islamic states, are, at present, characterised by economic backwardness.⁸⁷ Even though a few among them are capital surplus countries, it can be said that they, too, are not developed in the real sense of the term.⁸⁸ It is necessary for the Islamic states to make sincere efforts to accelerate the rate of economic growth. The path to economic growth is not a smooth one because it may involve pains, sacrifices and adjustments of different sorts in which resource mobilization efforts occupy a prime position. Resources are usually mobilized through tax and non-tax means.

Generally, fiscal policy is used by governments around the world to influence the level of aggregate spending in the economy in order to curtail inflation and ensure the economy is not overheated. Governments rely substantially on taxes to fund their activities. Taxation is the most important source of revenue for the modern governments, thus, taxes and tax systems are among the essential potent policy tools at any policy-makers disposal. In many situations, tax policies can foster or hinder community plans on development in their entirety. This underscores the need to focus on Islamic taxation with a view to ascertaining the extent to which it ensures social security for the people in Islamic states.

⁸⁷ See Sayed Afzal Peerzade, '*Towards Self-Enforcing Islamic Tax System: An Alternative to Current Approaches*,' J. KAU: Islamic Econ. Vol. 18, No. 1, Karnataka State Women University, Bijapur, India, (2005 A.D/ 1426 A.H.) at p. 3.

⁸⁸ Reference may be made to various issues of World Development Report of the World Bank and Human Development Report of UNDP so as to obtain a clear idea about the present state of economic affairs in Muslim countries.

One of the stated goals of Islamic societies, with almost unanimous agreement, is justice. In that sense, one may infer that theoretically the function and intention of the Islamic tax system including the issue of allowable expenditures for tax purposes is designed to facilitate the movement of an Islamic state towards achievement of Islamic goals, among which is the establishment of a just Muslim community. A tax system that aims at alleviating poverty, satisfying the people's needs and improving income distribution among the members of the community is one of the factors required to accomplish the Islamic goals. This, in conclusion, is the philosophy circumscribing Zakaat as a form of tax in Islam.