ISLAMIC CO-OPERATIVE MODEL AS ALTERNATIVE TO INTEREST BASED CO-OPERATIVE SCHEMES

Adepoju Razaq Idowu (PhD)
adepojuidowu2014@gmail.com
Department of Religious Studies,
Tai Solarin University of Education,
Ijagun, Ogun State, Nigeria.

1.0 Introduction

The history of the emergence of co-operative societies is difficult to trace. But available records confirmed that co-operative activities were not alien to the Babylonian farmers. It can also be established that man, throughout history, culture and civilization, had devised methods or legal means of co-operating either to seek wealth, secure possessions or minimize impact of loss on properties. The Roman Colleges and the Anglo Saxon guilds were examples of ancient institutions notable for wealth protection co-operations (Vardit, 1985). The Aaro and Esusu concepts in the south Western Nigeria were and are forms of co-operation among the people.

Records also showed that the Industrial Revolution of the late 18th Century led England to a series of co-operative experiments which failed one after the other because of financial mismanagement (Seeberger, 2014). For example, in 1761, the Fenwick Weavers' Society came into existence in Fenwick, East Ayrshire, Scotland to sell discounted oatmeal to local workers and later its services were extended to granting assistance in forms of savings and loans. Also in 1810, Roben Owen, a social reformer, (known as the father of cooperation) and his partners purchased the New Lanark mill from Owen's father –in-law and created from it a standard discounted retail shops which shared profits with its employees. Owen eventually left New Lanark to organize other forms of cooperative societies and from his experiences started putting together cooperative ideas and thinking. By 1828, there had existed a newspaper called 'The Cooperator' established by William King to promote Owen's thinking on cooperative (Uthman, 2009).

There were also efforts at establishing cooperative societies at Glassgow, Indiana and Hampshire which did not succeed on the long run. Indeed by the early 1830s, there were more than 300 co-operative societies in the United Kingdom but they ran into problems through giving credits or lack of business experience. Sometimes, they were not able to recruit new members to move the cooperative into a new generation (Wilson, 2012)

However, the modern co-operative movement had its origin traceable to the Rockdale Society of Manchester, England in the 19th century. Known as the Rockdale Society of Equitable Pioneers and formed in 1844, the society opened the gate for modern cooperative activities. The first food store opened by the society operated two evenings in a week to sell butter, sugar, flour and oatmeal (Seeberger, 2014). To raise money for the shop, each of the 28 original members contributed 2 pence or 3 pence every week and with a loan from the Weavers Association, they were able to gather 28 pounds with which the business started (Wilson, 2012)

The success recorded by the Rockdale society can be explained within the failures of the past co-operative societies in England. The intelligence gatherings on the factors responsible for the failure of the previous societies strengthened Rockdale and brought about the popular Rockdale Principles for Business Practice. These principles were used for the small food store. The principles centred on;

- Open Membership

- Limited interest on share capital
- Cash trading
- Bonus on patronage
- Sales of pure and unpolluted goods
- Democratic control
- Education of members
- Political and Religious neutrality

The principles, aside from the fact that they assisted the society to grow phenomenally, also became the set standard for conventional cooperative ideas. Branch stores and wholesales department were opened for other co-operative societies. They diversified into non-food products such as clothing and hardware, manufacturing their own products like cloth, soap, boots etc. Eventually, the Rockdale Society established its own tea farm in India and consequently, its own ships to bring the tea from India (Wilson, 2012).

It was from this beginning in England that co-operative movement extended to other industrialized capitalist countries (including USA) as well as countries with planned economies like the then Soviet Union and China. By the 20th century, co-operative movement gradually spread around the world.

2.0 Co-operative Society: Definition

A cooperative organization consists of a group of people with common interest who come together to protect the interest and utilize it to better the lot of the group members by engaging in all forms of economically viable and profitable ventures (Uthman, 2009)

The International co-operative Alliance (ICA-an independent, non-governmental association which unites co-operative societies worldwide) at its 1995 world congress, defined co-operative as an autonomous association of persons united voluntarily to meet their common economic, social and cultural needs and aspirations through jointly-owned and democratically-controlled enterprises.

The United States Department of Agriculture (USDA) in 1987 adopted the following definition*:* A co-operative is a user-owned, user-controlled business that distributes benefits on the basis of use

Article 5 of the ICA Constitution stipulates that any association of persons, or of societies, shall be recognized as a co-operative society provided that it has for its object the economic and social betterment of its members by means of an enterprise based on mutual aid, and that it conforms to the ICA statement on the co-operative identity as approved by its General Assembly.

Co-operative societies are organized on the values of self-help, mutual responsibility, solidarity, democracy, equality and accountability. Every member of such societies is considered equal and joint owner of the society. Members are therefore expected to tailor their behaviours towards ethical values of honesty, openness and care for others. It is the prevalence of these values that determines the survival of co-operative efforts.

The goal of co-operative activities is **human development and empowerment achieved through brotherhood and large number** which may be difficult for individuals to achieve.

3.0 Conventional co-operative societies

The coming up of Rochdale on 21st December, 1844 at 8pm, which ensured that workers could have access to reasonably priced quality food at true weights and measures, gave birth to conventional cooperative activities. From the modest start of Rochdale, the ideas spread rapidly as other groups saw the benefit of cooperation. By the beginning of the 20th century, there were 1650 cooperative associations in United Kingdom including over 100 productive societies manufacturing items from clothing to hardware.

Visitors came from all parts of the world to Rochdale and then adopted the Rochdale cooperative model to meet their different needs in their country (Wilson, 2012) The principles on which western co-operatives operate are itemized as follows:

- Open and voluntary membership without religious or political discrimination
- Democratic control
- Limited **interest** on capital if any
- Equitable distribution of surplus
- Education for all members, officers, employers and the public.
- Co-operation among co-operators

At the 1995 congress held in Manchester, other principles were added to the above. They are:

- Members economic participation
- Autonomy and independence
- Concern of community

Conventional cooperative societies are conceived on certain colourations which are uniform and define cooperative activities. The colourations are:

- Cooperative societies operate under certain provisions that are authorized by the law of a country or state, as the case may be.
- The capital base for the society is raised through sale of shares and membership levies as may be deemed necessary from time to time.

- The society is managed by members who are elected by other members at general meetings.
- Each member of the society has voting right irrespective of number of shares own.
- Members share in the surplus earnings of the society on the basis of the shares appropriated.
- Membership is open and new members are admitted through share purchase.
- Death or withdrawal of a member does not inhibit the operation of a cooperative organization.
- Shares are not automatically transferable in cooperative arrangements.

4.0 Islamic Co-operative Arrangement

The relevance of Islam to every situation of man is based on the fact that Allah the Creator of the universe and what is therein knows what is best for man and therefore revealed the Qur'an for the purpose of guidance to him. The religion gives a unique view of man's existence in every sphere of life and placed responsibilities on him so that when such responsibilities are carried out, no matter in what sphere it is, he is considered to be worshipping Allah. This makes Islam to assert itself as relevant to all forms of space and time, process of history, all dimensions of life and to all aspects of human existence (Gatawa, 2013).

It must be emphasised that Islam recognized the imperative of man's material well-being to the fulfillment of his responsibilities. Hence, the Qur'an says "O you who believe, do not forbid yourself of the good things which Allah had made lawful for you and do not exceed the limits"

The Qur'an and the Prophet of Allah (SAW) also took a positive attitude to economic matters. The Qura'an says: "It is He who has produced you from the earth and settled you therein to develop it" (Q6:10). The Prophet (SAW) was reported to have said "There is a reward for anyone who cultivates land, who produces and feeds a living being" (Gatawa, 2013).

It should however be made clear that the economic behaviour of a Muslim is deeply controlled by his firm belief in Allah, the Day of Judgement and life after death. According to Navaid (2000), the ethical philosophy of Islam can be summarized by four axioms; Unity, Equillibrium, Free Will and Responsibility. Therefore, economic activities in Islam are guided by the basic values enunciated in the Qur'an and Sunnah and as explained in the books of fiqh (jurisprudence)

The legality of co-operative activities in Islam can be traced to the theories of brotherhood ('ukhwwat), Unity (ittihād) and Cooperation (ta'wwun) as stated in the Noble Qur'an and expatiated by the Sunnah of the Prophet (SAW)

The Qur'an says on brotherhood and unity

> And hold fast together to the rope which God (stretches out for you) and be not divided among yourselves. And remember the favour of Allah on you when you were enemies, then He united your hearts so by His favour you became brethren, and you were on the brink of a pit of fire, then He saved you from it, thus does Allah make clear to you His communications that you may follow the right way. (Q3: 103)

The Prophet (SAW) expatiated on this verse when he said

> …A Muslim is the brother of a Muslim: he neither oppresses him nor disgraces him, he neither lies to him nor does he hold him in contempt… It is evil enough for a man to hold his brother Muslim in contempt. The whole of a Muslim for another Muslim is inviolable: his blood, his property and his honour (Hadith 35 of Nawawi)

The Qur'an established the principle of cooperation and mutual assistance in the following verses:

> Cooperate with one another in furthering virtue and Gods consciousness and do not cooperate with one another in furthering evil and enmity (Q 5:2)

The Qur'an further says:

> Verily, this community of yours is one community and Iam your Lord and Sustainer, remain then, conscious of Me (Q 23: 53)

The Prophet (SAW) explained:

> A believer to another believer is like a building whose different parts reinforce each other. The Prophet (SAW) then clasped his hands with the fingers interlaced (Bukhāri, vol.8)

To drive home these principles, the Prophet (SAW) says;

> None of you is (truly) a believer until he wishes for his brother what he wishes for himself (Bukhāri, vol.1)

It must be emphasized that all the values considered as the ideals of co-operative activities are enjoined by Islam. The practical demonstration of self-help and co-operation was seen among the *Muhājirūn* (emigrants from Makkah) and the *Anṣār* (helpers in madinah).

5.0 Features and Principles of Islamic Co-operative societies

The features and principles guiding Islamic cooperative society are fundamentally the same as with Islamic banks and other Islamic financial

Institutions (IFIs). This is because Islam has uniform rules for economic dealings and financial transactions (Navaidi, 2010) The features and principles are:

- Interest-free operations
- Profit & Loss Sharing (PLS)
- Asset-backed financing
- Ethical Investment (Halal businesses and products)
- Shariah Advisory Board (SAB)
- Benevolent Loan (Qardah Hassanah)

Their principles should therefore be:

- Prohibition of Interest in all forms of transactions
- Undertaking investment and trade activities on the basis of fair and legitimate profits (economic Justice)
- Prohibition of Monopoly
- Cooperation for the social benefit of the society
- Development of all trades and enterprises that are *Shari'ah* compliant.

6.0 Differences between the two co-operative arrangements

The major differences in the two systems are in the areas of operation and investment. **While Islam forbids interest in its entirety, the western co-operative system allows minimal interest charges on loan repayment.**

The prime concern of Islam is to do away with all forms of injustice (Zulm) and the establishment of justice ('Adl) in all spheres of human endeavour and most especially in the economic sphere. The prohibition of interest (Riba) is the backbone of Islamic monetary policy. This policy tool, together with the fiscal policy, stands as a catalyst to actualize the socio-economic goals and objectives of the Islamic economic system (Daud, 2013).

It is in line with this that Faridi (1983) observed that the goals of Islamic economic system should be:

- The achievement of justice and equity;
- Provision of the socio-economic needs of the community or socio-economic welfare;
- Enhancement of the community's economic resources or economic growth; and
- Improvement in the cultural milieu of the community.

So Islam condemned interest (riba) in all its ramifications and puts in its position lawful profit generated from lawful business enterprise. The Qur'an says:

> Those who devour usury (ribā) will not stand except as stands one whom the Evil one by his touch hath driven to madness. This is because they say: 'Trade is like usury'. But God has

> permitted trade and forbidden usury. Those who after receiving direction from their Lord, desist shall be pardoned for the past: their case is for God (to judge). But those who repeat (the offence) are companions of Fire; they will abide therein (forever) (Q2:275).
>
> God will deprive usury of all blessing, but will give Increase for deeds of charity: For He loves not creatures Ungrateful and wicked. (Q2:276)
>
> And if you do not refrain then take a notice of war from Allah and His messenger but if you repent, you shall have your capital sums. Deal not unjustly (by asking more than your capital), and you shall not be dealt with unjustly (by receiving more than your capital sums) (Q2:279)
>
> That which you lay out (in ribā) for increase through the property of (other) people, will have no increase with God: But which you Lay out for charity, seeking the Countenance of God, (will increase): It is these who will get a recompense multiplied (Q30:39)

This means that loan granted under Islamic cooperative arrangements is granted without interest. The borrower pays back exactly what he has borrowed and probably whatever cost must have accrued in processing the loan.

Added to that is the fact that Islamic finance **lay much emphasis on and only approves of ethical investment and asset-backed financing and there are no considerations for that in the western system.**

Islamic cooperative societies, just like other Islamic Financial Institutions (IFIs), can only invest funds generated from their members by offering a number of products (which will be discussed later) which are broadly divided into primary modes (or equity financing) and secondary modes (or debt financing). The primary modes or equity financing refer to *Mudarabah* (profit sharing), *Mushārakah* (joint venture) and the shares of Joint Stock Companies (a combination of *Mushārakah* and *Mudarabah*). The secondary modes or debt financing are *Murābaḥah* (cost plus), *Ijarah* (leasing), *Ijarah thumma al-bay* (hire purchase), Salam (forward delivery contract and *Istisna'* (contractual production) (IIIBF, 2015). All these modes of financing are asset-based financing different from fund advancement.

Also it is the position of Islam that man's economic activities should be limited to things that are approved by *Shari'ah* (Islamic law) as lawful. For example investments in intoxicants, games of chance or gambling, piggery, organizations thriving on usury or interest etc are forbidden. These and other prohibitions are considered as not only unbeneficial to human but also capable of creating social disorder.

The Islamic concept of financial ethics therefore encompasses; justice and fair dealing, honesty and gentleness in transaction, prohibition of *najash* (bidding up the price of commodity without the intention of taking delivery), prohibition of *khalabah* (over-projecting the quality of a product) full disclosure in business, free market and fair pricing and fulfilling the covenants of contracts and paying liabilities.

It is therefore within this ethical concept that Islamic finance does not approve;

- Production and sale of impure goods
- Production and sale of goods that are not useful to mankind
- *Riba* or interest
- *Gharar* or uncertainty
- *Maysir* or gambling (IIIBF, 2015)

It can therefore be summarily said if the question is posed, why Islamic co-operative? that the western system operates on certain principles that are prohibited by Islam. This same reason accounts for banking, Insurance, Mortgage etc.

7.0 Islamic Financial (Investment) Instruments

As alternatives to interest bearing transactions, Islamic economics offer various forms of investment products. Some of them are:

Mushārakah (Joint Venture)

Literally, it means sharing. In the business context, it is a joint enterprise in which all the partners share the profit or loss of the joint venture in accordance to the amount invested in the business. It means that the return on *Mushārakah* is based on the actual profit earned by the joint venture.

For Mushārakah to be valid, the parties

- Must be capable of entering into a contract
- Must take place with free consent of the parties, free of any duress, fraud or misrepresentations.

Every partner in *Mushārakah* has a right to take part in its management. However the partners may agree upon a condition that the management shall be carried out by one of them.

Mushārakah can be terminated;

- If any partner gives notice to this effect
- If any of the partners dies during the currency of the contract. The heirs in this case have the option of either drawing the share of the deceased from the business or to continue with the contract.
- If any of the partners becomes insane or incapable of effecting commercial transactions (Usmani, 2002)

Diminishing Mushārakah

A form of equity partnership where one of the partners promises to gradually buy the equity share of the other partner(s) until title to the equity is completely transferred to the buying partner.

Muḍārabah (Profit Sharing)

This is a special kind of partnership arrangement where a partner provides money for commercial enterprise while the other partner manages the enterprise. The financier is called "*Rabb-ul-māl*" and the managing partner is called "*Muḍārib"*

Where the financier specifies a particular business for the *Muḍārib*, *Muḍārabah* becomes restricted (al-Muḍārabah al-muqayyadah). But if he has left it open for the *Muḍārib* to undertake whatever business he wishes (al-Muḍārabah al-mutlaqah) then *Muḍārabah* is unrestricted.

Profit sharing in *Muḍārabah* must be mutually agreed upon by the partners from the beginning on a definite proportion. Mostly, the *rabb-ul-māl* takes a greater proportion as a compensation for the risk he stands in case of loss or liquidation.

In case of loss, the *rabb-ul-māl* bears the financial loss except where negligence is established against the *Muḍārib*.

Note that the *Muḍārib* cannot claim any periodical salary or fee or remuneration for the work done in *Muḍārabah*. All the schools of Islamic *fiqh* agree on this (Usmani, 2002)

Muḍārabah contract can be terminated at any time by either of the two parties by a notice to the other party.

Murābaḥah (Mark Up Sale or Cost Plus)

This is a product widely used by Islamic banks and other Islamic financial institutions all over. It entails an agreement between two parties where one purchases a commodity for the other with the condition of adding a profit margin to the real cost of the commodity. The profit may be in lump sum or percentages.

- The basic ingredient of *Murābaḥah* is that the seller must disclose the actual cost he incurred in acquiring the commodity and the profit he intends to add. This makes the difference between *Murābaḥah* and *Musāwamah* sales. Payment in the case of *Murābaḥah* may not necessarily be deferred (going by its original fiqh connotation) but with the banking transactions it is deferred and most often on installment basis (Usmani, 2002).

Some other basic rules for *Murābaḥah* as enunciated by Marifa's Academy (2014)include:

- The subject of sale must exist at the time of sale.
- The subject of sale must be in the ownership of the seller at the time of sale.
- The object must be in the physical or constructive possession of the seller at the point of sale.
- The sale must be instant and absolute.
- The object of sale must not be *ḥarām* product (forbidden by Islam)
- There must be certainty of price.
- The sale must be unconditional
- There should not be any condition of roll-over

Ijārah (Leasing)

It is similar to installment leasing agreement and it is used by financial institutions to provide funding for plant and machinery purchases. A specified asset is purchased and rent out to client in return for rent payments.

Literally *Ijārah* means to give something on rent. As an Islamic finance terminology, it can be used for two different situations. It could mean to employ the services of a person on wages. In this situation, the employer is called *musta'jir*, the employee, ajir and the wage, *ujrah.*

The second type is to transfer the usufruct (right of usage) of a particular property to another person in exchange for a rent claimed from him over a period of time. Here *Ijārah* is synonymous to leasing. The lessor is called *Mu'jir*, the lessee is called *musta'jir* and the rent payable is called *'ujrah*.

Basically, the rules of *ijārah* as a connotation for leasing are similar to the rules of sale because in both cases something is transferred to another person for a valuable consideration. The only difference between the two is that in the case of sale the corpus (right of ownership) is transferred to the purchaser as soon as the contract of sale is sealed and delivered. Whereas in ijarah, the corpus of the property remains with the lessor, only the usufruct is transferred to the lessee (Usmani, 2002)

Some basic rules of leasing:

- The subject of leasing must have a valuable use i.e. things that cannot be used cannot be leased.
- For the contract of lease to be valid, the corpus must remain with the owner. Therefore anything consumable while being used cannot be leased e.g. money, eatables, some ammunitions, fuel etc.
- While the corpus of property remains with the owner, all liabilities emerging from the ownership shall be borne by the lessor e.g. taxes but the liabilities referable to the usage shall be borne by the lessee.
- The period of lease must be stipulated in clear terms.

- The lessee cannot use the property for any purpose other than the purpose stipulated in the agreement.
- The lessee is liable to compensate the lessor for every harm or damage caused by any misuse to the leased asset.
- The leased asset must be clearly identified by the parties e.g. it cannot be 'one of my two shops'
- The rent must be determined at the time of contract for the whole period of lease.

Leasing can be terminated by the expiration of period of leasing, by mutual consent of the parties or unilaterally by the lessor if the lessee contravenes any term of the agreement (Marifa's Academy, 2014)

Ijārah Thumma al-ba'i (Hire Purchase)

It is a form of contract where parties enter into two types of contracts which take effects serially to form complete lease/purchase transactions. The first contract is an *ijārah* that outlines the terms for leasing or renting over a fixed period. The second contract of *ba'i* comes into effect as soon as the terms of the ijarah are fulfilled (Marifa's Academy, 2014)

Istisna' (Commissioned Manufacturing)

This is purposely used for assets which are constructed or manufactured. The financial institution pays the developer/contractor, generally in predetermined installments, who then manufactures the plant or equipment, or purchases the commodity. The Marifa's Ademy (2014) defines it as a contract of sale of specified items to be manufactured or constructed with an obligation on the part of the seller to deliver them to the purchaser upon completion.

Salam

It is a contract agreement to purchase a specified type of commodity at a predetermined price to be delivered at a specified future date and in a specified quantity and quality.

There are some other ones like *ba'i mu'ajjal* (Deferred payment), *Salaf* (Cash advancement) and the ones presently used in the Islamic Republic of Iran like *Jo'alah* (Transaction based on commission), *Muzāra'ah* (Farm land contract), *Musaqat* (Orchards or Gardens contract) etc. All these modes of finance involve the transfer of assets and are not based on making money from money alone as is the case with interested-based transactions (Marifa's Academy, 2014)

8.0 Impacts of Islamic cooperative societies on the economy

An Islamic cooperative society, just like other Islamic Financial Institutions (IFIs), is capable of creating positive impacts on its members in terms of economic empowerment. It liberates members from the burden of interest and opens the door for healthy economic participation. Micro finance lending becomes easier as the potential of man as a social and interactive being is enhanced. Apart from the above mentioned, an Islamic cooperative society;

- Serves as an alternative system for those who hitherto have detested conventional cooperative societies
- Assists in massive mobilization of funds outside conventional financial institutions for productive use
- Enhances economic involvement and inclusion of the unbanked population
- Aids investment on neglected sectors like Agriculture with products like *Mozaraah* and *Musaqat*
- Is a poverty alleviation tool through products like *Mudarabah*, *Murābaḥah, ba'i Salam* and *Qarda hasanah*
- Is capable of creating more jobs through its asset financing
- Would assist in the empowerment/capacity building of the very poor.

Conclusion

The three concepts of *ittihad* (unity), *ukhwwat* (brotherhood) and *ta'wwun* (cooperation) as taught by the Qur'an and expatiated by the *Sunnah* of the Prophet (SAW) provided the basis for cooperative arrangement in Islam. But while Islam subscribes to economic cooperation among human beings, it imposes its economic ideals on whatever the cooperative arrangement would be. For example, interest, in its entire ramification, is prohibited in all economic dealings and so Islamic cooperative societies cannot operate on interest basis. Such cooperative arrangements cannot also deal in things prohibited by Islam. It is on the basis of these prohibitions that Islamic cooperative societies can only grant benevolent loans, finance assets and engage only in ethical investments. There are a number of financial products which the Islamic model of cooperative can make use of in this regard.

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