

SALAM & ISTISNA

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Meaning of Bai-Salam

- *Bai-Salam* is a term used to define a sale in which the buyer makes advance payment, but the delivery is delayed until some time in the future. Usually the seller is an individual or business and the buyer is the bank.
- The *Bai-Salam* sales serve the interests of *both* parties.
- The seller receives advance payment in exchange for the obligation to deliver the commodity at some later date. He benefits from the Salam sale by locking in a price for his commodity, thereby allowing him to cover his financial needs whether they are personal expenses, family expenses or business expenses.
- The purchaser benefits because he receives delivery of the commodity when it is needed to fulfill some other agreement, without incurring storage costs. Second, a Bai-Salam sale is usually less expensive than a cash sale. Finally a Bai-Salam agreement allows the purchase to lock in a price, thus protecting him from price fluctuation

Steps of Bai-Salam

- Cash sale or Sale on Credit - The bank pays the agreed upon price at the time of the contracts inception. The seller agrees to the delivery of the commodity some specified date in the future.
- Delivery and Receipt of the Commodity on the Specific due Date: There are several options for delivery available to the bank
- a) The bank may receive the commodity and resell it to another party for cash or credit.
- b) The bank may authorize the seller to find another buyer for the commodity.
- c) The bank may direct the seller to deliver the commodity directly to a third party with whom the bank has entered into another agreement.
- The Sale Contract: The bank agrees to sell the commodity for cash or a deferred price, which is higher than the Salam purchase price. The buyer agrees to purchase and to pay the price according to the agreement

Rules of Bai-Salam

- It is a condition that the commodity known by both parties to the agreement. Misunderstandings about the commodity may lead to disputes, which could void the contract.
- It is a condition that the quality of the commodity be monitored closely, as very little variation from specifications in the contract are allowable. If the commodity cannot be monitored for quality standards, a Salam transaction is impermissible.
- It is a condition that the commodity be deliverable on the due date. If there is uncertainty about the ability to deliver the commodity at the due date, a Salam transaction is impermissible.
- It is permissible to draw a Salam sale contract for a total to be delivered increments on different specified future dates.
- It is a condition that the commodity is a liability debt. The seller is obliged to deliver the commodity when it is due, according to the specifications stipulated in the contract, whether or not his firm produces the commodity or obtained from other firms.
- Salam sales are impermissible on existing commodities

Rules of Bai-Salam

- Salam is impermissible on Land lots and real estates.
- It is a condition that the purchase price in Salam is specified and advanced to the seller at the time of signing of contract.
- It is a condition in a Salam sale that the due date is known to avoid confusion, which may lead to a dispute.
- It is a condition that the place of delivery be stated in the contract if the commodity requires special handling and delivery arrangements.
- It is permissible to take a mortgage on Salam debt to guarantee that the seller satisfies his obligation by delivering the commodity on the due date.
- It is impermissible for the buyer of a Salam commodity to sell the commodity before receiving it. It is known that the Salam commodity is a liability debt to the seller and not a commodity that exists. However, it is permissible for the buyer to draw a parallel Salam contract without connecting it to the first Salam contract.

Application of Bai-Salam

- Salam sales are frequently used to finance the agricultural industry. Banks advance cash to farmers today for delivery of the crop during the harvest season. Thus banks provide farmers with the capital necessary to finance the cost of producing a crop.
- Salam sale are also used to finance commercial and industrial activities. Once again the bank advances cash to businesses necessary to finance the cost of production, operations and expenses in exchange for future delivery of the end product. In the meantime, the bank is able to market the product to other customers at lucrative prices.
- In addition, the Salam sale is used by banks to finance craftsmen and small producers, by supplying them with the capital necessary to finance the inputs to production in exchange for the future delivery of products at some future date.

ISTISNA SALE

- Equivalent to a manufacturing or construction contract that allows phase or progress payments, lump-sum payments, advances, etc.
- One of only 2 unique Islamic transactions that is actually a sale of an item before it comes into existence
- Gharar is avoided via detailed specification
- Flexibility in payment and delivery terms

Steps of Istisna Sale

- **Istisna Sale Contract:** The Buyer expresses his desire to buy a commodity and brings a request to purchase the commodity to the bank. The method of payment is set forth in the agreement. The bank agrees to deliver the commodity to the buyer at some agreed upon time in the future.
- **The Parallel Istisna Contract:** In order that the bank is able to deliver said commodity in the Istisna's agreement, the bank enters into a parallel Istisna agreement with a third party to either manufacture or otherwise deliver-said commodity. Obviously, the bank stipulates a price that is lower than that agreed to in the original agreement and requires delivery on or before the date stipulated in the original contract.
- **The seller, in the parallel agreement, agrees to manufacture the specific commodity and to deliver it on the due date agreed upon.**
- **Delivery and Receipt of the Commodity:** The seller in the parallel Istisna agreement, delivers the commodity to the bank on the agreed upon date. The bank, in turn, delivers the product to the buyer of the original Istisna contract, in accordance with the original agreement. In this way, all parties fulfill their obligations to the contract.

Rules of Istisna'a Sale

- It is a condition in the Istisna contract to clearly define dimensions and specifications of the product being purchased. This is important to ensure that there is no room for dispute over what is required.
- The Istisna contract is only used for objects that can be manufactured. It can not be used to purchase corn, wheat, barley, fruit or any natural product.
- The object sold in a Istisna contract is a fixed liability debt and it is permissible for the object to be a custom manufactured product, made in accordance with certain specifications.
- The maker should supply the materials. If they are supplied by the buyer, the contract is Ijara and not Istisna.
- Once the contract is drawn the ownership of the asset is confirmed to the buyer and the purchase price is confirmed to the manufacturer.

Rules of Istisna'a Sale

- It is not a condition in the Istisna'a contract to advance the price. Usually part of the price is paid in advance and progress payment is made until delivery
- It is a condition that the time of delivery be specified in the agreement to avoid confusion that may lead to a dispute over the transaction.
- It is a condition that the place of delivery be stated in the contract if the commodity requires special handling and delivering arrangements.
- The buyer may stipulate in the Istisna contract that the commodity shall be manufactured or produced by a specific manufacturer, or manufactured with specific materials. This is not permitted in a case of Salam Sale.

Salam & Istisna

- There are some comparative differences between Istisna and Salam.
- **1:In the subject matter of Istisna is the thing or goods which is to be manufactured.**
- But in Salam the commodities are normally agricultural products, metals etc.
- **2:The price in Salam sales is paid in advance.**
- It is not necessary in Istisna where the payment may be made at the time of the contract or progressively according to the stage of completion of the manufacturing process.
- **3:The parties in the contract of Salam, cannot unilaterally terminate the contract without the agreement of the other.**
- The parties in an Istisna contract are allowed to cancel the contract before the manufacturer starts the work.