



Legal and Shariah Analysis of Commercial Paper Discounting and Islamic Banking Financing Alternatives

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Abstract: This study examines the legal and Shariah dimensions of commercial paper discounting and evaluates whether Islamic banking instruments can serve the same financing function. It seeks to clarify the legal characterization of discounting under positive commercial law, assess its compatibility with Islamic jurisprudence, and identify Shariah-compliant instruments capable of providing equivalent liquidity solutions within Islamic banking. The study employs a qualitative normative–doctrinal approach, integrating comparative legal analysis with analytical fiqh methodology. It analyzes statutory provisions governing commercial paper discounting—particularly within Iraqi commercial law—and reviews classical and contemporary juristic debates that classify the transaction as a loan (*qard*), a sale of debt (*bay' al-dayn*), or a transfer of rights (*hawalah*). The data, derived from statutory texts and authoritative juristic sources, are examined through content and comparative analysis, with source triangulation applied to ensure validity and doctrinal coherence. The findings indicate that, in its conventional form, discounting constitutes a credit-based transaction in which the bank advances funds below the nominal value of a commercial instrument and subsequently claims its full value at maturity. Although legally valid under commercial law, this arrangement generally entails elements of *Ribā al-faḍl* or *Ribā al-nasi'ah* from a Shariah perspective, as it involves a predetermined increase linked to deferred payment. Juristic reinterpretations that frame discounting as a sale or transfer mechanism do not fully eliminate the embedded interest component. The study concludes that Islamic banking instruments—such as murābahah financing, organized tawarruq, and salam contracts—can achieve similar economic objectives without violating Shariah principles, particularly those concerning asset backing, risk sharing, and the prohibition of *Ribā*. By combining contemporary legal analysis with classical jurisprudential reasoning, this research contributes to the theoretical refinement of Islamic finance and provides a structured foundation for the development of ethically grounded and sustainable banking practices.

Keywords: Discounting; Islamic Banking; *Murabaha*; *Ribā*; Shariah Compliance.



Introduction

Discounting of commercial papers is a very important operation in the contemporary commercial system because commercial papers like promissory notes, bills of exchange, and checks are short-term financial instruments to provide liquidity and expedite the fulfillment of business commitments. The modern literature has highlighted the significance of these instruments in easing the operations in the market and accomplishing the goals of traders as well as banks, since they are sales or credit instruments that enable quick turnover of capital and instigate trade by offering short-term credit. Research shows that the motive of legislators in the regulation of these instruments in the systems of commercial law is the need to secure haste, credit, and recording of rights into the books of law, which are in line with the Sharia goals of maintaining wealth and commercial operations. This puts these tools at the centre of contemporary economic transactions.¹

Discounting under the Iraqi commercial law has been described in Article 283 of the Commercial Code No. (30) of 1984 (as amended) as an obligation between the bank and the beneficiary where the bank is obliged to pay the value of a commercial paper or any other negotiable instrument to the beneficiary in advance in lieu of transferring the actual ownership, and the beneficiary must also pay the bank in that case the original debtor fails to do so. This definition contains major components of the transaction, such as transfer of ownership and the obligation of the beneficiary and represents the types of banking credit contracts. It is said to be a composite operation, which involves the first part, the consensual contract, and the second part is the endorsement procedure, which involves the transfer of ownership. This brings to attention the interrelation between the general commercial contract rules and the endorsement of commercial papers as it relates to Iraqi legislation.²

Although this is the legislative description, inherent questions still arise as to whether commercial paper discounting is a neutral credit contract, such as a sale or a transfer, or whether it is an interest-bearing loan. This discussion of characterization is not confined to legal studies but to the Sharia of Islamic jurisprudence, which does deal with transacting business with issues of complex Sharia, mostly the ban on *Ribā* (usury/interest). The majority of the scholars believe that a discount transaction would need an additional amount in terms of time or banking service, which is unacceptable according to Sharia. Under classical discounting, the bank offers a sum of money that is lower than the stipulated nominal value and collects the entire sum at maturity, similar to *Ribā al-Nasya* or *Ribā al-Fadl* of Islamic jurisprudence. This description shows the

¹ Obeid Hasan Saleh Abdulmajid, Habibullah Zakaria, and Awal Adam Saad, "Commercial Paper (Short-Term) Importance and the Statement of Its Root and Legitimate Makassed," *Journal of Islam in Asia* 17, no. 2 (2020), <https://doi.org/10.31436/jia.v17i2.969>.

² Badawi, Saadia El-Badawi El-Sayed Ahmed. "Legal Effects Arising out of the Commercial Securities Discount Contract: A Comparative Study." *Journal of Legal and Economic Studies* 8, no. 4 (December 2022): 870–920. <https://doi.org/10.21608/jdl.2022.272448>

disparity between the current commercial system of law and the needs of Islamic law in the regulation of financial transactions.³

Conversely, there are scholars who have taken different sides of the argument and have taken the discounting process as an actual sale of the discounted paper. They claim that the bank obtains complete rights under endorsement and collection and that the legal relationship is between a sale and a given consideration. Nevertheless, this theory has not escaped Sharia issues, as it has been criticized that it may be subject to *Ribā al-Fadl* or *Ribā al-Nasaya*, especially where a person pays more than is required, thus violating the Sharia principles regarding the sale of cash or negotiable instruments.⁴

Another group of scholars has attempted to conceptualize commercial paper discounting as a transfer of rights (*hawalah*) from the client to the bank. However, this jurisprudential characterization is criticized for failing to establish the required equivalence in amount and type between the debts, a condition essential to the validity of *hawalah* under Islamic law. Consequently, the Fiqh literature indicates that most characterizations of the traditional discounting process yield results inconsistent with Sharia requirements, confirming that conventional discounting remains an interest-bearing transaction prohibited under Islamic law unless stripped of the interest element or restructured as a Sharia-compliant contract.⁵

The research gap lies in the fact that many previous studies, whether in positive law or Islamic jurisprudence, have addressed commercial paper discounting from either a jurisprudential perspective or a general legal discussion. However, they have not fully integrated the legal characterization under commercial law with a comparative Fiqh analysis that highlights points of convergence and divergence between the civil law framework and Sharia-compliant Fiqh characterization. Moreover, only a limited number of studies have proposed practical Sharia-compliant alternatives that replicate the functions of traditional discounting and provide the required liquidity without falling under the prohibition on interest.⁶

From this standpoint, the scientific significance of this study becomes evident, as it seeks to fill this gap by providing an independent analysis that combines civil commercial law and its modern legal characterizations on one hand, and Islamic jurisprudence with the Sharia assessment of this process on the other, while referencing analytical and critical studies available in open-access sources. This approach enriches the scholarly

³ Abd al-Jabbar Awdah, Asma'. "Discounting Commercial Papers in the Balance of Islamic Banks." *Journal of College of Islamic Sciences* 69 (March 30, 2022). <https://doi.org/10.51930/jcois.21.69.0609>.

⁴ Sadia El-Badawi El-Sayed Ahmed Badawi, "The Legal Effects Arising from the Commercial Paper Discount Contract: A Comparative Study," *Journal of Legal and Economic Studies* 8, no. 4 (December 2022): 870–920, <https://doi.org/10.21608/jdl.2022.272448>.

⁵ Abd al-Jabbar Awdah, Asma'. "Discounting Commercial Papers in the Balance of Islamic Banks." *Journal of College of Islamic Sciences* 69 (March 30, 2022). <https://doi.org/10.51930/jcois.21.69.0609>.

⁶ Khallaf, Mohammed Omar. "Discounting Commercial Papers and Its Applicability in Islamic Banks." *Algerian Journal of Financial and Banking Studies* 7, no. 1 (December 20, 2017): 105–140. <https://asjp.cerist.dz/en/article/75022>.

dialogue between comparative law and comparative Fiqh on one of the most complex banking operations in the modern era.⁷

In brief, this study serves as a good scholarly basis to prove that commercial paper discounting is not an ordinary banking process but a complicated legal practice that poses some basic questions regarding the legal nature, characterization of contracts, and Sharia-compliant compatibility of the Fiqh. This renders it an excellent source of scholarly interest, which contributes both theoretical and practical significance to contemporary commercial law and Islamic finance.⁸

Method

This study adopts a qualitative doctrinal approach with a descriptive–analytical design to examine commercial paper discounting from both positive law and Islamic jurisprudence (Fiqh) perspectives. It combines a comparative legal method with analytical fiqh inquiry to assess the legal structure and Sharia implications of the transaction. The data are drawn from primary legal materials, including Iraqi Commercial Law and relevant comparative legislation, as well as classical and contemporary fiqh works, juristic opinions, and authoritative fatwas. These are complemented by scholarly journal articles and prior critical studies on commercial discounting practices. Through this framework, the research systematically identifies the contractual elements, legal relationships, and the nature of rights and obligations arising from discount agreements in contemporary commercial law.

The analysis proceeds through qualitative content analysis and comparative evaluation. It examines how commercial paper discounting is classified in civil law and how it is interpreted in Fiqh—whether as an interest-bearing loan (*qard ribawi*), a sale (*bayʿ*), or a transfer of debt (*hawalah*). Each characterization is critically assessed in light of core Sharia principles, particularly the prohibition of *Ribā*, time-based increments, and the requirement of equivalence in debt exchanges. An inductive approach is then employed to synthesize the legal and Fiqh findings, identify areas of tension between conventional practice and Sharia standards, and formulate practical alternatives. To strengthen the credibility of the study, the research relies on source triangulation by cross-examining statutory provisions, juristic opinions, and contemporary academic analyses. This method ensures doctrinal consistency and supports the development of Sharia-compliant solutions—such as *Murabaha*, *tawarruq*, and *salam* contracts—that can be applied effectively within modern financial institutions.

⁷ Obeid Hasan Saleh Abdulmajid, Habibullah Zakaria, and Awal Adam Saad, “Commercial Paper (Short-Term) Importance and the Statement of Its Root and Legitimate Makassed,” *Journal of Islam in Asia* 17, no. 2 (2020), <https://doi.org/10.31436/jia.v17i2.969>.

⁸ Badawi, Saadia El-Badawi El-Sayed Ahmed. “Legal Effects Arising from the Commercial Securities Discount Contract: A Comparative Study.” *Journal of Legal and Economic Studies* 8, no. 4 (December 2022): 870–920. <https://doi.org/10.21608/jdl.2022.272448>.

Results and Discussion

Legal Characterization of Commercial Paper Discounting

The commercial paper discount agreement is finalized between the two parties, the beneficiary or the discount applicant, and the discounting bank. Discounting is carried out by authorizing the commercial paper, transferring its ownership, and the rights incorporated in it to the bank. Simultaneously, the beneficiary is still committed to settle its nominal value in the event of default by the original debtor to settle the obligation at maturity. By the Iraqi law, commercial paper is determined to be discounted under the Iraqi Commercial Code No. (30) Articles 283/First/f) of the amended and current Iraqi Commercial Code as: "*An agreement under which the bank undertakes to pay in advance the value of the commercial paper or any other negotiable instrument to the beneficiary in exchange for transferring its ownership to the bank, with the beneficiary obligated to reimburse the bank if the original debtor fails to pay.*" Based on this definition, it is perceived that the Iraqi legislator focused on the fact that the transaction was consensual, and the ownership of the commercial paper was transferred to the bank to accelerate its value.

The French legislator, on the other hand, defines discounting as "*a short-term credit operation under which banks or financial institutions provide the client with a monetary amount, from which interest, fees, and collection costs are deducted, with the advanced amount equaling the value of the rights embedded in the commercial paper endorsed in favor of the bank.*" Notably, this definition definitely defines discounting as a credit operation and does not limit its performance in banks only, but it can be performed by other financial institutions. However, it has in common with the Iraqi definition a major part of the transaction, which is the transfer of ownership of the commercial paper.⁹

Banking discount process is described as a complicated legal operation, which involves two transactions that are interrelated towards realizing one economic goal. The first case is a credit contract, which is a willed agreement subject to rules that apply to any consent of such agreements. The second transaction is the commercial paper in itself, which is the endorsement by which property of the rights contained in it is transferred, and which is regulated by the provisions of the negotiable instruments law, and the rules in particular that regulate their circulation.¹⁰

The law of commercial paper discounting is based on the principles of agreement because it is a consensual contract that is established on the performance of its fundamental terms, which are the mutual agreement, a valid object, and a legal cause, and does not imply particular formal requirements in order to be valid. In this contract, the bank lends out the value of the commercial paper ahead of its maturity in exchange for transferring its ownership, although it remains entitled to recourse against the beneficiary in the event that it fails to get the full value of the original debtor. The bank then subtracts an amount of this transaction that includes the cost of discounting, such as the discount rate (interest), any commission, and collection charges,

⁹ Zakaria, Mohammed. "The Legal Nature of the Bank Discount Contract." *Journal of Legal Studies*, no. [issue], Algeria, 2016, 153.

¹⁰ Mohamed Abdel Aal Okasha, *International Commercial Law: International Banking Operations (A Study of the Applicable Law to Banking Operations of an International Nature)*, 2nd ed. (Egypt: Dar Al-Jami'a Al-Jadida, 2012), 304.

such that the amount advanced is less than the face value of the paper, which reflects its actual value at the time of discounting.¹¹

Commercial jurisprudence considers commercial paper discounting to be a banking credit operation that cannot be strictly categorised as a classic contract of sale, hawalah (transfer of debt), or a loan with interest on it, although it has some elements in common with each of these. It is a free banking activity and transfers to the rights entrenched in commercial paper with the view of bringing liquidity and credit stimulus to commercial dealings, with no effect as to a loan in its usual meaning as a banking loan.¹²

The commercial paper discounting takes a significant role in the contemporary commercial law since it is an effective credit-financing instrument, and as such, the holder of the paper could transform future rights into instant liquidity. This description is not restricted to the very fact of buying the paper but is the complex of the duties and the rights of the law that govern the interaction of the bank and the client in terms of the acceptance of the discount, the effects of the non-payment, and the way to defend the rights of the bank.¹³

In light of the above, the scholarly understanding of commercial law in most jurisdictions in the modern day tends to accept the commercial paper discounting as a legitimate banking credit service, which falls under commercial law. It helps in the fulfillment of the goals of commercial circulation and easing the transactions by enabling parties to convert the future receivables into instant liquidity prior to maturity.¹⁴

The mutual benefits of the discounting process to both the bank and the client make it stand out compared to other banking operations. It is a lucrative tool of the bank and generates financial payment in the form of interest and commission that is paid to clients who enjoy the discounted price. On the other hand, with this process, the client is able to access instant liquidity without having to wait until the commercial paper matures, a process that would match the business needs and ensure the smooth running of operations. Moreover, discounting provides the bank with a set of guarantees that may not be available to the same extent in other banking operations, some of which are derived from the endorsements on the discounted commercial paper, while others arise from the obligations established under the discount contract itself.¹⁵

Characterization in Islamic Jurisprudence and Fiqh Debate

The characterization of commercial paper discounting has sparked extensive debate among Islamic jurists, due to the conflict of its traditional form with the general rules governing

¹¹ Nada Rahir Al-Fain, "The Shariah Qualification of Commercial Paper Discounting: A Study in Light of Islamic Sharia's Position on the Discounting Process and the Juristic Approaches Proposed by Contemporary Scholars to Render It Lawful," *Al-Rafidain Journal of Law* 8, no. 27 (March 2006): 149180.

¹² Najat Mansour al-Reeh Muhammad, *The Legal Nature of Discounting Commercial Papers by the Bank* (master's thesis, Graduate College, University of Neelain, Sudan, 2018).

¹³ *Ibid*

¹⁴ Rana Mujahid Ali Abbas, *The Legal Regulation of Commercial Paper Discounting in the Palestinian Legislation* (master's thesis, Arab American University, 2022).

¹⁵ Nada Rahir Al-Fain, "The Shariah Qualification of Commercial Paper Discounting: A Study in Light of Islamic Sharia's Position on the Discounting Process and the Juristic Approaches Proposed by Contemporary Scholars to Render It Lawful," *Al-Rafidain Journal of Law* 8, no. 27 (March 2006): 149180.

financial transactions, particularly the prohibition of *Ribā* (usury/interest). The discounting process is whereby the bank pays the value of the commercial paper to the holder of the paper before maturity in exchange for offsetting a part of its value, which is a conditional gain depending on the time passing.

Fiqh Debate on the Characterization of the Discounting Process

1. The View That It Constitutes an Interest-Bearing Loan (the Majority Opinion)

The advocates of this opinion state that discounting of the commercial papers is not and cannot be a sale of rights in the paper and a transfer (*hawalah*) of the rights, but a loan with interest. The bank does not plan to buy the rights attached to the commercial paper, but instead it is looking to extend funds to the client in exchange for receiving its nominal value at the time of maturity, as well as an extra amount in terms of interest.

According to the views of this side, the bank does not get actual ownership of the commercial paper; instead, it gets possession of the commercial paper as security. This can be proved by the fact that in case of maturity date and none of the obligors remits the amount required, there is an immediate recourse against the discount applicant without necessarily having to go up to the last obligor who skips settlement. This means that the relationship between the bank and the discount applicant is lender-borrower as opposed to buyer-seller of a right.

Moreover, the client will only use discounting when he or she is in urgent need of funds, whereas the bank will only get the rights but not the security of a creditor: it will hold the paper and get back its value at the maturity date at a discount fee that is even greater than the interest that was agreed upon. This is, in a real sense, a usurious rate of return (*Ribā*).¹⁶ On this basis, if the discounting process is considered a loan, it is deemed impermissible under Sharia, as it involves interest and constitutes a loan that generates profit for the lender.¹⁷

According to Minhaj al-Salihin, discounting a bill of exchange at the bank in the manner of a loan where the beneficiary borrows from the bank an amount less than the nominal value of the bill, and the bank then claims the full value from the obligor is considered a *hawalah* 'ala al-bari' (transfer of debt to an innocent third party) and constitutes prohibited *Ribā*. This is because the bank's stipulation to deduct a portion of the bill's value constitutes an impermissible increase under Sharia, whether it is in exchange for the remaining term or for the bank performing certain tasks, such as registration or collection. It is not permissible for the lender to condition any financial benefit upon the borrower.¹⁸

As stated in Al-Mughni and Al-Sharh al-Kabir: "Any loan in which an increase is stipulated is unequivocally impermissible. Ibn al-Mundhir said: It is unanimously agreed that if the lender conditions any increase or gift upon the borrower, then the loaned amount on that basis, and if the increase is taken, it constitutes *Ribā*. It has also been narrated from Ubayy ibn Ka'b, Ibn'

¹⁶ Aziz Al-Akili, *Explanation of Commercial Law*, vol. 2: Commercial Papers and Banking Operations (Amman, 2002), 466.

¹⁷ Abdullah Abdul Rahim Al-Abadi, *The Position of Islamic Law on Contemporary Islamic Banks* (Sidon–Beirut: Modern Library Publications, 1981), 39.

¹⁸ Al Baraka, "Economic Fatwas: Issues Related to Commercial Documents," Al Baraka Website, accessed [1 AUGUST 2020], http://www.albaraka.com/resource/fatawi/commercial_doc4.htm.

Abbas, and Ibn Mas'ud (may Allah be pleased with them) that they prohibited any loan that generates profit for the lender."¹⁹

In Sharh al-Durar al-Bahiyah, the principle prohibiting a loan that generates benefit for the lender is reaffirmed, based on the narration of Anas (may Allah be pleased with him), in which the Prophet ﷺ said: "If one of you lends a loan and the borrower gifts something or makes the lender carry it on an animal, the lender should neither ride it nor accept it, unless this was agreed upon between them beforehand."²⁰

From the above, it is evident that Islamic law prohibits commercial paper discounting because it involves usurious gain (*Ribā*) received by the bank. However, if this transaction were stripped of its interest, it could be considered permissible under Sharia. In practice, though, commercial banks conduct discounting operations without regard for the *riba*-related prohibitions inherent in the traditional process.

2. The View That It Is Characterized as a Sale

A group of scholars has adopted the view that the discounting process should be characterized as a sale. They argue that when the bank discounts a commercial paper, it does not focus on the underlying right that gave rise to the paper, but rather on the paper itself and the financial value it derives from the endorsements on it. From this perspective, the bank is purchasing the discounted paper, regardless of whether it represents a right of the drawer, if the endorsements exist and constitute a valid debt.

Part of the Egyptian jurisprudence supports this view, emphasizing that through discounting, the bank acquires the instrument and all rights arising from it. It has recourse against the endorsers, including the client who requested the discount. This recourse is based on the instrument itself, not on the agreement between the bank and the client as an endorser, and it is established on the principle of guaranteeing the sold item.²¹

If the discounting process is considered a sale, it is impermissible under Sharia, as it falls within the category of prohibited sales for several reasons. One primary reason is that the discount involves both *Ribā al-Fadl* (usury in kind) and *Ribā al-Nasaya* (usury on deferred payment). When the bank discounts the paper, it effectively lends the holder a fixed amount of cash in exchange for receiving the paper at less than its original value. This constitutes a type of unequal exchange in money of the same kind, whereby the bank obtains a discounted gain for the period, which falls within what Sharia has prohibited.²²

In this context, if the consideration is of the same type and class, such as gold for gold, Sharia requires equality in quantity and immediate delivery. Deferral in such a case carries a

¹⁹ Muwafaq al-Din Ibn Qudamah and Shams al-Din Ibn Qudamah al-Maqdisi, *Al-Mughni wa al-Sharh al-Kabir*, vol. 4 (Beirut, Lebanon: Dar al-Fikr al-Arabi, 1972–1392 AH), 360.

²⁰ Sunan Ibn Majah, Hadith 114, commentary by Al-Shawkani, *Al-Durar al-Mudhee'ah Sharh al-Durar al-Bahiyah*, vol. 2, 114 (Beirut, Lebanon: 1978–1398 AH).

²¹ Muhammad Al-Shawkani, *Al-Durar al-Mudhee'ah Sharh al-Durar al-Bahiyah*, vol. 2 (Beirut, Lebanon: 1978–1398 AH), 59.

²² Abdullah Abdul Rahim Al-Abadi, *The Position of Islamic Law on Contemporary Islamic Banks* (Sidon–Beirut: Modern Library Publications, 1981), 39.

prohibited meaning and may be intended to give the appearance of a sale to an otherwise deferred loan.²³

Sharia explicitly addresses this issue, as stated in *Matālib Ulil-Nihā* in the chapter on *Ribā*, prohibiting the sale of gold for gold, silver for silver, barley for barley, wheat for wheat, dates for dates, and salt for salt, except on a like-for-like basis and hand to hand. If the types differ, a value difference is permissible, provided the exchange is immediate (hand-to-hand). This is supported by the Prophetic tradition, which states that any increase or excess constitutes *Ribā*.²⁴

It is authentically narrated from 'Ubadah ibn al-Samit (may Allah be pleased with him) that the Messenger of Allah ﷺ said: "Gold for gold, silver for silver, like for like, hand to hand; whoever adds or asks for an increase has committed *Ribā*." (Narrated by Al-Tirmidhi, who graded it as *hasan sahih*).

In Islamic jurisprudence, *Ribā al-Fadl* is defined as the excess in the principal when the exchanged assets are of the same kind and measured by weight or volume. *Ribā al-Nasaya*, on the other hand, refers to the excess due to deferral until maturity, or the excess of the principal over the owed amount, in assets that are either of different kinds when measured by weight or volume, or not measured at all when of the same kind.²⁵

As stated in *I'lam al-Muwaqqin*, *Ribā* is of two types: apparent (*jāli*) and hidden (*khafī*). Apparent *Ribā*, which is *Ribā al-Nasaya*, is prohibited due to the great harm it entails, while hidden *Ribā*, which is *Ribā al-Fadl*, is prohibited because it serves as a means leading to the apparent form. Legally, the first is explicitly forbidden, while the second is prohibited to the first.²⁶

As stated in the narration of Abu Sa'id al-Khudri (may Allah be pleased with him) from the Prophet ﷺ: "Do not sell a dirham for two dirhams, for I fear for you *al-rimā*, and *al-rimā* is *Ribā*." This prohibited *Ribā al-fadl* because the Prophet ﷺ feared it would lead to *Ribā al-nasiya*. That is, if they sold one dirham for two, they could gradually move from immediate profit (*Ribā al-fadl*) to deferred profit, which is *Ribā al-nasiya*. This is a very close causal connection, and it reflects the wisdom of Sharia in closing off this pathway and forbidding both the immediate and deferred unequal exchange of dirhams.

Another form of *Ribā* observed in the discounting process is known as "*da'wa ta'ajjul*" (reduce and expedite). Ibn Rushd defined it as a case in which a person takes an amount in a deferred debt, even if its value is less than the original debt. Those who prohibit this form argue that it resembles the forbidden increase on deferred payment (*Ribā al-nasiya*), because both

²³ Al-Jamal Gharib, *Islamic Banks and Financing Institutions*, 1st ed. (Jeddah, 1398 AH), 126.

²⁴ Muhammad Al-Shawkani, *Al-Durar al-Mudhee'ah Sharh al-Durar al-Bahiyah*, vol. 2 (Beirut, Lebanon: 1978–1398 AH), 157.

²⁵ Mohammed Al-Faleh Al-Qudah Zakaria, *Al-Salam wa al-Mudarabah min 'Awamil al-Taysir fi al-Shariah al-Islamiyyah* (Amman: Ta'a, 1984), 65.

²⁶ Ibn al-Qayyim al-Jawziyyah, *I'lam al-Muwaqqi'in 'an Rabb al-'Alamin*, vol. 2 (Beirut: Dar al-Fikr, n.d.), 153.

assign a financial consideration to the passage of time, which Sharia does not permit if it effectively charges the debtor for interest or its equivalent.²⁷

3. The View That It Constitutes a Transfer of Rights (Hawalah)

Proponents of this view argue that the commercial paper discounting process constitutes a transfer of rights (hawalah) from the client to the bank. The client assigns to the bank the rights they hold against a third party in exchange for the bank advancing the value of the paper.²⁸ Even if this characterization is assumed to be valid for the sake of juristic argument rather than doctrinal acceptance, the discounting operation would still be deemed invalid from the perspective of Islamic jurisprudence. This is due to the absence of a fundamental condition for the validity of hawalah, namely, the equivalence in amount between the transferred debt and the debt to which it is transferred.²⁹

Matalib Uli al-Nuha states, in the chapter on hawalah, that one condition for the validity of a transfer of debt is the equivalence of the two debts in amount. Accordingly, hawalah is invalid if a smaller debt is transferred against a larger one, such as transferring ten against five, or vice versa, such as transferring five against ten, due to the disparity in amounts. However, it is valid to transfer a smaller amount equal to a corresponding portion of a larger debt, for example, five out of ten. The difference in the underlying causes of the two debts does not affect the validity of the transfer, even if one debt arises from a loan and the other from the sale price.³⁰

Mālikī jurists further stipulated, for the validity of hawalah, that the debt owed by the transferor (al-muḥīl) must be equal to the debt owed by the transferee (al-muḥāl 'alayh) in both amount and description. Equality in amount means that the creditor (al-muḥāl lahu) may not receive from the transferee more than what is originally due to him from the transferor. Thus, if a person is owed a debt of five and the debtor transfers him to another person who owes the debtor ten, the transfer must be limited to five only, without any increase. Any increase would be impermissible: if the original debt is a loan, the increase would constitute *Ribā*; and if it represents the price of a sold commodity, the increase would amount to the sale of a debt for a debt (*bay' al-dayn bi-l-dayn*), which is not permitted under Islamic law.³¹

Based on the foregoing, it becomes clear that characterizing the discounting of commercial papers as an assignment of debt does not rest on a sound juristic basis, as it involves a violation of the conditions required for the validity of assignment under Islamic jurisprudence, particularly the requirement of equivalence in the amount of the debt.

It is evident from the foregoing that the predominant juristic characterization of the discounting process in its traditional form is that it constitutes a usurious transaction prohibited

²⁷ Ibn Rushd al-Qurtubi, *Bidayat al-Mujtahid wa Nihayat al-Muqtasid*, vol. 2 (Egypt, 1966).

²⁸ Samihah Al-Qalyoubi, *Commercial Law (Banking Operations and Commercial Papers)* (Cairo: Dar Al-Nahda Al-Arabiya, 1986), 85, note 1.

²⁹ Sami Hasan Ahmad Mahmoud, *Development of Banking Operations in Compliance with Islamic Sharia*, 2nd ed. (Jordan, 1982), 284.

³⁰ Al-Suyuti al-Ruhibani, *Mutalib Awli al-Nahiy fi Sharh Ghayat al-Muntaha*, vol. 3 (Damascus, 1961), 325.

³¹ Abdul Rahman Al-Jaziri, *Fiqh According to the Four Schools of Thought*, vol. 3, Transactions Section (Beirut, Lebanon: Dar al-Kutub al-Ilmiyyah, 1988), 21.

under Islamic law, as it involves a conditional increase in return for time, regardless of the differing juristic attempts to characterize it. This necessitates the search for lawful banking alternatives that are consistent with the objectives of Islamic Sharia and that achieve economic justice.

Sharia-Compliant Alternatives in Contemporary Banking Practice

To overcome the juristic challenges associated with the traditional discounting of commercial paper, contemporary Islamic banking and finance rely on several contractual structures that aim to achieve economic functions like those of discounting, such as providing liquidity and credit, without falling into the prohibition of usury (*Ribā*) or violating the principles of Islamic law. These structures have received wide attention in Islamic jurisprudence and practical Islamic finance, and among the most prominent of them are:

1. *Murabaha* (Cost-Plus Sale)

Murabaha is one of the most widely used financing instruments in Islamic banks. It is simply a cost-plus sale contract in which the bank purchases an asset or commodity at the client's request and sells it back to the client at a price that includes the purchase cost plus an agreed-upon profit margin, often with deferred payment through installments. The permissibility of this contract under Sharia is based on the bank's actual ownership of the asset prior to resale and the transparency of the agreed profit. This ensures that the transaction is free from usurious interest (*Ribā*), which is prohibited under Islamic law.³²

Juristic analysis highlights that *Murabaha* is based on two essential elements: the disclosure of the original cost (purchase price) and the specification of the agreed profit. These two elements constitute the common basis for defining *Murabaha* across the four Sunni schools of Islamic jurisprudence, ensuring that the contract remains a valid and permissible sale under Sharia when both conditions are fulfilled.³³

One common practical application in Islamic banks is *Murabaha* to the Purchase Orderer, in which the client instructs the bank to purchase a specific commodity on their behalf, and the bank then sells the commodity to the client at a deferred-payment price that includes an agreed-upon profit margin. This application is particularly important for financing tangible assets such as real estate, vehicles, and equipment, providing a Sharia-compliant alternative to conventional interest-based financing.³⁴

Murabaha is not merely a financing tool; it can also contribute to financial inclusion and poverty alleviation when applied through innovative models such as *Murābahah-Ta'āwun*, in which a group of clients cooperatively finances assets under the supervision of an Islamic bank. This approach enhances access to funding while fully avoiding transactions involving *Ribā* (usury).³⁵

³² A. Abdulkadir, "Murabaha in Islamic Banks: A Fiqhi Study (Al-Murabaha fi al-Masaref al-Islamiyyah)," *International Journal of Al-Turath in Islamic Wealth and Finance* 1, no. 1 (2020): 112–145, <https://doi.org/10.31436/ijaiwf.v1i1.395>.

³³ Ibid

³⁴ A. Sikiru Olanrewaju and S. Abdullahi Busari, "Murābahah-Ta'āwun Financing: An Innovation in Islamic Personal Financing (Al-Murabaha Al-Tamwiliyya Al-Ta'awuniyya: Ibtikar fi al-Tamwil al-Islami al-Shakhsi)," *International Journal of Fiqh and Usul Al-Fiqh Studies* 3, no. 1 (2019): 103–108, <https://doi.org/10.31436/ijfus.v3i1.135>.

³⁵ Ibid

It is essential to adhere to Sharia principles in practical application, particularly in light of contemporary banking practices. This necessitates robust Sharia supervision to ensure the contract remains consistent with Sharia objectives and avoids structures that resemble interest-based loans.³⁶

Murabaha is one of the most prominent contracts that reconcile financing needs with Sharia-compliant principles in contemporary Islamic jurisprudence, particularly in commercial and consumer financing.³⁷

Murabaha can serve as a Sharia-compliant alternative to traditional commercial paper discounting, providing the client with liquidity and advance financing without engaging in interest-based debt. For example, if a trader holds commercial paper representing a deferred receivable from the sale of future goods and requires liquidity before its due date, the bank can purchase the required goods on behalf of the client and resell them at a predetermined profit margin, with payment deferred in installments. In this way, the client obtains the necessary cash financing, while the bank ensures ownership of a tangible asset, maintains Sharia compliance, and achieves the same economic functions as traditional commercial paper discounting.

2. Banking Tawarruq (Islamic Commodity-Based Financing)

In Islamic banking, Tawarruq is a financing mechanism used when a client requires cash liquidity without owning a specific commodity that requires financing. Under this arrangement, the client purchases a commodity from the bank on a deferred-payment basis and subsequently sells it to a third party for immediate cash, while committing to pay the deferred price in installments. The objective of this procedure is to provide the client with instant liquidity in a manner compliant with Sharia principles. When conducted in accordance with the rules governing sale, delivery, and legitimate ownership, Tawarruq constitutes a Sharia-compliant alternative to conventional interest-based loans.

Banking Tawarruq is particularly used for liquidity management, personal financing, and working capital financing within Islamic banks, and is regarded as a practical application of the Tawarruq sale contract developed by jurists to address contemporary financing needs. However, scholars continue to differ on the legitimacy of structured banking Tawarruq. Some juristic councils and Sharia supervisory boards have approved Tawarruq as a Sharia-compliant instrument for liquidity financing. In contrast, others contend that it may become a formal arrangement that fails to reflect the substance of a genuine sale, thereby rendering it subject to juristic criticism.³⁸

³⁶ Makounou Abdoul Karim and Saheed Abdullahi Busari, “Murabaha Contract as a Shariah-Compliant Alternative to Interest-Based Financing: An Analytical Study from the Perspective of Maqasid Al-Shariah (‘Aqd al-Murabaha Kabdal Shar’i lil-Tamwil al-Ribawi: Dirasah Tahliliyyah Naqdiyyah min Manẓur Maqasid al-Shariah),” *Al-Burhān: Journal of Qur’ān and Sunnah Studies* 9, no. 2 (2025): 221–238, <https://doi.org/10.31436/alburhn.v9i2.394>.

³⁷ Principles of Shariah-Compliant Banking Operations, FIN, accessed January 30, 2026, <https://fin.com.sa/ar/courses/Principles-of-Shariah-Compliant-Banking-Operations/info>

³⁸ Abdelaziz Idzoubair, “Simulated Contracts in Islamic Banks: Organized Bank Tawarruq as a Model (Al-‘Uqud al-Suriyya fi al-Masaref al-Islamiyya: Al-Tawarruq al-Masrafi al-Munazzam Anmuthajan),” *International Journal of Al-Turath in Islamic Wealth and Finance* 4, no. 2 (2023): 66–80, <https://doi.org/10.31436/ijaiwf.v4i2.810>.

Structured Tawarruq is widely used by Malaysian banks and is considered an effective solution for liquidity management, whereas in other countries, such as Indonesia, fatwas regard this practice as impermissible in Islamic banking.³⁹

Juristic criticism of banking Tawarruq notes that some contemporary practices may result in a financial outcome resembling an interest-based loan if genuine commodity trading is absent or if the bank dominates the buying and selling process. This underscores the need to review and enforce application rules to ensure full compliance with Sharia principles. The distinction⁴⁰ between individual Tawarruq and structured banking Tawarruq lies in their juristic acceptance: the former is generally more widely accepted by scholars when the conditions of a genuine sale are met, whereas the latter faces Sharia objections related to the transaction's intention and purpose, as well as the lack of an actual transfer of the commodities.⁴¹

Tawarruq is a financing arrangement used when a client requires immediate cash liquidity without owning a commodity they wish to finance. Under this arrangement, the client purchases a commodity from the bank on a deferred-payment basis and subsequently sells it to a third party to obtain immediate cash. The objective of this process is to provide liquidity while paying in installments, offering a Sharia-compliant method of accessing funds without *Ribā*, provided that the conditions of sale, ownership, and delivery are properly observed. Structured banking Tawarruq is based on the principles of sale and purchase and has been incorporated into the practices of Islamic financial institutions as a Sharia-compliant financing solution. However, juristic differences remain regarding its permissibility and certain aspects of its practical implementation.⁴²

In this way, banking Tawarruq can be regarded as a Sharia-compliant alternative to traditional commercial paper discounting, as it fulfills similar functions, providing liquidity and credit while fully adhering to Islamic legal requirements concerning sale, ownership, and delivery.

3. Salam (Prepaid Forward Sale)

Salam is a contract in which the delivery of goods is deferred to a later date in exchange for an advance payment. It is one of the oldest Sharia-compliant alternatives for financing activities that require upfront liquidity for production or trade. In the banking context, Salam can be used to finance agriculture or manufacturing, where the bank pays the producer in advance for the goods and takes delivery at a later agreed date, thereby providing liquidity to the farmer or producer without involving *Ribā*. The contract is Sharia-compliant when its

³⁹ Muhamad Yusuf Abdillah, Mighfari Elsha Rabi, and Rizal Nazarudin Firli, "Tawarruq Application in Islamic Banking: A Comparative Study Between Malaysia and Indonesia," *Al-Arbah: Journal of Islamic Finance and Banking* 2, no. 1 (2020), <https://doi.org/10.21580/al-arbah.2020.2.1.5540>.

⁴⁰ M. F. Roslan et al., "Application of Tawarruq in Islamic Banking in Malaysia: Towards Smart Tawarruq," *International Journal of Management and Applied Research* 7, no. 2 (2020): 104–119, <https://doi.org/10.18646/2056.72.20-008>.

⁴¹ LSabt, Abdullah. "Athar Tatbiq al-Tawarruq al-Masrafi al-Munazzam 'ala Sigh al-Tamwil al-Islamiyya al-Mabniyya 'ala Fiqh al-Buyu'." *Dafatir Iqtisadiyah* 14, no. 2 (December 30, 2023): 351–366.

⁴² Muhammad al-Jundi, "Tawarruq and Its Contemporary Banking Applications in Islamic Fiqh," *Alukah.net* (January 11, 2010), accessed January 30, 2026, <https://www.alukah.net/culture/0/25457/>

conditions regarding the specification of the goods, delivery time, and contractual clarity are fully satisfied.⁴³

In contemporary banking practice, Salam is used as an effective instrument for financing the agricultural sector and primary industries. In this arrangement, an Islamic bank pays the producer in advance for the crop or manufactured goods and receives the commodity at a later agreed date or sells it through a parallel contract. This method is fully compliant with Sharia principles, as it provides liquidity without resorting to interest-based loans and simultaneously ensures a link to the real economy. Contemporary studies have noted that Salam represents "a suitable financing tool for productive activities with defined production cycles, particularly agriculture, as it provides advance liquidity while managing risks through the contract."⁴⁴

The implementation of Salam in Islamic banks contributes to achieving Sharia objectives, particularly by supporting production and reducing financial speculation compared to debt-based financing instruments.⁴⁵ In the contemporary banking context, Salam can be used to provide clients with cash liquidity as an alternative to traditional commercial paper discounting, raising juristic issues related to *Ribā* or partial debt trading.

Conclusion

This paper affirms that commercial paper discounting, though accepted as a valid credit tool in the contemporary commercial law, has inherent incompatibilities upon closer scrutiny from a Shariah perspective. Being a banking operation, it combines a contractual consent with endorsement operations and has a unique legal nature in positive law. The Shariah analysis, however, proves that the form of conventional discounting, whether by way of a loan, sale of debt, or transfer of rights, constitutes the structure of *Ribā*, either by way of a conditional increment over time or disparity in exchange of money. The findings thus reinforce the dominant juristic position that traditional discounting constitutes an interest-based transaction prohibited under Islamic law. At the same time, the research establishes that Islamic banking instruments such as *murābahah*, organized *tawarruq*, and *salam* can fulfil equivalent liquidity and financing objectives while adhering to the foundational principles of Shariah. Considering these findings, the study underscores the necessity for Islamic financial institutions to institutionalize Shariah-compliant alternatives that align with the higher objectives (*maqāṣid*) of Islamic law, especially the advancement of justice, openness, and fair trade. It is proposed that future studies should not concentrate on the doctrinal analysis but on empirical and comparative research studies that discuss the use of these other instruments in practice in various legal systems and regulatory contexts. More research can also be done on new hybrid forms that can embrace the idea of commercial efficiency and compliance with the strict Shariah rules, hence helping in the further development of sustainable and ethics-based Islamic financial structures.

⁴³ Ali Abbas Samiran Al-Halbousi, "Islamic Murabaha in the Islamic Economy," *Tilmeez Journal* (January 30, 2021)

⁴⁴ El-Gamal, Mahmoud A. *Islamic Finance: Law, Economics, and Practice*. Cambridge: Cambridge University Press, 2006.

⁴⁵ Obaidullah, Mohammed. "Salam and Parallel Salam." *Islamic Research and Training Institute (IRTI), Islamic Development Bank, Occasional Paper*, 2001.

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Author Contributions Statement

Tunis Abu Bakr Rahman contributed to the conceptualization and design of the study, developed the research methodology, conducted the primary investigation, and prepared the original draft of the manuscript, as well as supervised the overall research process. Widad Mahdi Jasim was responsible for data curation, formal analysis, and validation of the findings, and contributed substantially to reviewing and editing the manuscript. Nooruldeen Mustafa Al-Gburi contributed to the literature review, provided essential resources, supported data visualization and project administration, and participated in reviewing and refining the manuscript. All authors have read and approved the final version of the manuscript.

AI Usage Statement

In the preparation of this manuscript, artificial intelligence (AI) tools were used solely to assist with language refinement, grammar checking, and improving overall clarity of expression. The use of AI did not involve the generation of research data, analysis, interpretation of findings, or formulation of core arguments. All conceptual development, methodological design, data analysis, and substantive content were conducted independently by the authors. The authors take full responsibility for the accuracy, integrity, and originality of the work presented in this manuscript.

Conflict of Interest

The authors declare that there is no conflict of interest related to this study. The research was conducted independently without any commercial, financial, or personal relationships that could influence the results.

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