

Islamic Economic System: Principles, Comparisons, and Public Finance

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Executive Summary

The Islamic Economic System is a comprehensive framework derived from practical religious legislation (Shari'a) that governs the earning, spending, and investment of money. Its ideological foundation rests on the principles that all wealth ultimately belongs to Allah, with humans acting as stewards, and that a balance must be maintained between individual prosperity and social justice. Key characteristics include a system of dual property (protecting both private and public interests), restricted economic liberty guided by moral and legitimate regulations, and a strong emphasis on social solidarity through mechanisms like Zakat (obligatory alms).

This system stands in contrast to conventional economic models. Unlike Capitalism, which champions absolute individual liberty and self-interest, the Islamic model filters economic decisions through a moral framework, prohibiting earning “at any way.” Unlike Socialism, which centralizes ownership and control in the state, the Islamic economy recognizes and protects private property while ensuring community welfare.

Public finance within this system is distinct, with revenue sources divided into periodic (Zakat, Jizya, Kharaj) and non-periodic categories (spoils of war, customs duties). Public expenditure is strictly governed by principles of beneficial use (maximizing utility), economic use (avoiding extravagance), and official authorization, with the overarching goal of fulfilling public needs and ensuring social security.

1. Foundations of the Islamic Economy

The Islamic economic system is defined by its unique ideological, theoretical, and applied aspects, all rooted in religious principles.

Definition and Core Concepts

- **Linguistic Origin:** The term “economy” in Arabic derives from the word *قصد* (*qasd*), which signifies “the straightness of the road” and “the rationing of something,” implying a moderate path between immoderacy and scrimping.

- **Formal Definition:** Islamic Economy is the knowledge of practical religious legislations, derived from detailed proofs, that regulates the earning, spending, and investing of money.

Ideological Framework

The economic activity in Islam is based on a set of controlling regulations and values:

- **Divine Ownership of Wealth:** The foundational belief is that all money and resources belong to Allah, and humans are appointed as guardians or successors over them. This stewardship comes with accountability.
 - **Quranic Basis:** "spend out of that in which He has made you successors" (وأنفقوا) (مما جعلكم مستخلفين فيه).
 - **Prophetic Teaching:** "Man's feet will not move on the Day of Resurrection before he is asked about his life, how did he consume it, his knowledge, what did he do with it, his wealth, how did he earn it and how did he dispose of it, and about his body, how did he wear it out."
- **Economic Balance and Social Justice:** While Islam permits variations in wealth and income among individuals, it mandates the maintenance of social justice, economic balance, and good living standards for all members of the community.
- **Dual Property Rights:** The system upholds and protects both private and public forms of property.
 - **Prophetic Example:** The Prophet (ﷺ) forbade city-dwellers from acting as brokers for desert-dwellers to prevent price inflation (protecting public property) and prohibited buying from foreign merchants before they knew the market price (protecting private property).

Analytical and Applied Aspects

- **Theoretical/Analytical Aspect:** This involves analyzing economic phenomena and relationships through the lens of Islamic principles. It often challenges the assumptions of non-Islamic economics. For example, while conventional theory suggests consumption rises with income, Islam advises against extravagance.

- **Quranic Guidance:** "And do not make your hand [as] chained to your neck or extend it completely and [thereby] become blamed and insolvent."
- **Prophetic Warning:** "May he be miserable, the worshipper of the dinar and dirham... If he is given anything, he is satisfied; but if not, he is unsatisfied."
- **Applied Aspect (Economic Policy):** This is the study and implementation of policies and applications that align with Islamic rules to address the economic problems of a community at any given time.

Relationship with Other Sciences

- **Islamic Jurisprudence (Shari'a):** Jurisprudence identifies the religious verdict on an economic issue (e.g., usury is forbidden), while economics studies the effects of that verdict (e.g., the impact of prohibiting usury on money and investment).
- **History:** The economic events, ideas, and systems from Islamic history provide crucial data and concrete proofs for researchers to analyze past and present economic phenomena.
- **Mathematics and Statistics:** These sciences are important tools for economic researchers to analyze transactions and design programs and plans to achieve society's economic goals.

2. Comparative Analysis of Economic Systems

The Islamic economic system possesses unique characteristics that distinguish it from Capitalism and Socialism.

Characteristics of the Islamic Economy

1. **Dual Property:** It seeks a balance between the interests of the individual and the community, provided they do not contradict.
2. **Restricted Economic Liberty:** Economic freedom is not absolute; it is governed by legitimate regulations on how money is earned and spent. The accountability for wealth is a central theme.

3. **Social Solidarity:** The system mandates social support through the obligation of fulfilling Alms (Zakat), charities, and other acts of benevolence.

Comparison with Conventional Systems

Feature	Capitalism	Socialism / Communism	Islamic Rationalism
View of Life	Worldly life & confused about Hereafter life	Worldly life is the only life & no Hereafter life	Worldly life & Hereafter life
Primary Goal	Self-satisfaction	Self-satisfaction through state intervention	Satisfaction of ALLAH
Decision Making	Self-interest & Rationalism is the sole authority	Rationalism and state is the sole authority	Individualism & Rationalism through moral filtering
Market Structure	Competitive market: survival for the fittest	State control the market	Combination of competition and state intervention: Humanity & Philanthropy
Value System	No value judgment	No value judgment	Social, national, cultural values are considered
Role of Religion	Independent of revealed religion; Religion is unreliable	No religion	Religion is key determinant
Method of Earning	Earning at any way	Earning at any way	Earning at honest way

Disadvantages of Conventional Systems

- **Capitalism:**
 - Imbalance in wealth distribution among people.
 - Occurrence of crises and unemployment.

- Leads to merchandise monopoly.
- Allows for absolute freedom in earning and expenditure, regardless of moral implications.
- **Socialism:**
 - Contradicts the human instinct for ownership preference.
 - Demotivates individuals by reducing them to a machine-like status, thereby demolishing productivity motives.
 - Historically associated with hard poverty in nations that adopt it.

3. Key Economic Terminology

The following terms are central to understanding economic discourse, with specific conditions added by the Islamic framework.

- **Wealth:** The sum of productive and consumable economic assets possessed by an individual or society at a given moment. The concept does not include services.
- **Commodity:** A tangible economic product that has a physical form. For a good to be considered a commodity in Islamic economics, it must meet four conditions:
 1. It must be beneficial.
 2. It must be relatively rare.
 3. It must be tradable.
 4. **It must be permissible according to Islamic law (Shari'a).** This condition takes precedence over all others.
- **Services:** An intangible economic product with no physical form. Like commodities, services must be permissible under Islamic law. Therefore, services from establishments like cinemas and nightclubs are not recognized.
- **Income:** The return received by an owner of a production factor for contributing to the production process.
- **Utility:** The inherent ability or power of a good or service to satisfy a specific human need.
- **Consumption:** The portion of income spent on consumer goods and services that directly satisfy needs.

- **Saving:** The portion of income that is not spent on consumption.
- **Investment:** The creation of new tangible capital (e.g., buildings, machinery, infrastructure) that represents a net increase in the productive capacity of society.
- **Public (Governmental) Sector:** The part of the national economy owned and operated directly by the state or its authorities (e.g., oil extraction, water desalination).
- **Private Sector:** The part of the economy not controlled by the government, including for-profit businesses run by individuals or companies.

4. Public Finance: Revenues and Expenditures

The management of state finances in the Islamic system is structured around unique revenue sources and ethically guided principles of expenditure.

Public Revenues in the Islamic Economy

Islamic revenue sources are categorized as periodic (the main, recurring resources) and non-periodic.

1. Periodic Resources:

- **Zakat (Alms):** The third Pillar of Islam, an obligatory annual giving of 2.5% of a Muslim's disposable income and wealth above a minimum threshold (*nisab*). It is a form of worship and self-purification, strictly designated for eight categories of recipients mentioned in the Quran, including the poor, the needy, and freeing captives.
- **Jizya:** A per capita yearly tax levied on certain non-Muslim subjects (*dhimmi*) in exchange for state protection, exemption from military service, and the right to practice their religion. Women, children, the poor, the elderly, and monks were typically exempt.
- **Al-Kharaj (Land Tax):** A tax levied on agricultural land, particularly land acquired during Islamic conquests.

2. Non-Periodic Resources:

- **Fifth of the Spoils of War:** Movable property seized from an enemy during armed conflict. Four-fifths are distributed among the soldiers, while one-fifth is allocated for the welfare of the Muslim community.
- **Fay’:** Money or assets obtained from non-Muslims without fighting, such as through peace treaties. It is spent for the benefit of the Muslim community.
- **Al Eshour (Customs Tax):** Fees collected from merchandisers, Muslim or non-Muslim, passing through Muslim lands. It served as a toll for protection and market access.
- **Loose Money:** Assets with no known owner, such as an inheritance with no heirs.
- **Charitable Endowments (Wakf):** An inalienable charitable endowment under Islamic law, where assets (land, buildings) are donated for religious or charitable purposes.

Public Expenditure in the Islamic Economy

The primary goal of public spending is to satisfy public needs, categorized as public services and social security services.

Historical Evolution of the Treasury:

- **Prophet Mohammed’s Era:** No formal treasury (*Bait Almal*) was needed. Revenues, mainly from wars, were distributed immediately.
- **Abu Bakr’s Era:** Maintained the same system and notably fought those who refused to pay Zakat, affirming its obligatory nature.
- **Omer Ibn Alkhattab’s Era:** As the Islamic state expanded, revenues increased. He established the state treasury (*Bait Almal*) and organized government affairs by creating ministries (*Aldewan*).
- **Othman Ibn Affan’s Era:** Revenues continued to grow and were distributed through increased salaries and grants.
- **Ali Ibn Abe Taleb’s Era:** Focused on economic development and land improvement.

Governing Rules of Public Expenditure:

1. **The Rule of Beneficial Use:** Spending must be directed to achieve the highest level of utility at the minimum cost, providing prosperity for the largest number of people.
2. **The Rule of Economic Use:** Spending must avoid extravagance and waste, focusing on basic and essential needs.
3. **The Rule of Authorization:** Money can only be spent after approval from the competent legislative authority through an officially approved law.

Study Guide for Islamic Economic System

Short-Answer Quiz

Instructions: Answer the following questions in two to three sentences, based on the provided source material.

1. What is the linguistic origin of the word “economy,” and what is the formal definition of Islamic Economy?

2. What are the three aspects that constitute the “Subject of Economy” within the Islamic framework?

3. Describe the core characteristics of the Islamic economic system as outlined in the lectures.

4. According to the source, what are the primary disadvantages of the Capitalist and Socialist economic systems?

5. What four conditions must be met for an item to be considered a “commodity” in Islamic economics?
6. Explain the difference between consumer goods and production goods, providing an example of each.
7. List and briefly describe at least three sources of public revenue in non-Islamic economic systems.
8. What are the two main categories of public revenue sources in the Islamic Economy, and what do they consist of?
9. Define Zakat and explain its purpose, its required rate, and who is obligated to pay it.
10. What are the three primary rules that govern public expenditure in Islam?

Answer Key

1. Linguistically, the word “economy” derives from the Arabic word (قصد), which means the straightness of the road and rationing, signifying a middle path between immoderacy and scrimping. The Islamic Economy is formally defined as the knowledge of practical religious

legislations that regulate the earning, spending, and investing of money, as derived from detailed proofs.

2. The three aspects are the ideological, the theoretical/analytical, and the applied. The ideological aspect covers values and rules, such as money belonging to Allah. The theoretical/analytical aspect involves analyzing economic phenomena, while the applied aspect is the study of policies that handle a community's economic problems.
3. The core characteristics of the Islamic economy are dual property, which balances individual and community interests; restricted economic liberty, which means earning and spending are governed by legitimate regulations; and social solidarity, which is fulfilled through obligations like Zakat and other charities.
4. The disadvantages of Capitalism include an imbalance in wealth distribution, the occurrence of crises and unemployment, merchandise monopoly, and absolute freedom in earning and spending. The disadvantages of Socialism include fighting the human instinct for ownership, turning humans into machines which demolishes productivity, and the prevalence of hard poverty in socialist nations.
5. For an item to be a "commodity," it must be beneficial, relatively rare, and tradable among society members. Crucially, Islamic economics adds a fourth condition that takes precedence: the commodity must be permissible according to Islamic law (Shari'a).
6. Consumer goods are tangible products that directly satisfy human needs, such as food (single-use) or a car (durable). Production goods are items used in the production process to create other goods, such as raw iron (single-use) or machinery (durable).
7. Sources of public revenue in non-Islamic systems include:
 - o **Taxes:** An obligatory monetary deduction levied by the government on income and business profits.
 - o **Fees (Charges):** A monetary cut paid by a person in exchange for a special service provided by the government.
 - o **Public Loans:** Money borrowed by a government from banks, individuals, or other countries to finance public spending, which creates national debt.
8. The two categories are periodic and non-periodic resources. Periodic resources are the main, recurring sources and consist of Zakat, Jezia (Jizya), and Al Kharaj (land tax). Non-periodic

resources are non-annual and include the fifth part of booties, heirless heritage, Al Fe'e (pillage), and Al Eshour (customs tax).

9. Zakat is a compulsory charitable donation, considered a religious obligation and the third Pillar of Islam. It is a set proportion of wealth (customarily 2.5%) paid by Muslims whose disposable income exceeds a minimum amount (nisab) to purify their wealth and support specific categories of recipients, such as the poor and needy.

10. The three rules governing public expenditure are:

- **The rule of beneficial use:** Directing expenditures to achieve the highest utility with minimum cost for the most people.
- **The rule of Economic use:** Avoiding extravagance and spending on basic needs without waste.
- **The rule of Authorization:** Spending money only after approval from the competent legislative authority.

Essay Questions

Instructions: Formulate comprehensive answers to the following questions, drawing upon all relevant information from the source material. Answers are not provided.

1. Using the table “Economic Doctrines of life and Main theme of Rationalism,” compare and contrast the fundamental principles of Capitalism, Communism, and Islam across at least five different dimensions (e.g., life philosophy, decision-making authority, market structure, religious role).
2. Discuss the relationship between Islamic jurisprudence (Shari'a), history, mathematics, and the science of economics. Explain how these fields interact and provide examples for each relationship as detailed in the source.

3. Elaborate on the concepts of “dual property” and “restricted economic liberty” within the Islamic economic system. How do these principles aim to create a balance between individual interest and public welfare, and how do they fundamentally differ from the philosophies of Capitalism and Socialism?
 4. Provide a detailed overview of the primary sources of public revenue in an Islamic state. For Zakat, Jizya, and Al Kharaj, describe what each tax is, who is obligated to pay it, who is exempt, and what the funds are generally used for.
 5. Trace the evolution of the state treasury (Bait Al Mal) and public expenditure management from the era of the Prophet Mohammed through the caliphates of Abu Bakr, Omer Ibn Alkhattab, and Othman Ibn Affan. Describe the key economic changes and administrative developments that occurred in each era and the reasons behind them.

Glossary of Key Terms

Term	Definition
Al Eshour (Customs tax)	Fees collected by the government from a merchandiser who passes through Muslim land or access roads. It acts as a toll for protection or a duty on foreign goods.
Alms (Zakat)	The allocated amount in the wealth of certain individuals for a certain group of people at a certain time. It is a compulsory giving of a set proportion of one's wealth (customarily 2.5%) to charity, regarded as a type of worship and self-purification.
Capitalism Economy	An economic system based on the idea that the person is the sole owner of the money he earns and has full discretion to do whatever he wants with this money.
Commodity	A tangible economic product that is beneficial, relatively rare, tradable, and permissible according to Islamic law.
Consumption	The portion of income spent on consumer goods that directly satisfy needs.
Economy (Linguistic Origin)	From the Arabic word (قصد), meaning the straightness of the road and the rationing of something, indicating a balance between immoderacy and scrimping.
Fay'	Money that returns to Muslims from non-Muslims without fighting, through peace treaties, or from their own money. It is spent for the benefit of Muslims.
Fees (Charges)	A monetary cut by the government, or one of its administrative organizations, obligatory paid by a person for a special service which is fulfilled by the government to cover his needs.
Fifth of the spoils of war	One-fifth of all movable property captured from an enemy during armed conflict. This portion is for Allah, the Messenger, his relatives, orphans, servants, and needy travelers, to be spent on the welfare of Muslims.
Income	The return received by the owner of a production member in return for contributing to the production process.
Islamic Economy	The knowledge of the practical religious legislations through the detailed proofs that regulates earning, spending and investing money.
Investment	The creation of new tangible capital, represented by productive capacity. It is a net increase in the real capital of society (e.g., buildings, machinery, infrastructure).

Jayziah (Jizya)	A per capita, yearly tax historically levied by Islamic states on certain non-Muslim subjects (dhimmi) in exchange for protection, exemption from military service, and the right to practice their faith.
Land tax (Al Kharaj)	A tax levied on agricultural land, particularly land that was acquired during Islamic conquests.
Loose money	Money which has no owner, such as a heritage which has no heirs or deposited money which has no holder.
Private Sector	The part of the economy that isn't controlled by the government, including any for-profit business run by individuals or companies.
Public (Governmental) Sector	The part of the national economy that is owned and operated directly by the state or through other public authorities established by the state.
Public Loans	A sum of money obtained by a government from other countries, banks, or individuals, with an obligation to return the payments and pay interest. Also known as national or sovereign debt.
Public revenues	A state's annual income from which public expenses are met.
Saving	The portion of income that is not spent; the portion remaining after consumption.
Services	An intangible economic product that has no physical form. Can be consumer services (education, transportation) or productive services (training, maintenance).
Socialist Economy	An economic system based on the idea that wealth and production means are property of the whole community. Individuals have no rights to them and only take rewards for services provided.
Spoils of war (booty)	Movable property, goods, money, or resources lawfully captured or seized from an enemy during armed conflict.
State Budget	The financial activity of the government that means obtaining the technical resources of the country and spending them to fulfill public needs and realize social and economic targets.
Taxes	The obligatory monetary deduction of an individual's revenue according to his potentialities levied by the government on workers' income and business profits, or added to the cost of some goods, services, and transactions.

The charitable endowments (Wakf)	An inalienable charitable endowment under Islamic law, typically involving donating a building, land, or other assets for Muslim religious or charitable purposes with no intention of reclaiming the assets.
Utility	The ability or power of a good or service to satisfy a specific human need.
Wealth	At the individual level, the sum of productive and consumable economic assets possessed at a given moment. At the macro level, the sum of productive and consumer economic resources existing in the overall society.