THE PROHIBITION OF GHARAR

DEFINITION

✧ The Arabic word *gharar* is a fairly broad concept that literally means deceit, fraud, uncertainty, danger, peril, delusion, or hazard that might lead to destruction or loss.

✧ *Gharar* refers to any transaction of probable items whose existence or characteristics are not certain, due to lack of information, ignorance of essential elements in the transaction to either party, or uncertainty of the ability of one party to honor the contract.

✧ The Prophet (s.a.w) has forbidden the purchase of the unborn animal in the mother’s womb, the sale of the milk in the udder without measurement, the purchase of spoils of war prior to distribution, the purchase of charities prior to their receipt, and the purchase of the catch of a diver.

✧ All jurists agree that *gharar* should be avoided in commercial exchange contracts. As Islamic *Shari’a* forbids *riba* (interest) because it leads to exploitation and injustice in the society, it also forbids *gharar* in any transaction to protect the two parties from deceit, ignorance and uncertainty.

✧ All Islamic financial and business transactions must be based on transparency, accuracy, and disclosure of all necessary information so that no one party has advantages over the other party. Islam has clearly forbidden all business transactions, which cause injustice in any form to any of the parties. It may be in the form of hazard leading to uncertainty in any business, or deceit or fraud or undue advantage.

✧ The rationale of Prohibition of *gharar* is to ensure full consent and satisfaction of the parties in a contract. Without full consent, a contract may not be valid. Full consent can only be achieved through certainty, full knowledge, full disclosure and transparency.

✧ While the prohibition of *riba* is absolute, some degree of *gharar* or uncertainty is acceptable in the Islamic framework.
TYPES OF GHARAR

1. *Gharar Yaseer* (minor or slight)
   - This type of gharar is tolerated and will not invalidate a contract. Gharar yaseer may include the following cases:
     1. The uncertainty is slight or trivial.
     2. Contract is unilateral or charitable (*al tabarru’at*) such as gift or bequest.
     3. There is a public need for the transaction or contract (consideration of *maslahah*), for example, *bai’ al salam, istisna’*.

2. *Gharar Fahish* (major or excessive)
   - This type of gharar is not tolerated and may result in contract voidability.

CAUSES OF GHARAR

- It is important not to use *gharar* interchangeably with the broad concept of risk. *Gharar* is prohibited but not all types of risk are prohibited.
- Avoiding the causes of *gharar* results in clearing the ambiguity and reducing risk.
- The main cases of forbidden *gharar* can be summarized in the following:

1. **Uncertainty of ownership and Possession**
   - The sale of an item that may not exist or it is not in the possession of one of the parties and there is uncertainty about its future possession, such as the sale of birds in flight, fish not yet caught, stray (runaway) animal, or the unborn when the mother is not part of the sale.
   - *Gharar* also exists when there is no ownership or incomplete ownership such as selling something owned by another person without authority.
   - The reason for the prohibition of *gharar* is the risk or uncertainty, which casts doubts on the delivery of the item and settlement of the contract.
2. Inadequacy and Inaccuracy of Information

- Information is central to the Islamic system of contracting. All parties to the contract must make accurate and adequate disclosure of all relevant information enough to make reasonable estimates of the outcomes.
- Absence of adequate and accurate information (jahl) is a source of gharar. The absence of information for either party may be due to deliberate action of the counter-party, or it may also be due to contracting under a situation of uncertainty with mutual consent. In both cases, the contract becomes susceptible to prohibition.
- Lack of knowledge (jahl) could be with regard to the price or the item, the characteristics of the price or of the item, the quantum of the price or the quantity of the item, or the date of future performance.
- Islam emphasizes the need to protect the “informationally” weaker party. Several Ahadeeth illustrate this concern of protecting the weaker party. Such ahadeeth include the one that prohibited a sale whereby a townsman meets a tribesman outside the market place and buys the tribesman’s goods at a price cheaper than the price prevailing in the market, thus taking advantage of the seller’s ignorance of the market price.
- Other ahadeeth stress that the “informationally” disadvantaged party gets an option to rescind the contract subsequent to the time to contracting.

3. Interdependent and conditional contracts

- Shari’a does not permit interdependent contracts such as combining two sales in one contract, or two sales are linked jointly.
- Gharar exists if the sale price is dependent on a specific event, or the parties are not sure if the sale may or may not take place.
- Gharar exists on conditional sales so the fulfillment of one sale is conditional upon the fulfillment of the other, or the sale is conditional on external event such as, I will sell if snow falls.
Jurists, therefore, require that in composite products, the multiple contracts must be independent of each other.

4. Pure Games of Chance (Al-Qimar & Al-Maysir)
   - The term *gharar* is also used in the context of pure games of chance.
   - *Qur’an* prohibits contracting under conditions of uncertainty and gambling (*qimar*). The two words, uncertainty and gambling are not synonymous, though related.
   - Uncertainty is same as *gharar* and under such conditions, exchange or contracting is reduced to a gamble

CURRENT ISSUES

- In contemporary financial transactions, the two areas where *gharar* most profoundly affects common practice are insurance and financial derivatives.
- Jurists often argue against the financial insurance contract, where premium is paid regularly to the insurance company, and the insured receives compensation for any insured losses in the event of a loss. In this case, the jurists argue that the insured may collect a large sum of money after paying only one monthly premium. On the other hand, the insured may also make many monthly payments without ever collecting any money from the insurance company. Since “insurance” itself cannot be considered an object of sale, this contract is rendered invalid because of the forbidden *gharar*.
- Of course, conventional insurance also suffers from prohibition due to *riba* since insurance companies tend to invest significant portions of their funds in government bonds, which earn them *riba*.
- The other set of relevant contracts which are rendered invalid because of *gharar* are forwards, futures, options, and other derivative securities. Forwards and futures involve *gharar* since the object of the sale may not exist at the time the trade is to be executed.