

## A FRAMEWORK OF INDIRECT TAXATION SYSTEM IN PUBLIC FINANCE FROM SYARIAH PERSPECTIVES

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### ABSTRACT

The subject matter of public finance follows the development in state activities and corresponding economic philosophy. With the passage of time and policies of state, the scope of public finance expanded to cover more areas. The development of new political, economic, social, formulation of fiscal and monetary policies made profound differences in the present as compared to the past public finance problems. The fiscal system practiced by Muslim state in the past was consistent, operational, efficient and worked within the value of an Islamic society perspectives. The scholars of the period expressed practical wisdom and economic insight to bear on fiscal issues as evidenced by contribution of among others by Abu Yusuf Yaqub bin Ibrahim (d. 798 A.D.) which showed enormous economic insights in solving these problems and highlighted the distinctive value-based orientation of the mobilization of the resources of revenue and its disbursement in accordance with the objectives of Islamic Syariah. This article explores the model and wisdom of indirect tax practices as being implemented by past Islamic leaders in fulfilling their obligations towards managing the nation while protecting the people's wellbeing.

**Key words:** Islamic Fiscal System, Islamic Taxation, Islamic Indirect Tax, Abu Yusuf Yaqub bin Ibrahim, Al-Qardhawi, Chapra

## INTRODUCTION

In Islamic Fiscal System, there are several public finance resources mentioned in Al-Quran such as *Zakat* (obligatory charity), *Waqf* (non-obligatory charity) and *Jizyah* to eligible person to contribute some of his/her wealth to the needy. *Zakat* means to clean or to purify one's wealth / earning for the will of Allah SWT and must be conveyed to the *Asnaf* i.e. 8 groups of people entitled to receive the *Zakat*. The proceeds from *Zakat* is for the betterment of the recipients and is not allow to be used for other purpose (Sahih International, The Noble Quran, At-Tawbah 9:60). *Waqf* on the other hand, is defined as "a voluntary, permanent, irrevocable dedication of a portion of one's wealth in cash or kind to Allah to be used for a betterment of Muslim mankind" (Sahih International, The Noble Quran, Ali Imran 3:92). Meanwhile, *Jizyah* is a tax imposed to a non-Muslim who is residing under Muslim rules (Sahih International, The Noble Quran, At-Tawbah 9:29).

*Kharaj* and *Al-Usyr* was introduced later by Khalifah Umar Al-Khattab. Oxford Dictionary defines *Kharaj* as a land tax which is imposed on developed land and *Usyr* is a tax imposed on importation of goods by non-Muslim traders to Muslim country. As cited Johari & Ibrahim, other forms of tax imposed apart from *Zakat*, *Waqf* and *Jizyah* as mentioned in Al-Quran was based on *Ijtihad*. It was imposed on one's wealth and uphold the spirit of justice. *Ijtihad* as define by Britannica Encyclopaedia is "a technical term of Islamic law that describes the process of making legal decision by independent interpretation of legal sources i.e. the Quran and the Sunnah."

In practice, tax is classified into two (2) categories which is direct tax and indirect tax. Britannica Encyclopaedia defined a direct tax as "a form of tax collected directly by the government from the person who bear the tax burden" e.g. corporate tax, income tax etc. Meanwhile, an indirect tax e.g. import duty, goods and services tax etc., is defined as "a form of tax collected by mediators who transfer the amount collected to the government" (Encyclopedia Britannica, global.brittanica.com, retrieved 2016). The economists have put forward many theories or principles of taxation at different times to guide the state as to how justice or equity in taxation can be achieved.

Shinkafi & Ali (2017) emphasize that the major thoughtfulness of Islamic economy and

finance are human and social welfare, consumption, wealth spending (distribution and management), monetary policies, debts, market exchange, taxation, social security, investment and capital, business and trade, commerce and industry, law of transactions, etc. They further consider Islamic economy as:

*“[...] a field of knowledge that prepares the realisation of human well-being through allocation and distribution of scarce resources that conform with the Islamic point of view without unduly curbing individual freedom or creating continued macroeconomic and ecological imbalances.”*

It has been mentioned early in Al-Quran in verse Q65:7 as follows:

“Let a man of wealth spend from his wealth, and he whose provision is restricted - let him spend from what Allah has given him. Allah does not charge a soul except [according to] what He has given it. Allah will bring about, after hardship, ease.”

(Sahih International: At-Talaq 65:7)

Islamic scholars agree that economic affairs are to be managed so as to provide social and economic justice to citizens (Zaman A. , 2008). Pertaining to the tax matters, contrasting views on the imposition of tax by the government continue to be debated (Rosman, Mohd Yusof, Abu, & Syed Abdullah, Cukai Barang dan Perkhidmatan (GST) Berdasarkan Perspektif Fiqh Kontemporari, 2015). The first group who consider the act as Haram (forbidden) based on the Quranic verse below:

“And O my people, give full measure and weight in justice and do not deprive the people of their due and do not commit abuse on the earth, spreading corruption.”

(Sahih International: Al-Hud 11:85).

The following hadith and verse of Al-Quran acknowledge the impose of other forms of tax which did not mentioned in Al-Quran or practiced by Prophet Muhammad (Peace Be Upon Him):

“It was reported by Fatimah binti Qais, Prophet Muhammad (Peace Be Upon Him) said: Indeed, there is a due on property other than zakah (Narrated by Al-Tirmidhi, Hadith 659). Then Prophet Muhammad (Peace Be Upon Him) recited the following verses:

Righteousness is not that you turn your faces toward the east or the west, but [true] righteousness is [in] one who believes in Allah, the Last Day, the angels, the Book, and the

prophets and gives wealth, in spite of love for it, to relatives, orphans, the needy, the traveller, those who ask [for help], and for freeing slaves; [and who] establishes prayer and gives zakah; [those who] fulfil their promise when they promise; and [those who] are patient in poverty and hardship and during battle. Those are the ones who have been true, and it is those who are the righteous.”

(Sahih International: Al-Baqarah 2:177)

Al Azraq & Ahmad (1980) mentioned that *Siyasah Syariah* is a complete guidance for humankind including a fair and justice manner in wealth management, either in the process of acquiring it or in the process of spending it. Verse Q2:188 in the Quran provides a comprehensive and clear statement on this matter as cited below:

*“And do not consume one another's wealth unjustly or send it [in bribery] to the rulers in order that [they might aid] you [to] consume a portion of the wealth of the people in sin, while you know [it is unlawful].”*

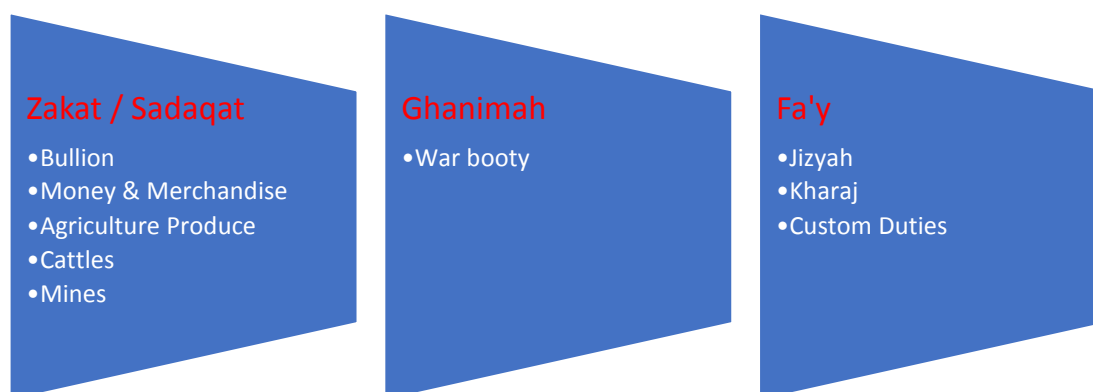
(Sahih International: Al-Baqarah 2:188).

Hence, in fulfilling the state obligations to manage the country and at the same time meeting the basic needs / welfare of its citizens, it is timely to relook at the model and wisdom of past leaders in imposing indirect tax policy.

**CLASSIFICATION ON SOURCES OF REVENUE BY ABU YUSUF YAQUB BIN IBRAHIM  
(D. 798 A.D.)**

Figure 1

*The classification on sources of revenue by Aby Yusuf*



Source: Azmi, S. (1995)

In Islam, the primary source of law is the Noble Quran which established the moral and ethical foundation of Muslim community. With its complete guidance for Muslims in fulfilling obligations, The Prophet, Caliphs and exegetes elaborated these obligations and analyse the fundamental issues in Islam. Hadiths of Prophet Muhammad (PBUH) interpret and clarify areas that seem unclear in the Quran during which the Prophet giving guidance about among others property related issues, collection and usage of tax, etc. Jurisprudence is based on divine revelations, independent reasoning or analogical deductions and consultations.

As shown in the graphic above, some of the taxable items are mentioned in the Quran or by Prophet himself, while others have been added or altered in later years by subsequent Caliphs. The customs duties on trade articles classified under Fa'y category, were introduced by Caliph Umar initially towards Harbi traders at certain entry points of goods to reciprocate the same rate imposed on Muslim traders in Harbi's land. It was later imposed on Dhimni and Muslims traders when he observed the increasing trade activities within the Muslim territory and particularly between the Muslim and Harbi lands.

## **MODEL OF A GOOD TAX POLICY FROM ABU YUSUF YAQUB BIN IBRAHIM'S ECONOMIC THOUGHT**

Abu Yusuf's ideas regarding fiscal issues were based on Islamic principles of equity and justice with primary concern on the maintenance of a healthy treasury and interest of the people (as shown in the Figure 2). For this, he had frequently quoted the verses of Quran, Sunnah of the Prophet and practice of pious Caliphs especially Caliph Umar. He further laid down canons of taxation on which taxes should be collected i.e. fairness, justices, equity, convenience and ability to pay.

The underlying principles emphasized by Abu Yusuf to fulfil the above can be summarized as follows:

- i. Quality of tax administration, honest and just dealing of tax payers and fair distribution of income.
- ii. Defining tax base and tax rate
- iii. Approach to the tax equity
- iv. Flexibility in imposing the taxes; and
- v. Fair distribution of income

The above principles are clear indications that Abu Yusuf main focus pertaining to tax collection and its disbursement was the quality of tax administration and equity as well as justice. Ultimately, these principles would be able to fulfil state obligations with sufficient revenue while protecting the interest of the people at large.

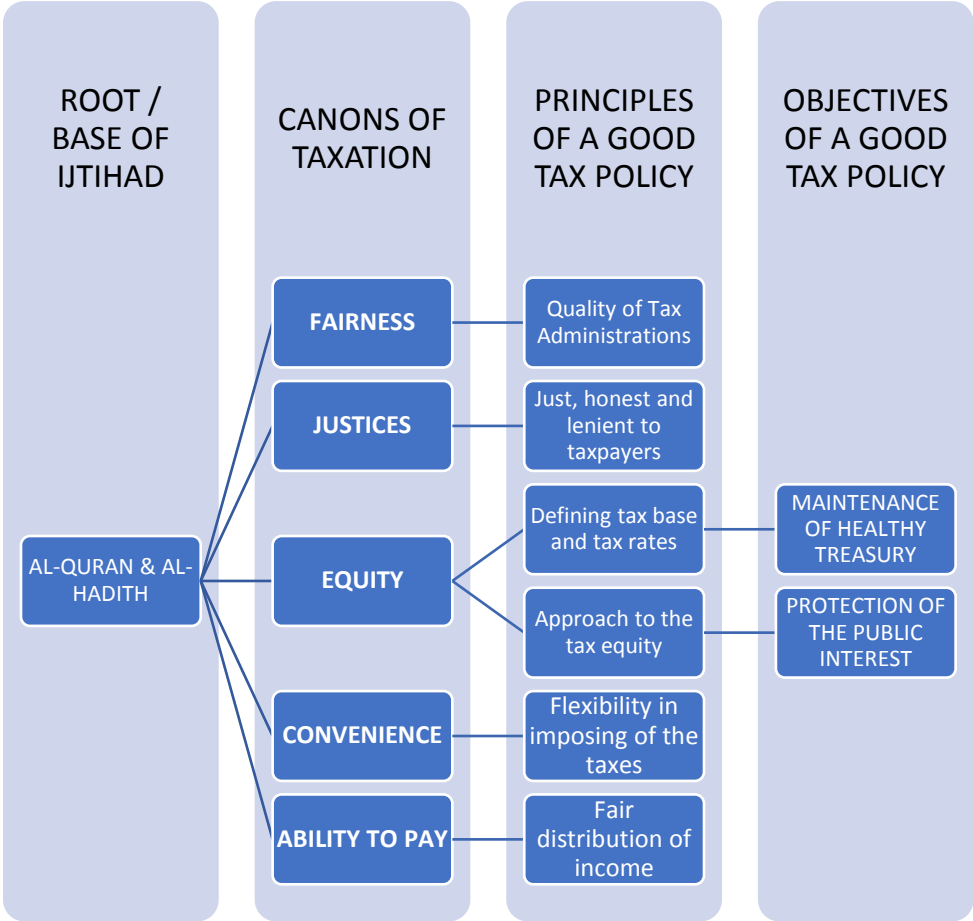


Figure 2  
 Abu Yusuf Yaqub Bin Ibrahim’s Model of A Good Tax Policy

Source: Azmi, S. (1995)

**COMPARISON OF OTHER ISLAMIC SCHOLARS THOUGHT ON THE PRINCIPLES OF A GOOD TAX POLICY BASED ON ABU YUSUF’S FRAMEWORK**

Public Finance is one of the major theme which has been widely discussed in classical Islamic writings. However, it is surprising that Abu Yusuf’s economic thought laid out in his Kitab Al-Kharaj missed the attention of researchers. We managed to come across the recent research done by Mauluddin (2015), which reinstate Islamic Scholars thoughts, namely Yusuf Al-Qardhawi and M. Umer Chapra pertaining to the wisdom and principles in imposing the taxes by the state (as shown in Table 1). Al-Qardhawi outlines 4 conditions of just / fair tax and must be supported by all citizens; i.e. tax as a means of income for nation’s wealth and there are no other sources available, just and fair burden among taxpayers, income collected is to be used for the wellbeing of the citizens and not for sinful use, and finally consent from

Islamic Scholars and experts to be sought before imposing such tax. While Chapra outlines 3 conditions of just in imposing tax; tax imposed to finance necessity needs for the sake of realising ‘maqasid syariah’, an affordable rate not to burden the citizens and impose equally among eligible taxpayers, and to use the collections diligently.

Table 1

*Comparison of Other Islamic Scholars Thought on The Principles Of A Good Tax Policy Based On Abu Yusuf’s Framework*

<b>ABU YUSUF YAQUB BIN IBRAHIM</b>	<b>YUSUF AL-QARDHAWI</b>	<b>M. UMER CHAPRA</b>
Quality of Tax Administrations	Tax as a means of income for nation’s wealth and there are no other sources available.  Consent from Islamic Scholars and experts to be sought	Tax imposed to finance necessity needs for the sake of realising ‘Maqasid Syariah’
Just, honest and lenient to taxpayers  Defining tax base and tax rates  Flexibility in imposing of the taxes  Approach to the tax equity	Just and fair burden among taxpayers	An affordable rate not to burden the citizens and impose equally among eligible taxpayers
Fair distribution of income	Income collected is to be used for the wellbeing of the citizens and not for sinful use	To use the collection diligently

## CONCLUSION

As noted in the introductory chapter of this paper, the fiscal policy and development of Public Finance based on Syariah principles have been practiced by Prophet Muhammad (PBUH) followed by Caliphs and past leaders. However, only in eight century A.D. that the manuscript of the fiscal system being written by Abu Yusuf Yaquub bin Ibrahim, the Chief Justice of Abbasid Caliphate. With active involvement in public life and practical problems, his works represent high degree of pragmatism and practical wisdom. His work outlines the fiscal system which emphasized the economic responsibilities of the Ruler, principles of efficiency, equity and justice in tax administration.

He suggested that the economic life of people is the role of the state which the state should work for the general prosperity of the people while maintaining growth of the economy. Some



of the important functions of the state is to ensure the efficiency and equity of tax collection as well as proper administration of public revenue and expenditure. He stressed the need to preserve the individual interest as well as the requirement of the treasury in suggesting the imposition of different taxes.

His economic thoughts derived from noble source of Al-Quran, practice of the Prophet (As-Sunnah) and Caliphs especially Caliph Umar and laid down the principles of fairness, justices, equity, convenience and ability to pay in outlining / imposing taxes. Ultimately, it fulfil the state obligations to protect the interest of the people and benefit of the treasury.

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