

Application of Islamic Financing Options in the Operations of Yobe State Cooperative Multi-Purpose Society (YSU-CMS)

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Abstract

According to Nigerian Cooperative Societies Act, (2004), a Cooperative Society is a voluntary association of individuals, united by common bond, who have come together to pursue their economic goals for their own benefits. The Islamic co-operative finance system involves coming together to raise halal fund by people of similar ideology and orientation, who contribute their gains in monetary terms to establish a business on profit and loss sharing basis and give loans to members based on mutual understanding without attaching any form of interest. The Yobe State University Cooperative Multi-Purpose Society (YSU-CMS) aims at promoting socio-economic well-being of its members and providing them with economically viable ventures and loan opportunities. This paper aims at assessing the operations of YSU-CMS in the light of the general principles of Islamic Finance, in order to find out whether it is in conformity with the Islamic teachings or not? In addition, it highlights the general principles that the Islamic co-operative finance system should follow. The researcher adopted analytical and descriptive approaches in this study. The main findings of the paper have shown that some components of YSU-CMS are in conformity with the dictates of Sharia, while others vary. It also revealed that the application of Islamic modes of financing from the angles of Islamic microfinance (ISMF) operations provide base upon which YSU-CMS products can be converted into *Shari'ah* – compliant products.

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INTRODUCTION

There are various sources through which funds could be generated to finance an investment, but the most reliable sources are interest free co-operative societies. Interest-oriented co-operative societies create a great sense of fear and psychological imbalance on loan seekers and loan-takers in the sense that there is no objectivity in the arrangement. It is based on speculations and uncertainties. This is why it has become a common-knowledge that the conventional co-operative society cannot rescue those who hold headlong to it for salvation from their financial mess.

The basic characteristics of the Islamic interest-free co-operative society are: amassing wealth from halal source, engaging in profit-oriented halal investment; prudence financial management and granting interest-free loan to members based on mutual understanding. Islam enjoins co-operation in all acts of righteousness, as stated in to the Holy Qur'an,

".....Help you one another in Al-Birr and At-Taqwa (virtue, righteousness, piety); but do not help one another in sin and transgression. And fear Allah. Verily, Allah is Severe in punishment" (Q5:2).

The investment products offered by the Yobe State University Cooperative Multipurpose Society (YSU-CMS) are to a large extent *Shari'ah* compliant, though the law establishing it did not describe the products on that basis. This paper outlines the applicability of Islamic modes of financing in the operations of YSU-CMS. It will also suggest some adjustments that will guarantee the compatibility of the products with Islamic financial instruments.

The paper will be presented in five major sections starting with the conceptual overview of cooperative society. This will be followed by brief history of cooperative movement in the second part and Islamic point of view on Cooperative Society in the third part. An outlay of the operational framework of YSU-CMS will be presented in the fourth part categorized into loan scheme, real estate, trading and investment financing. The fifth part is a presentation of financing modes in Islamic system applicable to the YSU-CMS products as *Shari'ah* compliant and their applications upon which the paper concludes.

Cooperative Society as a Concept

Etymologically, the term co-operation is derived from the Latin word *co-operari*, where the word 'co' means 'with' and *operari* means 'to work'. Thus, co-operation means working together. According to the International Labor Organization (ILO), cooperative society as an association of

person usually of limited means, who have voluntarily joined together to achieve a common economic end through the formation of a democratically controlled business organization, making equitable share of the risk and benefit of the undertaking. This has been modified by the General Assembly Act of 1995, as "an association of people with common economic interest, who have agreed to create a financial pool out of which they lend money among themselves at a reasonable interest rate.

Furthermore, the International Cooperative Alliance (ICA), which is the apex body for cooperative movement in the world also defined cooperative in its General Assembly held in Manchester in 1995, as "A co-operative is an autonomous association of persons united voluntarily to meet their common economic, social, and cultural needs and aspirations through a jointly-owned and democratically-controlled enterprise" (Munker, 2013).

Gatawa and Aliero, (2015) opined that a cooperative society is basically an organization for the establishment of a self supporting community, owned by and operated for the benefit of those using its services.

From the foregoing definitions on cooperatives therefore, a cooperative society is as a business that is owned and controlled by the people who use its services and whose benefits are shared among the people with a view of enhancing social inclusion, social protection and community-building.

Historical Overview of Cooperative Societies In Nigeria

The concept of Cooperative has existed in Nigeria before the coming of the White men; almost every Ethno-linguistic Group in Nigeria has its own traditional informal financial organizations variously referred to as "*adashi*" "*esusu*" or "*isusu*" in the local languages.

These Traditional Cooperatives institutions had been exported as far as other West Africa and Central African Countries, and they cover all human Societies from Marketing, Credit, Consumer, Building, Group Farming, Craft Workers' societies (Nwagbara, 2018).

According to Gatawa and Aliero, (2015) the history of cooperative movement as a social and economic change began in Europe as a reaction to the early 19th century industrial revolution. This Industrial Revolution and the increasing mechanization of the economy that transformed society threatened the livelihoods of many workers

and forced many skilled and unskilled workers into poverty trap.

This situation has therefore taught these workers to come together by pooling their resources to open a shop selling food items they could not otherwise afford. They struggled to pool together one pound each, within three months they did not only started the shop but have also been able to introduce a variety of items in the shop. This development gave rise to some form of movements which metamorphosed to cooperative movement. Thus, Cooperative communities are now wide spread around the world with very many success stories to tell.

In Nigeria, the modern cooperative system was introduced in 1926 when the Ministry of Agriculture in the Colonial Government of Sir Graeme Thomson recognized and re-organized the Cocoa Producers' Cooperative of Agege Planters' Union and Egba Farmers' Union in the Cities of Abeokuta and Ibadan into Marketing Cooperatives to drive the sales of their Produce. Later in 1935, the Cooperative Societies Ordinance was introduced, as a legal framework for the operations of cooperative societies in Nigeria.

From 1936- 1956, formal cooperatives have spread from the western to the eastern and northern parts of Nigeria. It is however, important to mention that the idea of cooperative movement is yet to gain popular recognition in the Northern part of Nigeria when compared with their Eastern or Western counterparts (Gatawa and Aliero, 2015).

Marx and Seibel, (2012) concluded that cooperative societies based on indigenous savings and credit associations were more effective in mobilizing personal savings and in terms of all other economic indicators than cooperatives without such a basis. Therefore, cooperatives societies have an important role to play in the economic system for the efficient development of any industry in Nigeria, since they combine the personal, collective, and public interests.

Cooperative Society from an Islamic Perspective

The concept of Cooperative societies could be classified based on the Qur'anic concept of *ta'awun* (i.e. Cooperation) which was derived from *Suratul-Mai'dah*, Allah says:

“.....*Help one another in Al-Birr and At-Taqwa (virtue, righteousness, piety); but do not help one another in sin and transgression. And fear Allah. Verily, Allah is Severe in punishment” (Q5:2).*

This implies to cooperate and support one another in various facets of life as long as such mutual cooperation is based on piety and

righteousness. This principle of cooperation is also in line with Prophetic teaching of being ones brother keeper. Related to this principle is the concept of *Ukhwah* (Brotherhood) – Q49:10 with far reaching implications for the type of faith and Islam being practiced today by Muslims (Mustafa, D. and AbdulSalam, H. 2017). This modern economic institution contributes in no small measure towards strengthening the business enterprising spirit and the principle of social solidarity, which promotes and enhances the social security system of the *Ummah*.

Furthermore, Sadeq (1990) identified the principle of cooperation as significant for the economic prosperity of Muslim nations. According to him, cooperation among Muslim countries is a requirement in the Islamic code of life. It would provide the enabling environment for development in socio-economic spheres without going into the politico-economic and socio-cultural dominance of the non-Muslim and often anti-Islamic nations of the world.

At this juncture, it could be deduced that the virtues and objectives of cooperatives are largely in line with *maqasid ash-Shari'ah* (objectives of the *Shari'ah*). Thus, the operation and activities of cooperatives in Muslim countries could therefore be justified. However, the elements of *riba* (interest), prohibited business ventures like pork, alcohol, prostitution and a host of others shall certainly be considered unlawful for Islamic cooperative societies.

In a nutshell, Islamic co-operative societies could be formed to satisfy the personal financial needs of members and to provide interest free loans to meet certain contingencies. Hence, its socio-economic importance cannot be under estimated as it promotes mutual cooperation, economic empowerment and social development (Badamasi, S. and Dahiru A. 2017).

Operational Framework of YSU-CMS: Islamic Perspective

The history of Yobe State University Multipurpose Cooperative Society (YSU-CMS) could be traced back to June 2015, when members of the Academic Staff Union of Universities (ASUU), Yobe State University Branch resolved to establish an investment fund that could be used for low risk investment. This is what metamorphosed into Yobe State University Multipurpose Cooperative Society (YSU-CMS) in 2018. It has started with a membership of 168 members and was registered at the department of cooperatives of the Ministry of Youth and Sport, Yobe State.

As a cooperative multipurpose society, it began with a few services which include trade financing, real estate financing and benevolent loan scheme. Since its inception, the society has been growing from strength to strength. In terms of membership it has risen from its founding 168 members in 2015 to 280 registered members; it has total assets of about 20 million Naira as at August end 2019.

The services provided by the Yobe State University Multipurpose Cooperative Society (YSU-CMS) could be categorized under three broad headings as follows:

a. Trade Financing

This service is undertaken under a number of activities as discussed hereunder:

1. Main Supply:

This facility is pure trading business, where YSU-CMS will purchase items required by the members in-bulk and resale to them to members at a profit margin.

2. Shop Supply:

This is an arrangement between cooperative and some provision stores outside. where YSU-CMS will purchase items required such items bevarages, food items, cooking oils, etc. by the members in-bulk and resale to them to members at a profit margin, with a maximum repayment period of three (3) months. For now this facility is conducted in shop supply.

3. Sallah Ram Supply:

This facility encompasses supply of Sallah rams to members at a profit margin with a maximum repayment period of three (3) months.

b. Real Estate

Under this scheme there are two major areas of intervention which are housing scheme and acquisition

1. The Land Acquisition Scheme:

The Land Acquisition Scheme is a situation where the cooperative will buy pieces of land with the hope that the land will appreciate in future and be sold on profit. If alternatively a member is interested it will be sold to him at a profit margin.

2. Cooperative Housing Scheme:

Under this facility, 82 Members of ASUU Village Initiative were given a loan of total sum of N3,000,000 for the purchase of 14.68 hectares of land. This arrangement targets at building houses for interested members under National Housing Scheme based on specified guide lines.

c. Loan Scheme:

According to article 34(iii) of YSU-CMS, the

rates of interest on loans shall be as recommended by Management Committee and approved in a General Assembly. In case of default in repayment, penalty will be an amount twice the normal rate. In line the aforesaid provisions, two benevolent loan facilities are introduced and made accessible to all members of the YSU-CMS without attaching any form of interest. They are as follows:

1. Soft Loan Scheme:

This facility allows a member to access a benevolent soft loan at zero interest rate under the following conditions:

- a) The applicant is not indebted to YSU-CMS
- b) The amount should not exceed 50% of his/her total contribution.
- c) The applicant applies using recognized form for soft loan (free of charge)
- d) The applicant has not previously defaulted his repayments
- e) The applicant agrees to repay within a maximum period of five months

2. Special Loan Scheme:

This facility also allows a member with special socio-economic or educational need to access a benevolent special loan at zero interest rate under the following conditions:

- a) The applicant is not indebted to YSU-CMS
- b) The applicant must prove his/her special need
- c) The applicant applies using recognized form for special loan (free of charge)
- d) The applicant has not previously defaulted his repayments
- e) The applicant agrees to repay within a maximum period of twenty months
- f) The applicant must produced two guarantors among members of the society

d. Islamic Perspective

Having looked into the services offered by the Yobe State University Cooperative Multipurpose Society (YSU-CMS) from Islamic perspective, it is evident that both the trade financing and real estate scheme are to a large extent *Shari'ah* compliant, though the law establishing it did not describe the products on that basis. However, the loan scheme currently does not involve any interest on both soft and special loan schemes; though the Bye Law of YSU-CMS made provision for interest.

According to article 34(3) of YSU-CMS Bye Law (2018), the rates of interest on loans shall be as recommended by Management Committee and approved in a General Assembly. In case of default

in repayment, penalty will be an amount twice the normal rate. Once this provision is put into effect, it will contradict basic principles of Islamic finance.

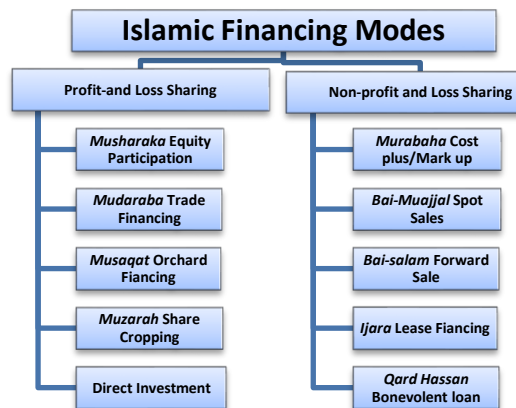
According to Chaudhry (1999), Islam considers interest as the most exploitive institution for humanity and has abolished its roots in its every form and manifestation. According to the Holy Qur'an taking of interest is tantamount to war against God and His Apostle. Allah says:

“O ye who believe, fear Allah, and give up what remains of your demand for usury, if ye are indeed believers. If ye do not, take notice of war from Allah and His messenger: but if ye turn back, ye shall have your capital sums; deal not unjustly, and ye shall not be dealt with unjustly”. (Q2:278-279).

In a nutshell, certain elements of conventional cooperative societies, which negates the basic principles and ethics of Islamic financial system shall be abhorred and considered illegal. Among such elements that will fall within this category are: business and activities relating to *riba*, alcohol, pork, prostitution, pornography among others.

Convertibility of YSU-CMS Products into Islamic Financing Modes

The holy Quran declares trade to be lawful means of livelihood as opposed to *riba*, which is forbidden for being oppressive and exploitative. The financing modes in Islamic financial system are categorized into three: concessionary, participatory and trade financing respectively. The three categories are similarly classified into another two broader categories; profit – loss sharing and non-profit-Loss sharing (Iqbal and Mirakhor (1987).



Adopted from Mizanur Rahman, 2017

- a. Profit and loss sharing Modes:
The following are most commonly practiced profit and loss sharing modes:
 1. Musharaka Equity Participation
Musharakah is an equity participation mode of contract involves partners providing funds for

a venture, with profit and loss shared according to an agreed ratio in accordance with their capital contributions. There are many modes under this instrument, but the most suitable for Islamic Cooperative societies is the diminishing *Musharakah*. It is a recent development where a financier and the client participates either in joint ownership of a property/equipment or in a joint commercial enterprise. A share of financier is further divided into units of the share and gradually periodically till the entire units of the financier are purchased by the client. Eventually, the client become the sole owner of the enterprise (Gatawa and Aliero, 2015).

2. *Mudaraba* Trade Financing
A *Mudarabah* transaction is an investment partnership which implies contract between an investor (or financier) and an entrepreneur or investment manager known as the *Mudarib*, who is responsible for the management of the business and provides professional, managerial and technical expertise for initiating and operating the business enterprise or project. In this contract, risk and rewards are shared. In the case of a profit, both parties receive their agreed-upon share of the profit. In the case of a loss, the investor bears any loss of capital while the *Mudarib* loses his time and effort (Obaidullah, 2006).
3. *Musaqat* Orchard Financing
Musaqat is a type of partnership in which the owner of an orchard agrees to share a stipulated portion of the produce of the orchard's trees with a worker, in exchange for the latter's irrigation of the garden. This mode could also be suitable for Islamic Cooperative societies financing (Gatawa and Aliero, 2015).
4. *Muzara'ah* Share Cropping:
Muzara'ah is an output-sharing contract specifically for agricultural production where a land owner provides a piece of land and a client contributes efforts and expertise to grow a crop therein. The total yield (ghallah) of the land is divided between the two partners according to specific percentages. This transaction achieves the interests of both parties (the land owner and the agent). The land owner may not be able to cultivate its land or work in it. The agent may not have the land he needs to employ its resources. This mode could also be suitable for Islamic Cooperative societies financing (Gatawa and Aliero, 2015).
5. Direct Investment
Generally, Islam encourages investments in

any fund whether personal or public; with the aim of safety and maintenance of fair returns on amount invested, but such investment must be free from any element of prohibition (Sayyid Sabiq, 1983). Unlike conventional financial institutions, financing in Islam is always asset-based financing which creates real assets and inventories, since money is not regarded as a subject matter of trade except in some special cases. Therefore, all investments under Islamic cooperative society must be asset-based.

- b. Non-Profit-and-Loss Sharing Modes:
The following are most commonly practiced non-profit and loss sharing modes:
 1. Murabaha Cost plus/Mark up
According to Afaanah, (1996), a *Murabahah* transaction is a sale at a stated profit. It entails that the investor purchases an asset from a third party and sell it to the client at a stated profit on a spot or deferred payment basis. This instrument is relevant to Islamic cooperative society; the society will stand as the investor so as to buy the asset from the third party and sell it to the client based on agreed upon profit.
 2. Bai-Muajjal Spot Sales
Bai' Mu'ajjal is a deferred payment sale contract in which the parties agree to payment of the price at a time in future. A deferred payment sale contract is valid if the date of payment is set unambiguously. That means, the date can set with reference to a specific date (e.g., December 24) or a specific period (e.g., six months from the date of delivery of goods or services, thus if there is ambiguity in the date of payment, the sale is considered void. The deferred price could be set higher than the spot price as long as the price is set at the time of purchase. In an interest-based system, the seller would impose penalties (interest) on the buyer in case of a late payment. Such would not be permissible under Islamic financial system (Usmani, 2016).
 3. *Bai-salam* Forward Sale:
Salam is a forward sale contract where the full price of the goods is paid in advance at the time of contract but can be delivered at a specified time in the future. It is similar to a modern forward sale contract. Under Islamic financial system, a sale cannot normally be effected unless the goods are in existence at the time of the contract. However, this type of sale is an exception provided the goods are defined and the time of delivery is fixed. This mode of financing is often applied in the agricultural

sector and covers all tangible goods which are capable of being definitely described as to quantity, quality and workmanship. Therefore, Islamic cooperative society can advances money without interest for various inputs and in exchange receives a share of the produce, which it then sells after delivery or sell the goods to a third party before delivery through a parallel contract of Salam (IIBI, 2019).

4. *Ijara* Lease Financing

Ijarah, lexically refers to leasing or to give something on rent. In Islamic jurisprudence, however is used for two different situations. Firstly, to employ the service of a person on wages. Secondly, it relates to *usufructs* of assets and properties. In this context, it refers to transfer the *usufruct* of a particular property to another person in exchange for a rent claimed on him (Obaidullah, 2006). As in a normal lease transaction, a lessor who owns the leased asset will lease it to another party (the lessee) in exchange for payment of rental. The lessee will get the full benefit of using the lease asset within the specified period for as long as he adheres to the lease terms and conditions. At the end of the lease period, the leased asset will be returned to the lessor. There are some other variants of leasing which incorporate the transfer or option to transfer ownership of the leased asset from the lessor to the lessee at the end of the lease period; these are referred to as; *Ijarah Thumma Bai* - Lease Agreement Incorporating sale of leased asset at the end of the lease period.

Ijarah Muntahiya Bil Tamleek - Lease Agreement with option to own the leased asset at the end of the lease period.

Ijarah Wa Iqtina - Lease Agreement with option to acquire the leased asset at the end of the lease period. It is often used in the context of home purchasing.

5. Qard Hassan Benevolent loan

This refers to a virtuous loan that is interest-free and extended on goodwill basis, mainly for welfare purposes, the borrower is only required to pay back the borrowed amount. Islam allows loan as a form of social service among the rich to help the poor and those who are in need of financial assistance. A debtor may voluntarily choose to pay an extra amount to the lender/creditor over the principal amount borrowed (without promising it) as a token of appreciation (IIBI, 2019).

CONCLUSION

It has also been proven beyond reasonable doubt that Islamic economy has a very sound financial system, which is ethically oriented, asset-based and linked to real economic activities. The system also emphasizes that any financial dealing involving gambling, dealings in pork, alcohol, ammunition, pornography and any other unethical products, goods or services are non-permissible.

The concept of Islamic co-operative as it is being practiced in other countries is comparatively new in Nigerian society, and thus it has not been fully understood even by many Nigerian Muslims. Consequently, there is a need for both Muslims and non-Muslims to be informed on how the practices of Islamic Co-operative in Nigeria differ from conventional ones especially in their operations to provide the incentive needed for conventional co-operative members to consider establishing Islamic co-operative.

However, Islamic co-operative has no religious inbuilt discrimination and its products are available and accessible to anybody regardless of belief. Consequently, members under the YSU-CMS should start making a collective effort towards establishing a Shariah compliant cooperative society, so as to douse the apathy among them to accept a cooperative society that suits their preferences and recognizes their religious values and beliefs.

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