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HETTER ISKA

Charging interest (*ribbit*) on a loan made to a fellow Jew is prohibited by the Torah.[1] The rabbis compare the severity of this transgression to the denial of the Exodus from Egypt.[2] Those guilty of committing the offense are included in the category of those held as unworthy of participating in the eschatological Resurrection.[3]

In this article we examine the basic features of this prohibition to show how the legal device of a *hetter iska* makes it possible for observant Jews to function in the modern business world.

There are four types of *ribbit*: (1) *ribbit deoraita* (biblically prohibited interest), which is frequently termed *ribbit ktzutza* and is violated only when two distinct conditions are satisfied: (a) there must be an outright loan (*derekh halvaah*)—not simply a profit accruing from a sale; and (b) the interest must be explicitly stipulated—excluding, for example, a gift made by the borrower either before or after the loan was granted;[4] (2) *ribbit d'rabonon*, which is interest forbidden by a rabbinic extension of the law and is frequently referred to as "dust of interest" (*avak ribbit*); among items covered by this prohibition is interest received in the course of a business transaction (*ribbit derekh mekakh umemkar*);[5] (3) *mehze k'ribbit* (the appearance of *ribbit*) such as the seizing of a debtor's slave and utilizing his services;[6] and (4) *ribbit dvarim* (interest in terms of words); where the lender does not receive actual money or objects of value but is treated deferentially or given other honors by the borrower.[7]

The Talmud (*Baba Metsia* 61a) notes that, had the Torah not specifically forbidden *ribbit*, the prohibition could not have been deduced from the prohibition of robbery, since the borrower had freely agreed to pay *ribbit*. By the same token, the prohibition against receiving interest could not have been derived from the prohibition against fraud, since the borrower freely and knowingly agrees to the arrangement.

In the course of regular business activities, these prohibitions are

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often violated. Vendors frequently reduce prices in exchange for immediate cash payments. This clearly constitutes *agar natar* (payment for waiting).[8] In such cases, if the customer postpones payment, the vendor is rewarded for waiting for his money, or the buyer is rewarded for his willingness to wait for late delivery in return for a reduction or price.[9] If the item involved is one in which there is a fixed price that is commonly known, *shumato yadua*, this practice is forbidden even if the terms were not actually stipulated in advance.[10] Dealing with a bank or insurance company owned by Jews may involve violations of prohibitions against *ribbit d'rabonon* (i.e., when one purchases a home with a mortgage or when interest-bearing returns on premiums are left with the company). The only way in which the problem can be avoided is to transform the entire transaction into one where the earnings are treated as profits and not interest. This is the underlying rationale of the *hetter iska*. But before we can resort to a *hetter iska*, one must understand the operation of its basic mechanism since, according to many *poskim*,[11] awareness of the terms of the *hetter iska* is indispensable to safeguard against violation of the prohibition of *ribbit*. Similarly, if the parties involved merely treat the *hetter iska* as a formality but have no intention of abiding by its conditions they, too, violate the prohibition against the taking of interest.[12] This can be compared with the *Shulhan Arukh's*[13] treatment of the sale of *hametz*, when the seller locks the door of the room in which the *hametz* is stored. Such an act negates the sale. There is no real intention of selling the *hametz*, even though the sale has been completed according to halakhic stipulations.

The Mishnah (*Baba Metsia* 68a) describes an *iska* (a joint business venture in which a creditor invests money with a borrower and refuses to share both profits and losses) as follows: "One may not commission a tradesman on half-profit basis unless one sets the wage as a worker." In the words of the Talmud (*Baba Metsia* 106b), an *iska* constitutes a half-loan and a half-trust. A borrower takes his profits or losses from the loan part. The creditor accepts responsibility for the trust part, on which his profits or losses are based. This type of venture, however, is forbidden unless the commissioner pays wages to the borrower. Without such an arrangement, the free labor provided by the borrower in working to sell or invest the loan part of the transaction would be considered interest, for it represents reward for the loan received. The borrower may not forego the wages for his labor, since payment of *ribbit* is not permitted even with the approval of the borrower. But, since the *iska* involves only *ribbit d'rabonon* and not *ribbit deoraita*, the sages are satisfied with the payment of the relatively small amount of wages that are due to an unemployed

worker (*k'poel batel*).[14] If, for example, a carpenter accepted a commission to sell provisions as part of the *iska* he must, in addition to the 50 percent profit, be paid the amount that an average individual can command for changing from a more strenuous type of labor to a work of a lighter nature[15] (Rashi, Rif; Tosafot, however, provide a different explanation).[16] Actually, this type of payment is necessary only when no arrangement for payment of wages was made before the parties embarked on the joint business venture; however, if stipulated in advance, even as small an amount as a *pruta* would be sufficient to avoid the prohibition of interest.[17] Another option available would be to stipulate that while the parties will distribute the profit evenly, the laborer would receive an additional percentage as wages. Another alternative would be an arrangement where the investor receives a higher proportion of the risk and a lower proportion of the profit.[18]

Another form of *iska* relates to situations where a commissioner entrusts a laborer with a certain amount to be used to earn profits for the commissioner, with the proviso that the "trust" be converted into a loan whenever the profits reach an amount agreed on by both; from this point on, all profits belong to the laborer. The investor transfers to the borrower $100 at the investor's own risk and stipulates that once a profit of $100 is made, the entire sum of $200 is turned into a loan, with the borrower then assuming all risks. But the borrower must receive the wages for his work performed during the "trust" period of the venture. They may also enter this type of *iska* in a different manner. In the first period the funds are treated as a loan and the profits go entirely to the laborer; subsequently, when a mutually agreed on amount is reached, the original investment is converted into a trust, and the profits belong to the investor.[19]

Two basic forms of *iska* are permitted: (1) the invested funds are divided into trust and loan portions, with the profits of the former belonging to the investor and of the latter to the laborer; and (2) the time period of the *iska* venture is divided between loan and trust. During the trust period, the profits belong to the investor; during the loan period, they belong to the borrower. The order of the respective loan and trust periods is of no consequence. In essence, the *hetter iska* transforms what normally would have been an ordinary loan into a joint business venture, with investors and borrowers agreeing to share both profits and losses. The lender becomes the investor and the borrower becomes the commissioner who, in turn, becomes a trader or salesman on their joint behalf. The borrower is compensated for his labor, and thus the prohibition of *ribbit* is avoided in this form; the profit received by the lender represents not interest but

a regular financial profit obtained through a business transaction.

Yet a real business transaction must allow for the possibility that the lender may actually lose his investment; otherwise, the *hetter iska* is nothing but a fiction. In fact, some *poskim* question the *hetter iska* inasmuch that neither party has any real intention of forming a joint business venture.[20] But, in the opinion of most authorities, the transaction is permissible because theoretically the lender may actually exercise this option.

In view of the fact that the *hetter iska* is based on the possibility that the lender may suffer a loss, it is desirable to devise a procedure that would reduce the risks of losing one's "investment." Basically, there are two methods available. In the first, the lender stipulates that any claim of loss on the part of the borrower must be proved by two reliable "'witnesses"; otherwise the entire principal must be returned to the lender. In the second, the creditor imposes on the borrower extremely difficult conditions. He may, for example, require him to store the money underground and furnish witnesses that this condition was satisfied. In the event that the debtor fails to follow these instructions, the borrower becomes liable for the amount of the original investment. According to many *poskim*, such conditions may be imposed even though the lender knows in advance that the borrower will not adhere to them.[21]

It must be noted, however, that there remains the theoretical possibility that the borrower will be able to prove that he sustained a loss or that he really adhered to the conditions, in which case, the lender might suffer a loss.

A similar approach may be utilized by the lender to insure his profit. The borrower agrees to pay the lender half the profits; it is further stipulated that the borrower must prove to the lender's satisfaction that he is paying him the entire amount due him. The lender, in turn, would stipulate that the only proof acceptable is an oath. However, the lender offers the borrower the opportunity to be released from his obligation to take an oath (many individuals are hesitant to take an oath) through a payment of a mutually agreed on amount.[22] In this case the *hetter* rests on the possibility that the borrower will eventually take an oath that no profit was realized.

It is essential that both the lender and the borrower understand the mechanism of the *hetter iska*. The text of the *hetter iska* may not include terms such as "loan" or "interest, " since such expressions would contradict the very essence of the *hetter*.[23] All stipulations and conditions must be in writing. The amount of the principal, not a total sum to be repaid, should be stated since, in the event that no profit will accrue, payment of the full amount would entail violation

of *ribbit ktzutza.*

In the event of the death of one of the parties, the terms of the *hetter iska* continue until payment is made.[24]

Many *poskim* agree[25] that during the *iska* the borrower may not grant any unusual favor to the lender, since this would amount to an indirect reward for a loan (*avak ribbit*). If a loan is secured by a third party, in the opinion of many *poskim*,[26] the obligation to the lender must also involve a *hetter iska* .

A number of authorities[27] maintain that the validity of the *hetter iska* is contingent on the borrower's intention to invest the principal. If, moreover, 50 percent is used for personal objectives, the *hetter iska* is invalid. As soon as the borrower has spent the lender's share of the money (i.e., the trust portion of the money that was entrusted to him for the sole purpose of investing and not for his private use), the trust portion becomes a loan, with the borrower assuming the risk (as is the case with anyone who illegally makes use of an object with which he was entrusted for safekeeping). Consequently, any return of money to the lender ceases to represent profits from the trust portion and becomes "reward for the loan."

A *hetter* applicable for a bank loan for personal and not investment purposes was suggested by Rabbi Moshe Sternbuch.[28] As noted previously, a lender can attempt to insure himself against loss of profit by stipulating that the borrower must take an oath that he did not make a greater profit than stated and, subsequently, declining to take the oath, pay the lender the amount mutually agreed on (*sikum hitpashrut*). In this case the profit is technically treated not as interest but a compensation for relieving the debtor from the requirement of taking an oath. Similarly, the lender could specify that the funds may be used only for *iska* purposes. Subsequently, the borrower may then proceed to spend the money in any manner he sees fit, inasmuch as he will not take the oath but will pay the *sikum hitpashrut*. This method, however, is not feasible if the agreement were to state specifically that the money may be used for rent, food, or any other private needs of the borrower: in such a case the loan agreement would clearly be in contradiction with the *hetter iska*. A similar device has also been attributed to the Tchebiner Rav *ztl*.[29]

It should also be noted that bank deposits as well as bank loans involve questions of *ribbit*. According to Rav Yosef Eliayhu Henkin *ztl*,[30] bank deposits do not involve a violation of the laws, since funds are deposited in a bank primarily for safekeeping. Interest payments are only a secondary consideration, especially since there is no explicit stipulation at the time of the deposit that interest is to be paid. Because only *ribbit d'rabonon* is involved, a *hetter iska* could be used.

There is another mitigating consideration that renders banking less problematic from a religious point of view. Banks are corporations; the members of the management are not individually responsible to the depositor. Hence there is a real possibility that the depositor may even lose the principal, but the prohibition of interest applies only when the lender is guaranteed the return of his money under all circumstances.[31] To be sure, FDIC insurance of bank deposits pose special problems with respect to the applicability of Rav Henkin's *hetter* . However, because not the bank but individual depositors are insured, the problem is not insurmountable.

Rav Moshe Sternbuch, expressing a similar view,[32] applies the *hetter* also to bonds issued by the State of Israel and life insurance companies where the person insured may withdraw his deposits with interest. On the basis of these *hetterim*, one may deposit money in a bank owned by Jews even without a *hetter iska*.

Bank loans and mortagages constitute a more difficult problem, since the borrower is obligated to repay the interest under any and all circumstances. Rav Henkin suggests that interest paid to the bank should be treated not for compensation for the loan but as payment for the bank's overhead. He compares this to the view of the Mishnah (*Baba Batra* 10:3), which obligates the borrower to pay the fee for the writing of the contract.[33] Similarly, the borrower assumes part of the expenses of the bank that provides him with the loan.

There is another consideration that might be invoked with respect to paying interest on a bank loan. One is permitted to offer a person compensation for help to obtain a loan from a third party (*Sekhar amira*; *Baba Metzia* 69b.) In keeping with this reasoning, the bank would be entitled to receive a fee for its services in arranging a loan between the depositors and the borrower; the interest could be defined as this fee. Similar considerations, according to Rav Henkin, could also be applied to charity institutions or non-profit organizations that lend money on interest. It can be argued that interest could be treated as payment toward the expenses of the institution.

Rav Sternbuch permits bank loans on the basis of another reason.[34] He invokes a ruling that has been attributed to Rashi.[35] Accordingly, interest is prohibited only when the transaction is carried on directly between the parties themselves, but not when they employ agents. Since taking interest is prohibited by the Torah, one can no longer apply the legal principle that "An act performed by an agent has the same validity as if it had been personally performed."[36] In criminal cases no individual can be held responsible for the deed of another.[37] To be sure, many authorities strongly disagree with this approach.[38] There is considerable doubt whether Rashi had actually

made the ruling attributed to him. It is argued that the manner in which the lender actually received the money should hardly make any difference. Rashi's contested view is explained by Rav Sternbuch in the following manner.[39] Since only the agent and not the lender stipulates the payment of interest, we are not really involved with a case of *ribbit ketzutza*. The borrower is responsible to the agent and not to the lender. The borrower, in turn, deals only with the management and not with the depositors whose money is loaned. Therefore, even without a *hetter iska*, one would be allowed to borrow from a bank with interest.[40]

Another frequently encountered problem relates to what is termed "interest in the guise of a sale" (*Sekhar hakdamat maot*). The Mishnah (*Baba Metsia* 5:7) prohibits the sale of produce before its market price is established since, by purchasing in advance at a price below the eventual market value, the buyer would in effect receive interest. According to Rav Nachman (*Baba Metsia* 63b), "Any reward for waiting (*agar natar*) is prohibited." Hence any payment received in compensation for having left the money in the hands of another party is prohibited. The Talmud draws a distinction between rent and purchase. Since rent is due at the end of the month, a tenant may receive a discount for paying the rent in advance. But in case of a sale, the payment is determined at the time of the time of the *kinyan*. So the stipulation that the purchaser will receive a better price for prompt payment involves the violation of *ribbit*. In some cases, this liability may be incurred even without explicit stipulation. For this reason, a *hetter iska* would be necessary to legalize practices such as prepublication discount prices.

It must be stressed that in all these cases one cannot satisfy the requirements of a *hetter iska* simply by utilizing at the transaction *al pi hetter iska*. As indicated previously, in order to be valid, the principles governing the operation of the *hetter* have to be understood by the parties.

In conclusion, however, it is important to balance the technical aspects of the *hetter* with other relevant considerations. The Chafetz Chaim *ztl* emphasized that the sacred obligation to lend money to a fellow human being in need without charging interest is by no means obliterated by the *hetter iska*, which legalizes the making of profit through an investment. One should have faith that the Creator will provide us with our needs as rewards for the fulfillment of the *mitsvah*. The *hetter iska* merely protects one against the violation of the prohibition against *ribbit*. It does not absolve one of the obligation to practice *hesed* (loving kindness), which we fulfill to a higher degree when we loan money than when we give charity.

NOTES

1. Leviticus 25: 36-37, Deuteronomy 25: 20-21.
2. *Baba Metsia* 61b.
3. See Tosaphot *Baba Metsia* 70b at its conclusion.
4. *Yoreh Deah* 161, paragraph 5.
5. See *Yoreh Deah* 173-175, *Tur Yoreh Deah* 160.
6. See *Baba Metsia* 65a.
7. *Baba Metsia* 75b.
8. *Baba Metsia* 63b.
9. *Yoreh Deah* 173, paragraph 1.
10. Ibid.
11. See. *Hachmat Adam* 142, paragraph 3; Shaloh in his *Masechet Chullin; Tshuvot tzemach Tzedek, Yoreh Deah* 88; Chafetz Chaim, *Ahvat Chesed, Inyanei Gemilut Chasadim*; Harav Moshe Sternbuch, *Dat V'halachah*, Chapter 5.
12. *Sefer Dat V'halacha*, Chapter 5.
13. *Orackh Haim* 448, Mishna Brura, paragraph 12.
14. *Baba Metsia* 68a.
15. Rashi, ibid.
16. See Tosaphot *Baba Metsia*, ibid.
17. See references in *Brit Yehuda*, Chapter 36, note 8.
18. See *Baba Metsia* 68b.
19. See *Yoreh Deah* 167.
20. See *Ginat Veradim Klul* 6 *Siman* 7. See also *Kuntros Haribit* of the *Smah*, paragraph 22.
21. The first method is that of the Maharam. See the text of his *hetter iska* in *Nahlat Shiva*, Chapter 40. The second method was accepted by the *Ginat Veradim, Yoreh Deah, Klal* 6, paragraph 4.
22. Ibid.
23. *Kuntros Takanat Rabim*, mentioned in *Brit Yehuda*, Chapter 40, note 15.
24. For further detailed application of this halakhah see *Tshuvot Tur Ha'even* 45 and discussion in *Brit Yehuda*, Chapter 38, notes 45-48.
25. *Shulhan Arukh Harav*, paragraph 39. See also *Chavot Daat Yoreh Deah* 166, references in *Brit Yehuda*, Chapter 10, note 7.
26. *Tshuvot Imrei Yosher Cheleck Aleph* 189. *Brit Yehuda*, Chapter 40, paragraph 30.
27. *Shulhan Arukh Harav Yoreh Deah*, paragraph 42. Harav Moshe Sternbuch in *Dat V'halakha*, chapter 5, mentions a ruling by the Chazon Ish.
28. *Sefer Dat V'halakhah*, Chapter 5.
29. Ibid.
30. *Edut L'yisrael*, Ezrat Torah Fund, p. 171.
31. See *Baba Metsia* 63a and Tosaphot there beginning with "*Tzad Echod B'ribbit* ."
32. *Dat V'halakhah*, Chapter 5.
33. *Edut L'yisroel*, ibid.
34. *Dat V'halacha*, ibid.
35. This ruling of Rashi is mentioned in the *Mordechai*, paragraph 338, and Rama, *Yoreh Deah* 160, paragraph 16.
36. *Kidushin*, 41b.
37. *Kidushin*, 42b.
38. *Tur Yoreh Deah* 160, *Bet Yosef*, commentary of Taz on paragraph 16.
39. Loc. cit.
40. *Dat V'halakhah*, Chapter 5.