

- 2 Abdullah and Ismail, *International Financial Law Review*, September 2009 at www.iflr.com, last accessed on 2 December 2009.
- 3 Stichting Sachsen-Anhalt EURO100m Trust Certificates (*sukuk*) rated 'AAA' by Fitch Ratings as reported in the Germany Pre-sale Report, 9 July 2004.
- 4 William Wallis, 'Bankers Learn New Language to Manage Islamic Funds', *Financial Times* (London, 20 October 2004). See, more recently, speech by Clive Briault, Managing Director, Retail Markets, 'London: Centre of Islamic Finance', at the FSA Industry Forum, London, 17 October 2007; and HM Treasury paper, 'The Development of Islamic Finance in the UK: The Government's Perspective', December 2008 at www.hm-treasury.gov.uk , last accessed on 2 December 2009.
- 5 *Quran*, *al-Hadid*: 10; *al-Baqara*: 30; *al-Ahzab*: 72; *Sad*: 26.
- 6 *Quran*, *al-Maida*: 1 (n. 1); *al-Nisa*: 29.
- 7 Ibn Taymiyya, *Al-Fatawa al Kubra* (Dar al-Kutb al Ilmiyyah, Beirut, 1987), vol. 29, 16–18; M.T. Mansuri, *Islamic Law of Contracts and Business Transactions* (Adam Publishers, New Delhi, 2006), 3–4, 14–15.
- 8 Nabil Saleh, *Unlawful Gain and legitimate Profit in Islamic Law* (Cambridge University Press, Cambridge), 144.
- 9 Mansuri, *Islamic Law of Contracts and Business Transactions*, 5–6.
- 10 M. Hashim Kamali, *Freedom, Equality and Justice in Islam* (Ilmiah Publishers, Selangor, Malaysia, 2002), 35.
- 11 Al-Ghazali, *Ihya 'Ulum al-Din* A. 'Izz al-Din al Sirwan (ed.) (Dar al Kutb al Ilmiyyah, Beirut, 1985) sets out five objectives, clearly set out in the *Quran* and *sunna*; the protection of life, intellect, property, honour and conscience of a human being.
- 12 Ultimately, the objectives of the sharia are meant to lead to social welfare and ease (*maslaha*).
- 13 Al-Tirmidhi, *Sunan al-Tirmidhi* (Dar al Fikr, Beirut, 1980), vol.3, 141.
- 14 M. Hashim Kamali, *Islamic Commercial Laws: An analysis of Futures and Options* (Ilmiah Publishers, Selangor, 2002), 67. Kamali explains that it is not sufficient to presume that a contract is forbidden if it is not explicitly forbidden (in the primary sources).
- 15 The translation, in all cases, is insufficient to express the laden meaning of the Arabic text.
- 16 *Quran*, *al-Baqara*: 275.
- 17 *Quran*, *al-Baqara*: 278 (n.1).
- 18 *Quran*, *al-Rum*: 39.
- 19 The gist of the *riba* prohibition, in light of the *raison d'être* of the prohibition, is debatable whether it remains exploitative today.
- 20 El-Gamal, *Islamic Finance: Law Economics and Practice* (Cambridge University Press, Cambridge, Massachusetts, 2006), 51.
- 21 This is categorically stated in the *Quran*, *al-Baqara*: 275 '... those who devour *riba* will not stand except as stands one whom the devil has driven to madness by his touch'.
- 22 See chapter 5 below and El-Gamal, *Islamic Finance*, 50–7.
- 23 *Quran*, *al-Baqara*: 219.
- 24 De Teran, Natasha, 'Derivatives Extend the Reach of Islamic Finance', *The Banker* (25 June 2005), vol. 155, 49–51.

- 25 This highlights the difference between Islamic finance and conventional finance being one of risk sharing as opposed to risk assumption. This, however, does not derogate from the validity of the capital guaranteeing Islamic financial products available in Islamic finance.
- 26 Nathif Adam and Abdulkader Thomas, *Islamic Bonds: Your Guide to Issuing, Structuring and Investing in Sukuk* (Euromoney Books, London, 2004), 28–30. See also El-Gamal, *Islamic Finance*, 144.
- 27 It is said that everything that is to occur or materialise in the future is uncertain.
- 28 Adam and Thomas, *Islamic Bonds*, 28.
- 29 This argument is dealt with at length in chapter 6 and effectively negated.
- 30 Note the difference between predetermined *proportion* of profit and predetermined *amount* of profit.
- 31 Adam and Thomas, *Islamic Bonds*, 67. There ought to be no objection to issuing *sukuk* representing a partial ownership interest in the assets, and with it the relevant share of income or risk of loss.
- 32 For a discussion and critique of such structures of finance, see generally El-Gamal, *Islamic Finance*, 42–5.
- 33 *Quran, al-Baqara*: 275.
- 34 Hashim Kamali, *Islamic Commercial Laws*, 67–8. See chapter 5 on *riba* and chapter 6 on the nature of debt for a complete discussion.
- 35 Rodney Wilson, ‘Overview of the Sukuk Market’, in Nathif Adam and Abdulkader Thomas, *Islamic Bonds*, 3.
- 36 Wilson, ‘Overview of the Sukuk Market’. See, however, discussion in chapter 6, section 6.8 on the ‘asset-backed’ requirement.
- 37 The OIC Academy issued a fatwa concerning aspects of these bonds. See Decision 5 (D4/08/88) of the fourth session, Fiqh Academy Journal 3:2161.
- 38 Although there is no compulsion to comply with the rulings of the Fiqh Academy, they do carry considerable weight with most Islamic financial institutions and their sharia committees and advisers.
- 39 *Quran, al-Baqara*: 282.
- 40 Note that the Academy of Fiqh ruling alludes to the fact that non-personal debts are, to a restricted extent, part of financial assets.
- 41 Sharia Standards published by the Accounting & Auditing Organisation for Islamic Financial Institution (AAOIFI), www.aoifi.com, last accessed 7 September 2008.
- 42 There are many classes of assets in conventional finance that are *halal* as are many of the techniques used in conventional securitisation equally valid in Islamic ones.
- 43 The argument is elaborated on in chapter 8 at section 8.2.
- 44 Muhammad Taqi Usmani, *An Introduction to Islamic Finance* (Kluwer Law International, The Hague, 2002), xiv–xvii.
- 45 We deal with this argument in chapter 4.
- 46 Business loans, consumer loans, student loans, credit card receivables, etc.
- 47 Adam and Thomas, *Islamic Bonds*, 77.
- 48 See discussion on the sale of debt in chapter 6.
- 49 Armstrong, *Islam: A Short History*, 85.

4 *Gharar* in Islamic Law

- 1 The term 'commercial' is used to distinguish commercial transactions from domestic and social agreements, as is commonly done under the common law, for purposes of legal treatment, application and effect. See, E. McKendrick, *Contract Law: Text, Cases and Materials* (2nd edn, OUP, Oxford, 2005), 309.
- 2 Vogel and Hayes, *Islamic Law and Finance: Religion, Risk and Return* (Brill Leiden, Boston, 2006), 87.
- 3 The Hadith is reported through Abu Hurayra Ibn Omar, Ibn Abbas, and Annas Ibn Malik and is contained in Muslim's *Sahih* annotated by Al-Nawawi (d. 676/1277) *Kitab al Majmu'* (Maktabat al-Irshad, Jeddah, 1992), Vol. III, 156.
- 4 Ibn Hanbal indicating that its most correct version is handed down on the authority of Ibn Masoud, not the Prophet himself. See Vogel and Hayes, *Islamic Law and Finance: Religion, Risk and Return* (Brill, Boston, 2006), 88.
- 5 Reported by Bukhari cited in Vogel and Hayes, *Islamic Law and Finance*.
- 6 Reported by Muslim cited in Vogel and Hayes, *Islamic Law and Finance*.
- 7 Reported by Bukhari, Muslim, Abu Daud, Tirmidhi.
- 8 Al-Dhareer, *Al-Gharar in Contracts and its Effects on Contemporary Transactions* (Islamic Development Bank's Eminent Scholars' Lecture Series, Jeddah, 1997), 9.
- 9 Ibid. See also M. Tahir Mansuri, *Islamic Law of Contracts and Business Transactions* (Adam Publishers, New Delhi, 2006), 93.
- 10 The *Quran* uses the root word *gha-rra* and its derivatives such as *ghuroor* frequently in speaking of the deception of the physical world that detracts from works of goodness and belief in eternity. The word *ghuroor*, literally meaning deception, is used, for instance, in *al-Isra*: 64, *al-Luqman*: 33; *al-Hadid*: 20, among many others.
- 11 Al Dhareer, *Al-Gharar in Contracts*, 10.
- 12 Abdel Razeq Al-Sanhouri, *Masadir al Haqq fi al-Fiqh al-Islami* (Dar Ihyā' al-Turath al 'Arabi, Cairo, 1967–8), vol. III, 49. He uses 'want of knowledge (*jahl*)', instead of ignorance, as the essential element of *gharar*.
- 13 Kamali, *Islamic Commercial Laws: An analysis of Futures and Options* (Ilmiah publishers, Selangor, Malaysia, 2002), 85. Kamali describes *bai al maadum* (sale of non-existent object) and similarly the sale of something, the existence of which is doubtful as generally prohibited in Islam.
- 14 Ibn Rushd, *Bidayaat al Mujtahid wa Nihayaat al-Muqtasid* (Dar al Ma'rifa, Beirut, 1997), vol. 2, 156.
- 15 El-Gamal, *Islamic Finance: Law, Economics and Practice* (CUP, New York, 2006), 58.
- 16 El-Gamal, *Islamic Finance*, 60.
- 17 Vogel and Hayes, *Islamic Finance*, 88.
- 18 Vogel and Hayes, *Islamic Finance*, 89.
- 19 Ibid.
- 20 Ibn Abidin, *Hashiyyat Radd al Muhtar 'ala al-durr al-mukhtar sharh tanwir l-absar* (Mustapha Babi al-Halabi, Cairo, 1996), vol. 4, 147.
- 21 Sarakhsi, Abu Bakr Muhammad Ibn Ahmad, *Kitab al-Mabsut* (Dar al Ma'arif, Beirut, 1978), vol. 13, 194.
- 22 Ibn Al-Qayyim, *I'lam al Muwaqqai'in 'ala rabb al-'alamin*, edited by Taha 'Abd al-Ra'uf Sa'd (Dar al-Jil, Beirut, 1973), vol. 1, 357.

- 23 Tahir Mansuri, *Islamic Law of Contracts and Business Transactions* (Adam Publishers, New Delhi, 2006), 93–4.
- 24 See Al-Dhareer, *Al-Gharar in Contracts*, 14–17.
- 25 Ibn Juzayy, *Qawanin al-Ahkam al-Shari'iyah wa Masa'il al-Furu'iyah* (Dar al-Ilm al-Malayani, Beirut, 1979), 282–3.
- 26 Quoted in El-Gamal, *Islamic Finance*, 59.
- 27 Mansuri, *Islamic Law of Contracts and Business Transactions*, 81.
- 28 The evidential/conceptual distinction is considered in greater detail in section 4.5.
- 29 Al-Dhareer, *Al-Gharar in Contracts*, 44.
- 30 Mansuri, *Islamic Law of Contracts and Business Transactions*, 81.
- 31 Al Zuhayli, *Al-Fiqh al-Islami wa Adillatuh* (Dar al-Fiqr, Damascus, 1997), vol. 5, 2408, as referred to in El-Gamal, *Islamic Finance*, 58.
- 32 *Quran, al-Maidah*: 90. See El-Gamal, *Islamic Finance*, 58.
- 33 Al-Dhareer, *Al-Gharar in Contracts*, 38–43.
- 34 Nabil Saleh, *Unlawful Gain and Legitimate Profit* (Cambridge University Press, Cambridge, 1986), 59–61.
- 35 Al-Dhareer, *Al-Gharar in Contracts*, 39.
- 36 Nabil Saleh, *Unlawful Gain and Legitimate Profit*, 85.
- 37 Ibn al-Qayyim (1292–1350 ad/691 AH–751 AH) was a famous Sunni Islamic jurist, commentator on the *Quran*, astronomer, chemist, philosopher, psychologist, scientist and theologian. Although he is commonly referred to as 'the scholar of the heart,' given his extensive works pertaining to human behaviour and ethics. Ibn al-Qayyim's scholarship focused in the sciences of Hadith and *Fiqh*.
- 38 Ibn al-Qayyim al Jawziyyah, *I'lam al-muwaqqā'in 'ala rabb al-'alamin*, edited by Taha 'Abd al-Ra'uf Sa'd (Dar al-Jil, Beirut, 1973), vol. I, 357–61; vol. II, 153–4.
- 39 'Motive' can also be read *raison d'être*.
- 40 Al-Dhareer, *Al-Gharar in Contracts*, Kamali, *Islamic Commercial Laws and Saleh, Unlawful Gain and Legitimate Profit*.
- 41 The four main schools being the Shafi, Hanbali, Maliki and Hanafi schools of Islamic jurisprudence – all named after their founders.
- 42 Al-Dhareer, *Al-Gharar in Contracts*, 15, 23.
- 43 Al-Dhareer, *Al-Gharar in Contracts*, 16, describes the *arbutun* sale as one where the person buys an item and pays a certain amount of money to the seller on the understanding that if he did take the item the amount will form part of the total price but if he did not, he would forfeit the money already paid.
- 44 Al-Dhareer, *Al-Gharar in Contracts*, 16–17.
- 45 Al-Dhareer, *Al-Gharar in Contracts*, 18.
- 46 Al-Dhareer, *Al-Gharar in Contracts*, 23.
- 47 *Ibid*.
- 48 Ibn Juzayy, a Maliki author gives a list of 10 cases which constitute, in his view, forbidden *gharar*. See Saleh, *Unlawful Gain and Legitimate Profit*, 64.
- 49 Solaiman Ben Khalaf Al Baji, *Al-Montaqa: Annotations of Al-Muwatta* (Al-Saada Press, Cairo, AH 471), 287.
- 50 Al-Dhareer, *Al-Gharar in Contracts*, 51.
- 51 [1970] 2 All ER 228 per Lord Wilberforce at 248.
- 52 [1968] 3 All ER 785 at 793.

- 53 Beale (ed.), *Chitty on Contracts*, 30th edn (Sweet & Maxwell, London, 2008), vol. I, 223
- 54 Emphasis added. It is not a question of absolute certainty, which the courts acknowledge is impossible to attain, but sufficient certainty to create an enforceable contract.
- 55 Ewan McKendrick, *Contract Law: Text, Cases and Materials*, 2nd edn (OUP, Oxford, 2005), 138.
- 56 See *May and Butcher Ltd v King* [1934] 2 KB 17n; *Hillas v Arcos* (1932) 147 LT 503.
- 57 Beale, *Chitty on Contracts*, 223–4.
- 58 See section 4.2.
- 59 Beale, *Chitty on Contracts*, 240–3.
- 60 In *Walford v Miles* [1992] 2 AC 128 the House of Lords took the view that a duty to negotiate in good faith is unworkable in practice as it is inherently inconsistent with the interest of a negotiating party.
- 61 Encapsulated in the distinct approaches taken by the House of Lords in *Hillas v Arcos* (1932) 147 LT 503 and *May and Butcher Ltd v King* [1934] 2 KB 17n, respectively. See also, *Foley v Classique Coaches, Ltd* [1934] 2 KB 1, discussing the distinction between *May and Butcher* and *Hillas v Arcos*.
- 62 Beale, *Chitty on Contracts*.
- 63 McKendrick, *Contract Law*, 138.
- 64 *Hillas v Arcos* (1932) 147 LT 503, per Lord Wright, at 514.
- 65 Beale, *Chitty on Contract*, 203–22, 223–6.
- 66 *Walford v Miles* [1992] 2 AC 128. The court held that the duty to negotiate in good faith was unenforceable for uncertainty and inherently inconsistent with the position of a negotiating party. See Beale, *Chitty on Contracts*, 147.
- 67 *Welsh Development Agency v Export Finance Co. Ltd* [1992] BCLC 148. Undetermined facts do not render a contract ineffective, merely contingent on the ascertainment of those facts.
- 68 *G. Scammell & Nephew Ltd v Ouston* [1941] AC 251. See Beale, *Chitty on Contract*, 149.
- 69 McKendrick, *Contract Law*, 138.
- 70 [1934] 2 KB 17n.
- 71 In this context, a suppliant is one who petitions humbly of the king.
- 72 *May and Butcher v Regem* [1929] All ER Rep 679 at 680.
- 73 *Ibid.*
- 74 *May and Butcher v Regem* [1929] All ER Rep 679 at 682.
- 75 *May and Butcher Ltd v Regem* [1929] All ER Rep 679 at 682–3.
- 76 [1992] 1 All ER 453 at 461.
- 77 [1941] AC 251.
- 78 (1932) 147 LT 503.
- 79 [1941] 1 All ER 14 at 16.
- 80 [1941] 1 All ER 14 at 17–18.
- 81 *Hillas v Arcos* [1932] All ER Rep 494 at 495.
- 82 *Ibid.*
- 83 [1932] All ER Rep 494 at 500–1.
- 84 *May & Butcher* is currently almost unanimously disregarded by courts in deciding the issue of certainty of terms.

- 85 [1934] All ER Rep 88.
- 86 *Foley v Classique* [1934] All ER Rep 88 at 91–2, per Lord Scrutton.
- 87 *Ibid.*
- 88 Fletcher Challenge Energy Ltd v Electricity Corporation of New Zealand [2002] 2 NZLR 433.
- 89 [1934] 2 KB 17n.
- 90 Fletcher Challenge Energy Ltd v Electricity Corporation of New Zealand [2002] 2 NZLR 433.
- 91 Roy Goode, *Commercial Law* (3rd edn, Lexis Nexis, London, 2004), 73; See also, *Donwin Productions Ltd v EMI Films Ltd* (1984) *Times*, 9 March, Pain J. See also, *British Steele Corporation v Cleveland Bridge & Engineering Co. Ltd* [1984] 1 All ER 504.
- 92 See *Alstom Signalling Ltd v Jarvis Facilities Ltd* [2004] EWCH 1232; and also *Mamidoil-Jetioli Greek Petroleum Co. SA v Okta Crude Oil Refinery (No.1)* [2001] 2 Lloyd's Rep 76.
- 93 Roy Goode, *Commercial Law*, 83.
- 94 Roy Goode, *Commercial Law*, 84.
- 95 Beale, *Chitty On Contracts*, 124–5.
- 96 Beatson, J, *Anson's Law of Contract* (28th edn, OUP, New York, 2002), 61.
- 97 (1932) 147 LT 503 at 514.
- 98 *Brown v Gould* [1971] 2 All ER 1505.
- 99 *Gillat v Sky Television Ltd* [2000] 2 BCLC 103.
- 100 *May and Butcher v King* [1934] 2 K.B. 1. See also s 15(1) of the Supply of Goods and Services Act 1982.
- 101 *Foley v Classique* [1934] 2 KB 1.
- 102 [2006] EWHC 330 (Ch) paras 20–1.
- 103 See discussion in section 4.6.
- 104 For a contrasting approach to *May and Butcher* and consequent conclusion of the court, see *Sudbrook Trading Estate v Eggleton* [1983] 1 AC 444. See further, Jill Poole, *Text Book on Contract Law* (8th edn, OUP, Oxford, 2006), 95–6.
- 105 Jill Poole, *Text Book on Contract Law*, 91.
- 106 Roy Goode, *Commercial Law*, 87. For instance, the grant of first refusal of property as held in *Gardner v Coutts & Co.* [1967] 3 All ER 1064.
- 107 *Southern Foundries v Shirlaw* (1926) Ltd, [1940] AC 701. However, the courts are slow to imply a term on this ground. See Roy Goode, *Commercial Law*, 87–8.
- 108 For instance, implied into most contracts is the term that neither party will obstruct performance by the other. See *Mackay v Dick* (1881) 6 App Cas 251; *Bournemouth and Boscombe Athletic Football Club v Manchester United Football Club* (1980), *Times*, 22 May.
- 109 Such an implied term was not, however, actionable unless given as a warranty. See the famous case of *Chandelor v Lopus* (1603) Cro Jac 4. The prolonged influence of this case can be gauged from the fact that it was still being cited in 1957 in *Oscar Chess Ltd v Williams* [1957] 1 All ER 325. See also, Roy Goode, *Commercial Law*, 185.
- 110 *Scally v Southern Health and Social Services Board* [1992] 1 AC 294.
- 111 *Young and Marten Ltd v McManus Childs Ltd* [1969] 1 AC 454.
- 112 *Bolam v Friern Hospital Management Committee* [1957] 2 All ER 118; see *The Supply of Goods and Services Act 1982*, s 13.

- 113 See Saleh, *Unlawful Gain and Legitimate Profit*, 1–2.
 114 *Quran, Muhammad*: 19; *al-Tauba*: 24.
 115 *Quran, al-Rum*: 39.
 116 Karen Armstrong, *Muhammad: A Biography of the Prophet* (Phoenix Publishers, London, 2001), 68.
 117 It is mainly for this reason that 619 is known as the year of sorrow, for the Prophet is said to have grieved deeply upon losing his often only supporter, comforter and friend, Khadija. It is also thought that Khadija died because of the irreparable damage to her health caused by the food shortages.
 118 Armstrong, *Muhammad*.
 119 *Quran, al-Baqara*: 275.
 120 See Muhammad's saying (II) on *riba* in section 5.1.2.
 121 See chapter 1 on form versus substance of Islamic finance.

5 *Riba*: Meaning, Scope and Application

- 1 *Quran, al-Baqara*: 275; See also, in subsection 5.1.2., the saying of Muhammad where he rebukes Bilal for engaging in an apparently lawful barter-trade transactions as being 'the very essence of *riba*'.
- 2 M. T. Mansuri, *Islamic Law of Contracts and Business Transactions* (Adam Publishers, New Delhi 2006), 119.
- 3 El-Gamal, *Islamic Finance: Law Economics and Practice* (CUP, New York, 2006), 51–3.
- 4 Commercial, as we shall see in section 5.1. below, is widely defined to encompass any lawful trade or transactional dealings mutually consented to with the intention to be contractually bound.
- 5 *Quran, al-Baqara*: 275 and 282 are two key verses establishing this. We refer to them repeatedly throughout this chapter.
- 6 See 5.4 below for a fuller discussion of *riba* and consideration.
- 7 Dowry is addressed in the following verses of the *Quran, al-Nisa*: 4, 20–1 and 24–5; *al-Maida*: 5; *al-Ahzab*: 30 and *al-Mumtahina*: 60.
- 8 See section 5.4 below.
- 9 *Quran, al-Baqara*: 275.
- 10 *Quran, al-Baqara*: 175 and 182.
- 11 Mansuri, *Islamic Law of Contracts*, 84.
- 12 See *al-Baqara*: 282 and Muhammad's saying (II) at sub-section 5.1.2.
- 13 *Quran, al-Baqara*: 278
- 14 Tarek El-Diwany *The Problem with Interest* (2nd ed. Kreatoc Ltd, London 2003), 184–92.
- 15 Also expressed through the prohibition on gambling.
- 16 The term 'wealth' is used in the broad sense of value, not riches.
- 17 *Al-Baqara*: 278.
- 18 Among them being Abdulrahman ibn 'Awf.
- 19 Homa Katouzian, 'Riba and Interest in an Islamic Political Economy' (*Mediterranean Peoples Revue*, no. 14, Jan.–Mar. 1981), 97–109.
- 20 This is extrapolated from the distinction drawn between prohibited *riba* and *bay'* (commerce) in *Quran, al-Baqara*: 275. The phrase is adopted from Nabil Saleh's *Unlawful gain and legitimate profit* (CUP, Cambridge, 1986). The

distinction implies that gain (*riba*) may also be of the lawful kind and profit may be illegitimate.

- 21 *Quran, Ali-Imran*: 130–2.
- 22 *Quran, al-Baqara*: 275.
- 23 Extrapolated from the *Quran*'s distinction drawn in *al-Rum*: 39.
- 24 Roy Goode, *Commercial Law* (3rd edn, Lexis Nexis Butterworth, London, 2004), 579. See *Quran, al-Baqara*: 282.
- 25 *Quran, al-Baqara*: 282 and 275.
- 26 Amongst the four closest companions to the Prophet and the second Caliph after the Prophet's demise
- 27 Abdulkader Thomas (ed.) *Interest in Islamic Economics: Understanding Riba* (Routledge, London, 2006), 63.
- 28 The word *bay'* (sale) is a noun and thus, in Arabic, is preceded by the prefix *al* (the).
- 29 *Quran, al-Nisa*: 29; *Fatir*: 29.
- 30 *Al-Nisa*: 29.
- 31 *Quran, Ali-Imran*: 130
- 32 *Quran, al-Nisa*: 161
- 33 *Quran, al-Baqara*: 282, Yusuf Ali Translation. O ye who believe! When ye deal with each other, in transactions involving future obligations in a fixed period of time, reduce them to writing. Let a scribe write down faithfully as between the parties: let not the scribe refuse to write: as Allah Has taught him, so let him write. Let him who incurs the liability dictate, but let him fear His Lord Allah, and not diminish aught of what he owes. If they party liable is mentally deficient, or weak, or unable Himself to dictate, Let his guardian dictate faithfully, and get two witnesses, out of your own men, and if there are not two men, then a man and two women, such as ye choose, for witnesses, so that if one of them errs, the other can remind her. The witnesses should not refuse when they are called on (For evidence). Disdain not to reduce to writing (your contract) for a future period, whether it be small or big: it is more just in the sight of Allah, More suitable as evidence, and more convenient to prevent doubts among yourselves but if it be a transaction which ye carry out on the spot among yourselves, there is no blame on you if ye reduce it not to writing. But take witness whenever ye make a commercial contract; and let neither scribe nor witness suffer harm. If ye do (such harm), it would be wickedness in you. So fear Allah. For it is Good that teaches you. And Allah is well acquainted with all things. If ye are on a journey, and cannot find a scribe, a pledge with possession (may serve the purpose). And if one of you deposits a thing on trust with another, let the trustee (faithfully) discharge his trust, and let him Fear his Lord conceal not evidence; for whoever conceals it, – his heart is tainted with sin. And Allah knoweth all that ye do.
- 34 We return later to *Quran, al-Baqara*: 282, that is the only verse that mentions debt transactions (*dayn*) and future debt obligations between people yet makes no mention of *riba* at all. The entire verse is couched in terms of contractual agreement and commercial dealing. This is a clear indication that loan transactions fall within the category of 'trade', distinguished from *riba*, in *Quran* 2: 275.
- 35 Mansuri, *Islamic Law of Contract*, 126.

- 36 Reported by Muslim.
- 37 Dates are to be exchanged for dates of the same weight, measure, quality and on the spot. Dates cannot be exchanged for inferior or superior quality dates nor can dates be exchanged for barley, etc.
- 38 Reported by Muslim and Al-Nasai. See El-Gamal, *Islamic Finance*, 53.
- 39 A *sa* is a measure (of dates) and is akin to the expression, a bushel of wheat or barrel of oil, for instance.
- 40 *Quran, al-Nisa*: 29.
- 41 Oditah, *Legal Aspects of Receivables Financing* (Sweet & Maxwell, London, 1991), 1.
- 42 Mansuri, *Islamic Law of Contract*, 126.
- 43 It is however considered to be the worse of the two forms of *riba*.
- 44 Whereby interest was charged at maturity of debts from interest free loans or credit sales, and compounded at later maturity dates
- 45 This purported saying of Muhammad, not in any of the six chief collections, is related by the most respected scholars only on the authority of companions, not the Prophet. As a prophetic Hadith, scholars reject it as false. See Muhammad b. Ali al-Shawkani, *Nayl al awtar* (Mustafa Babi al-Halabi, Cairo, n.d.), 5: 262
- 46 Ibn Rushd, *Bidayat al-Mujtahid wa Nihayat al-Muqtasid* (Dar al-Ma'rifa, Beirut, 1997), vol. 3, 184.
- 47 See section 4.7 above.
- 48 El-Gamal, *Islamic Finance*, 53.
- 49 El-Gamal, *Islamic Finance*, 54.
- 50 Al-Misri, 'Hal Al-Faidah Haram bi Jami' Ashkaliha?' *Majallat Jami'at al Malik 'Abdulaziz lil-Iqtisad Al-Islami*, (2004), vol. 17, 1.
- 51 This conclusion has dire consequences for the prevalent sharia arbitrage conducted in the name of Islamic finance for the very products marketed as 'riba free' may be the very essence of *riba*.
- 52 Mark up (or cost plus margin) sale.
- 53 A variation of a sale and repurchase transaction involving 3 parties.
- 54 El-Gamal, *Islamic Finance*, 43.
- 55 El-Gamal, *Islamic Finance*, 55.
- 56 El-Gamal, *Islamic Finance*, 53.
- 57 Muhammad Saleem, *Islamic Banking – a \$300Billion Deception* (New York, 2005).
- 58 A.L.M. Abdul Ghafoor, *Interest, Usury, Riba and the Operational Cost of a Bank* (Percetakan Zafar Sdn Bhd, Kuala Lumpur, 2005).
- 59 Ibn Taymiyya, *Al-Fatawa al-Kubra* (Dar-al-Kutb al-Ilmiyyah, Beirut, 1987), vol. 29, 16.
- 60 Excessive to whom, by which standards and is it applicable to all sectors and jurisdiction?
- 61 A mechanism employed to determine the market interest rates for various borrowers based on credit worthiness and security of posted collateral.
- 62 The relevance of this distinction had otherwise only been mentioned once before Katouzian's paper in Syed Ahmad's 'The Concept and the Law of Riba in Modern Economic Environment' (Mimeo, 1978). Katouzian notes that Ahmad's paper focuses on the comparability of interest and merchant profit.

- 63 Eduardo Galeano, *Upside Down: A Primer for the Looking Glass World* (Picador, New York, 2000), 312.
- 64 See Muhammad's saying (II) in subsection 5.1.2 for illustration.
- 65 Adopted in *Currie v Misa* (1875) LR 10 Ex 153, 162.
- 66 (1966) 2 QB 617, Court of Appeal.
- 67 Ewan McKendrick, *Contract Law: Text, Cases and Materials* (2nd edn, OUP, Oxford, 2005), 161–2.
- 68 *White v Bluett* (1853) 23 LJ Ex 36. This (orthodox) view of consideration has, however, been challenged by several writers particularly Professor Atiya.
- 69 *Williams v Roffey Bros & Nicholls (Contractors) Ltd* [1991] 1 QB 1.
- 70 McKendrick, *Contract Law*, 165.
- 71 Treitel, *The Law of Contract* (12th edn, Sweet&Maxwell, London, 2008), 68.
- 72 McKendrick, *Contract Law*, 161–2.
- 73 McKendrick, *Contract Law*, 165.
- 74 [1960] AC 87, House of Lords.
- 75 *Williams v Roffey Bros & Nicholls (Contractors) Ltd* [1991] 1 QB 1.
- 76 [2009] All ER (D) 64 (Jan).
- 77 In *Antons Trawling Co Ltd v Smith* [2003] 2 NZLR 23 at para 93–4.
- 78 Oxford Paperback Dictionary, Thesaurus & Word Power Guide (OUP, Oxford, 2001), 11.
- 79 McKendrick, *Contract Law*, 164.
- 80 Treitel, *Law of Contract* (11th edn, Sweet & Maxwell, London, 2003), 68.
- 81 McKendrick, *Contract Law*, 164.
- 82 McKendrick, *Contract Law*, 165. See also, *Chappel & Co Ltd v The Nestle Co Ltd* [1960] AC 87, House of Lords.
- 83 (1875) LR 10 Ex 153, 162 in McKendrick, *Contract Law*, 163.
- 84 (1877) 2 App Cas 439 at 448.
- 85 *Quran, al-Nisa: 29 and al-Baqara: 275*. Generally, the *Quran* uses the term *aqd* for social and other obligations/contracts and the term *bay* for sale, trade or commercial transactions.
- 86 Beale (ed.), *Chitty on Contracts* (30th edn, Sweet & Maxwell, London 2008), vol. I, 253.
- 87 Beale, *Chitty on Contracts*, 240.
- 88 *Jones v Padavatton* [1969] 1 WLR 328; *Pettitt v Pettitt* [1970] AC 777; the presumption against an intention to form legal relations was rebutted in *Merritt v Merritt* [1970] 1 WLR 1211. See also *Gould v Gould* [1970] 1 Q.B. 275, where there was a division of opinion on the issue of contractual intention, the majority holding that there was no contractual intention where a husband on leaving his wife promised to pay her £15 per week so long as he could manage it.
- 89 *O'Brien v MGN Ltd* [2002] CLC 33; See also *Simpkins v Pays* [1955] 1 WLR 975 in which the presumption against an intention to form legal relations was rebutted.
- 90 *Esso Petroleum Ltd v Commissioners of Custom and Excise* [1976] 1 WLR 1; And see *Rose and Frank Co. v JR Crompton and Bros Ltd* [1925] AC 445 for a discussion on rebuttal of the presumption in commercial agreements.
- 91 [1919] 2 KB 571, Court of Appeal.
- 92 *Pearce v Merriman* [1904] 1 K.B. 80.
- 93 Beale, *Chitty on Contracts*, 241, citing *Synge v Synge* [1894] 1 Q.B. 466.

- 94 *White v Bluet* (1853) 23 LJ Ex 36.
 95 *Balfour v Balfour* [1919] 2 KB 571, Court of Appeal.
 96 [1955] 1 WLR 975.
 97 *Ibid.* at 979.
 98 J. Unger, 'Intent to create legal relations, mutuality and consideration' (1956) 19 MLR 96 at 98.
 99 [2001] EWCA Civ 274.
 100 [1991] 1 QB 1.
 101 Mindy Chen-Wishart, 'Consideration, Practical Benefit and the Emperor's New Clothes', in *Good Faith and Fault in Contract Law*, Beatson and Friedman (eds) (Clarendon Press, Oxford, 1995).
 102 (2003) NZLR 23.
 103 [2004] SEHC 71.
 104 Coote, 'Consideration and Benefit in Fact and Law', *Journal of Contract Law* (1990), 3, 23.

6 The Nature of Debt and the Legality of its Sale

- 1 Islamic law theory has it that debts may be 'sold' back to (their) creditors usually for either par value or at a discount. See Vogel and Hayes, *Islamic Law and Finance: Religion, Risk and Return* (Brill-Lieden, Boston, 2006), 115–117, for a discussion on Islamic law position. This is comparable to debt factoring or discounting of receivables under the common law as defined by Fidelis Oditah in *Legal Aspects of Receivables Financing* (Sweet & Maxwell, London, 1991), 44.
- 2 The maxim is alleged to be a saying of Muhammad albeit one of weak authentication. See, Hammad, '*Bay' al-Kali' bi al-Kali' fi al-Fiqh al-Islami*' (Markaz Abhath al-Iqtisad al-Islami, Jami'at al-Malik al-Abd al-Aziz, Jeddah, 1986), cited in Vogel and Hayes, *Islamic Law and Finance*, 115.
- 3 Literally meaning the exchange of two things both 'delayed' or the exchange of a delayed counter value for another delayed counter value.
- 4 The position is not, however, entirely clear as scholars permit the sale of a debt obligation by the creditor to the debtor but prohibit any such sale to a third party. See, Vogel and Hayes, *Islamic Law and Finance*, 116–17, 186.
- 5 An *Ijtihadic* issue is one on which there is no clear textual injunction and hence with regards to which Muslims can exercise independent reasoning so as to reach a conclusion, opinion or ruling.
- 6 In commercial affairs and all matters other than faith, the principle of permissibility applies as long as no clear text or Hadith exists to the contrary and the application remains within the objectives of the sharia, which shall be elaborated later in this chapter.
- 7 Sano Koutoub, *The Sale of Debt as Implemented by the Islamic Financial Institutions in Malaysia* (IIUM Press, Kuala Lumpur, 2004), viii.
- 8 Michael Bridge, *Personal Property Law* (3rd edn, OUP, Oxford, 2002), 6.
- 9 Oditah, *Legal Aspects of Receivables Financing*, 19–20.
- 10 Roy Goode, *Commercial Law* (3rd edn, Lexis Nexis Butterworth, London, 2004), 579.
- 11 S. Mahmasani, *The General Theory of the Law of Obligation and Contracts under Islamic Jurisprudence* (Dar al-Ilm lil malayin, Beirut, 1972), 67; Roy Goode, *Commercial Law*, 109, 579.

- 12 Michael Bridge, *Personal Property Law*, 14; Under Islamic legal theory this cessation of debt's existence happens through a transformation process called *ta'yin*, that is, debt is transformed into (physical) property.
- 13 Oditah, *Legal Aspects of Receivables Financing*, 1.
- 14 *Timmins v Gibbins* (1852) 18 Q.B. 722 at 726; *Littlechild v Banks* (1845) 7 Q.B. 739.
- 15 Oditah, *Legal Aspects of Receivables Financing*, 1.
- 16 Sachiko Murata, *The Tao of Islam* (State University of New York Press, New York, 1992), 2, 28. A distinction is made between the intellectual tradition and legalistic approach of the sharia scholars. The intellectual tradition is a deep current in Islamic thought that goes back to the *Quran* and the tradition of Muhammad. What distinguishes the intellectuals from the sharia scholars is that the former ask about the *why* of things, as well as the *how*, while the latter are mainly concerned with the *what* because they are largely concerned with telling people *what* to do.
- 17 M.T. Mansuri, *Islamic Law of Contracts And Business Transactions* (Adam Publishers, New Delhi, 2006), 198–9.
- 18 See section 5.1.2.
- 19 Vogel and Hayes, *Islamic Law and Finance*, 114–24. See also, El-Diwyany, *The Problem with Interest* (2nd edn, Kreatoc, London 2003), 83.
- 20 For a complete discussion, including Quranic verses and sayings of the Prophet, see chapter 5 on *riba*.
- 21 Sahih Muslim, Book 10, Number 3854.
- 22 Roy Goode, *Commercial Law*, 450. See *Moss v Hancock* [1899] 2 QB 111.
- 23 Goode, *Commercial Law*, 453.
- 24 Charles Proctor, *Mann on the Legal Aspects of Money* (6th edn, OUP, Oxford, 2005), 8.
- 25 Goode, *Commercial Law*, 452.
- 26 Bridge, *Personal Property Law*, 9.
- 27 Goode, *Commercial Law*, 579.
- 28 Roy Goode, *Consumer Credit* (A.W. Sijthoff, Leyden/Boston, 1978), vol. 3, ch. 40.
- 29 Goode, *Commercial Law*, 578.
- 30 Lawson and Rudden, *The Law of Property* (Clarendon Law Series, 2nd edn, Clarendon Press, Oxford, 1982), 27. See section 6.3.4.
- 31 Goode, *Commercial Law*, 451; see also Roy Goode, *Payment Obligations in Commercial and Financial Transactions* (Sweet & Maxwell, 1983), ch. 4.
- 32 *Miller v Race* (1758) 1 Burr 452.
- 33 Goode, *Commercial Law*, 451.
- 34 Goode, *Commercial Law*, 452.
- 35 Lawson and Rudden, *The Law of Property*, 27.
- 36 Now defined by statute in the Financial Services and Markets Act 2000 (Regulated Activities) Order 2001 (SI 2001/544).
- 37 [1996] 2 All ER 121 at 133–4.
- 38 [1997] 4 All ER 568 at 576.
- 39 Bridge, *Personal Property Law*, 1.
- 40 Bridge, *Personal Property Law*, 1.
- 41 *Ibid.*

- 42 Bridge, *Personal Property Law*, 5.
- 43 Bernard Rudden, 'Economic Theory v. Property Law' in Eekelaar & Bell (eds), *Oxford Essays in Jurisprudence* (Clarendon Press, Oxford, 1987), 243.
- 44 Rudden, 'Economic Theory v. Property Law', cites the Japanese CC 185; the Ethiopian CC 1204; the Louisiana CC 476–8 and the Thai CC 1298, among others.
- 45 Rudden, 'Economic Theory v. Property Law', 244.
- 46 Bougham LC in *Keppel v Bailey* (1834) My & K 517, 535.
- 47 Wilde B. in *Stockport Wwks v Potter* (1864) 3 H&C 300, 314.
- 48 O.W. Holmes, *The Common Law* (Cambridge, MA, 1967), 301, 316.
- 49 Rudden, 'Economic Theory v. Property Law', 246.
- 50 Gray and Gray, *Elements of Land Law* (OUP, Oxford, 2005), 107.
- 51 Gray and Gray, *Elements of Land Law*, 126.
- 52 Rudden, 'Economic Theory v. Property Law', 250.
- 53 Gray and Gray, *Elements of Land Law*, 127.
- 54 Bridge, *Personal Property Law*, 12.
- 55 See *Burton v London & Quadrant Housing Trust* [1998] QB at 845E, per Millett LJ.
- 56 *National Provincial Bank Ltd v Ainsworth* [1965] AC 1175 at 1248.
- 57 [2007] EWCH 220 (220) at para 72.
- 58 Bridge, *Personal Property Law*, 145.
- 59 Ibid.
- 60 Gray and Gray, *Elements of Land Law*, 127–8.
- 61 *National Provincial Bank Ltd v Ainsworth* [1965] AC 1175 at 1248.
- 62 *Dorman v Rodgers* (1982) 148 CLR 365 at 374 per Murphy J; *Delgamuukw v British Columbia* (1997) 153 DLR (4th) 193 at [113] per Lamer CJC.
- 63 *Dorman v Rodgers* (ibid.). See also K.J. Gray, 'Property, Divorce and retirement pension rights', in *Cambridge-Tilburg Law Lectures 1982* (Kluwer, 1986), 41–51.
- 64 Bridge, *Personal Property Law*, 7.
- 65 *Dorman v Rodgers* (1982) 148 CLR 365 at 368–70.
- 66 *Dorman v Rodgers* (1982) 148 CLR 365 at 371.
- 67 (1960) 104 CLR 186.
- 68 (1960) 104 CLR 186 at 205.
- 69 *Dorman v Rodgers* (1982) 148 CLR 365 at 371–2.
- 70 Reference is made to *Hoare & Co. v McAlpine* (1923) 1 Ch 167 at 175; and to Wallace and Grbich, 'A Judge's Guide to Legal Change in Property', *University of New South Wales Law Journal* (1979) vol. 3, 175.
- 71 *Dorman v Rodgers* (1982) 148 CLR 365 at 374–7.
- 72 Gray and Gray, *Elements of Land Law*, 128–9.
- 73 Rudden, 'Economic Theory v. Property Law', 249.
- 74 Gray and Gray, *Elements of Land Law*, 143.
- 75 Ibid., 102.
- 76 K. Gray, 'Property in Thin Air' [1991] CLJ 252 at 303–4.
- 77 *Dorman v Rodgers* (1982) 148 CLR 365 at 372 per Murphy J.
- 78 Gray and Gray, *Elements of Land Law*, 105. See also Jeremy Bentham, *An Introduction to the Principles of Morals and Legislation*, W. Harrison (ed.) (OUP, Oxford, 1948), 337.

- 79 Gray and Gray, *Elements of Land Law*, 102 quoting Hernando de Soto, *The Mystery of Capital: Why capitalism Triumphs in the West and fails Everywhere Else* (Bantam Press 2000), 42–3, that ‘property is not the [asset] itself but an economic concept about the [asset], embodied in a legal representation’. See also, *Yanner v Eaton* (1999) 201 CLR 351 at [18]. Also, *Kanak v Minister for Land and Water Conservation* (NSW) (2000) 180 ALR 489 at [31].
- 80 C.B. MacPherson, ‘Capitalism and the Changing Concept of Property’, in E. Kamenka and R.S. Neale (ed.), *Feudalism, Capitalism and Beyond* (Canberra 1975), 111.
- 81 Gray and Gray, *Elements of Land Law*, 102.
- 82 *Oxford English Dictionary* (Clarendon 1933), vol. VIII, 1496.
- 83 William C. Chittick, *The Self Disclosure of God: Principles of Ibn Arabi’s Cosmology* (State University of New York Press, Albany, 1998), xxiv.
- 84 Sano Koutoub, *The Sale of Debt as Implemented by the Islamic Financial Institutions in Malaysia* (IIUM Press, Kuala Lumpur, 2004), 64.
- 85 See section 6.1.
- 86 See section 6.4 generally and, specifically, views by Rudden, ‘Economic Theory v. Property Law’, 250, and Gray and Gray, *Elements of Land Law*, 128–9.
- 87 Decision 5 (D4/08/88), Fourth Session, *Fiqh Academy Journal* 3:2161.
- 88 Emphasis is mine.
- 89 [1965] AC 1175 at 1248.
- 90 Gray and Gray, *Elements of Land Law*, 128–9.
- 91 Zayla’i, *Tabyin al Haqa’iq*, vol. 4, 1717 as cited in Tahir Mansuri, *Islamic Law of Contract and Business Transactions* (Adam Publishers, New Delhi, 2006), 301.
- 92 Mansuri, *Islamic Law of Contracts And Business Transactions*, 301.
- 93 Beale, *Chitty on Contracts*, 1367. Chitty describes novation as taking place ‘where two contracting parties agree that a third, who also agrees, shall stand in the relation of either of them to the other. There is a new contract and it is therefore essential that the consent of all parties shall be obtained: in this necessity for consent lies the most important difference between novation and assignment’. Chitty cites the cases of *Rasbora Ltd v J.C.L. Marine Ltd* [1977] 1 Lloyd’s Rep. 645; *The Blankenstein* [1985] 1 W.L.R. 435; *The Aktion* [1987] 1 Lloyd’s Rep. 283, 310–11.
- 94 Beale, *Chitty on Contracts*, 1327.
- 95 *Ibid.*, 1362.
- 96 [1902] 2 .B. 660, 668 CA.
- 97 Beale, *Chitty on Contracts*, 1362.
- 98 *Al-Baqara*: 282–3.
- 99 *Quran, al-Baqara*: 282.
- 100 *Quran, al-Nisa*: 29.
- 101 *Quran: al-Baqara*: 275, pertaining to *riba*. See chapter 5, section 5.2.
- 102 Speculative uncertainty. For complete discussion and background see chapter 4.
- 103 El-Gamal, *Islamic Finance: Law, Economics and Practice* (Cambridge University Press, New York, 2006), 81, 90.
- 104 See section 4.4. and 4.5.
- 105 See section 6.2.
- 106 Literally meaning the exchange of two things both ‘delayed’ or the exchange of a delayed counter-value for another delayed counter value.

- 107 Beale, *Chitty on Contracts*, 983, defines a credit sale as an absolute contract of sale of goods in pursuance of an agreement under which payment of the whole or part of the purchase price is deferred.
- 108 Ibn Taymiyya in his book *Al Fatawa* vol. 3: 474 argues that the Hadith prohibiting the sale of two items at deferred delivery is the one universally accepted by scholars and not the version prohibiting the sale of debt with debt.
- 109 Vogel and Hayes, *Islamic Law and Finance*, 117.
- 110 [1997] 2 BCLC 460.
- 111 [1997] 2 BCLC 460 at 465–7.
- 112 Taqi Usmani, *An Introduction to Islamic Finance* (Kluwer Law International, The Hague, 2002), xiv–xvii.
- 113 El-Gamal, *Islamic Finance*, 14.
- 114 Koutoub, *The Sale of Debt*, 64.
- 115 Lawson and Rudden, *The Law of Property*, 27.
- 116 Art 125 of Majallat Al-Ahkam Al-Adliyya.
- 117 Rudden, ‘Economic Theory v. Property Law’, 244.
- 118 *In Re Bank of Credit and Commerce International SA* (No. 8) (1997) 4 All ER 568.
- 119 ‘It [the asserted charge] would be a proprietary interest in the sense that ... it would be binding upon assignees or a liquidator or trustee in bankruptcy’, [1997] 2 BCLC 577.
- 120 Lord Hoffman’s judgement is in contrast to Millett J’s earlier decision in, *Re Charge Card Services* [1989] Ch 497, that such a charge, taken by a bank over its own customer’s deposits, was conceptually impossible. See Goode, *Commercial Law*, 610.
- 121 *Re Bank of Credit and Commerce International SA* (No. 8) aka BCCI (No. 8) [1997] 4 All ER 568 at 574.
- 122 [1986] 3 All ER 289.

7 Securitisation

- 1 A primary Islamic capital market of sorts exists but not a secondary market as Muslim scholars maintain a ban on trading in financial assets. For greater detail, see chapter 6.
- 2 Typically receivables, such as home mortgage loans or credit cards receivables or leasing receivables. See Roy Goode, *Commercial Law* (3rd edn, Sweet & Maxwell, London, 2004), 147.
- 3 Vogel and Hayes, *Islamic Law and Finance: Religion, Risk and Return* (Brill-Lienden, Boston, 2006), 198.
- 4 Emphasis is theirs.
- 5 Vogel and Hayes, *Islamic Law and Finance*, 238.
- 6 In most cases a bank, investment institution, financier or company (i.e. an entity).
- 7 Mitchells and Butlers ‘What is a Securitisation’, www.mitchellsandbutlers.com/index.asp?pageid=456 accessed on 7 January 2009.
- 8 See chapter 1 for more detail.
- 9 The sale of asset by the originator to the SPV is required to be a true or clean sale that fully transfers ownership to the SPV for purposes of accounting rules and capital adequacy requirements among others.

- 10 If the asset was not 'truly sold' then it still belongs to the originator which in turn means that the SPV has merely borrowed it. The securities sold, therefore, represent the 'loan' taken by the SPV from the originator, not a sold asset. The loan character of the structure invokes the *riba* prohibition and renders any increase made on the transaction, prohibited.
- 11 That restricts the raising of finance to means such as sale, leasing, profit-sharing agreements but not through a money lending mechanism that involves interest or usury as conventional finance allows.
- 12 Philip Wood, *Project Finance, Securitisations, Subordinated Debt* (Sweet & Maxwell, London, 2007), 111. A sophisticated form of factoring or discounting receivables without recourse in order to raise money – instead of pledging the receivables.
- 13 Wood, *Project Finance, Securitisations, Subordinated Debt*, 111–12.
- 14 Also known as a bridging loan, that is, funds obtained from the originator or from the proceeds of sale of the notes or bonds to the investors.
- 15 The term subordination means that it is payable after the funding loan has been repaid.
- 16 Periodic payments owed arising out of a debt owed as a result of a contract of loan, mortgage, hire or sale on deferred payment.
- 17 See Goode, *Commercial Law*, 147–8, for explanation and illustration of a simple securitisation by sale of receivables.
- 18 Wood, *Project Finance, Securitisations, Subordinated Debt*, 114.
- 19 Philip Wood, Global Comparative Financial Law notes, BCL class of 2004/2005, University of Oxford.
- 20 The government of Qatar for example in the Qatar Global *sukuk* securitisation had as one of its objectives to support the development of its Islamic securities market.
- 21 Scott Hall, *International Finance: Law and Regulation* (Sweet & Maxwell, 2004), 338.
- 22 Belgium, France, Italy, Japan and Korea, all of which are 'mandatory notice' countries.
- 23 Philip Wood, *Project Finance, Securitisations, Subordinated Debt*, 134–5.
- 24 For Islamic finance, true sale compliance is vital because while conventional ABS typically assign right, *sukuk* must assign beneficial rights (via trust or an SPV) so as to be sharia compliant.
- 25 Wood, *Project Finance, Securitisations, Subordinated Debt*, 114.
- 26 Wood, *Project Finance, Securitisations, Subordinated Debt*, 156–7.
- 27 Roy Goode, *Legal Problems of Credit and Security* (4th edn, Sweet & Maxwell, London, 2008), 251.
- 28 *Orion Finance Ltd v Crown Financial Management Ltd* [1994] 2 BCLC 607 is a clear and relevant illustration of the effects of such re-characterisation.
- 29 Jan H. Dalhuisen, *Dalhuisen on International Commercial, Financial and Trade Law* (Hart Publishing, Oxford, 2000), 775–8.

8 Structuring a Securitisation to be Compatible with both the Sharia and Common Law

- 1 C.M. Henry, 'Financial Performances of Islamic versus Conventional Banks' in Henry and Wilson (eds), *The Politics of Islamic Finance* (Edinburgh University Press, Edinburgh, 2004), 104–25.

- 2 El-Gamal, *Islamic Finance: Law, Economics and Practice* (CUP, New York, 2006), 20–5; Henry, ‘Financial Performances of Islamic versus Conventional Banks’.
- 3 One tenth of the initial principal amount of the certificates.
- 4 This provision attracts criticism but it should be noted that LIBOR is only used as a bench mark and the returns themselves do not represent interest payments, but rather rental rates relating to a real underlying asset – the leased parcels of land. See Rodney Wilson, ‘Islamic bond: Your Guide to Issuing, Structuring and Investing in Sukuk’, in Adam and Thomas (eds) *Overview of the Sukuk Market* (London: Euromoney, 2004).
- 5 For a simple securitisation by way of sale of receivables, see Roy Goode, *Commercial Law* (3rd edn, Sweet & Maxwell, London, 2004), 147–8.
- 6 See section 6.8.
- 7 See Michael Duncan, Bimai Desai and Julie Rieger, ‘Islamic Bankers Take Role on International Projects’ *International Financial Law Review*, May [2004] 52. A bond issue is different from *sukuk* in that a bond issue involves the issue of debt instruments whereas the *sukuk* involves the issue of certificates containing an entitlement to an interest in the asset.
- 8 For a general discussion and critique on the ‘form-based’ orientation of Islamic finance, see El-Gamal *Islamic Finance: Law Economics and Practice*.
- 9 Depending on the jurisdiction, courts will study either the legal or economic, substance of the transaction. In Malaysia for instance, as in the UK, the courts will study the legal substance of the transaction as in cases involving the retention of title clauses, the objective of the transaction and the right to repurchase the property being irrelevant. Only the method (of dealing with the title/ownership in the assets) employed is scrutinised in determining whether the transaction is registerable as a charge.
- 10 Where certain characteristics of the transaction suggest that the transaction is more in the nature of financing rather than a sale, the SPV may risk the transfer or sale being re-characterised as one of security or financing.
- 11 [1994] 2 BCLC 607.
- 12 In *Orion*, the transaction was structured as a hire purchase that involved an assignment of the receivables (future book debts).
- 13 Trevor Norman, ‘Securitisation Structures within an Islamic Framework’ (July 2005, ISR Legal Guide), 22.
- 14 Issued by the sharia board of the Accounting and Auditing Organisation for Islamic Financial Institutions (AAOIFI) in May 2005.
- 15 Simon Gardner, *An Introduction to the Law of Trusts* (2nd edn, Oxford University Press, Oxford, 2003), 2.
- 16 See section 8.2.9.
- 17 Not to petition for the foreclosure of the SPV so as to cause the premature maturity of the securities.
- 18 The originator is insulated from the losses of the issuer or SPV.
- 19 Fitch Rating’s Emerging Markets Special Report ‘Securitisation and Sharia Law’, March 2005, 55. www.fitchratings.com, accessed 7 September 2006.
- 20 A. Abdel-Khaleq, ‘Offering Islamic Funds in the US and Europe’, *International Financial Law Review*, May [2004] 55 at www.iflr.com, last accessed on 10 March 2007.

- 21 In Malaysia, the Securities Commission (SC) established the Asset Securitisation Consultative Committee (ASCC) set up in March 2000 that has as its function to advise the SC on the steps needed to develop asset securitisation in the country. One of the issues it advises the SC on is tax and accounting impediments to securitisation.
- 22 Fitch Report, 'Securitisation and Sharia Law'.
- 23 Nik Ramlah, 'How Malaysia Plans to Dominate Islamic Markets', *International Financial Law Review* [2004] 61 at www.iflr.com, last accessed 10 March 2007.
- 24 Established by the Securities Commission (SC) in March 2000, one of the objectives of which was to advise the SC on how to develop asset securitisation in the country.
- 25 Malaysia Security Commission Report, 'Asset Securitisation in Malaysia: The way forward for the Malaysian Market's Asset Securitisation Consultative Committee (ASCC) November 2002, Appendix four.
- 26 It should be noted however that Malaysia enacted specific modifications to its tax code to allow for Islamic instruments to have peer status with conventional instruments, leveling the playing field for basic transactions as well as capital market activities. See, Walid Hegazy, 'Islamic Finance in Malaysia: A Tax Perspective', Paper presented at the proceedings of the 3rd Harvard University Forum on Islamic Finance (Middle Eastern Studies, Harvard University, Cambridge, MA, 1999), 215–24.
- 27 Malaysia Security Commission Report, 'Asset Securitisation in Malaysia'.
- 28 Without tax neutrality securitisation may lead to additional tax burdens for originators and if so, the originators' desire to enter into a securitisation may be considerably eroded.
- 29 Malaysia Security Commission Report, 'Asset Securitisation in Malaysia', 24–5.
- 30 Ireland, UK or Labuan, Malaysia.
- 31 Either due to cash shortages or due to the lack of appreciation of the substance of the concepts therein.
- 32 Morocco, for instance, passed a securitisation legislation in August 1999. The legislation provides that FPCT (SPV) is exempt from: (i) registration tax relating to its acquisition of assets, the issue or transfer of shares and bonds, amendment of its management regulations and any other acts relating to the functioning of the FPCT; (ii) business license tax; and (iii) corporation tax. The FPCT does, however, remain subject to certain provisions of corporate tax laws (declaratory obligations, accounting obligations, justification of expenses, book keeping, tax relating to investments proceeds, withholding). See report by Gide Loyrette Nouel, 'Emerging Markets Securitisation: Morocco' (25 November 2005), 23, www.gide.com, accessed 7 September 2006.
- 33 These legal issues were considered by Fitch Ratings in structuring the Caravan Securitisation of the Hanco-Rent-a-car fleet securitisation.
- 34 As seen in the discussion on the sale of debt, the scholars in Malaysia have adopted the minority view and by using the concept of *bayal-'ina* and *bay' al dayn* were able to permit the issuance of *bay' bi-thaman 'ajil* bonds. Both these contracts have been prohibited by scholars in the Middle East. It is also common that the views of contemporary scholars will differ from their more conventional counterparts or predecessors.

- 35 Clause 25 and 26 of the agreement described on its face as a ‘*Murabaha* financing agreement’ as per Tomlinson J in *Islamic Investment Company of the Gulf (Bahamas) v Symphony Gems IV & Others* [2002] QB Division (Com Ct).
- 36 It is no wonder therefore that Malaysia’s Islamic finance took off much faster than in the Middle East given the greater certainty by virtue of Malaysia being governed by common law (and the existence of specific banking legislation).
- 37 [2004] 2 All ER (D) 280.
- 38 Ibid.
- 39 Decision of Morison J [2003] 2 All ER (Comm) 849 affirmed.
- 40 See the report published by Fitch Rating in conjunction with Gide Loyrette Nouel titled ‘Securitisation and Sharia Law’. It is telling that the article does not distinguish, in its requirements, between conventional and *sukuk*-based securitisation structures.
- 41 [2003] 2 All ER (Comm) 849.
- 42 *Islamic Investment Company of the Gulf (Bahamas) v Symphony Gems IV & Others* [2002] QB Division (Com Ct) (unreported) heard by Tomlinson J. For a summary report see [2002] All ER (D) 171 (Feb).
- 43 [2004] EWCA Civ 19.
- 44 Ibid. at para 31.
- 45 [2004] EWCA Civ 19 at para 45.
- 46 [2001] 1 All ER (Comm) 103.
- 47 See section 3.2.7.
- 48 Adam and Thomas, *Islamic Bonds: Your Guide to Issuing, Structuring and Investing in Sukuk* (Euromoney Books, London, 2004), 13.
- 49 El-Gamal, *Islamic Finance: Law, Economics and Practice*, 16.
- 50 Ibid.
- 51 See section 7.6.
- 52 That would have negated a true sale (i.e. one cannot sell to one’s self) and hence runs the risk of being characterised as a loan to one’s self (subsidiary company).
- 53 Rahail Ali, ‘Sukuk Legal and Structuring Considerations’, posted at www.ajif.com, accessed 21 March 2006. Mr. Ali is a partner at the International law firm Denton Wilde Sapte, based in their Dubai Office.
- 54 This was a smart way of getting round both problems (creation of trust and choice of law and enforcement) because even if the alternative of having an off-shore SPV in a jurisdiction amenable to the trust had been used, the problem of choice of law and enforcement persists.
- 55 Malaysia Securities Commission’s Report on Asset Securitisation in Malaysia: ‘The way Forward for the Malaysian Market’, prepared by the Asset Securitisation Consultative Committee (ASCC) (November 2002), 22.
- 56 Malaysia is clearly a case in point that has become, by virtue of its progressive attitude towards its Islamic Capital Market (ICM), a leader to emulate in Islamic finance.
- 57 Kevin Brown, ‘Islamic financial sector needs firm regulation, says Malaysia’ (Singapore, 4 November 2009) www.ft.com, accessed 23 November 2009.

9 Islamic Finance in Malaysia: A Model to Emulate

- 1 The result of a working paper entitled '*Rancangan Membaiki Ekonomi Bakal-Bakal Haji*' presented by Royal Professor Ungku Aziz in 1959 to improve the economy of intending pilgrims.
- 2 Samer Soliman, 'The Rise and Decline of the Islamic Banking Model in Egypt', in Henry and Wilson, *The Politics of Islamic Finance* (Edinburgh University Press, Edinburgh, 2004), 267–8. Founded by Ahmad Najjar in 1963 as the first Islamic bank in Egypt, and the world. He based his bank on the German saving banks model, having earned his PhD in Germany in the field of social economics. Najjar, however, never made reference to Islam in its founding process due to fear that if he did it would be rejected 'in an era when hostility to the Islamic tendency was at its peak'.
- 3 This allows for interbank trading of Islamic financial instruments such as *mudharaba* (profit sharing) interbank investments (MIIs). The MII program allowed for Islamic banks in need of funds to obtain them from other Islamic banks by issuing profit-sharing certificates for a fixed investment period, from overnight to one year. The profit-sharing ratio is determined in advance, and the principal is repaid at the end of the loan period.
- 4 Dato', Dr. Awang Adek bin Husin deputy minister of finance 'The role of Malaysia in the internationalisation of Islamic finance', Labuan International Islamic Finance Lecture Series 1, 15 September 2006.
- 5 Dr. Zeti Akhtar Aziz, Governor of the Central Bank of Malaysia, 'Recent developments in Islamic finance in Malaysia', Keynote address at the Islamic Finance Issuers and Investors Forum 2006, Kuala Lumpur, 14 August 2006.
- 6 Kevin Brown in Singapore, 'Islamic financial sector needs firm regulation, says Malaysia', *Financial Times*, 4 November 2009 at www.ft.com.
- 7 Suleiman Abdi Dualeh 'Islamic Securitisation: Practical Aspects', World Conference on Islamic Banking, Geneva, 8–9 July 1998.
- 8 *Welsh Development Agency v Export Finance Co. Ltd* [1992] BCLC 148. See section 8.2.
- 9 Qatar in the Qatar's global *sukuk* in 2004.
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- 11 Stuart Gray 'Labuan' www.investoroffshore.com/html/specials December 2004.
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- 13 Datuk Ali Abdul Kadir, Chairman, Securities Commission, Malaysia, 'Wealth Creation and Asset Protection: The Complementary Roles of Offshore and Onshore Capital Markets', keynote address by YBhg at the Labuan Lecture Series, 2002.
- 14 Robin Wigglesworth, 'Creditors mobilise over Dubai debt plan', and 'Dubai World', *The Financial Times*, 2 December 2009, 1 and 18, respectively.

10 The Way Forward

- 1 Kishore Mahbubani, 'Lessons for the West from Asian Capitalism' in 'Future of Capitalism', *Financial Times*, 12 May 2009, 45.
- 2 Michael Skapinker, 'What is "socially useful" is subject to fashion', *Financial Times*, 8 September 2009, 13.

- 3 Simeon Kerr, 'Dubai Stuns Debt Market', *Financial Times*, 23 November 2009, 1, 18; See also, 'Future of Capitalism', *Financial Times*, 12 May 2009, 45.
- 4 Paul Kennedy, 'Read the big four to know capitalism's fate', in 'Future of Capitalism', *Financial Times*, 12 May 2009, 19.
- 5 Edmund Phelps, 'Uncertainty bedevils the best system' in 'Future of Capitalism', *Financial Times*, 12 May 2009, 46.

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